UNITED STATES BANKRUPTCY COURT
DISTRICT OF SOUTH DAKOTA
Southern Division

In re:	)	Bankr. No. 02-40922
	)	
THE CREDIT STORE, INC.	)	Chapter 7
Tax I.D. No. 87-0296990	)	
Debtor.	)	
	)	
John s. Lovald, Trustee,	)	Adv. No. 03-4017
Plaintiff,	)	
	)	
-vs-	)	DECISION RE: DEFENDANTS'
	)	MOTION TO DISMISS COMPLAINT
Thornton Capital Advisors, Inc.,	)	
and Recovery Partners II,L.L.C.,	)	
Defendants.	)	

The matter before the Court is the Motion to Dismiss First Amended Complaint to Avoid and Recover Fraudulent Transfer and Disallow Claim filed by Defendants Thornton Capital Advisors, Inc., and Recovery Partners II, L.L.C., and the response filed by Plaintiff-Trustee John S. Lovald. This is a core proceeding under 28 U.S.C. § 157(b)(2)(B). This Decision and accompanying Order shall constitute the Court's findings and conclusions under Fed.R.Bankr.P. 7052. As set forth below, the Motion will be granted in part and denied in part.

I.

On April 15, 2003, Plaintiff-Trustee John S. Lovald ("Trustee Lovald") filed an amended complaint against Defendants Thorton Capital Advisors, Inc., ("Thorton") and Recovery Partners II, L.L.C. ("Recovery Partners"). The amended complaint contained three counts. Trustee Lovald has consented to the dismissal without prejudice of Count III so it will not be discussed further.

In his Amended Complaint, Trustee Lovald stated that Thorton and Recovery Partners entered into a Repurchase Agreement with The Credit Store, Inc., ("Credit Store") on December 31, 2001, involving a certain pool of credit card receivables for $8,000,000, and some related security transactions. Trustee Lovald alleged that the transfer and related transactions under the Repurchase Agreement were not a sale, but instead were a disguised security agreement. Citing 11 U.S.C. §§ 548(a)(1)(A) and 550(a)(1), Trustee Lovald sought under Count I an avoidance of the second position security interest ("asset lien") that was given under the Repurchase Agreement to Thorton and Recovery Partners in substantially all of the Credit Store's assets. He alleged that this transfer was made on August 15, 2002, which was within one year of when the Credit Store filed bankruptcy, and that the transfer was an attempt to defraud creditors.

Under Count II, Trustee Lovald contended that the asset lien was voidable under §§ 548(a)(1)(B) and 550(a)(1) as a constructively fraudulent transfer. Trustee Lovald alleged that the Credit Store's financial status at the time the lien was given met one of the alternatives within the insolvency element of § 548(a)(1)(B) and that the consideration that Thorton and Recovery Partners gave the Credit Store for the asset lien was less than its reasonably equivalent value.

Defendants Thorton and Recovery Partners moved to dismiss

Trustee Lovald's Amended Complaint. As they described the Repurchase Agreement, it was comprised of (a) Thorton and Recovery Partners giving the Credit Store $8,000,000 to purchase certain credit card account receivables from Plains Commerce Bank; (b) the Credit Store transferring the receivables to Thorton and Recovery Partners; (c) the Credit Store obtaining an option to repurchase the receivables and Thorton and Recovery Partners obtaining the option to require the Credit Store to repurchase the receivables, and (d) the Credit Store giving Thorton and Recovery Partners a second priority lien in its other assets to secure the Credit Store's obligation to service the credit card account receivables and to comply with the repurchase option. Thorton and Recovery Partners argued that Trustee Lovald's Count I should be dismissed because he had failed to plead his allegations of fraud with particularity as required by Fed.R.Bankr.P. 7009(b). As to Count II, Thorton and Recovery Partners urged that it also be dismissed. They argued the asset lien could not be avoided as a constructively fraud transfer because the Credit Store had not and could not transfer anything of a value greater than the underlying debt that it secured.

In his response to Thorton and Recovery Partners's allegation that he had failed to plead his fraud count (Count I) with particularity, Trustee Lovald argued, citing cases outside this Circuit, that parties in bankruptcy cases are afforded "greater

liberality" and that his Amended Complaint provided enough detail to allow Defendants to answer. In the alternative, Trustee Lovald argued that he should be allowed to amend his Amended Complaint to address any deficiencies.

In response to the Motion to Dismiss regarding Count II, Trustee Lovald stood on his allegations. He continued to argue that when the asset lien was given the repurchase option and the servicing obligation were not present or antecedent debts that the asset lien could secure for equal value.

In a reply brief, Thorton and Recovery Partners continued to argue that Trustee Lovald's Amended Complaint failed to identify which of their acts demonstrated that the Repurchase Agreement was created and implemented for a fraudulent purpose. They also disputed Trustee Lovald's contention that the repurchase option and servicing obligation were not antecedent or present debts that could serve as the underlying debt for the asset lien. Thorton and Recovery Partners urged the Court to look at all the transfers under the Repurchase Agreement as a whole and not to isolate one or two for examination.

The matter was taken under advisement.

II.

When presented with a motion to dismiss by a defendant at this stage of the proceeding, the Court may consider the complaint and documents whose contents are alleged in the complaint and whose

authenticity is not questioned by any party. *Kushner v. Beverly Enterprises, Inc.*, 317 F.3d 820, 831 (8th Cir. 2003)(quoting therein *Rosenbaum v. Syntex Corporation (In re Syntex Corp. Securities Litigation)*, 95 F.3d 922, 926 (9th Cir. 1996). The Court may also consider exhibits appended to the complaint. Fed.R.Civ.P. 10(c); *Meehan v. United Consumers Club Franchising Corp.*, 312 F.3d 909, 913 (8th Cir. 2002).

A complaint should be dismissed for failure to state a claim only if it appears beyond doubt that the plaintiff can not prove any set of facts in support of his claim that would entitle him to relief. *Schaller Telephone Co. v. Golden Sky Systems, Inc.*, 298 F.3d 736, 740 (8th Cir. 2002). When analyzing the adequacy of a complaint's allegations under Fed.R.Civ.P. 12(b)(6), the Court must accept as true all of the complaint's factual allegations and view them in the light most favorable to the plaintiff. *Id.* However, the complaint may not contain "mere" conclusions. *DuBois v. Ford Motor Credit Co.*, 276 F.3d 1019, 1022 (8th Cir. 2002). To avoid dismissal, the complaint must contain sufficient facts to satisfy the legal requirements of the claim to avoid dismissal. *Id.*

Federal Rule of Bankruptcy Procedure 7009 states that Fed.R.Civ.P. 9 applies in adversary proceedings. Subsection (b) of Rule 9 provides:

> In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with

> particularity. Malice, intent, knowledge, and other condition of mind may be averred generally.

Contrary to the cases in other jurisdictions cited by Trustee Lovald, this Court did not find any decisions by the Court of Appeals for the Eighth Circuit that lessen this standard in bankruptcy cases. Moreover, Bankruptcy Rule 7009 does not indicate any less stringent application of Civil Rule 9(b) is contemplated.

In this Circuit, "the particularity required by Rule 9(b) is intended to enable the defendant to respond specifically and quickly to the potentially damaging allegations." *United States ex rel. Costner v. United States*, 317 F.3d 883, 888 (8th Cir. 2003)(cite therein). The complaint must be specific enough to give the defendant notice of the particular conduct that is alleged to constitute the fraud so that they can defend against the charge. *Id.* at 889 (quoting therein *United States ex rel. Lee v. SmithKline Beecham Clinical Labs.*, 245 F.3d 1048, 1051-52 (9th Cir. 2001)).

III.

After reviewing Count I of Trustee Lovald's Amended Complaint, the Court concludes that it lacks particularity regarding Thornton and Recovery Partners' alleged fraudulent acts. While Trustee Lovald has identified the elements for avoiding a fraudulent transfer under § 548(a)(1), he has not set sufficiently forth the circumstances which demonstrate that the asset lien was given to Thorton and Recovery Partners in an attempt to defraud the Credit

Store's creditors. *See Commercial Property Investments, Inc. v. Quality Inns International, Inc.*, 61 F.3d 639, 644 (8th Cir. 1995)(quoting therein *Bennett v. Berg*, 685 F.2d 1053, 1062 (8th Cir.1982)("'Circumstances' . . . include such matters as the time, place and contents of false representations, as well as the identity of the person making the misrepresentation and what was obtained or given up thereby."))

Trustee Lovald will be allowed to amend Count I of his Amended Complaint. Fed.R.Bankr.P. 7015 and Fed.R.Civ.P. 15(b). Rule 15(b) dictates that leave to amend be freely given when justice so requires.

> If the underlying facts or circumstances relied upon by a plaintiff may be a proper subject of relief, he ought to be afforded an opportunity to test his claim on the merits. In the absence of any apparent or declared reason--such as undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of amendment, etc.--the leave sought should, as the rules require, be 'freely given.'

Foman v. Davis, 83 S.Ct. 227, 230 (1962)(cited in *Assay v. Hallmark Cards, Inc.*, 594 F.2d 692, 695 (8th Cir. 1979). Other than some delay, the Court can find no prejudice to Thorton and Recovery Partners that may be occasioned by allowing Trustee Lovald to amend Count I of his Amended Complaint. *Sanders v. Clemco Industries*, 823 F.2d 214, 216-17 (8th Cir. 1987)("[D]elay alone is not a reason in and of itself to deny leave to amend; the delay must have

resulted in unfair prejudice to the party opposing amendment.") A deadline for the amendment will be set forth in the accompanying Order.

As to Count II, the Court is satisfied that the allegations therein, when read in a light most favorable to Trustee Lovald and when considered in tandem with the Repurchase Agreement, raise a valid cause of action under §§ 548(a)(1)(B). As argued by Trustee Lovald in his Amended Complaint, the consideration given by Thorton and Recovery Partners to the Credit Store for the asset lien is not easy to identify or value. Though Thorton and Recovery Partners state that the asset lien collateralized a debt created by the Repurchase Agreement, the nature and especially the value of that debt at the time the lien was given is not readily apparent.[1] If the asset lien was intended to serve as security for the Credit Store's obligations under the repurchase option and the servicing agreement, what was their value and could these obligations suffice as consideration for the asset lien when the lien was created? What impact does the servicing fee required by ARTICLE 3.1.(a) of

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[1] Though Thorton and Recovery Partners would like the Court to consider the asset lien as an integral element of the whole agreement, the Repurchase Agreement itself separates Thorton and Recovery Partners's purchase of the credit card receivables for the consideration of $8,000,000 (ARTICLE 1. SALE, PURCHASE, AND ASSUMPTION) from the other three key provisions of the Repurchase Agreement: ARTICLE 1. OPTION TO REPURCHASE; ARTICLE 3. SERVICING AND COLLATERAL RATIO; and ARTICLE 4. GRANT OF SECURITY INTEREST. Indeed, the Repurchase Agreement itself focuses on the repurchase obligation and the servicing obligation as the obligations that are secured by the asset lien.

the Repurchase Agreement have in terms of identifying the nature and value of the debt underlying the asset lien? These justiciable issues are adequately brought before the Court by Count II of Trustee Lovald's Amended Complaint and presented to Thorton and Recovery Partners for an answer. Accordingly, Thorton and Recovery Partners' request that Count II be dismissed because it does not adequately state a claim will be denied.

An appropriate order will be entered.

Dated this 20th day of June, 2003.

BY THE COURT:

Irvin N. Hoyt
Bankruptcy Judge

ATTEST:

Charles L. Nail, Jr., Clerk
By: _____
Deputy Clerk

UNITED STATES BANKRUPTCY COURT SEAL

NOTICE OF ENTRY
Under F.R.Bankr.P. 9022(a)
Entered
JUN 20 2003
Charles L. Nail, Jr., Clerk
U.S. Bankruptcy Court
District of South Dakota

I hereby certify that a copy of this document was electronically transmitted, mailed, hand delivered or faxed this date to the parties on the attached service list.

JUN 20 2003

Charles L. Nail, Jr., Clerk
U.S. Bankruptcy Court, District of South Dakota
By _____

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