Litigating the Ordinary Course of Business Defense in Preference Actions: What is Ordinary, and How Do You Prove It?

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Under Chapter 5 of Title 11 of the United States Code (the "Bankruptcy Code"), bankruptcy trustees and debtors-in-possession are authorized to avoid as preferential, transfers made by a debtor within 90 days before a debtor's bankruptcy filing (the "Preference Period").[1] However, the Bankruptcy Code provides for an ordinary course of business ("OCB") defense that immunizes preferential transfers from avoidance if such transfers were made either in the ordinary course of the parties' business or ordinary business terms for the relevant industry.[2]

The term "ordinary course of business" is not defined in the Bankruptcy Code. However, Congress has stated that while the OCB exception is designed to leave undisturbed normal financial relations, the exception does not detract from the policy of the preference section of the Bankruptcy Code, which is to discourage unusual action by either the debtor or its creditors during the debtor's slide into bankruptcy."[3] By its nature, the OCB defense is an affirmative defense,[4] which defendants must prove by a preponderance of the evidence.[5]

A. The Subjective Test v. Objective Test

Prior to the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (the "BAPCPA"),[6] creditors were required to show that a preferential transfer was made in both the ordinary course of the parties' business and within ordinary business terms for the

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[1] 11 U.S.C. § 547(b)(4). For "insiders," the Preference Period extends back to one year before filing.
[2] 11 U.S.C. § 547(c)(2)(A) and (B).
[3] *Carrier Corp. v. Buckley* (*In re Globe Mfg. Corp.),* 567 F.3d 1291, 1298 (11th Cir. 2009); *Marathon Oil Co. v. Flatau* (*In re Craig Oil Co.),* 785 F.2d 1563, 1566 (11th Cir. 1986).
[4] *Intercontinental Publ'ns, Inc. v. Perry (In re Intercontinental Publ'ns, Inc.),* 131 B.R. 544, 550 (Bankr. D. Conn. 1991).
[5] *Official Comm. of Unsecured Creditors of J. Allen Steel Co. v. Winner Steel Servs. (In re J. Allen Steel Co.),* 321 B.R. 764, 770 (Bankr. W.D. Pa. 2005).
[6] Pub. L. No. 109-8, 119 Stat. 23.

relevant industry. Post-BAPCPA, creditors need only show that a preferential transfer was made **either** in the ordinary course of the parties' business **or** within terms ordinary in the industry.[7] Thus, the OCB defense consists of two separate, independent defenses codified in 11 U.S.C. § 547(c)(2)(A) (the "Subjective Test") and 11 U.S.C. § 547(c)(2)(B) (the "Objective Test).[8]

The Subjective Test measures whether each preferential transfer was ordinary in comparison to the parties' business dealings during the time period prior to the Preference Period (the "Historical Period").[9] Factors relevant to the Subjective Test include, but are not limited to:

- the timing of the transaction or payment;
- the length of time the parties engaged in the type of dealing at issue;
- whether the subject transfer was in an amount more than usually paid;
- whether the payments were tendered in a manner different from previous payments;
- whether there was any unusual action by either the debtor or creditor to collect or pay on the debt; and
- whether the creditor did anything to gain an advantage in light of the debtor's deteriorating financial condition.[10]

The timing of the transactions or payments is particularly important for the Subjective Test.[11] Usually, late payments are presumptively unordinary, but defendants can rebut this presumption by showing that late payments were the standard course of dealing between the parties.[12] For many years, the reported decisions on the OCB defense focused only on the recovery of late payments. However, since 2000, many courts have rejected defendants'

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[7] 11 U.S.C. § 547(c)(2).
[8] *Id.*
[9] *Globe Mfg.*, 567 F.3d at 1298 (quoting *Logan v. Basic Distribution Corp. (In re Fred Hawes Org., Inc.)*, 957 F.2d 239, 244 (6th Cir. 1992)).
[10] *Logan Square East v. Peco Energy Co. (In re Logan Square East)*, 254 B.R. 850, 855 (Bankr. E.D. Pa. 2000).
[11] *Sparkman v. Johnson Concrete Co. (In re Mainline Contracting, Inc.)*, 2012 WL 2373666, at *1 (Bankr. E.D.N.C. June 22, 2012); *Barnes v. Karbank Holdings, LLC* (*In re JS & RB, Inc.)*, 446 B.R. 350, 359 (Bankr. W.D. Mo. 2011); *Liebersohn v. WTAE-TV (In re Pure Weight Loss, Inc.)*, 446 B.R. 197, 205 (Bankr. E.D. Pa. 2009).
[12] *Davis v. All Points Packaging & Distribution, Inc. (In re Quebecor World (USA), Inc.)*, 491 B.R. 363, 369 (Bankr. S.D.N.Y. 2013).

arguments for a "safe harbor" for payments made within credit terms as *per se* ordinary.[13] Instead, if the payments were earlier than the historical baseline average, they were not to be considered within the OCB.[14]

The Objective Test measures whether each preferential transfer was ordinary in comparison to the norms prevailing in the parties' respective industries. Although expert testimony is not always required, this defense is sometimes known as the "battle" of the experts.

B. Subjective Test: Determining the Appropriate Historical Period Baseline and Methods to Analyze and Present Raw Data to Prove OCB Defense

In order to analyze the payment timing for the Subjective Test, the first step is to establish a historical baseline of past practices between the parties. The greater the deviation from the historical baseline, the less likely a defendant will be able to satisfy the Subjective Test. Determining the relevant historical baseline is a statistical endeavor, which may result in divergent outcomes depending on the time period examined. The following choices should be considered:

(1) The 12-month prior history;
(2) The 24-month prior history;
(3) The 24-month prior history, after excluding the immediate 90 days prior to the start of the preference period; or
(4) The 24-month prior history, after excluding the immediate 180 days prior to the start of the preference period.

Each of these date ranges should produce a different historical weighted average based on either the days past due or the invoice date to payment date. Many courts have held that

[13] *See Lovett v. St. Johnsbury Trucking (In re Transp. Sys. Int'l, Inc.)*, 931 F.2d 494, 499 (8th Cir. 1991) (opining that even if preference period payments were all made within the credit term, such a practice would have been a drastic departure from previous practice and presumably would have preferred the carrier over other creditors); *TWA, Inc. v. World Aviation Supply, Inc. (In re TWA, Inc. Post-Confirmation Estate)*, 327 B.R. 706, 709 (Bankr. D. Del. 2005) (determining payments made within stated credit terms were not ordinary when prior history between parties had been late payments); *R.M. Taylor, Inc. v. Employers Ins. of Wausau (In re R.M. Taylor, Inc.)*, 245 B.R. 629, 637 (Bankr. D. Mo. 2000) (stating payments made before the due date were not within the ordinary course of business between the parties and evinced a clear preferential effect and was a substantial departure from prior dealings).

[14] *Id.*

the comparative historical baseline should be based on the time frame when the debtor was financially healthy.[15] Accordingly, excluding the 90- or 180-day pre-preference transaction period is intended to foster a comparison to when the debtor was, presumably, financially healthy. When presented with the option of using the 12-month prior history or the 24-month prior history as the baseline, one court held that a two-year Historical Period was more accurate than a one year Historical Period because the two-year period "more accurately reflect[ed] the parties' ordinary course of dealings during the period when the Debtor was in better financial health."[16] Further, some courts have even held that Historical Periods shorter than one year are insufficient to establish a historical baseline.[17] However, this does not mean that an OCB defense under 11 U.S.C. § 547(c)(2)(A) is unavailable to creditors who have no Historical Period business dealings with debtors.[18] Ultimately, the selection of the appropriate Historical Period depends on the facts and circumstances of each case, taking into consideration any events during

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[15] *See Fiber Lite Corp. v. Molded Acoustical Prods., Inc. (In re Molded Acoustical Prods., Inc.)*, 18 F.3d 217, 227 (3d Cir. 1994) ("'Ordinary business terms' for purposes of ordinary course of business preference avoidance exception are those that prevail in healthy, not moribund" companies); *Clark v. Balcor Real Estate Fin., Inc. (In re Meridith Hoffman Partners)*, 12 F.3d 1549, 1553 (10th Cir. 1993) ("Ordinary business terms therefore are those used in 'normal financing relations': the kinds of terms that creditors and debtors use in ordinary circumstances, when debtors are healthy"); *Siegel v. Russellville Steel Co. (In re Circuit City Stores, Inc.)*, 479 B.R. 703, 710 (Bankr. E.D. Va. 2012) (holding that the appropriate historical baseline in the matter at issue consisted of transactions occurring prior to the debtors' pre-petition "liquidity event," but did not include historical transactions occurring after the liquidity event (*i.e.*, a Historical Period akin to scenario 4 described *supra*); *Moltech Power Sys., Inc. v. Tooh Dineh Indus., Inc. (In re Moltech Power Sys., Inc.)*, 327 B.R. 675, 680-81 (Bankr. N.D. Fla. 2005) (noting that some courts have indicated that the baseline established should focus on a period well before the debtor experienced financial problems); *Plan Admin. Agent v. Coastal Indus. (In re Kevco, Inc.)*, 2005 WL 6443621, at *13 (Bankr. N.D. Tex. June 30, 2005) (stating that baseline period should extend back to before the debtor became financially distressed to when "ordinary" in layman's terms); *Gonzales v. DPI Food Prod. Co. (In re Furrs Supermarkets, Inc.)*, 296 B.R. 33, 41 (Bankr. D.N.M. 2003) (determining the comparison of ordinariness should be preferably before the debtor starting experiencing financial problems).

[16] *Davis v. R.A. Brooks Trucking, Co., Inc. (In re Quebecor World (USA), Inc.)*, 491 B.R. 379, 387 (Bankr. S.D.N.Y. 2013).

[17] *See Burtch v. Revchem Composites, Inc. (In re Sierra Concrete Design, Inc.)*, 463 B.R. 302, 306 (Bankr. D. Del. 2012); *Morris v. Sampson Travel Agency, Inc. (In re U.S. Interactive, Inc.)*, 321 B.R. 388, 393 (Bankr. D. Del. 2005).

[18] *Sklar v. Susquehanna Bank (In re Global Prot. USA, Inc.)*, 546 B.R. 586, 615 (Bankr. D.N.J. 2016) (a payment that is a first time transaction between the parties "may still be in the ordinary course if it did not favor certain creditors or encourage a race to the courthouse").

the Historical Period, such as a change in terms or change in debtor financial circumstances, which would advocate for the selection of one period of time over another.

After determining the appropriate historical baseline, the next step is to show that the Preference Period payments are ordinary in comparison to the historical baseline. There are two main approaches: (1) calculate the allowed OCB deviation from the historical weighted average (the "Average Lateness Method"), or (2) determine whether the Preference Period fit within the total range of Historical Period payments (the "Total Range Method").

For the Average Lateness Method, the historical weighted average obtained from the historical baseline serves as the mean (average) from which an acceptable OCB range is determined. The OCB range is computed in one of two ways:

(1) As a percentage of the historical weighted average; or
(2) As a selected number of days +/- from the historical weighted average.

For example, if the historical weighted average is 20 days, a deviation percentage of 30% would yield an OCB range of 14 to 26 days. Payments within the preference period that fell within this range would be credited as within the OCB. If instead, a deviation of 5 days was applied, the OCB range would be 15 to 25 days. Whether the party applies a percentage or days range is based upon both the credit terms and the historical weighted average.

It also may be very significant as to whether the historical weighted average is based upon days past due or upon invoice date to payment. Consider the following chart:

Term	PP Inv to Pay	Hist Inv To Pay	Diff by Days	% Change	PP Days Past Due	Hist Days Past Due	% Change
30	60	50	10	**20%**	30	20	**50%**
15	60	50	10	**20%**	45	35	**28.5%**
10	24	16	8	**50%**	14	6	**130%**

From a plaintiff's viewpoint, if there has been no contraction in credit terms, a days past due analysis will yield the greatest deviation in percentage terms from the baseline. However, defendants should present their case using invoice date to payment date as the results will appear less significant on a percentage basis. Figure (1) to these materials provides a graphical representation of an OCB range based on +/- 15 days from the historical weighted average.

If there is a change in terms during or right before the preference period then it may be possible to disguise a deviation in payment timing by using a days past due analysis. The argument for using a days past due analysis is enhanced if the change of terms can be tied to the creditor granting additional discounts to justify the reduced payment terms or where the debtor needs to ramp up orders for a special sale.[19] For example, if a debtor consistently paid based on invoice terms at 10 days from the due date and there was a change in terms from 60 days to 30 days, the debtor would still be paying 10 days late in both time periods and an argument can be made that there was no change in the payment pattern. However, if an invoice to payment analysis is performed on this same payment pattern, the debtor will be shown to have paid within 70 days during the historical period and 40 days during the preference period, a 57% change between the two time periods.

[19] *See Montgomery Ward, LLC v. OTC Int'l, Ltd. (In re Montgomery Ward, LLC)*, 348 B.R. 662, 679 (Bankr. D. Del. 2006).

For the Total Range Method, the smallest amount of days from the invoice date to the payment date and the largest amount of days from the invoice date to the payment date will be used to determine the Historical Period range. Then, the Preference Period payments that fit within the Historical Period range will be considered ordinary. For example, during the Historical Period, if the smallest amount of days from the invoice date to the payment date is 10 and the largest amount of days from the invoice date to the payment date is 150, the Historical Period range would be 10 to 150 and any Preference Period payments made within that range would be deemed ordinary. The Total Range Method is clearly an attractive option for defendants, as it has the potential to protect a wide range of payments from avoidance. However, it should be noted that some courts have rejected the Total Range Method because it "captures outlying payments that skew the analysis of what is ordinary," and thus, may impermissibly expand the ranges of ordinary transactions.[20] In order to alleviate this concern, some courts have used the Total Range Method, but did not include outliers in determining the appropriate Historical Period range.[21]

C. Subjective Test and Collection Pressure: How Much is Too Much?

The OCB defense should protect payments that do not result from unusual debt collection or payment practices.[22] Thus, courts have concluded that unusual collection activity during the Preference Period can support a finding that preferential payments were made outside of the OCB.[23] Generally, collection pressure is an issue that only arises in the context of

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[20] *Quebecor World*, 491 B.R. at 387-88 (citing *Jacobs v. Gramercy Jewelry Mfg. Corp.* (*In re M. Fabrikant & Sons, Inc.)*, 2010 WL 4622449, at *3 n. 2 (Bankr. S.D.N.Y. Nov. 4, 2010)).

[21] *See Goodman v. Reama, Inc. (In re Gulf Fleet Holdings, Inc.)*, 2014 WL 1168791, at *4 (Bankr. W.D. La. Mar. 21, 2014); *Yaquinto v. Arrow Financial Servs. (In re Brook Mays Music Co.)*, 418 B.R. 623, 629 (Bankr. N.D. Tex. 2009).

[22] *Craig Oil*, 785 F.2d at 1566.

[23] *See Frank v. Volvo Penta of the Americas, Inc. (In re Thompson Boat Co.)*, 173 F.3d 430, 430 (6th Cir. 1999); *Craig Oil*, 785 F.2d 1563; *Official Comm. of Unsecured Creditors of 360Networks (USA) Inc. v. U.S. Relocation Services, Inc. (In re 360Networks (USA) Inc.)*, 338 B.R. 194, 211 (Bankr. S.D.N.Y. 2005).

the Subjective Test. However, some courts will assess whether a creditor's collection activity is unusual when compared to industry norms.[24]

The two key issues to consider regarding collection pressure are: (1) whether the creditor engaged in unusual collection activities to induce the debtor to make a preferential payment; and (2) whether the debtor made a preferential payment in response to the unusual collection activities. In determining whether a creditor's collection activities are unusual, courts will often compare the collection efforts in the Preference Period with those in the Historical Period to ascertain whether the Preference Period collection actions significantly deviate from the OCB between the parties.[25] This is a highly factual analysis performed on a case-by-case basis.[26] To determine whether a debtor made a Preference Period payment in response to collection pressure, courts will consider the debtor's motive in making the payments. It is also important to note that the absence of unusual collection activity, on its own, will not suffice to establish a subjective ordinary course of business defense.[27]

A defendant can bolster an OCB defense by showing that it conducted similar collection activities during the Preference Period and the Historical Period. However, it appears that this may be limited to phone calls, letters, and emails.[28] In the context of changing credit terms,

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[24] *See Kevco,* 2005 WL 6443621, at *23 (defendant failed to support objective ordinary course defense where, among other deficiencies, defendant's expert failed to do any research with respect to collection practices in the industry and whether the efforts taken by defendant were consistent with industry practice); *Howard v. Canadian Am. R.R. Co. (In re Bangor & Aroostook R.R. Co.),* 324 B.R. 164, 173-74 (Bankr. D. Me. 2005) (considering, as part of the objective ordinary course analysis, how electric utilities in Maine deal with delinquent accounts, including the presence and extent of collection efforts); *Seaver v. Allstate Sales & Leasing Corp. (In re Sibilrud),* 308 B.R. 388, 398 (Bankr. D. Minn. 2004) (finding that the objective ordinary course of business exception did not apply because the evidence presented established that only defendant filed mechanic's liens, suggested promissory notes or attempted to otherwise negotiate a workout or restructure the outstanding debt, commenced litigation or obtained judgments against debtor, or sought to garnish debtor's wages).

[25] *Rifken v. Entec Distribution, LLC* (*In re Felt Mfg. Co., Inc.),* 2009 WL 3348300, at *8 (Bankr. D.N.H. Oct. 16, 2009).

[26] *Id.*

[27] *Davis v. Clarklift-West, Inc. (In re Quebecor World (USA), Inc.),* 518 B.R. 757, 765 (Bankr. S.D.N.Y. 2014).

[28] *See Mainline Contracting,* 2012 WL 5247173, at *8 (routine phone calls and emails throughout the Preference Period and Historical Period did not constitute unusual collection activity); *Grant v. SunTrust Bank (In re L. Bee*

courts have held that imposing stricter terms at some earlier point in the parties' relationship does not dictate that such activity is ordinary during the Preference Period.[29]

Examples of creditor actions that courts have held to constitute unusual collection activity are: repeated collection calls resulting in a debtor concluding that it would have to pay outstanding invoices in order to receive new product;[30] refusals to deliver new products unless a debtor agreed to make payment on outstanding invoices;[31] new requirements of a letter of credit and substantial down payment and prepayment;[32] executing a debt settlement or debt restructuring agreement with the debtor;[33] tightening credit terms and imposing a new credit limit;[34] bringing a lawsuit and obtaining a judgment against a debtor,[35] and contacting a debtor's employees to inquire about the status of payment coupled with the defendant's representative personally picking up checks from the debtor's headquarters.[36]

D. Objective Test: Proving an Ordinary Business Terms Defense

To satisfy the Objective Test and prove that a Preference Period transfer was made according to ordinary business terms, a defendant creditor must: (1) define the appropriate

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Furniture Co., Inc.), 203 B.R. 778, 783 (Bankr. M.D. Fla. 1996) (holding phone calls from a creditor after sending invoices and past due notices were routine and in the ordinary course of business throughout the parties' relationship); *Huffman v. New Jersey Steel Corp. (In re Valley Steel Corp.)*, 182 B.R. 728, 738 (Bankr. W.D. Va. 1995) (finding evidence that a creditor routinely made phone calls encouraging payment between 45 and 60 days after the invoice date was standard means of collection).

[29] *See Hechinger Inv. Co. of Delaware, Inc. v. Universal Forest Prods., Inc. (In re Hechinger Inv. Co. of Delaware, Inc.)*, 489 F.3d 568, 578 (3d Cir. 2007); *Prudential Real Estate and Relocation Services, Inc. v. Burtch (In re AE Liquidation, Inc.)*, 2015 WL 5301553, at *5 (D. Del. Sept. 10, 2015).

[30] *See Schwinn Plan Committee v. AFS Cycle & Co., Ltd.* (*In re Schwinn Bicycle Co.)*, 205 B.R. 557, 572–573 (Bankr. N.D. Ill. 1997). *But see, McCarthy v. Navistar Financial Corp. (In re Vogel Van & Storage, Inc.)*, 210 B.R. 27, 36-37 (N.D.N.Y. 1997) (in absence of economic threats or coercion to induce payment, collection calls reminding a debtor that a payment was past due were not unusual collection activity).

[31] *See Braniff, Inc. v. Sundstrand Data Control, Inc. (In re Braniff, Inc.)*, 154 B.R. 773, 781–782 (Bankr. M.D. Fla. 1993).

[32] *See Production Steel, Inc. v. Sumitomo Corp. of America* (*In re Production Steel, Inc.)*, 54 B.R. 417, 423 (Bankr. M.D. Tenn. 1985).

[33] *See J.P. Fyfe, Inc. of Florida v. Bradco Supply Corp.*, 891 F.2d 66, 71-72 (3d Cir. 1989).

[34] *See Hechinger*, 489 F.3d at 578.

[35] *See Sibilrud*, 308 B.R. at 396.

[36] *BFW Liquidation, LLC v. Blue Bell Creameries, Inc. (In re BFW Liquidation, LLC)*, 2016 WL 7383719, at *5 (Bankr. N.D. Ala. Dec. 20, 2016).

industry; (2) demonstrate the norms of that industry; and (3) show that the preferential payment fell within the norms in that industry.[37]

For the first prong of the Objective test, defining the relevant industry, there is a split of authority as to whether the court should look at the creditor's industry,[38] the debtor's industry,[39] or both industries.[40] However, as discussed below, it may be both industries post-BAPCPA. Once the relevant industry is defined, courts also consider how broadly or narrowly to define the industry. In *Tolona Pizza*, a leading decision on the ordinary business terms defense, the Seventh Circuit made clear that "ordinary business terms refers to the range of terms that encompasses the practices in which firms similar in some general way to the creditor engage."[41] Since that decision, courts inquiring into ordinary business terms frequently require defendants to present "evidence of prevailing practices among similarly situated competitors facing the same or similar problems."[42] To determine the types of firms that are "similar in some general way to the creditor," most courts review not only the creditor's activity, but the creditor's activity in relation to the debtor because creditors may have different practices depending upon with whom and in what capacity they are dealing.[43]

For the second prong of the Objective Test, demonstrating the norms of the relevant industry, many courts rely on expert testimony to establish the industry practice, including

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[37] *Webster v. The Management Network Group, Inc., (In re NETtel Corp., Inc.),* 364 B.R. 433, 453 (Bankr. D.D.C. 2006).
[38] *Advo-System, Inc. v. Maxway Corp.*, 37 F.3d 1044, 1048 (4th Cir. 1994).
[39] *Shodeen v. Airline Software, Inc. (In re Accessair, Inc.),* 314 B.R. 386, 394 (8th Cir. BAP 2004).
[40] *Ganis Credit Corp. v. Anderson (In re Jan Weilert RV, Inc.),* 315 F.3d 1192, 1197 (9th Cir. 2003).
[41] *In re Tolona Pizza Prods. Corp.*, 3 F.3d 1029, 1033 (7th Cir. 1993).
[42] *Jones v. United Savings and Loan Assoc. (In re U.S.A. Inns of Eureka Springs, Ark., Inc.),* 9 F.3d 680, 685 (8th Cir. 1993).
[43] *Moglia v. ISP Techs., Inc. (In re DeMert & Dougherty, Inc.),* 232 B.R. 103, 109–10 (N.D. Ill. 1999). *See also Eureka Springs*, 9 F.3d at 685 (holding that the relevant industry was savings and loans firms dealing with real estate firms, not savings and loans firms in general); *Schwinn Bicycle*, 205 B.R. at 573 (finding relevant industry that of treadmill manufacturers rather than broader sports or exercise equipment manufacturers); *Solow v. Ogletree (In re Midway Airlines, Inc.),* 180 B.R. 1009, 1016 (Bankr. N.D. Ill. 1995) (finding relevant industry consisted of the domestic air carrier legal services industry rather than the broader legal services or air carrier services industry).

the length of time that it takes other entities in that industry to be paid by customers.[44] Frequently, experts will rely upon information from the Risk Management Associates, Dunn & Bradstreet, and other business publications to determine the days to pay in the industry.

Although the use of expert testimony is common for the ordinary business terms defense, it can be quite costly and is not required as long as the rules of evidence regarding lay testimony are satisfied, namely Federal Rule of Evidence 701.[45] Defendants may use evidence of a competitors' credit practices to support an ordinary business terms defense.[46] For example, a court held that the testimony of the credit manager of the defendant's competitor was sufficient to establish the industry standard when such competitor held 90% of the industry.[47] Defendants can also meet their burden of proof by providing non-expert testimony from their employees, but such testimony must be based upon the employees' first-hand knowledge.[48] Thus, employees, unlike experts, cannot base their testimony on data from business publications.

Post-BAPCPA, defendants may face greater challenges when relying on the testimony of employees to meet their burden of proof on the ordinary business terms defense. The Eastern District of North Carolina's *National Gas* decision was the first to construe the post-BAPCPA

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[44] *Schnittjer v. Alliant Energy Co. and Interstate Power & Light Co. (In re Shalom Hospitality Inc.),* 293 B.R. 211, 215 (Bankr. N.D. Iowa 2003).

[45] Federal Rule of Evidence 701 states that "if the witness is not testifying as an expert, the witness' testimony in the form of opinions or inferences is limited to those opinions or inferences which are (a) rationally based on the perception of the witness, and (b) helpful to a clear understanding of the witness's testimony or the determination of a fact in issue, and (c) not based on scientific, technical, or other specialized knowledge within the scope of Rule 702."

[46] *Maxwell v. IDC (In re marchFirst, Inc.),* 381 B.R. 689, 697 (Bankr. N.D. Ill. 2008).

[47] *Frank v. Volvo Penta of the Americas (In re Thompson Boat Co.),* 199 B.R. 908, 916 (Bankr. E.D. Mich. 1996).

[48] *Sibilrud,* 308 B.R. at 397. *See also Eureka Springs,* 9 F.3d at 685 (a bank president's testimony on the real estate loan industry was acceptable); *Rice v. Hydro Temp Corp. (In re GS Inc.),* 352 B.R. 858, 866 (Bankr. E.D. Ark. 2006) (the testimony of the president of a company that had been in the relevant industry for 30 years was acceptable to prove the industry standard); *Midway Airlines,* 180 B.R. at 1017 (court accepted a law firm managing partner's testimony regarding his firms' competitors' credit practices, including how they handled aging accounts and accounts receivable as evidence of the industry standard).

ordinary business terms defense.[49] The defendant relied upon an affidavit of one of its loan officers, who had 30 years of banking experience, to establish industry terms.[50] In determining whether the defendant had met its defense, the court analyzed whether post-BAPCPA, the phrase "ordinary business terms" had new import in its new independent context.[51] Among other things, the court noted that the National Bankruptcy Review Commission recommended that the industry standard defense only be available where there is limited history between the parties.[52] This recommendation was consistent with pre-BAPCPA case law which gave more weight to the subjective ordinary course of business defense. However, Congress ignored this recommendation by establishing separate subjective and objective ordinary course of business defenses.[53]

Importantly, the court clarified that, under the BAPCPA, an ordinary business terms analysis not only required that both the creditor's and the debtor's industry standards be examined, but also "general business standards" as well.[54] The court addressed both parties' industries and found the defendant's affidavit was "too general to establish industry norms" and that "generality would render the subsection virtually meaningless."[55]

Although *National Gas* suggests that the burden of proof under the objective prong is more stringent under the post-BAPCPA statute, recent cases discussing the objective standard suggest that, at least in the Second and Sixth Circuits, courts are less inclined to deviate from

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[49] *Hutson v. Branch Banking & Trust Co. (In re National Gas Distribs., LLC)*, 346 B.R. 394 (Bankr. E.D.N.C. 2006).
[50] *Id.* at 399.
[51] *Id.* at 400.
[52] *Id.* at 401.
[53] *Id.* at 402.
[54] *Id.* at 404.
[55] *Id.* at 404-05.

the pre-BAPCPA standard.[56] Thus, while there are now two, distinct OCB defenses, there is a growing circuit split over whether the post-BAPCPA objective standard has become more difficult to prove. Whereas, in the past, a defendant's self-serving affidavits have been adequate proof of ordinary business terms, as a stand-alone defense more will likely be required in the Fourth Circuit. In the Second and Sixth Circuit, where there has traditionally been a liberal application of whether a transaction met the objective industry standard, this standard may remain the same post-BAPCPA.

For practical purposes, the extent of liability may dictate whether or not expert testimony is utilized. When the face value of the complaint counsels against the expense of expert testimony, the well-documented, credible testimony of more than one person with industry knowledge may be sufficient. However, when a defendant is exposed to increased liability, the conservative approach is to secure the services of at least one expert, with supplemental testimony provided by the corporate representative.[57]

There are several ways to satisfy the final prong of the Objective Test, which is proving that the Preference Period payment fell within the industry norms. Frequently, an expert will testify to a days to pay range from a business publication and, if the Preference Period payment falls within such range, the expert will opine that the Preference Period payment was made within ordinary business terms. It is also possible to use a single standard deviation from

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[56] *See Simon v. Gerdau MacSteel* (*In re Am. Camshaft Specialties, Inc.*), 444 B.R. 347, 364 (Bankr. E.D. Mich. 2011) (citing the Sixth Circuit standard that the transactions at issue must only resemble a majority of an industry's transactions, rather than a significant percentage, the court found that the transfers were made in accordance with ordinary business terms); *Pereira v. United Parcel Service of Am., Inc. (In re Waterford Wedgwood USA, Inc.),* 508 B.R. 821, 831 (Bankr. S.D.N.Y. 2014) (citing the Second Circuit standard that a creditor only needs to prove that the business terms of the transaction in question were "within the outer limits of normal industry practices").

[57] 4 *Norton Bankr. L. & Prac.* 3d § 66:22.

the mean and the Average Lateness Method, discussed above, to determine whether a Preference Period payment was ordinary in the industry.[58]

E. Conclusion

Both the subjective and objective OCB defenses provide defendants with the tools, depending on the circumstances, to dramatically and sometimes completely eliminate preference liability. The savvy defendant that keeps detailed and electronic payment records, as well as an ear on its industry practices, is a defendant well-prepared to respond to preference demands.

[58] *See Waterford Wedgwood*, 508 B.R. at 835-36.

Fig. 1- AGE BUCKET ANALYSIS

(*Explanation of chart found on following page)*

AcctNo	QBCABCD01	Aging Analysis Comparing Pref Period To Historical Period From			10/26/2005	To	10/22/2007	726	Days
ABC Sample Co., Inc.		**Transfers**	**New Value**	**Net of NV**					
NVALLOCB	3/4/2011	$156,130.05	$38,760.00	$117,370.05	$1,000,652.28		$0.00		
Pref Start	10/23/2007								
Petn Date	1/21/2008	Age Method	I2DEL						

This document was prepared to further settlement discussions. Consequently, Rule 408 of the Federal Rules of Evidence applies and neither this document nor any of its contents may be introduced as evidence

Columns	Preference Period	Historical Period	Considered Within the Ordinary Course of Business For Settlement Purposes	Data sou
A	Aging categories summing # of invoices and $ amt of invoices paid within age category.			
B & C	The % of Amount Paid within each age category ($ in Category divided by Total $)			
D	The percentage difference between the preference period and the historical "baseline".			
E & F	These columns show the total # of invoices paid, and #paid within preference and historical time periods			
G & H	Columns G & H show the total paid within each age category.			

Pref Period Aging Statistics - 5 Day Intervals - ALL Paid Invoices - Percent of Invoices by Bucket

A	B	C	D	E	F	G	H
	Pref Per	Historical	% Diff	Pref Per	Historical	Pref Per	Historical
Inv to Deliv	% by Amount		(B-C)/C	Number of Invoices		All Inv Total	Inv Total
				46	329	$ 156,130	$ 1,143,182
<-5	0.00%	0.00%		0	0	$ -	$ -
-5 to -1	0.00%	0.00%		0	0	$ -	$ -
0 to 5	0.00%	0.00%		0	0	$ -	$ -
6 to 10	0.00%	0.00%		0	0	$ -	$ -
11 to 15	0.00%	7.60%		0	25	$ -	$ 86,893
16 to 20	0.00%	20.69%		0	67	$ -	$ 236,489
21 to 25	4.58%	22.24%	-79%	2	72	$ 7,150	$ 254,190
26 to 30	0.00%	16.93%		0	55	$ -	$ 193,597
31 to 35	0.00%	13.14%		0	45	$ -	$ 150,262
36 to 40	17.81%	6.93%	157%	8	23	$ 27,810	$ 79,221
41 to 45	2.43%	4.76%	-49%	1	16	$ 3,800	$ 54,441
46 to 50	29.92%	5.08%	488%	14	17	$ 46,712	$ 58,127
51 to 55	8.84%	1.18%	647%	4	4	$ 13,798	$ 13,525
56 to 60	26.04%	1.15%	2156%	12	4	$ 40,660	$ 13,198
61 to 65	0.00%	0.00%		0	0	$ -	$ -
66 to 70	0.00%	0.00%		0	0	$ -	$ -
71 to 75	0.00%	0.00%		0	0	$ -	$ -
76 to 80	0.00%	0.00%		0	0	$ -	$ -
81 to 85	0.00%	0.00%		0	0	$ -	$ -
86 to 90	2.12%	0.00%		1	0	$ 3,313	$ -
91 to 95	0.00%	0.28%		0	1	$ -	$ 3,238
96 to 100	4.06%	0.00%		2	0	$ 6,336	$ -
Over 100	4.20%	0.00%		2	0	$ 6,550	$ -
OnAcct	0.00%	0.00%		0	0	$ -	$ -
	=======	=======		========	=======	=========	==========
	100%	100%		46	329	$ 156,130	$ 1,143,182

By % of Dollar Amount of Invoices

By $ Amt	Pref Period	Hist Period	Diff %
Above	0%	0%	N/A
OCB Range	22%	88%	-74%
Below	78%	12%	522%

Comparison of Average Invoice to Delivery Between Historical Baseline & Preference Period

Age Method	Pref Period	Prior Hist	Diff by
I2DEL	**Wavg**	**Wavg**	**Wavg**
All History	57.16	27.56	107%

(Explanation of Fig. 1)

This chart provides a graphical representation of an OCB range for payments made by a debtor to "ABC Sample Co., Inc." using +/- 15 days from the historical weighted average (Hwavg). Column A provides a breakdown of invoice aging in age "buckets": invoices paid 0-5 days after invoice date, 6-10 days after invoice date, 11-15 days after invoice date, etc. Column F provides both the total number of historical invoices and the distribution of the number of invoices falling within each aging bucket. Column H provides historical data as to the total amount of the invoices, again both with the overall total and the distribution in aging buckets. Column C provides this data in terms of percentages by dollar amount.

In this case, the Hwavg is 27 days, which would give a range of 12-42 days. As the subjective analysis does require an individual look at each case based upon the particular payment pattern of the case, some tailoring may be needed. Here, the range is adjusted to 11-40 days. This encapsulates 88% of the historical transactions between the parties.

The preference period data can then be compared to this historical information. Column E provides invoices by number, Column G provides the data by dollar amount, and Column B provides the percentages. A comparison of the two periods can be found at the bottom of the page. While 88% of all invoices (by dollar amount) were paid between 11-40 days historically, during the preference period only 22% of invoices were paid during this time period. Additionally, the historical weighted average was 27.56 days, compared to a shift in weighted average to 57.16 days in the preference period.