In the United States Bankruptcy Court

for the Northern District of Iowa

MIDWEST COMMUNICATIONS INC.	Bankruptcy No. 98-03559-D
Debtor(s).	Chapter 11

ORDER RE: MOTION FOR RELIEF FROM STAY

This matter came before the undersigned on January 15, 1999 on Motion of the Dubuque Bank and Trust Co. for Relief from the Automatic Stay or, in the Alternative for Adequate Protection. After the presentation of evidence and argument, the Court took the matter under advisement. This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(G).

STATEMENT OF THE CASE

Dubuque Bank & Trust Co. (DB&T) has an agreement to process electronic and credit card transactions for Debtor. As part of that agreement, it processes charge backs for which Debtor is ultimately liable. Because of Debtor's financial condition, DB&T states it is subject to liability for up to $70,000 per month for charge backs. DB&T wishes to terminate the agreement unless Debtor escrows $70,000 as adequate protection.

Debtor responds that it is operating its internet service with a positive cash flow. It believes DB&T is not at risk of liability for charge backs under the agreement. Debtor asserts it has substantial equity in its business assets which adequately protects DB&T. It argues DB&T is not entitled to cash as adequate protection.

FINDINGS OF FACT

At the hearing, David Kepler testified on behalf of DB&T as its compliance officer. He stated that under the parties' agreement, DB&T operates as the middle man between Debtor and its VISA/MasterCard customers. DB&T processes Debtor's customers' electronic and credit card payments. If a charge back occurs against Debtor's account, DB&T must reverse the transaction. DB&T becomes liable to pay the charge back if Debtor does not. Customers have about 120 days to request a charge back. A total of four to five months can pass after a customer's request for a charge back while it works its way through the system.

DB&T seeks a $70,000 deposit as adequate protection. It estimates this is the amount of money it processes monthly for Debtor. Under a worst case scenario, such as Debtor going out of business, $70,000 represents DB&T's total exposure to liability for charge backs under the parties' agreement. DB&T wishes to be insured against a total cessation of business by Debtor. It would accept the $70,000 fund being built up over six months.

A charge back problem arose last spring and summer when Debtor encountered difficulty with a subscriber list. Mr. Kepler allowed that those problems, occurring in a related but separate account, have now been resolved.

Debtor presented testimony by Edward Larson, its Chief Executive Officer. He testified that over the previous year, in the separate, related account, nine requests for charge backs occurred out of which there were seven refunds totaling about $500. Approximately 60% of billings are on 6-month accounts; the other 40% are monthly accounts. Most charges range from $7.95 to approximately $30.00. Mr. Larson testified the risk of total cessation of business is essentially nil. Debtor proposes to build up a fund of 50% of total charges, or $35,000, over six months as an offer of adequate assurance under §365(b).

CONCLUSIONS OF LAW

DB&T asserts that, pursuant to its agreements with Debtor, it is entitled to terminate if it is exposed to any potential loss. It argues that under §365(c)(2), these contracts are not the type which may be assumed by Debtor. DB&T requests relief from the automatic stay to terminate as allowed in the contracts.

If the parties' agreement is a financial accommodation of the kind described in §365(e)(2), DB&T may be allowed to cancel the contract because of the filing of bankruptcy. In re Wegner Farms Co., 49 B.R. 440, 443 (Bankr. N.D. Iowa 1985).

> Under §365(e)(2)(B) an executory contract "to make a loan or extend other debt financing or financial accommodations, to or for the benefit of the debtor" is excepted from the general rule which prohibits cancellation or termination of contracts because of insolvency or the filing of bankruptcy.

Id. The thrust of this section is limited to contracts to make loans or other traditional kinds of debt financing arrangements. Id.at 444 (citing legislative history). It is intended as a "limited and closely circumscribed exception[] to the general rule permitting a debtor to assume executory contracts and prohibiting nondebtor parties from terminating such contracts upon the filing of bankruptcy." Id.at 445.

In In re Thomas B. Hamilton Co., 969 F.2d 1013, 1014 (11th Cir. 1992), the court was required to determine whether a credit card merchant agreement between the debtor and a merchant bank may be assumed under §365(c)(2) or, in the alternative, may be terminated by the merchant bank. The agreement in Hamilton is essentially identical to the agreements between DB&T and Debtor. The court held that "the true legal nature" of the agreement was not to extend financial accommodations within §365(c)(2) and §365(e)(2)(B). Id.at 1022. It noted that legislative history indicates §365(c)(2) was intended to be limited to actual extension of cash or a line of credit and was not intended to be extended to contracts for goods and services with installment payments. Id.at 1018; see also In re Charrington Worldwide Enter., Inc., 110 B.R. 973, 975 (M.D. Fla. 1990) (finding carrier service agreement between airlines and debtor travel agency not a financial accommodation), remanded by 922 F.2d 847 (11th Cir. 1990) (table). "Subject to the bankruptcy court's approval, such agreements may be assumed by the trustee [or debtor-in-possession] and may not be automatically terminated due to a bankruptcy filing." Hamilton, 969 F.2d at 1018. The court held that the bank could not terminate the agreement as the bank had failed to demonstrate that the continued performance of the agreement would place it at unreasonable risk. Id.

The court in In re Best Prods. Co., 210 B.R. 714, 718 (Bankr. E.D. Va. 1997), followed Hamilton to find a private label revolving credit plan agreement does not constitute a financial accommodation under §365(c)(2) and (e)(2)(B). Thus, the bank was obligated to continue performing and to continue bearing the loss if any account could not be "charged back" to the debtor, until the bank was granted relief from stay. Id. The court stressed the Hamilton court's concerns that rehabilitation would be virtually impossible for any merchant who relies on credit card sales if these typical credit card merchant agreements were not assumable. Id.; Hamilton, 969 F.2d at 1020.

This Court agrees with the foregoing authorities and concludes that Debtor must be allowed to assume its agreements with DB&T. The contracts do not constitute "financial accommodations" under §365 (c). DB&T is prohibited from terminating the agreements under §365.

The Court may approve Debtor's assumption of the contract if it provides assurance that it can and will promptly repay charge backs in the future. 11 U.S.C. §365(b); Hamilton, 969 F.2d at 1021. "Adequate assurance" is to be given a practical, pragmatic construction. In re Prime Motor Inns, Inc., 166 B.R. 993, 997 (Bankr. S.D. Fla. 1994). "[T]he assurance of future performance is adequate if performance is likely (i.e. more probable than not); the degree of assurance necessarily falls considerably short of an absolute guaranty." Id. While an absolute guarantee of future performance is not required under §365(b), more than the debtor's speculative plans are needed. In re Washington Capital Aviation & Leasing, 156 B.R. 167, 173 (Bankr. E.D. Va. 1993).

In assessing adequate assurance of future performance under §365(b), "the test is not one of guaranty, but simply whether it appears that the [amounts due] will be paid and other obligations met." In re Embers 86th St., Inc., 184 B.R. 892, 902 (Bankr. S.D.N.Y. 1995). That court looked at such factors as evidence of profitability, a plan to earmark money for the other party, and willingness and ability to fund cure payments. Id. Adequate assurance of future performance can be found by looking at the history of the relationship between the parties, the intent of the agreements and the ability of the debtor to perform the contract in the future. See In re Optimum Merchants Serv., 163 B.R. 546, 557 (Bankr. D. Neb. 1994), vacated by consent order 199 B.R. 409 (D. Neb. 1995). Other factors can include the debtor's financial resources to perform under the agreements, continuity of the type of business the debtor is operating, the success of the debtor's business operation, and the debtor's willingness to comply with all terms of the agreements. In re Alipat, Inc., 36 B.R. 274, 278 (Bankr. E.D. Mo. 1984).

Debtor has offered to build up a fund of $35,000 over six months as adequate assurance of its future performance under the agreements with DB&T. It offered evidence that its business is currently profitable. DB&T has not had excessive exposure to liability from charge backs in the past. Debtor appears to have the resources to perform under the agreements now and in the future. In these circumstances, DB&T is not exposed to unreasonable risk and no cause exists to modify the automatic stay to allow DB&T to terminate the agreements.

WHEREFORE, the Motion of the Dubuque Bank and Trust Co. for Relief from the Automatic Stay or, in the Alternative for Adequate Protection is DENIED.

FURTHER, Debtor's offer to build up a fund of $35,000 over six months as adequate assurance of future performance is APPROVED.

SO ORDERED this 28th day of January, 1999.

PAUL J. KILBURG

Paul J. Kilburg
U.S. Bankruptcy Judge