UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
JACKSONVILLE DIVISION

In re:

HERITAGE FUNDING GROUP, INC. CASE NO. 07-492

Debtor.
_____/

NEW DEAL AUTO ACCEPTANCE, LLC,

Plaintiff,

v. ADVERSARY NO.: 07-302

RICHARD HOUGHTON, et al.,

Defendants.
_____/

ORDER DENYING MOTION FOR SUMMARY JUDGMENT FILED BY DEFENDANTS JON FORTENBERRY AND JON FORTENBERRY ENTERPRISES AND GRANTING CROSS MOTION FOR SUMMARY JUDGMENT FILED BY PLAINTIFF

This proceeding came before the Court upon Motion for Summary Judgment filed by Defendants Jon Fortenberry and Fortenberry Enterprises (the "Motion"), Plaintiff's Response to [the Motion] and Cross Motion for Summary Judgment against Jon Fortenberry and Fortenberry Enterprises (the "Response and Cross Motion"), Defendants' Reply to [the Response and Cross Motion] and Supplement to [the Motion] (the "Reply"), and Plaintiff's Response to [the Reply]. Upon a review of the pleadings and the applicable law, the Court finds it appropriate deny the Motion and to grant the Cross Motion.

Procedural Background

On February 8, 2007 Heritage Funding Group Inc. ("Heritage") filed a voluntary petition for relief under Chapter 11 of the Bankruptcy Code. On February 26, 2007 the United States Trustee appointed the Official Committee of Unsecured Creditors of

[Heritage] (the "Committee"). On November 15, 2007 the Court entered an Order Granting the Committee Derivative Standing to Pursue Avoidance Actions on Behalf of the Estate. On December 7, 2007 the Committee filed this adversary proceeding against twenty nine defendants, including Jon Fortenberry and Fortenberry Enterprises, seeking the avoidance of commission payments by Heritage within the four year period preceding the petition date pursuant to 11 U.S.C. §§ 544 and 548 and § 726.105, Florida Statutes.

On August 26, 2008, the Court entered an Order Approving the Amended Disclosure Statement, and Order Confirming the Amended Plan (the "Confirmation Order"). On September 15, 2008, in accordance with Sections 10.3 and 10.7 of the Amended Joint Plan of Reorganization and the Confirmation Order, the Committee dissolved and New Deal Auto Acceptance, LLC acquired all of the remaining assets of Heritage, including the avoidance rights of this adversary proceeding.

On March 30, 2009, Jon Fortenberry and Jon Fortenberry Enterprises filed the Motion. On April 16, 2009, the Court entered an Order Granting Motion to Substitute Party Plaintiff, substituting New Deal Auto Acceptance, LLC ("Plaintiff") as the plaintiff in the place of the Committee in this adversary proceeding. On April 30, 2009 Plaintiff filed the Response and Cross Motion. On May 7, 2009 Fortenberry filed the Reply. On May 12, 2009 Plaintiff filed its Response to the Reply.

Undisputed Facts

In October 1999 Jon Fortenberry, then 25 years old, began applying for jobs in sales. (Fortenberry Aff. ¶ 1.) Jon Fortenberry was hired as an independent contractor by Richard Houghton ("Houghton"), Kirk Friedman ("Friedman") and Jeff Shuken ("Shuken") to offer private placement units in movies they produced. (Id. at ¶ 3.) As a

condition of employment Fortenberry was required to form Jon Fortenberry Enterprises, a sole proprietorship. (Id.)

Thereafter, Larry Ford ("Ford"), with the aid of Hougton, Mike Bretzel ("Bretzel"), and Friedman, as undisclosed principals, incorporated Heritage. (Scanlon Aff. ¶ 3.) Heritage purchased and serviced sub-prime automobile loans. (Id. at ¶ 4.) Heritage purchased consumer-auto finance contracts from various auto dealers at a discounted price, and then assumed collection of the principal and interest in the finance contracts throughout their terms. (Id.) Heritage worked in conjunction with Liberty Automotive Group, Inc. ("Liberty"), a used automobile retailer owned by Bretzel. (Id. at ¶ 5.) Through the sale of used automobiles, Liberty generated promissory notes, which Heritage purchased. (Id.)

Through a private placement, Heritage devised a method to generate capital from private investors (the "Promissory Note Investment Scheme"). (Scanlon Aff. ¶ 6.) Individual brokers acting for or on behalf of Heritage in advancement of the Promissory Note Investment Scheme solicited private investors to invest funds in Heritage under terms by which the investors loaned money to Heritage in consideration of promissory notes of Heritage, signed by Ford as president on behalf of Heritage. (Id. at ¶ 7.) The promissory notes provided an annual interest rate ranging from 15% to 18%. (Id.)

Among these brokers was Jon Fortenberry, d/b/a Fortenberry Enterprises (collectively "Fortenberry"). (Scanlon Aff. ¶ 8.) Fortenberry was told that Houghton, Friedman, and Shuken along with Ford held equity positions in Heritage. (Fortenberry Aff. ¶ 5.) Fortenberry was told that Heritage had been in business for a few years and had been started with their money. (Id.) Fortenberry was told that Houghton, Friedman,

Shuken, and Ford were looking for lenders to help grow their business. (Id.) Fortenberry was provided with a sales brochure and told that he could only offer Heritage lending opportunities to current customers (of the movie private placement units) and that the offering was on a limited basis. (Id.) Fortenberry called clients and asked if they were interested in the new product. (Id.) If Fortenberry received a positive response, he asked the potential customer if they wanted to receive information about Heritage. (Id.) Fortenberry was told that the promissory notes he sold were collateralized at 150% by point of sale auto financing contracts. (Id. at ¶ 7.)

Loaning money to Heritage was limited. (Fortenberry Aff. ¶ 8.) When auto finance notes were available, Fortenberry was told how much money in auto contracts could be sold. (Id.) The auto contracts packages typically sold very quickly. (Id.) Once the packages were sold, clients were turned away. (Id.) During the period that Fortenberry worked for Heritage there was never a problem with the payment of interest to any of his clients or to anyone else. (Id. at ¶ 9.) There were never any payment defaults. (Id.) On a number of occasions clients wanted to get their principal back after the one year loan commitment period. (Id.) In each instance, Heritage fully repaid the principal to these clients. (Id.) Fortenberry was told that when a client wanted his or her principal back, the collateralized loan was sold to another bank to repay the client. (Id. at ¶ 14.)

During the time Fortenberry offered Heritage loans, he never had access to nor saw any financial reports, balance sheets or any other documentation concerning the financial condition of the company. (Fortenberry Aff. ¶ 10.) Instead, he relied on verbal representations that Heritage was a strong company

with more assets than debt and that every dollar a client loaned for the purchase of auto finance paper was collateralized 150% in auto finance paper. (Id.) The Heritage brochure stated the same thing. (Id.) Fortenberry also believed in Heritage's soundness because Houghton, Friedman, Shuken, Ford, and other brokers invested money in the company. (Id.) Additionally, Heritage's owners told Fortenberry that their families had invested in Heritage. (Id.)

While Fortenberry did not have access to Heritage's financial records, he was told by Heritage's management that any customer could look at the books, records and accounts of Heritage at any time. (Fortenberry Supp. Aff. ¶ 4.) Fortenberry expressed that information to his clients and recommended that they look at Heritage's books and other financial information before they made loans to Heritage. (Id.) A number of Fortenberry's clients visited Heritage's office in Florida and provided Fortenberry with positive feedback. (Fortenberry Aff. ¶ 11.)

Despite his lack of first hand knowledge as to Heritage's financial condition, Fortenberry made representations to buyers regarding the strength of Heritage's business, the capability of its principals, and Heritage's success in the automobile loan industry. (Kane Aff. ¶ 4.) Additionally, Fortenberry made representations to at least one buyer that the rate of return on the promissory notes was guaranteed and assured the buyer that his money was safe with Heritage. (Id. at ¶ 6.)

There is a factual dispute as to Fortenberry's rate of commission. Plaintiff alleges that Fortenberry received an initial 10% commission on the sale of the promissory notes and a 5% renewal. (Scanlon Aff. ¶ 10.) Fortenberry alleges that

he received an initial 7 % commission on the sale of promissory notes and a 3.5% renewal. (Fortenberry Supp. Aff. ¶ 2.) It is undisputed that Fortenberry received a total of $28,162.71 in payments from Heritage within the four year period proceeding the petition date. (Ex. B, Cross Motion for Summ. J.)

Buttner Hammock & Company, P.A. ("Buttner Hammock"), a Jacksonville, Florida based accounting firm, was retained by Heritage as an accountant and financial advisor for Heritage. Edward W. Buttner, IV ("Buttner"), in his capacity as principal of Buttner Hammock, executed an affidavit (the "Buttner Affidavit") regarding Buttner Hammock's analysis of the books and records of Heritage. (Ex. C to Motion for Summ J.)

Serving in this capacity, Buttner Hammock reviewed and analyzed the books and records of Heritage regarding its operations from the inception of its business operations in mid-2000 through the Petition Date. Based upon a detailed analysis of Heritage's books and records, Buttner Hammock prepared Profit & Loss Statements of the operations of Heritage for the years 2000 through 2007. (Ex. 1 to Buttner Aff.)

According to the Profit & Loss Statements of Heritage, for calendar years 2000 through 2007, the aggregate amount of net ordinary income before investor expenses, which included interest payments to investors and commission payments to brokers (the "Investor Expense"), was $434,564.97, and the aggregate amount of Investor Expense was $14,438,983.27. (Buttner Aff. ¶ 15.) Heritage never generated sufficient revenue from the operation of its loan portfolio, on an aggregate basis as well as a year-by-year basis, to pay the interest expense to investors and the commission expense to the brokers raising money for or on behalf of Heritage. (Id. at ¶ 16.)

Given Heritage's inability to fund the interest and commission expense from its business operations, and the absence of the infusion of capital from its principals, Heritage, for every year of its operations, used its capital investments from investors to pay in excess of 95% of the Investor Expense incurred during the calendar years 2000 to 2007. (Id. at ¶ 17.)

As of the Petition Date, Heritage owed money to over 300 investors, and the aggregate amount of outstanding indebtedness owing on account of investor notes generated under the Promissory Note Investment Scheme totaled $22,907,436.90, including accrued and unpaid interest. (Ex. D. to Motion for Summ. J.)

Summary Judgment Standard

Summary judgment under Rule 56 is appropriate "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c) (2007)(incorporated by Fed. R. Bankr. P. 7056). A moving party bears the initial burden of showing a court that there are no genuine issues of material fact that should be decided at trial. See Celotex Corp. v. Catrett, 477 U.S. 317 (1986); accord Clark v. Coats & Clark, Inc., 929 F.2d 604, 607 (11th Cir. 1991). A moving party discharges its burden on a motion for summary judgment by "'showing' – that is, pointing out . . . that there is an absence of evidence to support the nonmoving party's case." Celotex Corp., 477 U.S. at 325. In determining whether the movant has met this initial burden, "the court must view the movant's evidence and all factual inferences arising from it in the light most favorable to the nonmoving party." Allen v. Tyson Foods, Inc., 121 F.3d 642, 646 (11th Cir. 1997)(citing

Adickes v. S.H. Kress & Co., 398 U.S. 144, 157 (1970) and Fitzpatrick v. City of Atlanta, 2 F.3d 1112, 1115 (11th Cir. 1985)). In other words, the court must decide "whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 251-52 (1986).

If a moving party satisfies this burden, then a nonmoving party must come forward with specific facts showing that there is a genuine issue for trial. See Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 587 (1986). A nonmoving party must do more than simply show that there is some metaphysical doubt as to the material facts. See id. "Where the record taken as a whole could not lead a rational trier of fact to find for the non-moving party, there is no genuine issue for trial." Id.

Application to the Instant Case

Under Section 548(a)(1)(A),[1] and Section 544(b)(1)[2] and Section 726.105(1)(a), Florida Statutes,[3] a transfer may be avoided as actually fraudulent if it was made with the actual intent to hinder, delay, or defraud creditors. See 11 U.S.C. §§ 548(a)(1)(A) and

[1] Section 548(a)(1)(A) provides:

> The trustee may avoid any transfer (including any transfer to or for the benefit of an insider under an employment contract) of an interest of the debtor in property, or any obligation (including any obligation to or for the benefit of an insider under an employment contract) incurred by the debtor, that was made or incurred on or within 2 years before the date of the filing of the petition, if the debtor voluntarily or involuntarily--
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> (A) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted.

[2] Section 544(b)(1) provides:

> (1) Except as provided in paragraph (2), the trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

[3] Section 726.105(1)(a), Florida Statutes (2008), provides:

> A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

544(b)(1) and Section 726.105(1)(a), Florida Statutes (2008).[4] Section 548(c)[5] of the Bankruptcy Code and Section 726.109(1), Florida Statutes,[6] provide an affirmative defense for individuals to whom the debtor's property was transferred where the transferee gave value to the debtor and received the transfer in good faith. See 11 U.S.C. § 548(c) and Section 726.109(1), Florida Statutes (2008).

Both Fortenberry and Plaintiff seek summary judgment. Fortenberry argues that the payment of the validly due commission for services was a transfer for reasonably equivalent value and is therefore not an avoidable transfer under § 548. Fortenberry asserts that he had neither actual nor constructive knowledge of the existence of a Ponzi scheme or the insolvency of Heritage and is therefore entitled to the affirmative defense set forth in 11 U.S.C. § 548(c) and § 726.109(1) Florida Statutes.

Plaintiff argues that the undisputed facts demonstrate that Heritage operated as a Ponzi scheme. Plaintiff argues that the payment of commissions in furtherance of a Ponzi scheme are presumptively fraudulent and that the transfers are therefore avoidable as fraudulent transfers pursuant to 11 U.S.C. §§ 548(a)(1)(A) and 544(b)(1) and § 726.105(a), Florida Statutes. Plaintiff argues that Fortenberry is not entitled to the affirmative defense set forth in § 548(c) and § 726.109(1) Florida Statutes because he did

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(a) With actual intent to hinder, delay, or defraud any creditor of the debtor.

[4] Section 726.105, made applicable pursuant to Section 544(b)(1), is very similar to Section 548(a), however, the reach back period to recover avoidable transfers is extended to four years.

[5] Section 548(c) provides:

> Except to the extent that a transfer or obligation voidable under this section is voidable under section 544, 545, or 547 of this title, a transferee or obligee of such a transfer or obligation that takes for value and in good faith has a lien on or may retain any interest transferred or may enforce any obligation incurred, as the case may be, to the extent that such transferee or obligee gave value to the debtor in exchange for such transfer or obligation.

[6] Section 726.109(1), Florida Statutes (2006), provides:

> A transfer or obligation is not voidable under s. 726.105(1)(a) against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

not provide value to Heritage in exchange for the commission payments and even if he did, he did not receive the commission payments in good faith.

There is no factual dispute as to whether Heritage operated as a Ponzi scheme. For calendar years 2000 through 2007 the aggregate amount of net ordinary income before investors expenses, which included interest payments to investors and commission payments to brokers (the "Investor Expense") was $434,564.97 and the aggregate amount of Investor Expense was $14,438,983.27. Heritage never generated sufficient revenue from the operation of its loan portfolio on an aggregate basis as well as on a year by year basis to pay the interest expense to investors and the commission expense to the brokers raising money for or on behalf of Heritage. Given Heritage's inability to fund the interest and commission expense from its business operations, and the absence of the infusion of capital from its principals, Heritage, for every year of its operations, used its capital investments from investors to pay in excess of 95% of the Investor Expense incurred during the calendar years 2000 to 2007. As of the Petition Date, Heritage owed money to over 300 investors, and the aggregate amount of outstanding indebtedness owed on account of investor notes generated under the Promissory Note Investment Scheme totaled $22,907,436.90, including accrued and unpaid interest.

The existence of a Ponzi scheme is sufficient to establish actual intent to defraud, and therefore, all transfers in furtherance of the Ponzi scheme are fraudulent, In re World Vision Entertainment, Inc., 275 B.R. 641, 656 (Bankr. M.D. Fla. 2002) (stating that "any acts taken in furtherance of the Ponzi scheme, such as paying brokers commissions, are also fraudulent"). While some payments in furtherance of a Ponzi scheme are avoidable, others are not. World Vision, 275 B.R. at 658. None are automatically avoidable. Id.

As previously noted, § 548(c) of the Bankruptcy Code and § 726.109(1), Florida Statutes, provide an affirmative defense for individuals to whom the debtor's property was transferred where the transferee gave value to the debtor and received the transfer in good faith. See 11 U.S.C. § 548(c) and § 726.109(1), Florida Statutes (2008). A transferee who receives commission payments made in furtherance of a Ponzi scheme is entitled to assert an affirmative defense under § 548(c). Orlick v. Kozyak (In re Financial Federated Title & Trust, Inc.), 309 F.3d 1325, 1322-1333 (11th Cir. 2002) (reversing bankruptcy court holding that transferee who received payments in furtherance of Ponzi scheme which deepened debtor's insolvency was barred as a matter of law from asserting §548(c) good faith defense).

The first element of the defense is whether the transferee gave value to the debtor in exchange for the transfer. Section 548(d)(2)(A) defines "value" as "property, or satisfaction or securing of a present or antecedent debt of the debtor." 11 U.S.C. § 548(d)(2)(A). Courts assess "value" on a case-by-case basis looking at the surrounding circumstances of the particular transfer at issue. World Vision, 275 B.R. at 656. Value is present if the debtor receives a fair equivalent in exchange for its property or obligation. See Churchill Mortgage Investment Corp., 256 B.R. 664, 678 (Bankr. S.D.N.Y. 2000). (stating that the determination of whether value was given under Section 548 should focus on the value of the goods or services provided). In Churchill the court looked to the value provided for each individual transfer or commission payment instead of the value provided to the overall enterprise. In the instant case, there is no dispute that Fortenberry sold promissory notes in exchange for which he received commissions. Even accepting Plaintiff's alleged 10% commission on initial sales and 5% commission

on renewals, Plaintiff does not and could not contend that the commission is high. It is clear that Fortenberry gave value, his services, in exchange for the payment of commissions.

The second element of the affirmative defense requires that the transferee receive the transfer in good faith. Good faith is judged using an objective standard. World Vision, 275 B.R. at 659 (stating that good faith is established by looking at the actions and knowledge, both actual knowledge and imputed knowledge, of the transferee); In re M & L Business Machine Co., 84 F.3d 1330, 1337-39 (10th Cir. 1996) (stating that good faith should be measured using an objective standard which examines whether circumstances would place a reasonable person on inquiry of a debtor's fraudulent purpose); Hays v. Jimmy Swaggart Ministries, et al., 263 B.R. 203, 211 (M.D. La. 1999) (stating that "[g]ood faith is determined on a case-by-case basis using an objective standard").

With respect to a broker soliciting the sale of promissory notes, it is necessary to examine whether the broker sufficiently performed the steps that a prudent broker acting in good faith would take before selling the debtor's promissory notes. World Vision, 275 B.R. at 659-60. In World Vision the court held that a broker selling short term promissory notes must conduct a reasonable investigation into the legitimacy of the notes. Id. at 659. Although a reasonable investigation will vary from case to case depending upon the circumstances, as a general rule such investigation must include reviewing available investment ratings from qualified financial rating services and reviewing with a critical eye the company’s audited financial statements as well as other literature provided by the company discussing its sales history and the background of key

employees. Id. at 660. "A broker cannot rely on slick, marketing brochures or coverage, refrain from asking hard questions about the legitimacy of the product, and then assume a proper investigation was completed." Id. Absence these minimal steps, a broker who sells short term promissory notes has not completed the minimum due diligence required. Id.

The issue before the Court is the extent to which Fortenberry was required to verify the legitimacy of the promissory notes before he sold them. As the court in World Vision stated, "can a broker simply rely on promises made by a dishonest and fraudulent debtor and still act in good faith?" Id. at 659.

Fortenberry argues that the limitations on sales of investments to qualified investors, Heritage's policy that investments could not be sold after an offering had sold out, Heritage's timely payment of interest to all investors and timely repayment of loans when cashed in by investors, and the positive feedback from investors who had visited Heritage's offices in Florida would lead any reasonable person to conclude that he was selling product for a viable and profitable company.

The Court disagrees. As Plaintiff points out, Fortenberry's knowledge of the financial viability of Heritage was limited to information contained in Heritage's sales brochure and unsubstantiated allegations from third parties. If Fortenberry had reviewed an income statement or balance sheet of Heritage, he would have learned that approximately 95% of Heritage's Investor Expense was paid with capital from investors, as opposed to funds generated from Heritage's business operations. Fortenberry's defense that Heritage did not permit its brokers to inspect its financial records is unavailing and should have, if nothing else, given Fortenberry considerable pause. While

the Court recognizes that there were no available investment ratings from qualified financial rating services as to Heritage, the fact remains that Fortenberry did not perform any independent research and in fact completed no investigation whatsoever. Despite his lack of any firsthand knowledge as to Heritage's soundness, Fortenberry made representations as to the strength of Heritage's business, the capability of its principals, and Heritage's success in the automobile loan industry. Even viewing the evidence and the factual inferences arising from such evidence in the light most favorable to Fortenberry, the Court finds that Fortenberry did not perform the necessary steps that a reasonably prudent broker acting in good faith would take before selling the notes at issue.[7]

Because Fortenberry did not act in good faith, the defenses under § 548(c) and § 726.109 do not shelter the commission payments Heritage paid to Fortenberry and thus the sum of $28,162.71 of commission payments by Heritage to Fortenberry within the four year period preceding the Petition Date are avoidable as fraudulent transfers pursuant to 11 U.S.C. §§ 544 and 548 and § 726 Florida Statutes. Plaintiff is entitled to Summary Judgment as to Counts LIII and LIV of the Complaint. The Court will enter a separate judgment consistent with this Order.

DATED August 20, 2009 in Jacksonville, Florida.

/s/ Jerry A. Funk

Jerry A. Funk
United States Bankruptcy Judge

[7] Fortenberry also asserts that the reasonably prudent standard for brokers does not apply to him because he never held himself out to be a broker. Fortenberry asserts that he simply acted as a salesman for Heritage rather than a broker selling third party investment opportunities. Whatever Fortenberry chooses to classify himself as, the Court finds that the standards set forth in World Vision apply.

Copies to:

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