

FRAUDULENT TRANSFERS

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FRAUDULENT TRANSFERS

I. Introduction

A. Definition. "The fraudulent conveyance, as known in our law, may be roughly defined as an infringement of the creditor's right to realize upon the available assets of his debtor." G. Glenn, The Law of Fraudulent Conveyances § 1 (1931). More precisely, it is fraudulent for a debtor to transfer its assets to a third party with intent—either actual or constructive—to obstruct creditors from reaching the assets to satisfy their claims. See generally M. Cook, Fraudulent Transfer Liability Under the Bankruptcy Code, 17 Hous. L. Rev. 263 (1980).

B. Rule and Its Purpose. Fraudulent transfer law "imposes a substantive prohibition: the debtor may not dispose of his property with the intent or the effect of placing it beyond the reach of his creditors . . . and full compliance with recording acts will not save the transaction if the substantive prohibition is violated." Countryman, Cases and Materials on Debtor and Creditor 127 (2d ed. 1974). See Buncher Co. v. Official Committee of Unsecured Creditors of Genfarm LP IV, 229 F.3d 245, 250 (3d Cir. 2000) ("The purpose of fraudulent [transfer] law is to make available to creditors those assets of the debtor that are rightfully a part of the bankruptcy estate, even if they have been transferred away." (citing In re Cybergenics Corp., 226 F.3d 237, 241-42 (3d Cir. 2000))); Gandy v. Gandy (In re Gandy), 299 F.3d 489 (5th Cir. 2002) (because fraudulent transfer claims are creditor-based, "misconduct of the debtor is hardly a complete defense" to fraudulent transfer cause of action).

C. Effect. When determining whether a transfer is fraudulent, look to its effect on the debtor's estate: "[t]he touchstone . . . is the unjust diminution of the estate of the debtor that otherwise would be available to the creditor." G. Glenn, supra, § 195. The property transferred need not have value. Fed. Refinance Co. v. Klock, 352 F.3d 16, 25-26 (1st Cir. 2003) (held, transfer putting property that would otherwise be available out of creditors' reach, even if property is worthless, is a fraudulent transfer); Maple Mortgage, Inc. v. Chase Home Mortgage Corp. (In re Maple Mortgage, Inc.), 81 F.3d 592, 595 (5th Cir. 1996) (quoting Southmark Corp. v. Grosz (In re Southmark), 49 F.3d 1111, 1117 (5th Cir. 1995)) (held, transfer by debtor of funds obtained in purchase of mortgage servicing rights not recoverable by trustee as fraudulent transfer because debtor had only legal title to funds and no equitable interest in them; debtor found to be holding funds for those to whom money was owed); see, e.g., Melamed v. Lake County Nat'l Bank, 727 F.2d 1399, 1401-02 (6th Cir. 1984) (Act case) (holding that pre-petition setoff by bank to satisfy claim secured by lien on accounts receivable could not constitute fraudulent transfer because it did not diminish debtor's assets available to other creditors); Jackson v. Mishkin (In re Alder), 263 B.R. 406, 453-454, 458 (S.D.N.Y. 2001) (preferred customers could be held responsible, in their capacity as principals, for introducing broker's fraud, even though they may have had no knowledge thereof and may not have authorized broker to engage in such misconduct; the trades "constituted fraudulent acts actually intended . . . to hinder, delay or defraud [the debtor] or its creditors . . ."); Decker v. Advantage Fund Ltd., 362 F.3d 593, 596 (9th Cir. 2004) (fraudulent transfer claim based on transfer of unissued stock dismissed; held, "unissued stock is not an interest of the debtor corporation in property; it is merely equity in the corporation itself...[The] transfer [is therefore] not subject to question under § 548.").

It is just as important to examine whether the property that was transferred actually came from the debtor as it is to determine whether the alleged transferee actually received the property. Under the "mere conduit theory," which derives from Judge Cardozo's opinion in Carson v. Federal Reserve Bank of New York, 254 N.Y. 218, 235-36, 172 N.E. 475 (1930), a debtor that has mere possession of the funds, without more, does not necessarily possess sufficient control so as to warrant a finding that the funds were the debtor's property. Nordberg v. Sanchez (In re Chase & Sanborn Corp.), 813 F.2d 1177, 1180-82 (11th Cir. 1987) (debtor corporation was mere conduit for funds channeled through its account as part of scheme to repay personal debt of owner; transfer not subject to avoidance because transferred funds were never property of debtor's estate, and thus transfer did not deplete funds that otherwise would have been available for creditor distribution); Stevenson v. J.C. Bradford & Co. (In re Cannon III), 277 F.3d 838 (6th Cir. 2002) (debtor's personal funds that were deposited into an escrow account to repay misappropriated funds became part of the escrow account and are added to the sums held in express trust on behalf of debtor's clients). Cf. Nordberg v. Societe Generale (In re Chase & Sanborn Corp.), 848 F.2d 1196, 1199-1200 (11th Cir. 1988) (bank's brief possession of funds was merely as conduit for money controlled by other entities); APS Sports Collectibles v. Sports Time, Inc., 299 F.3d 624 (7th Cir. 2002) (affirmed dismissal of suit by lender against officers and directors of corporate transferee of fraudulent transfer; insider status of individuals not relevant; individuals had no personal liability as corporate officers under Uniform Fraudulent Transfer Act; no debtor-creditor relationship existed between lender and individual defendants). Courts often evaluate transactions in their entirety to ensure that the ultimate conclusions they reach are logical and equitable. Id. at 1199. For instance, in Gaudet v. Babin (In re Zedda), 103 F.3d 1195 (5th Cir. 1997), the Fifth Circuit emphasized "the inquiry under § 548(a)(2) -- the classic search for truth and the realities of transactions . . ." Id. at 1205. Thus, the Fifth Circuit held that the lower court committed reversible error by failing to allow parol evidence regarding the transfer and subsequent retransfer of a parcel of real estate. Id.¹ See also In re Int'l Admin. Servs., Inc., 408 F.3d 689, 705-06 (11th Cir. 2005) (debtor transferred assets through multi-step international transactions as part of asset protection plan; held, "mere conduit theory" was inapplicable because transferees could not be said to have acted without bad faith and as innocent participants to underlying fraud); Bonded Fin. Servs., Inc. v. European Am. Bank, 838 F.2d 890 (7th Cir. 1988) (bank that was payee of check deposited by corporation with instructions to credit to account of corporation's principal held to be mere financial intermediary that received no benefit and had no dominion over funds); Malloy v. Citizens Bank of Sapulpa (In re First Security Mortgage Co.), 33 F.3d 42, 43 (10th Cir. 1994) (following "dominion or control test to determine who is an initial transferee," set forth in Bonded case); United States v. Craft, 535 U.S. 274, 122 S.Ct. 1414, 1426 (2002) (held, federal tax lien may attach to taxpayer's interest in realty owned as tenancy by the entirety even when state law exempts such property from creditors' claims; taxpayer's later transfer of his interest in the property to spouse for nominal consideration ("one dollar") after IRS had filed notice of its tax lien caused Court to add that fraudulent transfer issues "in future cases" will be decided so as to enable Government to

¹ The debtor transferred record title of his home to his daughter so that she could qualify for a home improvement loan. The daughter later retransferred title back to her father and executed a "Counter Letter" describing the fact that the original transfer was made for convenience only and that she never paid any consideration for the first transfer. The lower court refused to allow the Counter Letter into evidence and held that the retransfer was made without reasonably equivalent value.

reach property transferred in "an attempt to evade the Government creditor."); Hatchett v. United States, 330 F.3d 875 (6th Cir. 2003) (retroactive application of Craft; federal tax liens may attach to property held by a delinquent taxpayer as a tenancy by the entirety; rev'd and remanded; Government's fraudulent transfer defense to Appellees' wrongful levy action not precluded); Moon v. Anderson (In re Hixon), 387 F.3d 695, 700 (8th Cir. 2004) (debtor was lifetime beneficiary of trust created by her nephew to avoid his creditors, and used trust funds to pay her personal expenses; held, debtor was owner of trust assets and her purchases could be avoided as fraudulent transfers.); Fed. Refinance Co. v. Klock, 352 F.3d 16, 25-26 (1st Cir. 2003) (property transferred need not have value; held, transfer putting property that would otherwise be available out of creditors' reach, even if property is worthless, is a fraudulent transfer); Stalnaker v. DLC, Ltd., 376 F. 3d 819, 823 (8th Cir. 2004) (although all creditors' claims settled, assets recovered by trustee were for benefit of estate; "bankruptcy estate is not synonymous with the concept of a pool of assets to be gathered for the sole benefit of unsecured creditors.").

D. Examples Of Fraudulent Transfers.

1. Debtor converts a sole proprietorship into a one-man corporation and transfers all his assets to the new entity. Shapiro v. Wilgus, 287 U.S. 348 (1932) (finding actual intent to delay creditors, despite good faith belief in propriety of acts).

2. Debtor arranges for a friend to purchase his property at an execution sale for a price substantially below its true value. Lefkowitz v. Finkelstein Trading Corp., 14 F. Supp. 898 (S.D.N.Y. 1936).

3. Debtor back-dates mortgage to defraud his creditors. Freudman v. Freudmann, 36 A.D.2d 968, 321 N.Y.S.2d 513 (App. Div. 2d Dept 1971).

4. Debtor agrees to rescind a profitable contract. Wilson v. Holub, 202 Iowa 549, 210 N.W. 593 (1926).

5. Debtor releases an interest in a decedent's estate. In re Clark, 488 Pa. 1, 410 A.2d 796 (1980); Schaefer v. Fisher, 137 Misc. 420, 242 N.Y.S. 308 (Sup. Ct. N.Y. County 1930).

6. Debtor-lessee agrees to cancel a valuable long-term lease. 348-352 West 27th St. Corp. v. Dropkin, 178 Misc. 815, 36 N.Y.S.2d 740 (Sup. Ct. N.Y. County 1942). Involuntary terminations of leases or executory contracts are also transfers which, under appropriate circumstances, are subject to attack as fraudulent transfers. Darby v. Atkinson (In re Ferris), 415 F. Supp. 33, 39-41 (W.D. Okla. 1976) (effective pre-petition lease termination by landlord while debtor-lessee was insolvent constituted fraudulent transfer for less than fair consideration). But see Coast Cities Truck Sales, Inc. v. Navistar Int'l Transp. Co. (In re Coast Cities Truck Sales, Inc.), 147 B.R. 674, 677-78 (D.N.J. 1992), aff'd, 5 F.3d 1488 (3d Cir. 1993) (pre-petition termination of dealership agreement does not constitute "transfer" for avoidance as fraudulent transfer; debtor-franchisee cannot revive properly terminated executory contract by fraudulent transfer avoidance).

7. Debtor transfers real property to a closely held corporation owned by his three children for "love and affection," when transfer renders him insolvent. Marine Midland Bank v. Stein, 105 Misc. 2d 768, 433 N.Y.S.2d 325 (Sup. Ct. N.Y. County 1980); see also Walker v. Treadwell (In re Treadwell), 699 F.2d 1050 (11th Cir. 1983); Tanner v. Smoot, 257 F.3d 401 (4th Cir. 2001), cert. denied Smoot v. Tavenner, 534 U.S. 1116 (2002) (debtor, claiming motivation of "love and affection", transfers exempt property to family-owned corporation, but court holds that transfer was fraudulent because made with intent to hinder, delay or defraud creditors); In re Marlar, 267 F.3d 749 (8th Cir. 2001) (no reasonable equivalent value when debtor transferred 700 acres of farmland to son for ten dollars plus love and affection).

8. While chapter 11 case is pending, majority shareholder of debtor corporation transfers controlling shares of corporation with fraudulent intent and without notice to creditors, resulting in merger of debtor-corporation with another entity and cessation of debtor-corporation's existence as a business entity. United States v. Goodstein, 883 F.2d 1362 (7th Cir. 1989), cert. denied, 494 U.S. 1007 (1990) (upholding former shareholder's conviction under criminal bankruptcy fraud statutes for fraudulently transferring controlling shares of debtor, reasoning that transfer of control of debtor was transfer of "ultimate 'interest'" in debtor's property with potential for great prejudice to creditors who have an interest in those who control assets of estate).

9. Debtor executes a confession of judgment to one creditor, knowing that it will hinder and delay another creditor who is not yet protected by a judgment. Spear v. Spear, 101 Misc.2d 341, 421 N.Y.S.2d 277 (Sup. Ct. Nassau County 1979).

10. Debtor corporation's controlling officers redeem worthless stock. Consove v. Cohen (In re Roco Corp.), 701 F.2d 978 (1st Cir. 1983).

11. Debtor conveys real property to himself and his wife, as tenants by the entirety, to shield property from execution by judgment creditors. Ford v. Poston, 773 F.2d 52 (4th Cir. 1985).

12. Debtor conveys income from his business to wife to shield property from tax liens. In re Blatstein, 192 F.3d 88, 97 (3d Cir. 1999) (husband's income derived from debtor's business, jointly owned with wife, was fraudulently transferred to wife's bank account under Pennsylvania Uniform Fraudulent Transfer Act; court refused to reclassify such income as dividend or equity distributions to shareholders; debtor intended to defraud creditors by depositing funds into wife's account because debtor's "credit and reputation with banks was poor, and because he 'was trying to keep the funds from being seized or frozen by the IRS or other taxing authorities, pursuant to a tax lien . . .'"; there is no requirement that debtor intend to defraud all creditors, but only "any creditor.") (internal cites omitted).

13. Debtor whose only substantial asset is judgment against defendants accepts less than full amount of judgment in satisfaction thereof. Nissim Hadjes, Inc. v. Hasner, 408 So. 2d 819 (Fla. Dist. Ct. App. 1982).

14. Debtor pays \$55,000 to outgoing president for purported covenant not to compete. Limperis v. Kolacny (In re Chicago Music Corp.), 36 B.R. 626 (Bankr. N.D. Ill. 1984).

15. Debtor makes payments of "interest" to investor in debtor's Ponzi scheme. Lawless v. Anderson (In re Moore), 39 B.R. 571 (Bankr. M.D. Fla. 1984). See also Hayes v. Palm Seedlings Partners-A (In re Agricultural Research and Technology Group, Inc.), 916 F.2d 528, 536 (9th Cir. 1990) (defendants should have known that "transferring funds to earlier investors from later investors and not from the proceeds of the underlying business would ultimately operate to the detriment of its creditors").

16. Debtor renounces testamentary devises in favor of family members, while under pressure from creditors. Nashville City Bank & Trust Co. v. Peery (In re Peery), 40 B.R. 811 (Bankr. M.D. Tenn. 1984); but see Blackwell v. Lurie (In re Popkin & Stern), 223 F.3d 764, 768 (8th Cir. 2000) (held, debtor never owned disclaimed property) (citing Simpson v. Penner (In re Simpson), 36 F.3d 450 (5th Cir. 1994) (Chapter 7 debtor's disclaimer of interest in testamentary disposition of father's property one day before filing of bankruptcy petition held not to be fraudulent transfer)); In re Atchison, 925 F.2d 209 (7th Cir. 1991), cert. denied sub nom. Jones v. Atchison, 502 U.S. 860 (1991).

17. Debtors make contributions to their church within one year prior to bankruptcy. Newman v. Midway Southern Baptist Church, 203 B.R. 468 (D. Kan. 1996) (debtor's church contributions could constitute fraudulent transfers). But the Religious Liberty and Charity Donation Protection Act of 1998, discussed in IV.B.17 *infra*, amended Code §§ 548 and 544(b) to prevent the trustee from challenging a good faith charitable gift as a fraudulent transfer, but not a gift made "with actual intent to hinder, delay or defraud" creditors. The legislation was enacted in response to cases like Christians v. Crystal Evangelical Free Church (In re Young), 148 B.R. 886 (Bankr. D. Minn. 1992), *aff'd*, 152 B.R. 939 (D. Minn. 1993) (contributions lacked reasonably equivalent value), *rev'd on other grounds*, 82 F.3d 1407, 1415-17 (8th Cir. 1996) (trustee's recovery of church donations by debtors, which were avoidable transfers because the debtors did not receive services in exchange for their contributions, held to violate the Religious Freedom Restoration Act) *vacated and remanded* 65 U.S.L.W. 3205 (1997) (remanded in light of City of Boerne v. Flores, 521 U.S. 507 (1997), held, Religious Freedom Restoration Act unconstitutional); *on remand*, 141 F.3d 854 (8th Cir. 1998) (2-1) (held, RFRA constitutional exercise of congressional power with respect to federal legislation violated neither separation of powers doctrine nor Establishment Clause of First Amendment; earlier decision reinstated), cert. denied, 119 S. Ct. 43 (1998).

18. Insolvent individual debtor guarantees corporate line of credit. Continental Bank v. Modansky, 159 B.R. 129 (S.D.N.Y. 1993), *aff'd*, 41 F.3d 1501 (2d Cir. 1994). The court in Modansky found that the debtor was insolvent on the date he transferred title to real estate to his wife without fair consideration, rendering the transfer fraudulent under Section 276 of New York's Debtor and Creditor Law. "Under New York law, a guarantee of a loan is a probable liability which must be considered in determining a person's solvency at the time of a transfer under DCL § 273." *Id.* at 133. The court held that beginning with the date the corporation was unable to pay its debts as they matured, the guarantee was a probable liability of the husband guarantor, which had the effect of rendering the husband insolvent. *Id.* at 134.

19. An insolvent debtor-taxpayer's irrevocable election to forego a net operating loss carryback. In re Feiler, 218 F.3d 948, 950-51 (9th Cir. 2000) ("We hold that a bankruptcy Trustee's § 548 avoidance powers take precedence over the otherwise irrevocable nature of a § 172 election [under the Internal Revenue Code], and therefore, that a trustee may avoid such a tax election as a fraudulent transfer. . . . [Debtors] deprived the bankruptcy estate of the benefit of the tax refund by waiving the carryback in order to preserve the future [tax] benefits . . . for themselves after bankruptcy."); compare In re Marvel Entm't Group, Inc., 273 B.R. 58, 85 (D. Del. 2002) (concept of separate NOLs for individual members of a consolidated tax filing group does not exist; accordingly, there can be no transfer for fraudulent transfer purposes when NOLs generated by debtor are used to reduce tax liability of consolidated group).

E. Codification Of Law Of Fraudulent Transfers.

1. Statute Of Elizabeth. Anglo-American fraudulent transfer law originated with the Statute of 13 Elizabeth, Chapter 5 (1571), which deemed void any conveyance made with intent "to delay, hinder or defraud creditors and others of their just and lawful actions, suits, debts. . . ." Fraudulent Conveyances, 13 Eliz., ch. 5 (1571). The Statute of Elizabeth is still part of the common law or statutory law of every American jurisdiction. 5 Collier on Bankruptcy, ¶ 548.LH[1], at 548-88 (Lawrence P. King ed., 15th rev. ed. 1997).

2. Uniform Fraudulent Conveyance Act. Five states, including New York, still retain the Uniform Fraudulent Conveyance Act ("UFCA"), first promulgated in 1918. The UFCA codifies the Statute of Elizabeth, but also deems voidable those transfers that are constructively, rather than actually, fraudulent. See I.E.3., infra, and N.Y. Debt. & Cred. L. art. 10 (McKinney 1945 & Supp. 1990). In practice, there is little difference between the application of fraudulent transfer law under the Statute of Elizabeth and under the UFCA, because states not adopting the UFCA have established extensive and similar presumptions and rules for inferring intent. See, e.g., Gyorok v. Davis, 183 So.2d 701, 703 (Fla. Dist. Ct. App. 1966) (prior to Florida's enactment of uniform law, Florida court held transfer for nominal consideration is prima facie evidence of fraudulent intent).

3. Bankruptcy Code. Section 548 of the Bankruptcy Code ("Code") establishes a federal law of fraudulent transfers, and enables the trustee to avoid transfers made and obligations incurred by the debtor within one year of the filing of a petition under Title 11, if certain financial tests are met or if actual intent to hinder, delay, or defraud creditors is established. Section 548 is derived from the UFCA and resembles it closely enough that case law under one statute is usually applicable to the other. See Kojima v. Grandote Int'l. LLC (In re Grandote Country Club Co. Ltd.), 252 F.3d 1146, 1152 (10th Cir. 2001) ("[T]he language of [Code] § 548 and the relevant portions of the [Uniform Fraudulent Transfer Act] are quite similar . . . Because this language is nearly identical, the holding of [a case decided under Code § 548] logically applies to [a case governed by the Uniform Fraudulent Transfer Act]."). Like the UFCA, the Code classifies fraudulent transfers as actually fraudulent (i.e., made with actual intent to hinder, delay, or defraud [section 548(a)(1)(A)]) or constructively fraudulent (i.e., made at a time when the debtor is financially troubled or inadequately capitalized [section 548(a)(1)(B)]). Section 544(b) of the Code also gives the trustee whatever avoiding powers an unsecured creditor with an allowable claim might have under applicable state or federal law, including the UFCA or Uniform Fraudulent Transfer Act (see I.E.4., infra), where adopted, and

Article 6 of the Uniform Commercial Code (bulk transfers; bulk sales). Blackwell v. Lurie (In re Popkin & Stern), 223 F.3d 764, 768 n.11 (8th Cir. 2000) (applying Missouri law [Uniform Fraudulent Transfer Act] to define the scope and meaning of a real property disclaimer (citing Michael L. Cook et al., Fraudulent Transfers, 804 PLI/Comm 473, 486 (Apr. 2000))). Verco Indus. v. Spartan Plastics (In re Verco Indus.), 704 F.2d 1134, 1137 (9th Cir. 1983) (bulk transfer not complying with Article 6 could be avoided under section 544(b)); Seligson v. New York Produce Exch., 378 F. Supp. 1076, 1106-07 (S.D.N.Y. 1974) (New York fraudulent transfer law applied).

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, enacted April 20, 2005 (the "2005 Amendments") makes key changes to section 548:

- Extends the current 1-year reachback period to 2 years, effective for cases commenced on or after April 20, 2006;
- Permits the trustee to avoid an insider transfer pursuant to an employment contract if the transfer was made outside the ordinary course of business and the debtor received less than reasonably equivalent value; no proof of insolvency required; effective for cases commenced on or after April 20, 2005;
- Permits the trustee to avoid transfers made within 10 years before the commencement of the case if the debtor makes a transfer to a self-settled trust of which it is a beneficiary with actual intent to hinder, delay or defraud a creditor.

4. Uniform Fraudulent Transfer Act. The Uniform Fraudulent Transfer Act ("UFTA") was approved by the National Conference of Commissioners on Uniform State Laws in 1984 as a replacement for the UFCA. To date, at least thirty-nine states and the District of Columbia have adopted the UFTA. The adoption of the UFTA by a state, however, does not pre-empt state common law remedies relating to fraudulent transfers. Fleet Nat'l Bank v. Valente (In re Valente), 360 F.3d 256, 261 (1st Cir. 2004) ("Our own case law rejects the proposition that the adoption of the UFTA by a state preempts all common law remedies relating to fraudulent transfers."). As the statute has become more widely adopted, it has had a significant impact on many areas of law, especially those involving leveraged buyouts, asset sales, and disputes with the Internal Revenue Service. The UFTA has borrowed heavily from the Bankruptcy Code and contains important changes from the UFCA, both in structure and in substance. The important changes, noted in greater depth below, include the following: the introduction of provisions making transfers to insiders voidable; generally enhanced creditors' remedies against transferees; the inclusion of a uniform statute of limitations; a new, more objective definition of insolvency than the one in section 101(32) of the Code; elimination of the "good faith" requirement contained in the UFCA's definition of "fair consideration"; enumeration of certain "badges of fraud"; omission of a provision directed specifically at transfers or obligations of insolvent partnership debtors; and certain new defenses for fraudulent transfer defendants. See generally Cook and Mendales, The Uniform Fraudulent Transfer Act: An Introductory Critique, 62 Am. Bankr. L.J. 87 (1988). A statutory cross-reference comparing the operative provisions of the Code, the UFCA, and the UFTA is attached.

II. Definitions And Procedure

A. Transfer. Transfer is defined in section 101(54) of the Code, as amended by the 2005 Amendments, to mean "(A) the creation of a lien; (B) the retention of title as a security interest; (C) the foreclosure of a debtor's equity of redemption; or (D) each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or departing with (i) property; or (ii) an interest in property."² Black & White Cattle Co. v. Granada Cattle Servs., Inc. (In re Black & White Cattle Co.), 783 F.2d 1454, 1462 (9th Cir. 1986) (Code definition of transfer "expressly encompasses transfers of an interest in property as distinct from transfers of the property itself."); Claussen Concrete Co. v. Walker (In re Lively), 74 B.R. 238, 239 (S.D. Ga. 1987) (judgment lien is transfer of an interest of debtor in property), aff'd, 851 F.2d 363 (11th Cir. 1988). See also Bustamente v. Johnson (In re McConnell), 934 F.2d 662, 664 (5th Cir. 1991) (\$600,000 down payment is "transfer" subject to § 548 notwithstanding failure to close deal; court rejected argument that no transfer occurred because debtor's default on contract extinguished his equitable interest); see, e.g., Hughes v. Lawson (In re Lawson), 122 F.3d 1237, 1240 (9th Cir. 1997) (Chapter 7 debtor's grant of deed of trust on her residence to her mother was "transfer" of property); Levine v. Weissing (In re Levine), 134 F.3d 1046, 1050 (11th Cir. 1998) (held, debtors' conversion of funds from non-exempt to exempt status through purchase of annuities constituted "transfer" for purposes of Florida fraudulent transfer law); Parker v. Saunders (In re Bakersfield Westar, Inc.), 226 B.R. 227, 230 (B.A.P. 9th Cir. 1998) (held, otherwise valid revocation of corporation's subchapter S election immediately prior to bankruptcy voidable as fraudulent transfer; IRS had unsuccessfully argued that Subchapter S election was not a property interest because it had no "present value"); Kojima v. Grandote Int'l. LLC (In re Grandote Country Club Co. Ltd.), 252 F.3d 1146, 1151-1152 (10th Cir. 2001) (no transfer by debtor when debtor's property transferred pursuant to tax deed under Colorado law; transfer deemed made by State, "free of all prior interests," not by debtor); In re Marvel Entm't Group, Inc., 273 B.R. 58, 85 (D. Del. 2002) (there can be no transfer for fraudulent transfer purposes when NOLs generated by debtor are used to reduce tax liability of consolidated group); Trinity Gas Corp. v. Taylor, 276 F.3d 699, 702 (5th Cir. 2002) (when property sellers exercise their right to reclaim or "redeem" property under Louisiana law, it effects a dissolution of the original sale that "primes any rights acquired by later judgments or judgment creditors."); In re Pulliam, 279 B.R. 916 (Bankr. M.D. Ga. 2002) (debtor withdrew funds from IRA with intent to pay creditors; after advice of lawyer that funds were exempt property, debtor re-deposited funds into IRA; held, rollover qualified as transfer because made with actual intent to hinder, delay, or defraud creditors); Duncan v. Duncan (In re Duncan), 329 F.3d 1195 (10th Cir. 2003) (attorney transfers property to himself and wife as tenants by the entirety during legal malpractice action; prior to entry of a final judgment, attorney files chapter 7; held, debtor barred from seeking state homestead and tenancy by the entirety exemptions under section 522(g) because transfer of property was voluntary and made with the intention to avoid creditors).

² The 2005 Amendments altered the definition of transfer under section 101(54). The definition of transfer before the 2005 Amendments included "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, including retention of title as a security interest and foreclosure of the debtor's equity of redemption." The old definition of transfer still applies to cases commenced before October 17, 2005.

To recover a transfer of property as fraudulent, the debtor must have possessed more than bare legal title to the property transferred. Krommenhoek v. A-Mark Precious Metals, Inc. (In re Bybee), 945 F.2d 309, 315 (9th Cir. 1991). Moreover, a debtor who has validly disclaimed a property interest may provide the beneficiary of the disclaimer with "a complete defense to [a] fraudulent transfer [suit] under [the] UFTA." Blackwell v. Lurie (In re Popkin & Stern), 223 F.3d 764, 768-769 (8th Cir. 2000) (applying UFTA and other Missouri law pursuant to Code § 544(b), disclaimer of gift from decedent's estate "relates back to the granting of the gift and treats the disclaimant as if he predeceased the donor. Accordingly, anything that devolves as a result of the disclaimer devolves as a matter of law from the donor to the beneficiary, not by a transfer from the disclaimant to the beneficiary. . . . [Debtor's] disclaimer . . . [is] not . . . subject to the claims of any creditor of the disclaimant."); accord Simpson v. Penner (In re Simpson), 36 F.3d 450, 452 (5th Cir. 1994) (held, applying analogous Texas law, "under the relation back doctrine, a [designated] beneficiary never possessed renounced property"); Jones v. Atchison (In re Atchison), 925 F.2d 209, 211 (7th Cir. 1991) (same under analogous Illinois law; disclaimant "had nothing to transfer"), cert. denied, 502 U.S. 860 (1991); Essen v. Gilmore, 259 Neb. 55, 607 N.W.2d 829, 834-35 (2000) ("Because a beneficiary who has renounced his . . . interest in property does not have and, pursuant to the relation-back doctrine, has not acquired rights in the asset renounced, he . . . cannot 'transfer' the property within the meaning of the UFTA. . . . [I]t is the majority view that a renunciation under the applicable state probate code is not treated as a fraudulent transfer of assets under the UFTA, and creditors of the person making a renunciation cannot claim any rights to the renounced property in the absence of an express statutory provision to the contrary."). Cf. Pioneer Liquidating Corp v. San Diego Trust & Sav. Bank (In re Consolidated Pioneer Mortgage Entities), 211 B.R. 704, 715 (S.D. Cal. 1997) (held, UCC security interest in deposited checks that arose in favor of bank when debtor withdrew provisionally credited funds was not "transfer" of interest in property because the creation of the security interest "does not require the customer to surrender an interest that it could otherwise retain"), aff'd in part, rev'd in part, 166 F.3d 342 (9th Cir. 1999); Bear, Stearns Sec. Corp. v. Gredd, 275 B.R. 190 (S.D.N.Y. 2002) (proceeds generated from debtor's short sales of stock³ and securities later purchased to cover those short sales are not interests in debtor's property within the meaning of section 548).

A court may also "collapse" several different but related transactions or transfers into one transaction for fraudulent transfer purposes. Orr v. Kinderhill Corp., 991 F.2d 31 (2d Cir. 1993); Voest-Alpine Trading USA Corp. v. Vantage Steel Corp., 919 F.2d 206 (3d Cir. 1990).

The UFTA's definition of transfer is, for all practical purposes, identical to that of the Code. A fraudulent transfer may include an absolute transfer, such as a gift or a sale, Schafer v. Hammond, 456 F.2d 15 (10th Cir. 1972), or a security transfer, such as a mortgage of real property, a pledge, or a security interest in personal property, In re Decker, 295 F. Supp. 501, 514 (W.D. Va. 1969), aff'd sub nom. Woodson v. Gilmer, 420 F.2d 378 (4th Cir. 1970), cert. denied, 399 U.S. 928 (1970). See also Kaler v. Craig (In re Craig), 144 F.3d 587, 593 (8th Cir.

³ "A short sale of stock is a speculative transaction where a security not owned by the seller is sold in the hope that the price of the security will decline, permitting the seller to later repurchase the security ("cover") and make a profit. Typically, the seller borrows the security from his broker and covers by later buying the identical stock and transferring it to his broker." Id. at 192, n.3.

1998) (held, under North Dakota's version of UFTA, debtor made indirect fraudulent transfer to wife when he directed that his loan funds be used to pay for residence titled in wife's name). The definition of "conveyance" in the UFCA is somewhat more limited than that of "transfer" in the Code and in the UFTA. Thus, certain types of involuntary transfers may be avoidable under the Code and UFTA, but not under the UFCA. See 5 Collier on Bankruptcy, ¶ 548.02[1][a], at 548-9 to 548-10 (Lawrence P. King ed., 15th rev. ed. 1997).

B. Avoidance and Recovery. Avoidance is a concept under which a trustee can nullify a transfer that diminishes the estate under Code sections 544 and 548. Recovery is a statutory mechanism through which property, or its value, may be returned to the estate under Code section 550. "[W]hen the avoidance of a transfer does not fully satisfy the estate, then the trustee may seek to recover the property transferred, but when the avoidance alone is a sufficient remedy, there is no need for the trustee to seek recovery." Suhar v. Burns (In re Burns), 322 F.3d 421, 427 (6th Cir. 2003). In Burns, the court held that a trustee could avoid an improperly witnessed mortgage under section 544(a)(3), which permits avoidance of a transfer that would be voidable by a bona fide purchaser under state law. Creditor argued that it was entitled to a lien on the property under section 550(e), which provides that a good faith transferee from whom a trustee recovers property is entitled to a lien to offset the cost of any improvement (here, the payment of a debt). Noting that the trustee neither sought, nor needed to seek, recovery under section 550, the court held "where there is no recovery under § 550(a), there are no protections under § 550(e)." Id. at 429. See also In re Coleman, 426 F.3d 719, 725-27 (4th Cir. 2005) (rejecting creditor's argument that Code § 550 creates an ambiguity in Code § 544: "once debtor avoided the [liens], no recovery was necessary; the avoidance itself was a meaningful event . . . Thus, the recovery statute (§ 550) has no application here.").

C. Insolvency. The Code definition of insolvency requires a simple "balance sheet" test and excludes from the fair value of the debtor's property any fraudulently transferred property as well as exempt property. See 11 U.S.C. § 101(32); Coleman v. Home Savs. Ass'n (In re Coleman), 21 B.R. 832, 835 (Bankr. S.D. Tex. 1982) ("[E]xempt property must be excluded when applying the balance sheet test for insolvency."). Contingent assets such as rights to contribution and subrogation must be valued for purposes of determining solvency. Manufacturers & Traders Trust Co. v. Goldman (In re Ollag Constr. Equip. Corp.), 578 F.2d 904, 908-09 (2d Cir. 1978). Contingent assets and liabilities, however, should not be considered at face value, but rather should be discounted by the probability that the contingency will materialize. See Nordberg v. Arab Banking Corp. (In re Chase & Sanborn Corp.), 904 F.2d 588, 594 (11th Cir. 1990); In re Xonics Photochemical, Inc., 841 F.2d 198, 200 (7th Cir. 1988); Covey v. Commercial Nat'l Bank of Peoria, 960 F.2d 657 (7th Cir. 1992) (contingent liability should be determined by multiplying total debt guaranteed by probability that debtor would be required to make good on guarantee); see, e.g., Travellers Int'l AG v. Trans World Airlines, Inc. (In re Trans World Airlines, Inc.), 134 F.3d 188, 197-198 (3d Cir. 1998) (deposit voidable as preference when debtor insolvent on date of transfer because value of debtor's liabilities exceeded that of its assets; "it is proper to consider contingent liabilities when evaluating the insolvency of a corporation pursuant to 11 U.S.C. § 101(32)(A)"; in treating debtor as going concern, court limited contingent liabilities to costs arising from foreseeable events that might occur while debtor remains in business), cert. denied, 118 S. Ct. 1843 (1998); Federal Deposit Ins. Corp. v. Bell, 106 F.3d 258, 264 (8th Cir. 1997) ("To correctly 'value the contingent liability

it is necessary to discount it by the probability that the contingency will occur and the liability become real." quoting In re Xonics Photochemical, Inc., 841 F.2d 198, 200 (7th Cir. 1988)); Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 155-156 (3d Cir. 1996) ("[I]f a debtor's treatment of an item as an 'asset' depends for its propriety on the occurrence of a contingent event, a court must take into consideration the likelihood of that event occurring from an objective standpoint," when making solvency determination on fraudulent transfer claim; under balance sheet test, "assets and liabilities are tallied at fair valuation to determine whether the corporation's debts exceed its assets" (quoting Mellon Bank, N.A. v. Metro Communications, Inc., 945 F.2d 635, 648 (3d Cir. 1991), cert. denied, 503 U.S. 937 (1992)); Official Comm. of Asbestos Personal Injury Claimants v. Sealed Air Corp. (W.R. Grace & Co.), 281 B.R. 852, 869 (Bankr. D. Del. 2002) (held, disposing of in limine motion, court relied on hindsight to find insolvency; "asbestos claims filed [against the debtor] after the transfer date may be considered in determining the debtor's solvency [on] the transfer date."); but see Lippe v. Bairnco Corp., 99 Fed. Appx. 274, 282 (2d Cir. 2004) (rejecting argument that under New York's version of the UFCA, "future claims" must be included when calculating solvency; "[T]he hypothetical existence of an unaccrued tort claim does not give rise to a debtor-creditor relationship. There is no existing debt.").

The UFCA provides a somewhat more complex definition. Under section 2(1) of the UFCA, "[a] person is insolvent when the present fair salable value of his assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured." "Present fair salable value" means the value that can be obtained if the assets are sold with reasonable promptness in an existing (not theoretical) market. United States v. Gleneagles Inv. Co., 565 F. Supp. 556, 578 (M.D. Pa. 1983), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987). Under this definition, a debtor may be insolvent for UFCA purposes even when the value of his assets exceeds the amount of his debts, if the assets are illiquid and the debts short-term. The appropriate methodology for valuation of illiquid assets (e.g., going concern or liquidation valuation) depends, in part, on whether bankruptcy is clearly imminent on the date of the challenged transfer. Moody v. Security Pacific Business Credit, Inc., 971 F.2d 1056, 1067 (3d Cir. 1992) (following majority rule of going concern asset valuation when bankruptcy not clearly imminent). If the transferor was in debt at the time of the transfer, the burden is upon the party seeking to sustain the transfer to prove that the transferor was either solvent at the time of the transfer or received fair consideration in exchange for the transfer. Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 144 (3d Cir. 1996) (creditors' committee seeking to avoid payment made by chapter 11 debtor had burden of establishing section 548(a)(2) elements).

The UFTA contains a new definition of insolvency: a "balance sheet" definition similar but not identical to that contained in the Code. Under UFTA § 2, a debtor is insolvent if the sum of his debts is greater than that of his assets "at a fair valuation," a term left undefined by the UFTA. Significantly, UFTA § 2(b) contains a rebuttable presumption that a debtor who is generally not paying his debts as they become due is insolvent. The debtor's "assets" are defined in UFTA § 1(2) to exclude (i) an interest in property held by the entireties to the extent that a

creditor with a claim against only one of the tenants may not reach such property;⁴ (ii) property to the extent encumbered by a valid lien (but, under UFTA § 2(e), debts are not included to the extent that they are secured by property thus excluded); and (iii) property "to the extent it is generally exempt under nonbankruptcy law." Comment (1) to UFTA § 2 states that this latter exclusion applies not only to property which a debtor may exempt from creditor process under homestead and other exemption laws, but also to an interest in a valid spendthrift trust.

The UFTA's definition of insolvency makes it easier than under prior UFCA law for creditors to prove a fraudulent transfer when insolvency is a material element. The plaintiff creditor need only show, in most cases, that the debtor has generally stopped paying his debts as they become due, placing the burden of proving solvency on the debtor. In re Advanced Telecommunications Network, Inc., 490 F.3d 1325, 1332 (11th Cir. 2007).

1. Proving Insolvency. "For purposes of § 548, solvency is measured at the time the debtor transferred value, not at some later or earlier time." Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 154 (3d Cir. 1996). Unlike a preference action⁵, however, there is no presumption of insolvency in a fraudulent transfer action. Thus, proof by direct evidence of the insolvency of the debtor on the critical date of the transfer may be difficult; "insolvency frequently must be determined by proof of . . . factors from which insolvency may be inferred." Constructora Maza, Inc. v. Banco de Ponce, 616 F.2d 573, 577 (1st Cir. 1980); see also Achille Bayart & CIE v. Crowe, 238 F.3d 44, 48 (1st Cir. 2001) ("The plaintiff has the burden of proving that there was some determinable amount of value in the assets of the debtor over and above the amount of the secured debt."). But the trustee must still prove "fair value" of the debtor's property, particularly because "book value" may not reflect "the property's fair value." Orix Credit Alliance, Inc. v. Harvey (In re Lamar Haddox Contractor, Inc.), 40 F.3d 118, 121 (5th Cir. 1994). An accountant's "conclusory opinion testimony . . . without any [supporting] evidence" will be insufficient when there are "substantial questions . . . as to the fair value of the Debtor's property." Id. at 122.

2. Retrojection. Courts have used the term "retrojection" to describe the process of working backwards from the time of the avoidance action to the date of the transfer to show factors from which the debtor's insolvency may be presumed. See, e.g., Briden v. Foley, 776 F.2d 379 (1st Cir. 1985); Misty Management Corp. v. Lockwood, 539 F.2d 1205, 1213 (9th Cir. 1976). When using the accounting technique of retrojection to prove insolvency, however, the trustee must show the absence of any substantial or radical changes in the assets or liabilities of the debtor between the retrojection dates. Foreman Indus., Inc. v. Broadway Sand & Gravel (In re Foreman Indus., Inc.), 59 B.R. 145 (Bankr. S.D. Ohio 1986); Kanasky v. Randolph (In re R. Purbeck & Assocs., Ltd.), 27 B.R. 953 (Bankr. D. Conn. 1983).

⁴ But see United States v. Craft, 545 U.S. 274, 122 S.Ct. 1414 (2002) (federal tax liens may attach to property held by tenancy by the entirety) (discussed I.C., supra).

⁵ "For the purposes of this section, the debtor is presumed to have been insolvent on and during the 90 days immediately preceding the date of the filing of the petition." 11 U.S.C. § 547(f).

D. Time Of Transfer. For purposes of § 548, a transfer is "made" when it becomes valid against a subsequent bona fide purchaser pursuant to applicable state law.⁶ 11 U.S.C. § 548(d)(1); see also Sandoz v. Bennett (In re Emerald Oil Co.), 807 F.2d 1234, 1237 (5th Cir. 1987); Dean Witter Reynolds, Inc. v. MacQuown (In re MacQuown), 717 F.2d 859, 862-63 (3d Cir. 1983) (Act case) (transfer of real property effective at time deed recorded); Lovett v. Shuster, 633 F.2d 98, 104 (8th Cir. 1980); Jackson Sound Studios, Inc. v. Travis, 473 F.2d 503, 506 (5th Cir. 1973). If the transfer is not perfected against a bona fide purchaser before the commencement of the case, the transfer is deemed to occur immediately before the date of the filing of the petition. 11 U.S.C. § 548(d)(1). In this way, the trustee can avoid secret (i.e., unperfected) liens. Madrid v. Lawyers Title Ins. Corp. (In re Madrid), 725 F.2d 1197, 1200 (9th Cir. 1984), cert. denied, 469 U.S. 833 (1984). The UFCA, in contrast, contains no comparable provision defining the time of transfer, and the time in which a transfer is actually made still controls. Under the UFTA, guidelines for determining when a transfer occurs are set forth in section 6(l). The transfer of an asset that is not real property or is a fixture is made when it is so perfected that a creditor cannot acquire a judicial lien (other than a lien under the UFTA) that would create an interest superior to that of the transferee. The difference among the three statutes may be significant in terms of the relevant statutory reachback period. See II.I., *infra*.

Prior to enactment of the Bankruptcy Amendments and Federal Judgeship Act of 1984, a conflict among the circuits existed on the issue of when a transfer occurs in the context of a mortgage foreclosure sale of a debtor's property. Compare Madrid v. Lawyers Title Ins. Corp. (In re Madrid), 725 F.2d 1197 (9th Cir. 1984), cert. denied, 469 U.S. 833 (1984) (a transfer is made for the purposes of section 548(d)(1) when the mortgagee's security interest is perfected by recording of the deed of trust (in Madrid, more than a year prior to bankruptcy, so that the transfer could not be avoided), and not when the property is sold at foreclosure) with Durrett v. Washington Nat'l Ins. Co., 621 F.2d 201 (5th Cir. 1980) (decided under section 67(d)(5) of former Bankruptcy Act, forerunner of section 548(d)(1)) (foreclosure sale less than one year before bankruptcy may be set aside as fraudulent, even though mortgage recorded more than one year prior to bankruptcy); Abramson v. Lakewood Bank & Trust Co., 647 F.2d 547 (5th Cir. 1981) (affirming Durrett), cert. denied, 454 U.S. 1164 (1982); First Fed. Savs. & Loan Ass'n of Bismarck v. Hulm (In re Hulm), 738 F.2d 323 (8th Cir. 1984), cert. denied, 469 U.S. 990 (1984) (not citing Durrett, but expressly declining to follow Madrid) (foreclosure of mortgage under North Dakota statutory scheme effects transfer within meaning of section 548(d)(1) and may therefore be avoided under section 548(a)).

In the 1984 amendments, the words "and foreclosure of the debtor's equity of redemption" were added to the definition of transfer in the Code. 11 U.S.C. § 101(54).⁷

⁶ Section 727(a)(2) (denial of debtor's discharge for actually fraudulent transfer within 1 year of bankruptcy), however, contains no such definition, and there is a split of authority regarding when a transfer is "made" under that section. 6 Collier on Bankruptcy, ¶ 727.02[2][c] at 727-14 to 727-15 (Lawrence P. King ed., 15th rev. ed. 1997). See also Finalco, Inc. v. Roosevelt (In re Roosevelt), 87 F. 3d 311, 318 (9th Cir. 1996), amended, 98 F. 3d 1169 (1996), cert. denied, 117 S. Ct. 1691 (1997) ("a transfer under § 727(a)(2) is "made" at the time it is valid between the parties to that transfer, irrespective of whether it is valid as against BFPs"); Dean Witter Reynolds, Inc. v. MacQuown (In re MacQuown), 717 F.2d 859, 863 (3d Cir. 1983) (transfer made "when it is good against bona fide purchasers"; court was interpreting § 14(c)(4), the substantive predecessor to § 727(a)(2)).

⁷ The 2005 Amendments preserve this clarification.

Although this change seems, objectively, to side with Durrett, it was originally part of a legislative package designed to overrule it. See Verna v. Dorman (In re Verna), 58 B.R. 246, 251 (Bankr. C.D. Cal. 1986) (held, third party purchaser of property at a noncollusive and regularly conducted foreclosure sale purchases property for reasonably equivalent value required by section 548); see also Alden, Gross & Borowitz, The Durrett Controversy And Foreclosure Sales, N.Y.L.J., Nov. 14, 1984, at 33, col. 1; Berman & Fierberg, Durrett, The Problem And Suggestions For Its Solution, 90 Com. L.J. 162 (1985).

Courts that address the issue after the effective date of the 1984 amendment (including the Ninth Circuit, which decided Madrid) concluded that a "transfer" occurs upon the foreclosure of a debtor's equity of redemption. Ehring v. Western Community Money Ctr. (In re Ehring), 900 F.2d 184, 187 (9th Cir. 1990) (1984 amendment changes analysis set forth in Madrid, and supports conclusion that foreclosure sale transfers or extinguishes debtor's interest in property). Accord Walker v. Littleton (In re Littleton), 888 F.2d 90, 92-93 n.6 (11th Cir. 1989). See also Bundles v. Baker (In re Bundles), 856 F.2d 815, 817 n.2 (7th Cir. 1988) (dicta) ("[w]e also note that many courts now consider the transfer issue to have been resolved definitively by the 1984 Amendments to the Bankruptcy Code."). But see In re Winshall Settlor's Trust, 758 F.2d 1136, 1138 n.3 (6th Cir. 1985) (dicta) (Madrid court correctly looked to section 548(d)(1) to determine when transfer for fraudulent transfer purposes occurs; 1984 amendment to definition of transfer has no effect on Madrid). Some courts have chosen to avoid the "transfer" timing issue and focus instead on whether the foreclosure sale results in "reasonably equivalent value." See IV.B.1, *infra*, discussing BFP v. Resolution Trust Corp., 511 U.S. 531 (1994), which moots the entire issue by its holding that "reasonably equivalent value" is always received at a regularly conducted, non-collusive foreclosure sale pursuant to state law.

E. Persons Who May Bring Action To Set Aside Fraudulent Transfer.

1. General Rule: Only The Trustee Has Standing. Under the Code, usually the trustee or debtor-in-possession (see 11 U.S.C. § 1107(a)) has the "avoiding power" and the right to commence an action alleging fraudulent transfers under sections 548 and 544(b). See, e.g., Hall v. Walter (In re Hall), 139 F.3d 911 (10th Cir. 1998) (unpublished decision) (section 1109(b) does not extend avoidance power to creditors; the only way defendant-creditor could have brought an avoidance action was "by making demand on the debtor-in-possession (Hall), having that demand refused, and then obtaining permission from the judge in the main case to proceed"); Nangle v. Lauer (In re Lauer), 98 F.3d 378, 388 (8th Cir. 1996) (held, limited partner of real estate partnership in which debtor was general partner lacked standing to bring claim under section 548 absent evidence that trustee was unable or unwilling to pursue claims on behalf of estate). Carlton v. Baww, Inc., 751 F.2d 781 (5th Cir. 1985); American Nat'l Bank v. MortgageAmerica Corp. (In re MortgageAmerica Corp.), 714 F.2d 1266, 1276 (5th Cir. 1983); Best Mfg. v. White Plains Coat & Apron Co. (In re Daniele Laundries, Inc.), 40 B.R. 404, 408 (Bankr. S.D.N.Y. 1984) ("It is axiomatic that a duly qualified trustee in bankruptcy represents the estate and is the only proper party to maintain any action under Code § 544(b) . . . and that the creditors of the estate have no right to proceed independently in their own names or on behalf of the estate."). See also National American Ins. Co. v. Landscaping Co., Inc., 187 F.3d 439, 441 (4th Cir. 1999) (sureties lacked standing to sue non-debtor company in district court based on claims for successor liability, tortious interference of contract and statutory and common law

conspiracy because such claims were similar in object and purpose to fraudulent transfer claims trustee could have brought against same party); Daily v. Fusco (In re All-Type Printing, Inc.), 274 B.R. 316 (Bankr. D. Ct. 2002) aff'd In re All-Type Printing, Inc., 80 Fed. Appx. 700 (2d Cir. 2003) (under section 544(b), trustee has no standing to bring strong-arm claim to avoid fraudulent transfer unless the record reveals the existence of one or more actual creditors whose claims arose prior to the date of the subject transfer). Cf. Klingman v. Levinson (In re Levinson), 158 B.R. 109 (N.D. Ill. 1993) (when trustee's right to pursue fraudulently conveyed assets expires, creditors may pursue state law remedies). The action, however, may be brought only if it will benefit the estate and not just the debtor. The Fourth Circuit has held that a debtor-in-possession did not have standing to bring a suit to set aside the pre-petition sale of a stock that increased in value because the creditors for whom the debtor-in-possession claimed to be seeking the recovery would approve the plan without the recovery, and only the debtor-in-possession would benefit from a surplus. Wellman v. Wellman, 933 F.2d 215 (4th Cir. 1991), cert. denied, 502 U.S. 925 (1991); In re PWS Holding Corp., 303 F.3d 308 (3d Cir. 2002), cert. denied Haskell v. PWS Holding Corp., 123 S. Ct. 1594 (2003) (individual creditor enjoined from bringing state law fraudulent transfer action after confirmation of plan; creditor's right to bring suit had been extinguished by confirmation order; creditor objected, and failed to appeal; court's enjoining of post-confirmation suit and sanction against individual creditor affirmed).

2. Creditors May Acquire Standing With Court Order. Under special circumstances, however, courts have permitted individual creditors or creditors' committees to bring such actions, especially when the debtor's estate lacks sufficient funds to bring the action itself. See, e.g., Canadian Pa. Forest Prod. Ltd. v. J.D. Irving, Ltd. (In re Gibson Group, Inc.), 66 F.3d 1436, 1446 (6th Cir. 1995) ("a creditor or creditors' committee may have derivative standing to initiate an avoidance action where: 1) a demand has been made upon the statutorily authorized party to take action; 2) the demand is declined; 3) a colorable claim that would benefit the estate if successful exists, based on a cost-benefit analysis performed by the court; and 4) the inaction is an abuse of discretion ('unjustified') in light of the debtor-in-possession's duties in a chapter 11 case."); In re Xonics Photochemical, Inc., 841 F.2d 198, 199 (7th Cir. 1988) (creditor seeking to avoid debtor's obligation in face of recalcitrant debtor-in-possession should either move for appointment of trustee or seek bankruptcy court authorization to bring derivative action to avoid the obligation); William B. Tanner Co. v. United States (In re Automated Business Sys., Inc.), 642 F.2d 200 (6th Cir. 1981) (court permitted creditor to bring fraudulent transfer action under Code because trustee claimed that estate lacked sufficient money to fund litigation). But cf. The Mediators, Inc. v. Manney (In re The Mediators, Inc.), 105 F.3d 822 (2d Cir. 1997) (creditors' committee had no standing to assert, on behalf of debtor-in-possession, debtor's aiding-and-abetting claims against third parties for conduct initiated by debtor; claims belonged to creditors, not to debtor, and creditors were time-barred); Lippe v. Bairnco Corp., 218 B.R. 294, 301 (S.D.N.Y. 1998), aff'd Lippe v. Bairnco Corp., 99 Fed. Appx. 274 (2d Cir. 2004) (trustee had no standing to assert claim against third party professionals for aiding and abetting corporation-debtor in scheme to defraud the company's creditors because claim "'belong[s] to the creditors qua creditors' . . . and cannot be asserted by the Company, its trustee in bankruptcy, a committee of unsecured creditors, or anyone else standing in the shoes of the debtor corporation." (citation omitted)); Glinka v. Murad (In re Housecraft Inds. USA, Inc.), 310 F.3d 64 (2d Cir. 2002) (held, secured creditor had standing in Chapter 7 case to join with trustee in bringing fraudulent transfer suit on behalf of estate; holding based on "best interests of estate"

precedent); Official Creditors' Comm. of Unsecured Creditors Of Cybergeneics Corp. v. Chinery, 330 F.3d 548 (3d Cir. 2003) (en banc) (7-4 decision) (held, chapter 11 creditors' committee had standing and could be authorized by court to pursue fraudulent transfer action when debtor failed to act), vacating and reversing 304 F.3d 316 (3d Cir. 2002); In re Smart World Technologies, LLC, 423 F.3d 166, 176-77, 180 (recognizing derivative standing doctrine, but declining to extend derivative standing on facts of case in Fed. R. Bankr. P. 9019 context). But see In re AppliedTheory Corp., 493 F.3d 82, 86-87 (2d Cir. 2007) (held, creditors' committee lacked standing to pursue equitable subordination claim when chapter 11 trustee had previously investigated claim and concluded it lacked merit and would not benefit estate); United Phosphorus v. Fox (In re Donald Furman Fox), 305 B.R. 912 (10th Cir. BAP 2004) (declining to follow Cybergeneics; held, Bankruptcy Code does not allow creditors to bring derivative suits on behalf of bankruptcy estate, only trustee can bring fraudulent transfer suit); In re Baltimore Emergency Servs. II Corp., 432 F.3d 557, 561-63 (4th Cir. 2005) (held, creditors' committee and secured creditor lacked derivative standing to sue debtors' insider to prevent interference with chapter 11 case when debtors never consented to suit and bankruptcy court failed to find suit was in estate's best interest or necessary and beneficial to efficient resolution of bankruptcy case (citing In re Commodore Int'l, Ltd., 262 F.3d 96, 100 (2d Cir. 2001)). The Fourth Circuit declined to decide whether derivative standing was permitted, holding that if derivative standing were permissible at all, the parties seeking it must show "the consent of the debtor-in possession or trustee and that suit is (a) in the best interest of the bankruptcy estate, and (b) is necessary and beneficial to the fair and efficient resolution of the bankruptcy [case]." Id. at 560. See also Carey v. Ernst, 333 B.R. 666, 679-80 (S.D.N.Y. 2005) (held, bankruptcy court's denial of standing to creditor to sue for fraudulent transfers in chapter 13 case was not clearly erroneous because Second Circuit has not crafted exception to standing rule for chapter 13 creditors and creditor failed to show "extraordinary circumstances" to justify application of section 105 powers).

3. The Chapter 11 Debtor-in-Possession Does Not Own Fraudulent Transfer Claims. The Third Circuit has held that state law fraudulent transfer claims, that the chapter 11 debtor-in-possession may pursue qua trustee, Code §§ 544(b), 1107(a), had not been sold to a third party in a court-approved sale of all the debtor's assets. In re Cybergeneics Corp., 226 F.3d 237, 243-47 (3d Cir. 2000) ("[P]ower to avoid [fraudulent] transfers . . . is no more an asset of . . . debtor in possession than it would be a personal asset of a trustee, had one been appointed in this case. Much like a public official has certain powers upon taking office as a means to carry out the functions bestowed by virtue of the office or public trust, the debtor in possession is similarly endowed to bring certain claims on behalf of, and for the benefit of, all creditors."). The Ninth Circuit, however has held that a trustee's avoidance powers were "transferable" to a creditor who purchased the estate's rights to certain sale proceeds if a creditor is pursuing interests common to all creditors . . ." Briggs v. Kent (In re Professional Inv. Properties of America), 955 F.2d 623, 626 (9th Cir. 1992); In re P.R.T.C., Inc., 177 F.3d 774, 782 (9th Cir. 1999) (trustee assigned to largest creditor avoidance power claims because estate lacked funds to pursue, but creditor required to remit to estate 50% of net proceeds if creditor pursued claims). See Par. 5 infra.

4. Avoidance By Post-Confirmation Creditor Representative. Section 1123(b)(3)(B) of the Code provides in relevant part that a reorganization plan may permit "the

retention and enforcement by the debtor, by the trustee, or by a representative of the estate appointed for such purpose, of any . . . claim or interest" belonging to the debtor or to the estate. According to the Tenth Circuit, "a party who is neither the debtor nor the trustee but who seeks to enforce a claim must establish two elements: (1) that it has been appointed; (2) that it is a representative of the estate." Retail Mktg. Co. v. King (In re Mako, Inc.), 985 F.2d 1052, 1054 (10th Cir. 1993), citing Citicorp Acceptance Co. v. Robison (In re Sweetwater), 884 F.2d 1323, 1334 (10th Cir. 1989); Zahn v. Yucaipa Capital Fund, 218 B.R. 656, 663, 665 (D.R.I. 1998) ("Pursuant to § 1123(b)(3)(B), a party, other than the debtor or the trustee, who seeks to prosecute avoidance claims must establish that: (1) it has been appointed; and (2) it is a representative of the estate"; distribution trustee had standing when bankruptcy court approved plan appointing him to bring claims and plan provides for the distribution of proceeds of a successful avoidance recovery to unsecured creditors). Appointment by the court "can be accomplished simply by approval of the plan." Mako, 985 F.2d at 1054. Moreover, "a successful recovery by the appointed representative [sh]ould benefit the debtor's estate and particularly the debtor's unsecured creditors." Id. As the Tenth Circuit explained, "post-petition avoidance actions should be pursued in a manner that will satisfy the basic bankruptcy purpose of treating all similarly situated creditors alike; one or more similarly situated creditors should not be able to pursue an avoidance action for their exclusive benefit." Sweetwater, 884 F.2d at 1328. Accord Briggs v. Kent (In re Professional Inv. Properties of America), 955 F.2d 623 (9th Cir. 1992); McFarland v. Leyh (In re Texas General Petroleum Corp.), 52 F.3d 1330, 1335 (5th Cir. 1995).

In Mako, the Tenth Circuit held that a non-debtor, non-trustee lacked clear standing under a reorganization plan to pursue post-confirmation avoidance actions. In affirming the lower court's granting of the defendant's motions for summary judgment dismissing the complaint, the court found that the provision of the reorganization plan "purporting to confer authority on [the non-debtor, non-trustee] to initiate avoidance actions after confirmation of the plan is vague." Mako, 985 F.2d at 1055. Because the plan had created a separate "litigation trustee" authorized to "act on behalf of all unsecured creditors," id., the court held that the third party lacked the requisite standing, reasoning as follows: "there must be clear evidence of the reservation of the avoidance powers [the third party] seeks to assert for it to have been appointed under the plan to exercise such powers." Id. The court found a judicial "presumption against reservation of avoidance powers without clear evidence," and emphasized that "post-confirmation avoidance proceedings [should be] for [the] benefit [of unsecured creditors,]" 985 F.2d at 1056, particularly when "as here, another person designated 'litigation trustee' has been appointed to act on behalf of the unsecured creditors." Id. Indeed, in Mako, the non-debtor, non-trustee was not "obligated in any way to distribute any proceeds realized from a successful prosecution of this avoidance action to the unsecured creditors of the estate," but was "seeking to recoup money it [had been] obligated to pay under § 1129(a)(1)(A)." Accord Harstad v. First American Bank (In re Harstad), 155 B.R. 500, 512 (Bankr. D. Minn. 1993) (when debtor brings "preference actions post-confirmation, [it] must specifically and unequivocally draft a plan provision notifying reasonable readers of the plan of their retention, [and]the recovery must be for the benefit of the estate and not the debtor"), aff'd, 39 F. 3d 898, 903, 905 (8th Cir. 1994). The reasoning of these cases is consistent with pre-Code law. See, e.g., Whiteford Plastics Co. v. Chase Nat'l Bank, 179 F.2d 582, 584 (2d Cir. 1950) (liens cannot be avoided under the Act when only the debtor will benefit).

5. Individual Debtor May Have Standing in Limited Cases. Code section 522(h) also confers upon an individual debtor the power to initiate a fraudulent transfer suit when the trustee does not do so and the property would have been exempt under section 522(g). Realty Portfolio, Inc. v. Hamilton (In re Hamilton), 125 F.3d 292, 297 (5th Cir. 1997) ("Section 522(h) specifically grants debtors standing to avoid certain involuntary transfers of exempt property, such as homesteads, if the trustees have not themselves attempted to avoid the transfers."); DeMarah v. United States (In re DeMarah), 62 F.3d 1248, 1250 (9th Cir. 1995) (applying a five-part test for section 522(h) exemption). Both the UFCA and the UFTA, in the non-bankruptcy context, recognize the fraudulent transfer action as an unpaid creditor's remedy.

F. Necessary Parties. Both the debtor/transferor and the transferee are necessary parties to a fraudulent transfer action. See General Motors Acceptance Corp. v. Key, No. IP 80-427-C (S.D. Ind. Jan. 28, 1981); Hamilton Nat'l Bank v. Halsted, 9 N.Y.S. 852 (App. Div. 1st Dept 1890), aff'd in relevant part, 134 N.Y. 520, 31 N.E. 900 (1892). But see Allan v. Moline Plow Co., 14 F.2d 912, 915 (8th Cir. 1926) (grantor held not to be indispensable party when he retains no legal or equitable interest in property conveyed); Etchegoyen v. Hamill (In re Farmer's Market), 22 B.R. 71, 75 (B.A.P. 9th Cir. 1982) (bank, which held alleged security interest in property fraudulently transferred by debtor's intermediary to new purchasers, was not indispensable party in fraudulent transfer action because buyers owed primary personal obligation to bank, and bank would not be harmed by fraudulent transfer determination); Moisters v. Waters (In re Waters), 8 B.R. 163 (Bankr. N.D. Ga. 1981) (debtor held not to be indispensable party because he no longer had interest in property transferred); Murray v. Murray, 358 So.2d 723, 725 (Miss. 1978) (grantee, but not grantor, necessary party to fraudulent transfer action). See Fed. R. Bankr. P. 7019.

G. Burden The trustee indisputably has the burden of proving transfers are fraudulent, and this burden never shifts to the transferee. Creditors' Committee of Jumer's Castle Lodge, Inc. v. Jumer, 472 F.3d 943, 948-9 (7th Cir. 2007) ("... the plaintiff ordinarily bears the burden of proving a fraudulent transfer."); Braunstein v. Walsh (In re Rowanoak Corp.), 344 F.3d 126 (1st Cir. 2003); Field v. United States (In re Abatement Env'tl. Res., Inc.), 102 Fed. Appx. 272 (4th Cir. 2004) (same). However, the burden of proof is not equivalent to the burden of going forward with the evidence. "Once the trustee establishes his prima facie case, he need not affirmatively disprove every other potential theory." Braunstein, 344 F.3d. at 131 (internal citations omitted). Accordingly, at that point, the burden of going forth with the evidence may shift to the transferee. See also In re Jackson, 459 F.3d 117 (1st Cir. 2006) (under New Hampshire's UFTA, burden of proof for actual intent is "clear, convincing and direct evidence"; burden of proof for constructive fraud is preponderance of the evidence).

H. Jurisdiction. Under 28 U.S.C. § 157(b)(2)(H), added by the Bankruptcy Amendments Act of 1984, proceedings to determine, avoid, or recover fraudulent transfers are "core proceedings" that may be heard and determined by bankruptcy judges, subject to appeal under 28 U.S.C. § 158. Teitelbaum v. Parameswaran (In re Parameswaran), 50 B.R. 780 (S.D.N.Y. 1985) (court has jurisdiction over action to set aside fraudulent transfer, pursuant to 28 U.S.C. § 157(b)(2)(H)); Blake v. Evans (In re Canion), 196 F.3d 579, 583 (5th Cir. 1999) ("fraudulent [transfer claims] are 'core' claims, 28 U.S.C. § 157(b)(2)(H) . . ."). Fraudulent

transfer suits that are based entirely on state law, made applicable under section 544(b) of the Code, are still "core proceedings" properly tried in the bankruptcy courts. Duck v. Munn (In re Mankin), 823 F.2d 1296 (9th Cir. 1987), cert. denied, 485 U.S. 1006 (1988); Epperson v. Entertainment Express, Inc., 242 F.3d 100, 107 (2d Cir. 2001) (judgment creditor's fraudulent transfer claims against judgment debtor's assets are within the scope of district court's jurisdiction since the claims did not seek to hold the purported transferees liable for the existing judgment, but rather sought to void allegedly fraudulent transfer to ensure collectability of the default judgment).

A bankruptcy court's authority to avoid payment obligations may be limited however when that avoidance interferes with certain regulatory functions of the government. In Federal Communications Comm'n v. Nextwave Personal Communications, Inc. (In re Nextwave Personal Communications, Inc.), 200 F.3d 43 (2d Cir. 1999), the court held that the lower courts lacked authority to avoid payment obligations of \$3.7 billion to the Federal Communications Commission under section 544 because such an avoidance would interfere with the FCC's system for allocating radio spectrum licenses and would interfere with the FCC's capacity as a regulator.

I. Type Of Proceeding. Fraudulent transfer actions are adversary proceedings pursuant to Fed. R. Banker P. 7001. See Havoco of America, Ltd. v. Hill, 197 F.3d 1135 (11th Cir. 1999) (challenge to exemption claimed by chapter 7 debtor on property he owned with wife as tenancy in entirety could not be challenged as a fraudulent transfer unless adversary proceeding commenced with wife joined as defendant); In re Gandy, 299 F.3d 489 (5th Cir. 2002) (held, fraudulent transfer complaint by chapter 11 debtor-in-possession need not be sent to arbitration despite existence of mandatory arbitration clause; bankruptcy court "had discretion to assess whether arbitration will be consistent with the Bankruptcy Code, [and had] not abused its discretion in denying ... the motions to compel arbitration"; and bankruptcy court may "decline to stay a proceeding [in favor of arbitration when the] underlying nature [of the action] derives exclusively from the provisions of the Bankruptcy Code.").

J. Type Of Trial. Historically, parties assumed that there was no right to a jury trial in a fraudulent transfer suit because the relief sought was supposedly equitable in nature. The Supreme Court of the United States, in Granfinanciera, S.A. v. Nordberg, 492 U.S. 33 (1989), rejected this view however, holding that the Seventh Amendment entitles a person, who has not submitted a claim against a debtor's estate, to a jury trial in a fraudulent transfer suit. When a bankruptcy trustee alleges an actual or constructively fraudulent transfer of monies, the defendant cannot be denied its Seventh Amendment right to a trial by jury so long as the defendant has not submitted a claim against the debtor's estate (the implication being that filing a claim may be an implied submission to the court's jurisdiction).

The right to a jury trial exists despite the statutory designation of fraudulent transfer actions as "core proceedings," triable by a bankruptcy judge sitting without a jury. 28 U.S.C. § 157(b)(2)(H). The Supreme Court ruled that although Congress may assign jurisdiction over claims asserting a "public" right, Congress lacks the power to strip parties asserting "private" rights of their constitutional right to a jury trial. Reasoning that fraudulent transfer suits are "quintessentially suits at common law that more nearly resemble state-law contract claims brought by a [debtor] corporation to augment the bankruptcy estate than they do creditors'

hierarchically ordered claims to a pro rata share of the bankruptcy res," the Court concluded that a bankruptcy trustee's right to recover a fraudulent transfer is more accurately characterized as a private rather than a public right. Granfinanciera, 492 U.S. at 56.

The Tenth Circuit extended the reach of Granfinanciera to require jury trials in fraudulent transfer actions even if the defendant had filed a proof of claim. Kaiser Steel Corp. v. Frates (In re Kaiser Steel Corp.), 911 F.2d 380 (10th Cir. 1990). The court reasoned that fraudulent transfer suits were plenary, and did not arise "as part of the process of allowance and disallowance of claims." (internal cites omitted) Id. at 389. Shortly thereafter, however, the Supreme Court reiterated its ruling that defendants who had filed proofs of claim were not entitled to a jury trial in a preference action, rejecting the "plenary" reasoning of the Tenth Circuit in Kaiser. Langenkamp v. Culp, 498 U.S. 42 (1990). The Court stated that "[i]f [after filing a proof of claim] the creditor is met, in turn, with a preference action . . . that action becomes part of the claims-allowance process which is triable only in equity." Id. at 331. See also Official Committee of Unsecured Creditors v. Schwartzman (In re Stansbury Poplar Place, Inc.), 13 F.3d 122 (4th Cir. 1993) (filing proof of claim in one case did not waive creditor's right to jury trial with respect to fraudulent transfer actions brought by jointly-administered debtor estates); Citicorp N. Am., Inc. v. Finley (In re Washington Mfg.), 133 B.R. 113, 117 (M.D. Tenn. 1991) (rejecting trustee's demand for jury trial on fraudulent transfer claim because defendant had filed proof of claim and avoidance action thereby became "equivalent to an objection to the creditor's claim"); In re Hechinger Inv. Co. of Del., 327 B.R. 537, 545-46 (D.Del. 2005) (held, fraudulent transfer action against pre-petition lenders not entitled to jury trial because "plaintiff's . . . fraudulent conveyance suit mirrors its objection to the [lenders'] claims. Consequently, plaintiff's fraudulent conveyance claims are part of the process of allowance and disallowance of claims . . ."). As a result, a creditor may be forced to choose between filing a timely proof of claim and preserving its right to a jury trial in a preference and fraudulent transfer action. First Fidelity Bank v. Hooker Invs. (In re Hooker Invs.), 937 F.2d 833, 837 (2d Cir. 1991) (creditor argued that order establishing bar date impermissibly abridged substantive rights by forcing creditor either to forego right to jury trial or distribution from the estate; held, lower court's decision against creditor unreviewable). See also Stainer v. Latimer (In re Latimer), 918 F.2d 136 (10th Cir. 1990), cert. denied, 502 U.S. 863 (1991) (defendants must request a jury trial and a transfer to district court; failure to request both results in waiver of right to jury trial); Committee of Unsecured Creditors v. 90th Street Garage Corp. (In re Term Industries, Inc.), 181 B.R. 31 (Bankr. S.D.N.Y. 1995), appeal dismissed as moot, No. 95-4658, 1995 WL 758608 (S.D.N.Y. Dec. 22, 1995) (action for avoidance of transfer and turnover of stock certificates transferred to affiliate was equitable action carrying no right to jury trial under Granfinanciera; alternatively, by asserting its own release in confirmed plan as defense, affiliate submitted itself to bankruptcy court's equitable jurisdiction and waived right to jury trial).

K. Appropriate Forum For Trial. In Granfinanciera, the Supreme Court specifically left open the question of whether bankruptcy courts may conduct jury trials in core proceedings. Granfinanciera, 492 U.S. at 59. The Supreme Court later declined to resolve a split in the circuit courts on this issue.

The Second Circuit has held that jury trials in core proceedings may be conducted by bankruptcy judges. Ben Cooper, Inc. v. Insurance Co. of Pa. (In re Ben Cooper, Inc.), 896

F.2d 1394 (2d Cir. 1990), vacated on jurisdictional grounds, 498 U.S. 964 (1990), reinstated, 924 F.2d 36 (2d Cir. 1991), cert. denied, 500 U.S. 928 (1991). The court reasoned that construing the Bankruptcy Code to allow jury trials in core proceedings is the only way to reconcile the requirements of the Seventh Amendment with Congress' intent in 28 U.S.C. § 157(b) to allow bankruptcy judges to conduct trials and issue final orders in core proceedings. *Id.* at 1402. More importantly, the court found no statutory or constitutional bars to a jury trial in the bankruptcy court. The court found that 28 U.S.C. § 1411, which preserves the right to a jury trial for personal injury and wrongful death tort claims, provided no guidance on the issue.

The Second Circuit further held that the Seventh Amendment's prohibition of reviewing jury findings other than in accordance with the common law would not be violated by the conduct of jury trials in core proceedings in the bankruptcy court because a district court's review of core proceedings is analogous to ordinary appellate review. *Id.* at 1403. The court also held that Article III of the Constitution would not be violated by jury trials in the bankruptcy court. Assuming that bankruptcy judges could enter final judgments in core proceedings without violating Article III, the court reasoned that jurors, who are less likely to be influenced by pressure from the executive and legislative branches, could also reach verdicts without violating Article III. *Id.* at 1403. The court assumed, without deciding, that 28 U.S.C. § 157(b) was constitutional.

Rejecting the Second Circuit's decision in Ben Cooper, the Eighth Circuit became the first of five circuit courts that subsequently held that bankruptcy judges may not conduct and preside over jury trials in core proceedings. In re United Missouri Bank of Kansas City, 901 F.2d 1449 (8th Cir. 1990). The court reviewed the history of federal bankruptcy law, and emphasized that the broad grant of authority in the Bankruptcy Reform Act of 1978, by which Congress probably intended to give bankruptcy judges the authority to conduct jury trials, was held unconstitutional in Northern Pipeline Constr. Co. v. Marathon Pipeline Co., 458 U.S. 50 (1982). The court held that the authority of bankruptcy judges is vested by Congress, and that absent a grant of express or implied authority, a bankruptcy judge may not conduct jury trials. In re United Missouri Bank of Kansas City, 901 F.2d at 1453, 1454. The court held that 28 U.S.C. § 157(b) did not give bankruptcy judges express authority to conduct jury trials. *Id.* at 1454. For authority to be implied, it must be "practically indispensable and essential in order to execute the power actually conferred." (citation omitted). *Id.* at 1456. The court found that the power to conduct jury trials was not necessary to carry out a bankruptcy judge's function to "hear and determine" and "enter appropriate orders and judgments" in core proceedings. *Id.* Because the court based its decision on a statutory analysis, it did not reach the constitutional issues. *Id.* at 1457. Accord Rafoth v. Nat'l Union Fire Ins. Co. (In re Baker & Getty Fin. Servs., Inc.), 954 F.2d 1169 (6th Cir. 1992).

The Tenth Circuit has also held that a bankruptcy judge may not conduct jury trials in core proceedings. Kaiser Steel Corp. v. Frates (In re Kaiser Steel Corp.), 911 F.2d 380 (10th Cir. 1990). The court specifically adopted the reasoning of the Eighth Circuit in United Missouri Bank. In particular, the court emphasized the repeal of 28 U.S.C. § 1481, which gave bankruptcy judges "the powers of a court of equity, law and admiralty," and the absence of any comparable provision in the 1984 Act. The Seventh Circuit followed the Tenth Circuit and held that a bankruptcy court cannot conduct a jury trial in a core proceeding because of the lack of

statutory authority or bankruptcy rule permitting the bankruptcy court to do so. In re Grabill Corp., 967 F.2d 1152 (7th Cir. 1992), reh'g denied, 976 F.2d 1126 (7th Cir. 1992). Accord Official Committee of Unsecured Creditors v. Schwartzman (In re Stansbury Poplar Place, Inc.), 13 F.3d 122 (4th Cir. 1993). The Supreme Court granted a writ of certiorari in the Ben Cooper case to resolve the conflict among the circuits. Insurance Co. of Pa. v. Ben Cooper, Inc., 497 U.S. 1023 (1990). Without reaching the merits, however, the Court vacated the judgment and remanded on jurisdictional grounds. Insurance Co. of Pa. v. Ben Cooper, Inc., 498 U.S. 964 (1990). On remand, the Second Circuit held that it had proper jurisdiction, and reinstated its prior judgment; the Supreme Court subsequently denied a writ of certiorari. Ben Cooper, Inc. v. Insurance Co. of Pa., 924 F.2d 36 (2d Cir. 1991), cert. denied, 500 U.S. 928 (1991).

The Bankruptcy Reform Act of 1994, Pub. L. 103-394, 108 Stat. 4106, effective October 22, 1994, permits jury trials in the bankruptcy court if the parties expressly consent and the district court specifically designates the "exercise of such jurisdiction," assuming that there is a "right to a jury trial" in the particular dispute. H.R. 5116, § 112, 103 Cong. 2d Sess., Cong. Rec. H10755 (daily ed. Oct. 4, 1994) (amending 28 U.S.C. § 157(e)). In view of these obstacles, jury trials in the bankruptcy court will, as a practical matter, be rare. But even when jury trials must be conducted by the district court, the bankruptcy court may retain jurisdiction over the action for pre-trial matters. In re HealthCentral.com, 504 F.3d 775, 787-88 (9th Cir. 2007) ("allowing the bankruptcy court to retain jurisdiction over pre-trial matters, does not abridge a party's Seventh Amendment right to a jury trial") (emphasis in original).

L. Statutes of Limitations

1. Statutory Reachback Periods. Under § 548(a), a trustee may attack a transfer as fraudulent in cases commenced before April 20, 2006 if the transfer was made within one year of the filing of the petition. The 2005 Amendments extend the § 548(a) one-year reachback period to two years for cases commenced on or after April 20, 2006. Under the UFCA or UFTA, available to the trustee by section 544(b), state statutes of limitations, which are generally longer, enable the trustee to avoid transfers not otherwise voidable under section 548. Buncher Co. v. Official Committee of Unsecured Creditors of Genfarm LP IV, 229 F.3d 245, 250-51 (3d Cir. 2000) ("When recovery is sought under section 544(b) . . . [t]he remedy . . . adopts the longer 'reach-back' provisions of state law."). See, e.g., Clear Creek, Inc. v. Royal Am. Corp. (In re International Resorts, Inc.), 46 B.R. 405 (N.D. Ala. 1984), aff'd mem., 751 F.2d 392 (11th Cir. 1984); Seligson v. New York Produce Exch., 378 F. Supp. 1076, 1106-07 (S.D.N.Y. 1974) (Act case applying New York law to give trustee six-year reachback); Hadley v. Acquafredda (In re Acquafredda), 26 B.R. 909, 911 (Bankr. M.D. Fla. 1983) (applying Florida law under section 544(b) because transfers made more than one year prior to bankruptcy); Roper v. City Nat'l Bank (In re Bethune), 18 B.R. 418, 419 (Bankr. N.D. Ala. 1982) (state ten-year statute of limitations was applicable in trustee's action under section 544(b) to recover fraudulent transfer). Additionally, UFTA § 9 contains a uniform statute of limitations: for fraudulent transfers other than transfers to insiders (discussed below), UFTA § 9(a) and (b) create a general four-year limitations period. See Campbell v. Carroll Indus., Inc. (In re Carroll Industries, Inc.), 153 B.R. 100 (Bankr. D. N.H. 1993) (UFTA statute of limitations applied retroactively). But see Fleet Nat'l Bank v. Valente (In re Valente), 360 F.3d 256, 261 (1st Cir. 2004) (held, four-year statute of limitations in UFTA § 9 does not prevent creditor from challenging fraudulent transfer

when applicable state law (resulting trusts) permits a fraud action), citing Macedo v. Bosio, 86 Cal. App. 4th 1044, 1051 (Cal. Ct. App. 2001). Finally, UFTA § 9(a) permits creditors to attack a transfer made with actual intent to hinder, delay or defraud creditors within one year after the transfer is or reasonably could be discovered by a defrauded creditor, if later than the general four-year limitations period. Judgment creditors have also been accorded state limitations periods when seeking to avoid fraudulent transfers. See Orr v. Kinderhill Corp., 991 F.2d 31 (2d Cir. 1993) (six-year New York statute of limitations for fraud applied to judgment creditor's action to avoid real estate mortgage; New York version of UFCA contains no statute of limitations).

M. Time For Bringing Suit. The 1994 Reform Act (§ 216), effective in "cases commenced under title 11" after October 21, 1994 (§ 702), and amending Code § 546(a)(1), provides that avoiding power suits (e.g., fraudulent transfer, preference actions) must be commenced by "the later of -- (A) 2 years after the entry of the order for relief; or (B) 1 year after the appointment or election of the first trustee" in a case "if such appointment or . . . election" occurs within two years of the commencement of the case. A bankruptcy court may, however, extend the filing deadline in certain cases. In re Int'l Admin. Servs., Inc., 408 F.3d 689, 699, 700-702 (11th Cir. 2005) (held, bankruptcy court has discretion to extend section 546(a)(1) filing period for suit under Rule 9006(b) of the Federal Rules of Bankruptcy Procedure and equitable tolling doctrine).

N. Time For Recovery Action. Under section 550(f), the trustee must commence any action to recover fraudulently transferred property from subsequent transferees within one year after avoidance of the transfer, or before the case is closed or dismissed, whichever is earlier. Cf. Beneficial Fin. Co. of Va. v. Franklin, 26 B.R. 636 (W.D. Va. 1983) (debtors barred from filing lien avoidance actions, after their cases were closed), vacated & remanded, 714 F.2d 127 (4th Cir. 1983). The UFCA contains no such time limitation, but a creditor is subject to any applicable state statute of limitations. See, e.g., N.Y. Civ. Prac. L. & R. 213 (McKinney 1990). If, however, the transferee has filed a proof of claim, the trustee may seek to disallow the claim under Section 502(d) even if the statute of limitations on the underlying fraudulent transfer claim has run. See El Paso City of Texas v. America West Airlines Inc. (In re America West Airlines), 217 F.3d 1161, 1167 (9th Cir. 2000) ("... § 502(d) may be used to disallow a claim even if the underlying avoidance action would be time barred.").

O. United States As Plaintiff. Whether the relevant state statute of limitations applies to the U.S. Government can depend on whether the particular state has adopted the UFCA or the UFTA. Compare United States v. Gleneagles Inv. Co., 565 F. Supp. 556 (M.D. Pa. 1983) (state statute of limitations not applicable to U.S. Government under UFCA), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, McLellan Realty Co. v. United States, 483 U.S. 1005 (1987); United States v. Wurdemann, 663 F.2d 50 (8th Cir. 1981) (state statute of limitations not applicable to U.S. Government seeking to recover fraudulent transfer); and United States v. Fernon, 640 F.2d 609 (5th Cir. 1981) (despite state law governing cause of action asserted by federal government, state statute of limitations not applicable to government suit to recover fraudulent transfer) with United States v. Vellalos, 780 F. Supp. 705 (D. Haw. 1992) (state statute of limitations barred U.S. Government from recovering alleged fraudulent transfer; UFTA commentary specifically rejected Gleneagles

holding and did not exempt federal government from state limitations period) abrogated in part by Bresson v. Commissioner of Internal Revenue, 213 F.3d 1173 (9th Cir. 2000). Freedom from state limitations periods has even been imputed to independent trustees when the trustee acts on behalf of all creditors and one of those creditors is the U.S. Government. See In re Hunt, 136 B.R. 437, 451 (Bankr. N.D. Tex. 1991) (avoidance actions by independent trustees not barred by state statute of limitations "since [the trustee] acquired the status of the United States pursuant to § 544(b) of the Code."), abrogated on other grounds by Compuadd Corp. v. Texas Instruments Inc. (In re Compuadd Corp.), 137 F.3d 880 (5th Cir. 1998).

P. Fair Consideration. Section 548 of the Code eliminates the "good faith" requirement in prior law for determining whether the transfer was made for fair consideration. As discussed below, the UFTA also eliminates the "good faith" requirement in its definition of "value" (section 3(a)), but that concept still plays a significant role in the proposed statutory scheme. The "good faith" requirement will remain, however, when the trustee uses section 544(b) in the five states where the UFCA is still in force. See IV.B., infra.

Q. The Court's Broad Power. A court has broad power to determine whether a fraudulent transfer occurred, including looking behind a consent judgment between a debtor and creditor. See Keating v. Spangler (In re XYZ Options), 154 F. 3d 1262, 1271 (11th Cir. 1998) (creditor not able to escape scrutiny with respect to fraudulent transfer merely because claim was reduced to judgment prior to bankruptcy when trustee was not a party and its interests were not represented; on remand, district court can "look behind judgment upon the appropriate showing of fraud and collusion."); Corzin v. Fordu (In re Fordu), 201 F.3d 693, 704 (6th Cir. 1999) (a marriage dissolution decree reciting that separation agreement was fair, just and equitable does not preclude bankruptcy court from finding that transfers effected under such agreement were voidable as fraudulent and preferential transfers because Bankruptcy Code requires "reasonably equivalent value.").

III. Actual Fraudulent Intent

A. The Statute. Section 548(a)⁸ of the Code provides:

(a)(1) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year⁹ before the date of the filing of the petition, if the debtor voluntarily or involuntarily—

(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. . . .

⁸ The Statute was amended in 1998 resulting in the renumbering of certain provisions of Section 548(a); certain cases cited herein refer to statutory section numbers before the amendment.

⁹ The 2005 Amendments to section 548(a) extend the reachback period to two years for cases commenced on or after April 20, 2006.

Section 7 of the UFCA, made applicable by section 544(b) of the Code, similarly provides that every conveyance made "with actual intent, as distinguished from intent presumed in law, to hinder, delay, or defraud either present or future creditors, is fraudulent as to both present and future creditors." In non-UFCA states, a trustee acting under section 544(b) will seek to apply the Statute of Elizabeth 13 (see I.E.1., supra). Whether a debtor actually intended to hinder, delay, or defraud his creditors by effecting a transfer is a question of fact to be determined by the circumstances of each case. Common indicia of fraudulent intent include: (1) actual or threatened litigation against the debtor; (2) the purported transfer of all or substantially all of the debtor's property, (3) insolvency or other unmanageable indebtedness on the part of the debtor, (4) a special relationship between the transferee and the debtor, and (5) retention by the debtor of property involved in a putative transfer with the debtor. Max Sugarman Funeral Home, Inc. v. A.D.B. Investors, 926 F.2d 1248, 1254 (1st Cir. 1991). See also Voest-Alpine Trading USA Corp. v. Vantage Steel Corp., 919 F.2d 206 (3d Cir. 1990) (actual intent found when debtor's assets were transferred for approximately half their value to new corporation controlled by debtor's shareholders, leaving debtor with no assets to satisfy its unsecured creditors); King v. Ionization Int'l, Inc., 825 F.2d 1180, 1186 (7th Cir. 1987) (debtor acts with actual intent when main purpose of transfer is to prevent lawful creditor from collecting a debt). Generally, "it is a question of fact whether a transfer was made with actual intent to defraud." Ed Peters Jewelry Co. v. C & J Jewelry Co., 124 F.3d 252, 261-62 (1st Cir. 1997). Actual intent to defraud must be proved by clear and convincing evidence. United States v. Gleneagles Inv. Co., 565 F. Supp. 556, 580 (M.D. Pa. 1983), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987); Glinka v. Bank of Vermont (In re Kelton Motors, Inc.), 130 B.R. 170 (Bankr. D. Vt. 1991) (applying state law standard of proof). The evidence must establish "a clear pattern of purposeful conduct." Pereira v. Checkmate Communications Co. (In re Checkmate Stereo & Elecs., Ltd.), 9 B.R. 585, 612-13 (Bankr. E.D.N.Y. 1981), aff'd, 21 B.R. 402 (E.D.N.Y. 1982); Bearden v. Baugh (In re Baugh), 60 B.R. 102, 105 (Bankr. E.D. Ark. 1986) ("[c]ircumstances must be so strong and well connected as to clearly show fraud"). But see Merrill v. Abbott (In re Independent Clearing House Co.), 77 B.R. 843, 860 (D. Utah 1987) (debtor that ran Ponzi scheme had actual intent to defraud future creditors as matter of law since no other reasonable inference was possible).

B. Badges Of Fraud. Because proving actual fraud is difficult, circumstantial evidence may be used: "the finding of the requisite intent may be predicated upon the concurrence of facts which, while not direct evidence of actual intent, lead to the irresistible conclusion that the transferor's conduct was motivated by such intent." 5 Collier on Bankruptcy, ¶ 548.04[2][a], at 548-23 to 548-24 (Lawrence P. King ed., 15th rev. ed. 1997). HBE Leasing Corp. v. Frank, 48 F.3d 623, 639 (2d Cir. 1995) (although judgment debtor's payments to attorneys for its codefendants in RICO action were not constructively fraudulent, case remanded to district court for factual inquiry as to actual fraudulent intent). See also Max Sugarman Funeral Home, Inc. v. A.D.B. Investors, 926 F.2d 1248, 1254 (1st Cir. 1991) ("The presence of a single badge of fraud may spur mere suspicion; the confluence of several can constitute conclusive evidence of an actual intent to defraud, absent 'significant clear' evidence of a legitimate supervening purpose."); Williamson v. Fireman's Fund Ins. Co., 828 F.2d 249, 252 (4th Cir. 1987) (fraudulent intent may be established by circumstantial evidence); Friedrich v. Mottaz (In re Friedrich), 294 F.3d 864 (7th Cir. 2002) (circumstantial evidence of fraudulent intent included transfer of \$400,000 to wife as gift when debtor owed over \$8 million in debts

and had five lawsuits pending against him); Teitelbaum v. Parameswaran (In re Parameswaran), 50 B.R. 780, 784 (S.D.N.Y. 1985) ("an inference of actual intent may be drawn from convincing evidence of extrinsic fraud"; a gratuitous transfer of valuable property gives rise to a presumption that the transaction was accompanied by actual fraudulent intent); Loftis v. Minar (In re Montanino), 15 B.R. 307, 312 (Bankr. D.N.J. 1981) ("the relationship of the parties together with all of the circumstances surrounding the transaction" may support a finding of actual intent notwithstanding lack of direct evidence of fraud). To prove actual intent, however, "[m]ere suspicion does not suffice." Glenmore Distilleries Co. v. Seideman, 267 F. Supp. 915, 919 (E.D.N.Y. 1967).

A number of "badges of fraud" have been employed by courts to determine whether actual intent to defraud exists: (1) a transfer of all the debtor's property; (2) retention of possession of property by the debtor, although title exists in another entity; (3) secrecy of the transfer; (4) existence of a trust between the debtor and the person to whom the property is conveyed; (5) transfer of the property while a suit against the debtor is pending; (6) the instrument effecting the transfer suspiciously states that the transfer is in fact bona fide; (7) consideration for the transfer is inadequate; and (8) the debtor makes a gift to a family member. See Twyne's Case, 3 Coke 80b, 76 Eng. Rep. 809 (Star Chamber 1601). See also Marc Rich & Co., A.G. v. United States (In re Grand Jury Subpoena Duces Tecum), 731 F.2d 1032, 1041 (2d Cir. 1984) (fraudulent nature of transfer may be inferred from relationship among parties and secrecy of sale; other "badges of fraud" include hasty, unusual transactions not in usual mode of doing business, and use of dummies or fictitious parties); Salomon v. Kaiser (In re Kaiser), 722 F.2d 1574, 1582-83 (2d Cir. 1983) (transfer of property by debtor to spouse while insolvent, and shifting of assets by debtor to corporation he controls, are badges of fraud); Continental Bank v. Modansky, 159 B.R. 129 (S.D.N.Y. 1993), aff'd, 41 F.3d 1501 (2d Cir. 1994) (when corporate guarantor transferred real estate to wife for unfair consideration while corporation was unable to pay debts as they came due, court held that timing and other circumstances of transfer warranted finding that transfer was made with actual intent to defraud creditors under N.Y. Debt. & Cred. L. § 276-a); ACLI Gov't Sec., Inc. v. Rhoades, 653 F. Supp. 1388, 1395 (S.D.N.Y. 1987) (transfer of real property from judgment debtor to his sister had "classic indicia of fraudulent intent": secret intrafamily transfer for inadequate consideration made nine days after jury verdict against judgment debtor), aff'd mem., 842 F.2d 1287 (2d Cir. 1988). United States v. Gleneagles Inv. Co., 565 F. Supp. 556, 580 (M.D. Pa. 1983) (when transferor and transferee have knowledge of creditors' claims and know creditors cannot be paid, and when consideration for transfer is lacking, court may infer intent to hinder, delay, or defraud creditors), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987); Hadar Leasing Int'l Co. v. D.H. Overmyer Telecasting Co. (In re D.H. Overmyer Telecasting Co.), 23 B.R. 823 (Bankr. N.D. Ohio 1982) (transfer by corporate debtor to other corporation when both entities were controlled by same individual constituted "badge of fraud"), aff'd, 53 B.R. 963 (N.D. Ohio 1984), aff'd, 787 F.2d 589 (6th Cir. 1986). Usually, more than one "badge of fraud" must be present to establish a pattern strong enough for a court to find actual intent. Kleinfeld v. Sun Land Properties, Inc. (In re Kranich), 53 B.R. 821, 823 (Bankr. M.D. Fla. 1985) (when badges of fraud "exist in combination, they 'may by their number and joint consideration be sufficient to constitute conclusive proof' of fraud") (citation omitted); Securities and Exchange Comm'n v. Whitworth Energy Resources Ltd., 26 Fed. Appx. 723, at *1 (9th Cir. Jan. 18, 2002) (badges of fraud included transfer to an insider (debtor's mother); threat of suit

when transfer occurred; son's retained control over property by mother's failure to record deed; transfer was concealed; and no reasonable equivalent value received (i.e., mother promised not to sue son)); Shelley v. Doe, 671 N.Y.S.2d 803, 806 (App. Div. 3d Dept 1998) (finding that enough indicia of fraud exist to warrant hearing on factual issues when the record shows "hurried, nonbusiness transfer between brothers, which must be scrutinized carefully, at a time when [the transferor brother] was under an indictment which would clearly expose him to criminal liability."). Once multiple badges of fraud have been established, the trustee is entitled to a presumption of fraudulent intent and the burden shifts to the transferee to prove some "legitimate supervening purpose" for the transfers at issue. Kelly v. Armstrong, 206 F.3d 794, 798 (8th Cir. 2000) (citations omitted); Village of San Jose v. McWilliams, 284 F.3d 785 (7th Cir. 2002) (debtors' attempts "to conceal, remove or destroy property cannot be later cured by remedial conduct, including undoing any transfers, if the [original] transfers occurred within one year of filing the bankruptcy petition."); In re Triple S Restaurants, Inc., 422 F.3d 405, 414-16 (6th Cir. 2005) (held, pre-petition transfer of life insurance policy from debtor to trust displayed several badges of fraud, shifting burden of proof to insurance policy beneficiary to show transfer did not harm debtor's unsecured creditors; "the burden of proof may shift even where consideration has not been shown to be inadequate").

UFTA § 4(a)(1), like UFCA § 7, provides that a transfer with actual intent to hinder, delay or defraud creditors is fraudulent as to both present and future creditors. Unlike the UFCA, however, the UFTA actually lists "badges of fraud." UFTA § 4(b) provides that a court may consider a nonexclusive list of eleven criteria, including the traditional "badges of fraud," such as a transfer to an insider (which includes, under UFTA § 1(7)(i)(A), a relative of the debtor or of a general partner of the debtor). The UFTA does not specifically weigh the indicia enumerated, but prior case law should apply. Comment (5) to UFTA § 4 states that the presence of one or more of the enumerated factors is evidence relevant to the debtor's intent, but does not create a presumption that a fraudulent transfer was made.

C. Elements Of Actual Intent. The elements of actual intent set forth in the statute ("hinder, delay, or defraud") are meant to be read disjunctively. Actual intent to defraud will be held to exist even if the debtor's purpose is not to deprive creditors of ultimate payment, but merely to hinder or delay creditors so as to obtain time to restore his affairs. Harman v. First American Bank of Md. (In re Jeffrey Bigelow Design Group, Inc.), 956 F.2d 479, 484 (4th Cir. 1992) (regardless of court's ability "to infer actual fraudulent intent from the presence of 'badges of fraud' . . . actual fraudulent intent requires a subjective evaluation of the debtor's motive . . . [A]n objective determination has bearing on whether constructive fraudulent intent exists, but is not conclusive for actual fraudulent intent.") (emphasis added); Shapiro v. Wilgus, 287 U.S. 348, 353-56 (1932) (individual debtor transferred all assets to newly-formed corporation in exchange for assumption of all debts in response to creditor's threat of suit; federal equity receivership commenced shortly after transfer because of debtor's admitted objective to protect assets from suit so as to obtain time to repay all creditors; held, receivership part of "scheme" to hinder or delay creditors); Consove v. Cohen (In re Roco Corp.), 701 F.2d 978, 984 (1st Cir. 1983) ("[f]raudulent intent does not require an intent to run the company aground; it requires merely an intent to hinder or defraud creditors."); Flushing Savings Bank v. Parr, 81 A.D.2d 655, 656, 438 N.Y.S.2d 374, 376 (App. Div. 2d Dept), appeal dismissed, 54 N.Y.2d 770 (1981) (citing Shapiro, court held that "hinder" and "delay" are in the disjunctive, and "exist independently of an intent

to defraud"; corporate debtor transferred major asset to controlling shareholder after corporate reorganization petition dismissed; transfer admittedly made "to preserve [property] from foreclosure for all its unsecured creditors . . ."). But see Stratton v. Sioux Falls Paint & Glass (In re Stratton), 23 B.R. 284 (D.S.D. 1982) (mere attempt to delay creditor, without fraudulent motive, does not make debtor's transfer of second mortgage to creditor fraudulent under § 548(a)(1)). See also Klein v. Klein (In re Klein), Nos. 88B-19937, 88A-357, 1991 WL 242169, at *7 (Bankr. N.D. Ill. June 21, 1991) (to void transfer that was made with intent to hinder or delay, but not to defraud, there must be "hindrance or delay greater than that implicit in a preferential transfer to certain creditors by an insolvent debtor.").

D. Proof Of Insolvency And Fair Consideration Not Material. Proof of insolvency is not material to a determination of actual intent to defraud. United States v. Green, 201 F.3d 251 (3d Cir. 2000) (applying Pennsylvania law; "[e]vidence of solvency was not a barrier to applying the presumption of actual fraud."). Similarly, fair consideration is not a material factor. See Pashaian v. Eccelston Properties, Ltd., 88 F.3d 77, 86 (2d Cir. 1996) (quoting Grumman Aerospace Corp. v. Rice, 199 A.D.2d 365, 366 (2d Dept 1993)) (applying New York law; when transfer is made with actual intent to defraud, transfer may be found fraudulent "even where fair consideration was paid and the debtor remains solvent."); Bullard v. Aluminum Co. of Am., 468 F.2d 11 (7th Cir. 1972) (transfer lacking good faith is fraudulent even though fair equivalent may have been given). Those factors may be relevant, however, in proving actual intent. See Hunter v. Society Bank & Trust (In re Parker Steel Co.), 149 B.R. 834, 855 (Bankr. N.D. Ohio 1992) (debtor's insolvency at time of loan repayment combined with release of principals' guarantee constituted actual fraud); Society of Lloyd's v. Collins, 284 F.3d 727, 730 (7th Cir. 2002) (fraudulent intent presumed without regard to actual intent when an insolvent debtor buys insurance policies with the intent of converting nonexempt property into exempt property, or in fraud of creditors); Warfield v. Byron, 436 F.3d 551, 558 (5th Cir. 2006) (held, receiver satisfied burden of showing fraudulent intent with evidence that transferor had created Ponzi scheme, and was "as a matter of law, insolvent from its inception" (citing Cunningham v. Brown, 265 U.S. 1 (1924))).

E. Denial Of Individual Debtor Discharge. Proof of actual intent to defraud creditors under section 548(a)(1)(A) may be the basis for denial of an individual debtor's discharge in a chapter 7 liquidation case under section 727(a)(2)(A). See e.g., In re Kontrick, 295 F.3d 724 (7th Cir. 2002) (debtor's discharge denied when he deposited paycheck into account over which he had no control). The debtor's discharge may be denied even if the debtor subsequently retrieves the fraudulently transferred property. Martin v. Bajgar (In re Bajgar), 104 F.3d 495, 497 (1st Cir. 1997) ("retransfer subsequent to filing a voluntary bankruptcy petition does not cure the fraudulent transfer, and, thus, does not avail the debtor discharge under Section 727."); Davis v. Davis (In re Davis), 911 F.2d 560 (11th Cir. 1990) (debtor denied discharge under section 727(a)(2)(A) despite recovering fraudulently transferred property upon advice of lawyer prior to bankruptcy); Salomon v. Kaiser (In re Kaiser), 722 F.2d 1574, 1582-83 (2d Cir. 1983) (debtor may not exploit homestead exemption to effectuate a fraud); Dean Witter Reynolds, Inc. v. MacQuown (In re MacQuown), 717 F.2d 859, 863 (3d Cir. 1983) (gratuitous transfer of house, and continued residence there after transfer, raised presumption of fraudulent intent necessary to bar discharge). See Smiley v. First Nat'l Bank of Belleville (In re Smiley), 864 F.2d 562, 567-68 (7th Cir. 1989) (whether debtor's transfer of nonexempt property to acquire

exempt Kansas homestead property was effected with intent to hinder, delay or defraud so as to warrant denial of discharge, fact that debtor (i) stood to gain large amount of money from his creditors if homestead exemptions were upheld, (ii) had knowledge of Kansas exemption law, and (iii) failed to volunteer information to creditors, was irrelevant; instead, court looked for extrinsic signs of fraud--e.g., debtor obtained credit in order to purchase exempt property; transfer occurred after entry of large judgment against debtor; debtor's conduct prior to bankruptcy evidenced pattern of sharp dealing; or debtor rendered insolvent by transfer); Norwest Bank Nebraska, N.A. v. Tveten, 848 F.2d 871, 874 (8th Cir. 1988) (in context of application for chapter 11 discharge, "absent extrinsic evidence of fraud, mere conversion of non-exempt property to exempt property is not fraudulent as to creditors even if the motivation behind the conversion is to place those assets beyond the reach of creditors.") (citations omitted); Devers v. Bank of Sheridan (In re Devers), 759 F.2d 751 (9th Cir. 1985) (in context of concealment of assets under 11 U.S.C. § 727(a)(2), fraudulent intent may be inferred from course of conduct); Bank of Pennsylvania v. Adlman (In re Adlman), 541 F.2d 999, 1003-04 (2d Cir. 1976) (with respect to denial of discharge, actual intent must be proved by extrinsic evidence; mere fact of transfer is not enough). A transfer of property made with actual intent to defraud creditors cannot be the basis for denial of a discharge under section 727 unless the property "remained transferred" up to and including the time the bankruptcy petition was filed. First Beverly Bank v. Adeeb (In re Adeeb), 787 F.2d 1339, 1345 (9th Cir. 1986) (denial of discharge under section 727(a)(2)(A) is construed liberally in favor of debtor and strictly against those objecting to discharge; debtor who transfers property within one year of bankruptcy with actual fraudulent intent may not be denied discharge "if he reveals the transfers to his creditors, recovers substantially all of the property before he files his bankruptcy petition, and is otherwise qualified for a discharge."). But see In re Davis, 911 F.2d at 562 (debtor denied discharge for fraudulent transfer of property recovered by debtor prior to filing).

F. Transferee's Intent Imputed To Debtor. When the debtor's transferee is in a position to dominate or control the debtor's disposition of property (e.g., when the transferee is a corporate officer), the transferee's intent to hinder, delay, or defraud creditors may be imputed to the debtor. The Personal and Bus. Ins. Agency v. PFS (In re The Personal and Bus. Ins. Agency), 334 F.3d 239, 247 (3d Cir. 2003) (sole owner of company commits fraud that is imputed to debtor; trustee appointed post-bankruptcy sought to avoid transfer by owner; held, owner's "conduct would not be imputed to the Trustee because it would lead to an inequitable result . . . Trustee had no 'antecedent debt,' and consequently no value was received for the payment made by [debtor] to PFS.").

G. Repo Participants. Under section 546(f), added by the Bankruptcy Amendments Act of 1984, section 548(a)(1)(A) is the only permissible basis for avoiding a transfer that is a margin payment (as defined in sections 741(5) and 761(15)) or a settlement payment (as defined in section 741(8)) made to or by a repo participant (as defined by section 101(46)) or financial participant (as defined in section 101(22A)) in connection with a repurchase agreement (as defined by section 101(47)).¹⁰ Thus, state fraudulent transfer law is not applicable to such payments, nor are the Code's provisions for avoidance based on

¹⁰ The 2005 Amendments applied section 546(f) to payments made by or to financial participants. This amendment applies to cases commenced on or after October 17, 2005.

constructively fraudulent intent. See Kaiser Steel Corp. v. Pearl Brewing Co. (In re Kaiser Steel Corp.), 952 F.2d 1230 (10th Cir. 1991) (settlement payment held not voidable as fraudulent transfer per § 546(e)), cert. denied, 505 U.S. 1213 (1991). See generally Bevill, Bresler & Schulman Asset Management Corp. v. Spencer Sav. & Loan Ass'n, 878 F.2d 742 (3d Cir. 1989) (section 546(f) bars chapter 11 trustee from avoiding as preferential a transfer of securities constituting "settlement payment" to repo participant).

H. Swap Participants. Under section 546(g), added by the 1990 Amendments to the Code, section 548(a)(1)(A) is the only permissible basis for avoiding a transfer under a swap agreement (as defined in section 101(53B)) made by or to a swap participant (as defined in section 101(53C)) or financial participant (as defined in section 101(22A)) in connection with a swap agreement.¹¹

IV. Constructively Fraudulent Intent

A. Types Of Constructively Fraudulent Transfers. A transfer of an interest in property or incurrence of debt may be deemed constructively fraudulent under the Code if such transfer or incurrence is for less than reasonably equivalent value and is made or incurred at a time when (1) the debtor is insolvent or as a result of which the debtor becomes insolvent [section 548(a)(1)(B)(ii)(I)]; (2) the debtor is engaged in business and will have unreasonably small capital to conduct its business after the transfer is made or obligation is incurred [section 548(a)(1)(B)(ii)(II)]; or (3) the debtor is about to incur debts beyond his ability to pay as they mature [section 548(a)(1)(B)(ii)(III)]. Effective for cases commenced on or after April 20, 2005, the 2005 Amendments also enable the trustee to avoid an insider transfer pursuant to an employment contract if the transfer was made outside the ordinary course of business and the debtor received less than reasonably equivalent value. This avoidance power does not require proof of insolvency [section 548(a)(1)(B)(ii)(IV)].

B. Reasonably Equivalent Value. To describe the adequacy of the property exchanged in the fraudulent transfer context, section 548 of the Code replaces the old Bankruptcy Act's "fair consideration," a term which derives from and is still employed by the UFCA, with the term "reasonably equivalent value." The significant difference between the two standards is that the latter eliminates the requirement of good faith. As defined in section 548(d)(2)(A), "'value' means property, or satisfaction or securing of a present or antecedent debt of the debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor."

When a transfer is attacked under state law, made available by section 544(b) of the Code, the applicable standard will revert to that of "fair consideration" in UFCA states such as New York (N.Y. Debt. & Cred. L. §§ 272-275 (McKinney 1945 & Supp. 1990)) or the "reasonably equivalent value" criterion in states governed by the UFTA. Under § 3 of the UFCA, "fair consideration" is given for property or an obligation:

¹¹ The 2005 Amendments applied section 546(g) to payments made by or to financial participants. This amendment applies to cases commenced on or after October 17, 2005.

- (a) When in exchange for such property, or obligation, as a fair equivalent therefor, and in good faith, property is conveyed or an antecedent debt is satisfied, or
- (b) When such property, or obligation is received in good faith to secure a present advance or antecedent debt in amount not disproportionately small as compared with the value of the property, or obligation obtained.

Only that portion of the value either directly or indirectly received by the transferor is included for purposes of determining whether fair consideration was received for the transfer. HBE Leasing Corp. v. Frank, 48 F.3d 623, 638-39 (2d Cir. 1995) ("to determine whether a debtor indirectly received fair consideration . . . the fact-finder must first attempt to measure the economic benefit that the debtor indirectly received from the entire transaction, and then compare that benefit to the value of the property the debtor transferred . . . The mere fact the debtor received a benefit is therefore insufficient to find fair consideration."). Rodino v. Barondess (In re Good Time Charley's, Inc.), 54 B.R. 157, 161 (Bankr. D.N.J. 1984) ("Any benefit to a third party is not factored into the fair consideration equation."); see, e.g., Securities and Exchange Commission v. Res. Dev. Int'l, LLC, 487 F.3d 295, 301 (5th Cir. 2007) (corporation paid legal fees on behalf of Ponzi scheme organizer; held, corporation did not receive reasonably equivalent value for transfer because corporation's net worth was diminished and creditors received no benefit from legal fees); Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 153-54 (3d Cir. 1996) ("while the chance of receiving an economic benefit is sufficient to constitute 'value,' the size of the chance is directly correlated with the amount of 'value' conferred"; debtor failed to receive reasonably equivalent value when it expended \$390,000 in commitment fees for loan that had little chance of closing); but see VFB, LLC v. Campbell Soup Co., 482 F.3d 624, 631-34 (3d Cir. 2007) (held, debtor's \$500 million payment for stock purchase constituted reasonably equivalent value because of \$1.1 billion market capitalization of acquired businesses); Creditors' Committee of Jumer's Castle Lodge, Inc. v. Jumer, 472 F.3d 943, 947 (7th Cir. 2007) (held, account receivable obtained by debtor's principal shareholder not worth full book value; debtor "received over \$5 million and gave up around \$4 million. . . ."; "reasonably equivalent value" received by debtor); Redwood Raevine Corp. v. Hayes (In re Hannover Corp.), 310 F.3d 796, 802 (5th Cir. 2002), cert. denied Hays v. Jimmy Swaggart Ministries 128 S. Ct. 2075 (2003) (options to purchase property had value even if party was ultimately unable to exercise them because "for purposes of § 548 the value of an investment, even a risky one . . . is to be determined at the time of purchase."). See generally, Cook & Gelber, "Fraudulent Transfer Analysis Turns Sour," The Bankruptcy Strategist, at 1 (June, 2007).

The "good faith" requirement has generally been interpreted to mean that the transferee must pay a fair equivalent and take in good faith. Cohen v. Sutherland, 257 F.2d 737, 742 (2d Cir. 1958); Bearden v. Baugh (In re Baugh), 60 B.R. 102 (Bankr. E.D. Ark. 1986) (transfer of money from son to father, which rendered son insolvent and removed money from reach of son's creditors, yet still permitted son use of money, was fraudulent for lack of good faith). See also Hayes v. Palm Seedlings Partners-A (In re Agricultural Research and

Technology Group, Inc.), 916 F.2d 528, 539 (9th Cir. 1990) (defendant who actively took part in Ponzi scheme lacked good faith). "Good faith" will be found to exist when:

- (a) The transfer resulted from an arm's length bargain, free of insider manipulation. Bullard v. Aluminum Co. of Am., 468 F.2d 11, 13 (7th Cir. 1972).
- (b) The transferee had no knowledge of insolvency or fraudulent intent on the part of the transferor. United States v. Tabor Court Realty Corp., 803 F.2d 1288, 1296 (3d Cir. 1986) cert. denied, 483 U.S. 1005 (1987); Cohen v. Sutherland, 257 F.2d at 742-43.
- (c) The transferee did not knowingly participate in the transferor's purpose to defeat other creditors, nor lack good faith in valuing the property transferred. Gilmer v. Woodson (In re Decker), 332 F.2d 541, 547 (4th Cir. 1964), cert. denied, 379 U.S. 834 (1964); and even when
- (d) Good faith has been found to exist even when the transferee had actual or constructive notice of any fraudulent scheme – in other words, even "when the transferee knows that the funds transferred were fraudulently acquired." Sharp Int'l Corp. v. State Street Bank & Trust Co. (In re Sharp Int'l Corp. & Sharp Sales Corp.), 403 F.3d. 43, 54 (2d Cir. 2005) ("[g]ood faith is an elusive concept in New York's constructive fraud statute Bad faith does not appear to be an articulable exception to the broad principle that 'the satisfaction of a preexisting debt qualifies as fair consideration for a transfer of property' [citing cases]. . . . [The bank's] knowledge of the [management] fraud, without more, does not allow the inference that [the bank] received the \$12.25 million payment in bad faith.").

See generally Note, Good Faith And Fraudulent Conveyances, 97 Harv. L. Rev. 495 (1983).

As with the constructive fraud sections of the Code, each of the UFCA's constructive fraud sections (sections 4-6) requires two elements: that the transfer be made for less than fair consideration and that an underlying condition posited by each section exist--i.e., insolvency (section 4), undercapitalization (section 5), or anticipation of incurring debts beyond the debtor's capacity to repay them (section 6).

The "concept of reasonably equivalent value unfortunately has not been defined in the Code. . . . 'Congress left to the courts the obligation of marking the scope and meaning of [reasonably equivalent value].'" Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 148 (3d Cir. 1996) (alterations in original) (citations omitted). Any test for reasonably equivalent value under section 548 of the Code will

necessarily encompass many of the same elements found in prior case law. Whether reasonably equivalent value has been given for a transfer of property is a question of fact. Barber v. Golden Seed Co., 129 F.3d 382, 387 (7th Cir. 1997) ("[T]he formula for determining reasonably equivalent value is not a fixed mathematical formula; rather, the standard for '[r]easonable equivalence should depend on all the facts of each case. . . ." (alteration in original); Texas Truck Ins. Agency, Inc. v. Cure (In re Dunham), 110 F.3d 286, 288-89 (5th Cir. 1997) (held, clearly erroneous standard is a proper standard to review reasonably equivalent value determination); Gaudet v. Babin (In re Zedda), 103 F.3d 1195, 1206 (5th Cir. 1997) ("Whether a transfer is made for a reasonably equivalent value is, in every case, largely a question of fact."); Nordberg v. Arab Banking Corp. (In re Chase & Sanborn Corp.), 904 F.2d 588, 593 (11th Cir. 1990); Jacoway v. Anderson (In re Ozark Restaurant Equip. Co.), 850 F.2d 342, 344 (8th Cir. 1988); Gray v. Snyder, 704 F.2d 709 (4th Cir. 1983); Consove v. Cohen (In re Roco Corp.), 701 F.2d 978, 981 (1st Cir. 1983); Klein v. Tabatchnick, 610 F.2d 1043, 1047 (2d Cir. 1979); Halsey v. Winant, 258 N.Y. 512, 523, 180 N.E. 253, cert. denied, 287 U.S. 620 (1932). Cf. Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 147 (3d Cir. 1996) (whether debtor "was insolvent or received 'less than fair consideration' are mixed questions of law and fact").

The trustee bears the burden of proving lack of reasonably equivalent value under § 548. Barber v. Golden Seed Co., 129 F.3d 382, 387 (7th Cir. 1997). Important elements of determining equivalence include fair market value and "whether the sale was 'an arm's length transaction between a willing buyer and a willing seller.'" Barber v. Golden Seed Co., 129 F.3d 382, 387 (7th Cir. 1997) (quoting In re Bundles, 856 F.2d 815, 824 (7th Cir. 1988)).

1. "Reasonably equivalent value" is the price in fact received for the property at the foreclosure sale, so long as that sale satisfied all the requirements of state foreclosure law. BFP v. Resolution Trust Corp., 511 U.S. 531 (1994); Lindsay v. Beneficial Reinsurance Co. (In re Lindsay), 59 F.3d 942, 948 (9th Cir. 1995) ("Gross inadequacy of price is a ground for setting aside the foreclosure, under BFP, if state law so provides, but it is not a federal standard independent of state law enabling a bankruptcy court to set aside a foreclosure sale. Likewise, commercial reasonableness is a ground only if it is a state ground."); cf. Kojima v. Grandote Int'l. LLC (In re Grandote Country Club Co. Ltd.), 252 F.3d 1146, 1152 (10th Cir. 2001) (tax sale upheld) ("Although BFP did not address a tax sale . . . BFP has been extended to the tax sale context. . . . [T]he decisive factor in determining whether a transfer pursuant to a tax sale constitutes "reasonable equivalent value" is a state's procedure for tax sales, in particular, statutes requiring that tax sales take place publicly under a competitive bidding procedure."). See Federal Communications Comm'n v. Nextwave Personal Communications, Inc. (In re Nextwave Personal Communications, Inc.), 200 F.3d 43, 58 (2d Cir. 1999), cert. denied, 121 S. Ct. 298 (2000) ("[P]rinciples of auction law . . . confirm and reinforce the rationality of the FCC's interpretation of its regulations. . . . [Debtor] became liable [at the close of auction] for full payment on the Licenses at the stated price."). But see In re GW1 PCS 1, Inc., 230 F.3d 788, 808-10 (5th Cir. 2000), cert. denied 533 U.S. 964 (2001) (disagreeing with Nextwave because of special rules of FCC auction).

Prior to the Supreme Court's ruling in BFP, at least two approaches were used to determine "reasonably equivalent value." Barrett v. Commonwealth Federal Savings & Loan

Assoc., 939 F.2d 20 (3d Cir. 1991); Cooper v. Ashley Communications, Inc. (In re Morris Communications NC, Inc.), 914 F.2d 458, 466 (4th Cir. 1990). One is the "mathematical approach." Durrett v. Washington Nat'l Ins. Co., 621 F.2d 201 (5th Cir. 1980) (in dicta, court held that less than 70% of fair market value is not reasonably equivalent value). The other, more meaningful approach, considers the facts of each case. Bundles v. Baker, 856 F.2d 815 (7th Cir. 1988) (facts considered: fair appraisal of property; range of advertisements; and competitiveness of bids). The Barrett court applied the reasoning of Bundles and refused to set aside a foreclosure sale from which the debtor received approximately 69.5% of the property's fair market value. The court further held that the sale should be compared to a typical "foreclosure" sale and not a "private" sale.

The Eleventh Circuit also abandoned Durrett on the ground that Durrett ignored relevant factors, and held that the court must "conduct a thorough inquiry of all relevant facts and circumstances." Harman v. First American Bank of Md. (In re Jeffrey Bigelow Design Group, Inc.), 956 F.2d 479 (4th Cir. 1992) (reasonably equivalent value determined from standpoint of creditors; court must determine net effect on debtor's estate regarding funds available to unsecured creditors; if unsecured creditors are no worse off, then there is reasonably equivalent value); Zentek GBV Fund IV, LLC v. Vesper, 19 Fed. Appx. 238 (6th Cir. 2001) (note to acquire subsidiary's assets, which provided that note would be forgiven if subsidiary became insolvent, was fraudulent transfer since some claims of unsecured creditors were not paid in full).

2. Subsequent to BFP v. Resolution Trust Corp., 511 U.S. 531 (1994), courts still inquire into the facts of each case. See, e.g., Barber v. Golden Seed Co., 129 F.3d 382, 387 (7th Cir. 1997) (standard for "[r]easonable equivalence should depend on all the facts of each case"; important elements are fair market value and whether there was an arm's length transaction), quoting Bundles v. Baker (In re Bundles), 856 F.2d 815, 824 (7th Cir. 1988).

3. Consideration sufficient to support an ordinary contract, i.e., "good" consideration, will not necessarily be "fair" consideration or constitute reasonably equivalent value for purposes of section 548. Cohen v. Sutherland, 257 F.2d at 742. HBE Leasing Corp. v. Frank, 61 F.3d 1054, 1060 (2d Cir. 1995) ("contingent property interests relinquished" by fiancé in prenuptial agreement with judgment debtor held not to constitute 'fair consideration' under fraudulent transfer law).

4. Value given on account of an antecedent debt is usually considered reasonably equivalent value. 11 U.S.C. § 548(d)(2)(A) ("value' means . . . satisfaction or securing of a present or antecedent debt . . ."); In re First Alliance Mortg. Co., 471 F.3d 977, 1008-09 (9th Cir. 2006) (held, repayments of fully secured obligation, resulting in equivalent reduction in debtor's liability, "do not hinder, delay or defraud creditors because . . . transfers do not put assets . . . out of their reach"); Meyer v. Meyer (In re Meyer), 244 F.3d 352 (4th Cir. 2001), cert. denied Shaia v. Meyer 534 U.S. 893 (2001)(creditor's release of mortgage against debtor's property is valuable consideration); Strongin v. Int'l Acceptance Bank, 70 F.2d 248, 252 (2d Cir. 1934), cert. denied, 293 U.S. 575 (1934); Lisle v. John Wiley & Sons, Inc. (In re Wilkinson), 196 Fed.Appx. 337, 343 (6th Cir. 2006) (unpublished decision) (debtor's payment to a third party on behalf of creditor in exchange for a dollar-for-dollar reduction in creditor's debt considered "reasonably equivalent value"). Under New York law, however, payment of an antecedent debt does not constitute fair consideration if the transferee is an officer, director or

major shareholder of the transferor. Pashaian v. Eccelston Properties, Ltd., 88 F.3d 77, 86 (2d Cir. 1996) (citations omitted). Moreover, a debtor only receives value for a transfer to a creditor if the transfer satisfies part or all of the transferee-creditor's claim against the debtor. See, e.g., Jobin v. McKay (In re M & L Business Machine Co.), 84 F.3d 1330, 1341 (10th Cir. 1996), cert. denied, 117 S. Ct. 608 (1996) (investor in chapter 7 debtor's Ponzi scheme with no actual knowledge of fraud had colorable claim for restitution of investment under Colorado law; debtor therefore received reasonably equivalent value, in form of reduction of restitution claim, for payments it made to investor, and payments could not be avoided by trustee as fraudulent transfer for less than reasonably equivalent value); Sender v. Buchanan (In re Hedged-Investments Assoc.), 84 F.3d 1286, 1290 (10th Cir. 1996) (Chapter 7 debtor who orchestrated Ponzi fraud scheme did not receive value for transfers made to investor, with no out-of-pocket losses, in the scheme; investor subject to fraudulent transfer provisions of the Code: "transfers could not have satisfied an antecedent debt . . . which means [debtor] received no value in exchange for transfer . . . which brings the transfers within the requirements of 11 U.S.C. § 548(a)(2)."); United States v. Frykholm, 362 F.3d 413, 417 (7th Cir. 2004) (insolvent orchestrator of Ponzi scheme did not receive "new" or reasonably equivalent value when she issued defrauded investor promissory note on account of funds he previously invested.).

5. An income execution entered against a debtor, and all payments made pursuant to the income execution to satisfy a judgment, did not constitute a fraudulent transfer because the debtor had received value in the transaction which ultimately led to the judgment entered against her. Alston v. Grandee Beer Distributors, Inc. (In re Alston), 49 B.R. 929 (Bankr. E.D.N.Y. 1985).

6. An executory promise performed before a transfer is attacked may be deemed "fair consideration" to the extent consideration "was actually given on completion of the transaction." Harper v. Lloyd's Factors, 214 F.2d 662, 663 (2d Cir. 1954); see also Munford v. Valuation Research Corp. (In re Munford, Inc.), 98 F.3d 604, 612 (11th Cir. 1996) (LBO target received fair consideration for severance payments made to its officers, because officers agreed to and did continue working until closing). But a judgment debtor's payment to his attorney for future legal fees and expenses "over an extended period of time and in several courts" was held not to be "fair consideration" because "the work contemplated was neither 'fixed' nor 'definite,' but was rather of considerably uncertain scope and duration. . . ." HBE Leasing Corp. v. Frank, 61 F.3d 1054, 1060-61 (2d Cir. 1995).

7. Good will, in a business context, may in certain circumstances constitute reasonably equivalent value. Colfax, Inc. v. D'Agostino (In re J.K. Chems., Inc.), 7 B.R. 897, 898 (Bankr. D.R.I. 1981). Mere self-serving statements, however, do not suffice to establish good will; evidence such as a long record of highly profitable operations, a valuable customer list, or a trade name developed by the company, is needed. Consove v. Cohen (In re Roco Corp.), 701 F.2d at 983-84. But see Vadnais Lumber Supply, Inc. v. Byrne (In re Vadnais Lumber Supply, Inc.), 100 B.R. 127, 136 (Bankr. D. Mass. 1989) (corporation's payments for covenants not to compete in connection with a stock repurchase held to be without consideration; corporation already owns its good will, so no transfer of value takes place when it acquires a covenant that helps to preserve its good will).

8. Value does not have to be received directly. The debtor may receive reasonably equivalent value, or some part thereof, through a benefit conferred upon a third party. Frontier Bank v. Brown (In re Northern Merchandise Inc.), 371 F. 3d 1056 (9th Cir. 2004) (held, corporate debtor's receipt of proceeds from loan made to shareholders constituted "reasonably equivalent value" in exchange for security interest debtor granted to lender); Leibowitz v. Parkway Bank & Trust Co. (In re Image Worldwide, Ltd.), 139 F.3d 574, 582 (7th Cir. 1998) ("indirect benefits to guarantor may be considered when determining whether a corporation receives reasonably equivalent value for a guarantee"; bankruptcy court did not clearly err in finding that debtors' guarantees of affiliates' obligations to bank were fraudulent transfers in violation of UFTA because debtor corporation "did not receive reasonably equivalent value for its guarantees"); HBE Leasing Corp. v. Frank, 48 F.3d 623, 639 (2d Cir. 1995) (judgment debtor received fair consideration for its payments to attorneys for its codefendants in RICO action; "multiple co-defendants . . . threatened with joint and several liability . . . mounted a common defense, and one defendant paid the legal fees of the others . . ."); Rubin v. Manufacturers Hanover Trust Co., 661 F.2d 979, 991 (2d Cir. 1981) (fair consideration may exist when "the consideration given to the third person has ultimately landed in the debtor's hands, or if the giving of the consideration to the third person otherwise confers an economic benefit upon the debtor"); Field v. United States (In re Abatement Env'tl. Res., Inc.), 102 Fed. Appx. 272, 277 (4th Cir. 2004) (fair consideration may exist when "the consideration given to the third person has ultimately landed in the debtor's hands, or if the giving of the consideration to the third person otherwise confers an economic benefit upon the debtor."); Frontier Bank v. Brown (In re Northern Merchandise Inc.), 371 F. 3d 1056 (9th Cir. 2004) (held, corporate debtor's receipt of proceeds from loan made to shareholders constituted "reasonably equivalent value" in exchange for security interest debtor granted to lender); In re Van Dyck/Columbia Printing, 263 B.R. 167, 176 (D. Conn. 2001) ("Section 548 provides for avoidance of a transfer only if 'the debtor . . . received less than a reasonable equivalent in exchange' for that transfer. In other words, the statutory focus is on what the debtor received, not from whom it was received."), aff'd in relevant part by 289 B.R. 304 (D. Conn. 2003); Corporate Jet Aviation, Inc. v. Vantress (In re Corporate Jet Aviation, Inc.), 57 B.R. 195 (Bankr. N.D. Ga. 1986), aff'd, 82 B.R. 619 (N.D. Ga. 1987), aff'd, 838 F.2d 1220 (11th Cir. 1988). Indirect benefit or value may exist in the form of additional business opportunities that existing lines of credit make available or, in the LBO context, the synergies that may result from the acquisition. Mellon Bank, N.A. v. Metro Communications, Inc., 945 F.2d 635, 647 (3d Cir. 1991), cert. denied sub nom. Committee of Unsecured Creditors v. Mellon Bank, 503 U.S. 937 (1992); but cf. United States v. Gleneagles Inv. Co., 565 F. Supp. 556 (M.D. Pa. 1983).

9. Under section 548(d)(2)(C), added by the Bankruptcy Amendments Act of 1984, a repo participant or financial participant (see III.G., supra) receiving a margin or settlement payment takes for value to the extent of such payment.¹²

10. Under section 548(d)(2)(D), added by 1990 amendments to the Code, a swap participant or financial participant (see III. H., supra) receiving a transfer in connection with a swap agreement takes for value to the extent of such transfer.¹³

¹² The 2005 Amendments applied section 548(d)(2)(C) to financial participants for cases commenced on or after October 17, 2005.

11. The relevant date for determining fairness of consideration is that of the transfer; subsequent depreciation or appreciation of the value of the consideration does not affect its adequacy for purposes of Section 548. Cooper v. Ashley Communications, Inc. (In re Morris Communications NC, Inc.), 914 F.2d 458, 475 (4th Cir. 1990) (fact that stock appreciated substantially after purchase is not ground for invalidating sale; "critical time for judging the propriety of the sale was the time of the sale"); Greene v. Newman (In re Newman), 15 B.R. 658 (S.D.N.Y. 1981) (present value of note payable over period of years must be assessed in order to determine whether value of consideration given in exchange for note is sufficient). When determining reasonable equivalent value, court should consider value at the time the obligations arose. See Federal Communications Comm'n v. Nextwave Personal Communications, Inc. (In re Nextwave Personal Communications, Inc.), 200 F.3d 43, 56 (2d Cir. 1999), cert. denied, 121 S. Ct. 298 (2000) (based upon FCC's interpretation of its own regulations, as supported by principles of auction law, auction sets fair market value of licenses since debtor incurred the obligation at the close of auction); contra, In re GW1 PCS 1, Inc., 230 F.3d 788, 810 (5th Cir. 2000) ("C-block auction was not a typical auction. Under the C-block auction rules, the winning bidder is not entitled to the license until after receiving subsequent FCC approval and does not become obligated for the full bid price until the notes securing the full bid price are thereafter signed.").

12. Transfers made solely for the benefit of third parties are not reasonably equivalent value. Butler v. Nationsbank, N.A., 58 F.3d 1022, 1029 (4th Cir. 1995); Klein v. Tabatchnick, 610 F.2d at 1047; Central Nat'l Bank v. Coleman (In re B-F Bldg. Corp.), 312 F.2d 691, 694 (6th Cir. 1963) ("In the usual case . . . the payment of another's debt is held to be a transfer without fair consideration."); William Iselin & Co. v. Boardwalk Regency Corp., 703 F. Supp. 1084, 1087 (S.D.N.Y. 1989) (corporation did not receive fair consideration when controlling individual's use of corporate checks to pay his personal gambling debts bestowed no benefit upon corporation); Hall v. Arthur Young & Co. (In re Computer Universe, Inc.), 58 B.R. 28 (Bankr. M.D. Fla. 1986) (payment of shareholder debt by corporation is generally avoidable by trustee, unless debtor received benefit of original consideration); Gill v. Brooklier (In re Burbank Generators, Inc.), 48 B.R. 204 (Bankr. C.D. Cal. 1985) (payment by debtor corporation of employee's legal fees with respect to racketeering charges was solely for benefit of employee). The Fifth Circuit, however, has ruled that much hoped for and anticipated future business opportunities constituted reasonably equivalent value, even though the business opportunities never materialized. Butler Aviation Int'l, Inc. v. Whyte (In re Fairchild Aircraft Corp.), 6 F.3d 1119, 1126-27 (5th Cir. 1993) (aircraft manufacturer's payments for commuter airline's fuel in attempt to keep airline afloat constituted reasonably equivalent value when (i) commuter airline was part of USAir system and manufacturer viewed USAir as "potential major customer" and (ii) keeping airline "marketable" gave manufacturer opportunity to recoup its investment and make additional sales in event that buyer could be found).

(a) Reasonably equivalent value in the case of a "downstream" transfer is easily demonstrated--i.e., a transfer from a parent to a wholly-owned subsidiary, at least in situations where (a) the subsidiary/transferee is solvent and adequately capitalized and

¹³ The 2005 Amendments applied section 548(d)(2)(D) to financial participants for cases commenced on or after October 17, 2005.

(b) the transfer to the subsidiary is not part of a series of transactions that has the effect of removing value from the reach of the parent's creditors. Thus, the parent's ownership interest in a wholly-owned, solvent subsidiary usually assures that the parent will be found to have benefited from any benefit conferred upon the subsidiary as a result of the transfer. Lawrence Paperboard Corp. v. Arlington Trust Co. (In re Lawrence Paperboard Corp.), 76 B.R. 866, 871 (Bankr. D. Mass. 1987). See Rosenberg, Intercorporate Guaranties And The Law Of Fraudulent Conveyances: Lender Beware, 125 U. Pa. L. Rev. 235, 238 (1976). But see Orr v. Kinderhill Corp., No. 91-CV-353 (N.D.N.Y. March 30, 1992) (in voiding bank's liens against certain real estate that had formerly been owned by Kinderhill Corp. and then transferred to its subsidiary, which was then spun-off, court held that parent company's (i.e., Kinderhill Corp.'s) transfer of property to its newly-formed wholly-owned subsidiary was not supported by fair consideration, even though value of stock presumably increased as result of transfer), aff'd on other grounds, 991 F.2d 31 (2d Cir. 1993) (court found it unnecessary to address question of whether transfer to wholly-owned subsidiary is prima facie without consideration because transfer by Kinderhill Corp. (parent) to its subsidiary at time when litigation was pending against Kinderhill Corp. was but one of a series of restructuring steps that had effect of removing any value associated with the property from reach of Kinderhill Corp.'s creditors). If the subsidiary is insolvent, however, it may be impossible to show that the parent benefited from the downstream transfer. See Commerce Bank v. Achtenberg, No. 90-0950-CV-W-6, 1993 U.S. Dist. LEXIS 16136, at *4 (W.D. Mo. Nov. 10, 1993) (no presumption of reasonably equivalent value when parent guaranteed loan to insolvent subsidiary); Murphy v. Avianca, Inc. (In re Duque Rodriguez), 77 B.R. 937 (Bankr. S.D. Fla. 1987) (transfer by parent on behalf of insolvent subsidiary diminished net worth of parent and was not made for reasonably equivalent value).

(b) A transfer for the benefit of a third party will be more likely to lack reasonably equivalent value if it is "upstream"--i.e., from a subsidiary to a parent, including the guaranty by a subsidiary of a parent's obligation, or "cross-stream"--i.e., from one subsidiary to another. See, e.g., In re FBN Food Services, Inc., 82 F.3d 1387, 1393-94 (7th Cir. 1996) (trustee sued debtor's shareholder, shareholder's corporate parent and others, alleging that transfer of settlement proceeds to corporate parent was fraudulent transfer; court affirmed avoidance of transfer; restaurant franchiser paid portion of debtor's settlement proceeds to debtor's shareholder, and corporate parent applied that amount to reduce debt on loan it made to another company in which shareholder held interest); Clark v. Security Pacific Business Credit, Inc. (In re Wes Dor, Inc.), 996 F.2d 237, 243 (10th Cir. 1993) (pledge of subsidiary's assets to secure parent's outstanding loans was fraudulent transfer); Central Nat'l Bank v. Coleman (In re B-F Bldg. Corp.), 312 F.2d 691, 694 (6th Cir. 1963) (cross-stream transfer held fraudulent, when debtor corporation granted lien on its property to bank in exchange for bank's release of note executed by affiliated corporation). Equivalent value can nevertheless be found in such transactions. For example:

(i) The transferor may receive an indirect benefit (see IV.B.8, supra). Harman v. First American Bank of Md. (In re Jeffrey Bigelow Design Group, Inc.), 956 F.2d 479 (4th Cir. 1992); Rubin v. Manufacturers Hanover Trust Co., 661 F.2d 979, 991 (2d Cir. 1981); Barr & Creelman Mill & Plumbing Supply Co. v. Zoller (In re Dolomite 3 Corp.), 109 F.2d 924 (2d Cir. 1940).

(ii) The corporate entities may be collapsed (i.e., treated as alter egos or consolidated). If affiliated entities are actually the same for purposes of the transaction, funds advanced to one will be equivalent value for a payment made or security interest given by the other. See Mayo v. Pioneer Bank & Trust Co., 270 F.2d 823 (5th Cir. 1959), cert. denied, 362 U.S. 962 (1960); Telefest, Inc. v. VU-TV, Inc., 591 F. Supp. 1368 (D.N.J. 1984) (in dicta, court stated that B-F Building rule is inapplicable "'if the debtor and the third party are so related or situated that they share an 'identity of interests', because what benefits one, will in such case, benefit the other to some degree.'" (citation omitted)); McNellis v. Raymond, 287 F. Supp. 232 (N.D.N.Y. 1968), aff'd in relevant part, 420 F.2d 51 (2d Cir. 1970); Official Unsecured Creditors Comm. v. Ampco-Pittsburgh Corp. (In re Valley-Vulcan Mold Co.), 5 Fed. Appx. 396 (6th Cir. 2001) (intercompany transfer was fair consideration paid to equalize partners' individual contributions to the partnership); Babitt v. Vebeliunas (In re Vebeliunas), 332 F.3d 85 (2d Cir. 2003) (wife's purchase and transfer of property to trust was for value and not fraudulent transfer; debtor-husband subsequent fraud could not be imputed to trust created by wife since none of the benefits debtor received from the property evidenced control of the trust, alter ego theory inapplicable since wife was not party to fraud; property not subject to turnover). See VI.A., infra.

13. Release of support obligation, although not mandated by judicial decree, may constitute reasonably equivalent value for debtor spouse's transfer of interest in house. Gray v. Snyder, 704 F.2d 709, 712 (4th Cir. 1983).

14. As mentioned in II.C., supra, the Durrett problem has been resolved by a holding that "reasonably equivalent value" is always received in a foreclosure sale when that sale is conducted in compliance with the applicable state law. See BFP v. Resolution Trust Corp., 511 U.S. 531 (1994) (resolving split among circuits by ruling that "reasonably equivalent value" for foreclosed property is price actually received at foreclosure sale, but only if sale satisfies state foreclosure law requirements). See also In re Winshall Settlor's Trust, 758 F.2d 1136, 1139 (6th Cir. 1985); Lawyers Title Ins. Corp. v. Madrid (In re Madrid), 21 B.R. 424 (B.A.P. 9th Cir. 1982), aff'd on other grounds, 725 F.2d 1197 (9th Cir. 1984), cert. denied, 469 U.S. 833 (1984). BFP therefore replaces the standard previously adopted by a number of courts that the amount received at a foreclosure sale is not necessarily reasonably equivalent value. For prior rulings, holding that a reasonably equivalent value is not necessarily the amount received in a foreclosure sale, see Bundles v. Baker (In re Bundles), 856 F.2d 815 (7th Cir. 1988) (no irrebuttable presumption of reasonably equivalent value in noncollusive foreclosure sales); Grissom v. Johnson (In re Grissom), 955 F.2d 1440, 1446 (4th Cir. 1992) ("absent fraud, collusion or irregular or unlawful procedures, courts should presume that a legitimate foreclosure sale brings a price reasonably equivalent to the property's value"; trustee seeking to avoid foreclosure sale must establish specific facts that undermine confidence in reasonableness). The presumption that the proceeds of a foreclosure sale, conducted in adherence to state law, constitute reasonably equivalent value has been adopted by the drafters of the UFTA. Thus section 3(b) provides that for purposes of sections 4(a)(2) and (5) (constructively fraudulent transfers), "reasonably equivalent value" is given when a person acquires an asset of the debtor at "a regularly conducted, noncollusive foreclosure sale." Although the Durrett court, in dicta, implied that a transfer for less than 70% of fair market value lacked fair consideration, most

courts following the Durrett rationale adopted a case-by-case approach on this particular issue. See Walker v. Littleton (In re Littleton), 888 F.2d 90, 93 (11th Cir. 1989); Grissom v. Johnson (In re Grissom), 955 F.2d at 1445-48. In a decision by a different panel, even the Fifth Circuit appears to criticize its Durrett decision in view of contrary authorities in other circuits. Besing v. Hawthorne (In re Besing), 981 F.2d 1488 (5th Cir. 1993) (Court's dismissal on the merits of Debtor's claims in civil suit against Hawthorne not a transfer for less than reasonably equivalent value; "judgment conclusively established that Debtors' claims against Hawthorne had no merit. . . . Disposition of Debtors' claims [therefore] constituted a transfer for reasonably equivalent value as a matter of law.") ("In Durrett v. Washington Nat'l Ins. Co. . . . a panel of this circuit applied a purely mathematical test, holding that a foreclosure sale which brought only 57.7 percent of the market value of a debtor's property was subject to avoidance. In so holding, the Durrett court also observed that it had found no case in which a transfer for less than 70 percent of market value had been approved. . . . This dictum spawned the so-called 'Durrett rule,' which, when mechanically applied, invalidates any transfer for less than 70 percent of fair market value Other circuits, indeed the majority of the circuits that have addressed the issue, reject Durrett's purely mathematical analysis in favor of a broader 'totality of the circumstances' standard.") (internal citations and citations of contrary authorities omitted). Id. This issue was addressed again by the Fifth Circuit in Ingalls v. Erlewine (In Re Erlewine), 349 F. 3d 205 (5th Cir. 2003), where, pursuant to a divorce decree, community property was subject to unequal division, with the husband taking the larger share. Post-divorce, the wife filed a bankruptcy petition, and the trustee subsequently sought to avoid the divorce decree on the ground the unequal division of community property constituted a lack of reasonably equivalent value. The Fifth Circuit disagreed, and, relying on Besing and BFP, upheld the validity of the decree, declined to apply a rigid mathematical formula and held: (i) "[in BFP] the Court . . . took account of the states' interest in the security of titles to real property, an interest that would be threatened if every foreclosure could be undone in the federal bankruptcy court. Some of the same concerns are present in this case;" (ii) the divorce was "fully litigated;" and that (3) despite the divorce court's unequal division of property, the Debtor had therefore received reasonably equivalent value as a matter of law. Id. at 212, 213.

The repurchase of stock or equity by an insolvent corporation or partnership from former shareholders or partners of the debtor may, but need not necessarily, be fraudulent. The equity of an insolvent debtor may have value if the debtor's expected future earnings and performance are taken into account. Anderson Indus., Inc. v. Anderson (In re Anderson Indus., Inc.), 55 B.R. 922 (Bankr. W.D. Mich. 1985) (effect of insolvency on value of corporation's stock raises question of fact sufficient to defeat motion for summary judgment). But see, Buncher Co. v. Official Committee of Unsecured Creditors of Genfarm LP IV, 229 F.3d 245, 252-53 (3d Cir. 2000) (held, partnership did not receive fair consideration when it "transform[ed] [limited partner's] failed investment into a secured creditor relationship, to the detriment of the partnership's unsecured creditors."); Vadnais Lumber Supply, Inc. v. Byrne (In re Vadnais Lumber Supply, Inc.), 100 B.R. 127, 136 (Bankr. D. Mass. 1989) ("[b]ecause [a] corporation already owns its own assets, its ownership of an interest in those assets adds nothing"; held, corporation's repurchase of its own stock was without consideration). Consove v. Cohen (In re Roco Corp.), 701 F.2d 978, 982 (1st Cir. 1983) (held, redemption by debtor corporation of sole shareholder's shares was fraudulent transfer in that debtor received less than reasonable equivalent value; redemption increased liabilities to an amount substantially higher than total

assets); Nicolaci v. Anapol, 387 F. 3d 21, 27 (1st Cir. 2004) (common-law right of indemnity does not apply to fraudulent transfer claim asserted by chapter 7 trustee against debtor's former shareholders based on pre-petition stock purchase transaction.).

15. Prior to the passage of the Religious Liberty and Charity Donation Protection Act of 1998 (discussed infra) charitable contributions were avoidable as fraudulent transfers because reasonably equivalent value is not received for payments made out of a sense of moral obligation. Christians v. Crystal Evangelical Free Church (In re Young), 152 B.R. 939 (D. Minn. 1993) (charitable contributions are gratuitous transfers, although debtors feel morally obligated to tithe; church did not provide services in exchange for contributions), rev'd on other grounds, 82 F.3d 1407, 1418 (8th Cir. 1996) (trustee's recovery of church donations by debtors, which were avoidable transfers because debtors did not receive services in exchange for their contributions, held to violate Religious Freedom Restoration Act), vacated and remanded, 117 S. Ct. 2502 (1997) (remanded in light of City of Boerne v. Flores, 521 U.S. 507 (1997) holding Religious Freedom Restoration Act unconstitutional) on remand to Christians v. Crystal Evangelical Free Church (In re Young), 141 F.3d 854, 856 (8th Cir. 1998) (reinstating previous decision), cert. denied, 119 S. Ct. 43 (1998). See also Scholes v. Lehman, 56 F.3d 750, 759-760 (7th Cir. 1995) (Posner, J.), cert. denied sub nom. African Enterprise, Inc. v. Scholes, 116 S. Ct. 673 (1995) (refusing to apply state fraudulent transfer law less rigorously when religious organization received transfer); Weinman v. Word of Life Christian Center (In re Bloch), 207 B.R. 944, 948, 951 (D. Col. 1997) ("[section 548(a)(2)] requires that the debtor must have been provided with something of economic, as opposed to religious or spiritual, value" in order to prevent avoidance of transfer). But see In re Missionary Baptist Found. of America, Inc., 24 B.R. 973 (Bankr. N.D. Tex. 1982) (transfers to nonprofit corporation formed by debtor's principal held not actual or constructive fraudulent transfers even though debtor insolvent and unable to pay creditors' claims when due; reasonably equivalent value found in "good will" generated by charitable purpose of donations); Ellenberg v. Chapel Hill Harvester Church, Inc. (In re Moses), 59 B.R. 815, 819-20 (Bankr. N.D. Ga. 1986) (no fraudulent transfer when debtors' donations to church involved valuable "services" by church such as providing facilities for religious services, day care, marriage and business counseling).

16. On June 19, 1998, the President signed into law the "Religious Liberty and Charity Donation Protection Act of 1998", Pub. L. No. 105-183 (1998) (the "Act"). The Act came about as a direct result of the decision in City of Boerne v. Flores, 521 U.S. 507 (1997), where the Supreme Court declared the Religious Freedom Restoration Act of 1993 unconstitutional. The new legislation, among other things, amends Code §§548 and 544(b) to prevent the trustee from challenging a good faith charitable gift as a fraudulent transfer. Specifically, the Act (i) amends §548(d) to adopt the definitions of "charitable contribution" and "qualified religious and charitable entity or organization" contained in the Internal Revenue Code; (ii) amends §548(a)(2) [governing constructively fraudulent transfers] to provide that a "transfer of a charitable contribution to a qualified religious or charitable entity or organization shall not be considered to be a [constructively fraudulent transfer] in any case in which--(A) the amount of that contribution does not exceed 15 percent of the gross annual income of the debtor for the year in which the transfer of the contribution is made; or (B) the contribution made by a debtor exceeded the [prescribed] percentage amount of gross annual income . . . if transfer was consistent with the practices of the debtor in making charitable contributions" and (iii) amends

§544(b) to prevent the trustee from using applicable state fraudulent transfer law to attack a qualified "charitable contribution." Other provisions in the Act make the legislation retroactive by providing that it is applicable in cases "pending or commenced on or after the date of enactment. . . ." See Universal Church v. Geltzer, 463 F.3d 218 (2d Cir. 2006) (held, to compute 15 percent of gross income, look to annual aggregate charitable donations, not each donation individually; additionally, the Act does not violate the Free Exercise and Establishment clauses of the First Amendment). See also In re Buxton, 228 B.R. 606 (Bankr. W.D. La. 1999).

17. A debtor receives value for an investment that fails to generate a positive return only if at the time of the transfer, "there is some chance that the contemplated investment will generate a positive return. . . ." Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L., Inc. (In re R.M.L., Inc.), 92 F.3d 139, 152 (3d Cir. 1996) (debtor did not receive value for commitment fees paid to potential lender in connection with issuance of committal letter because the loan was highly conditional and had little chance of closing). But a debtor does receive reasonably equivalent value for bets placed at a casino. Allard v. Flamingo Hilton (In re Chomakos), 69 F.3d 769, 771 (6th Cir. 1995), cert. denied, 116 S. Ct. 1568 (1996) (held, pre-bankruptcy gambling losses cannot be recovered by trustee as fraudulent transfer for less than reasonably equivalent value; "the placing of a bet gives rise to legally enforceable contract rights . . . which constitute property not unlike futures contracts purchased on the margin . . . [T]he contractual right to a payoff if the market moves the right way . . . constitutes a value reasonably equivalent to the money at risk.").

C. Transfers By Insolvents. Under section 548(a)(1)(B)(i)-(ii)(I), a transfer of an interest in property or an incurrence of an obligation is voidable as fraudulent if a debtor receives less than reasonably equivalent value for the transfer or obligation and was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation. When asserting a constructive fraudulent transfer under Code § 548(a)(1)(B)(ii)(I) it is necessary to produce evidence that the debtor was insolvent. See Dunham v. Kisak, 192 F.3d 1104, 1110 (7th Cir. 1999) (transfer of debtor's interest would not be set aside as fraudulent transfer when record contains no evidence that debtor was insolvent as required by section 548(a)(1)(B)(ii)).

As discussed in II.B., supra, insolvency means debts in excess of assets (less exempt property). Unlike prior law, the trustee need not allege or prove the existence of an actual creditor at the time of transfer by the insolvent. The elements of constructive fraud under section 548(a)(1)(B)(i)-(ii)(I) are the easiest to prove.

The UFCA contains a similar provision in section 4, as does the UFTA in section 5(a).

D. Transfers By Persons In Business. A transfer of an interest in property or an incurrence of an obligation is voidable under section 548(a)(1)(B)(i)-(ii)(II) if such transfer was made or such obligation was incurred in exchange for less than reasonably equivalent value and the debtor

was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital.

Insolvency need not result from such a transfer or incurrence to make it fraudulent. See Steph v. Branch, 255 F. Supp. 526 (E.D. Okla. 1966), aff'd, 389 F.2d 233 (10th Cir. 1968). Moreover, the absence of fraudulent intent will not prevent a transfer or incurrence under this section from being constructively fraudulent. Fidelity Trust Co. v. Union Nat'l Bank, 313 Pa. 467, 169 A. 209 (1933), cert. denied, 291 U.S. 680 (1934). Unreasonably small capital may be found under section 548(a)(B)(ii)(II) even if the enterprise continues on the same scale after the transfer; leveraged acquisitions are particularly prone to that possibility. United States v. Gleneagles Inv. Co., 565 F. Supp. 556 (M.D. Pa. 1983) (shareholders breached duty to creditors by redeeming stock with loan secured by corporate assets), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987); Wells Fargo Bank v. Desert View Bldg. Supplies, Inc. (In re Desert View Bldg. Supplies, Inc.), 475 F. Supp. 693 (D. Nev. 1978), aff'd mem., 633 F.2d 225 (9th Cir. 1980); In re Atlas Foundry Co., 155 F. Supp. 615 (D.N.J. 1957). See VI., infra. Proof of unreasonably small capital may be established by evidence showing that the debtor was constantly behind in paying its bills or that it continued its business under financial risk. Teitelbaum v. Voss (In re Tuller's, Inc.), 480 F.2d 49 (2d Cir. 1973); New York Credit Men's Adjustment Bureau, Inc. v. Adler, 2 B.R. 752, 756 (S.D.N.Y. 1980). But see Credit Managers Ass'n of Southern California v. Federal Co., 629 F. Supp. 175 (C.D. Cal. 1985) (held, business not undercapitalized for fraudulent transfer purposes; court adopted as reasonable the positive cash flow projections developed by lender at time of transfer).

The corresponding sections of the UFCA and UFTA are section 5 and section 4(a)(2)(i), respectively. Under section 5 of the UFCA, a debtor's capital must be examined "throughout a reasonable period of time surrounding the precise date of the alleged transfer . . . The critical inquiry when considering whether a transfer or conveyance has left a company with an unreasonably small capital is . . . one that weighs raw financial data against both the nature of the enterprise itself and the extent of the enterprise's need for capital during the period in question." Barrett v. Continental Illinois Nat'l Bank & Trust Co., 882 F.2d 1, 4 (1st Cir. 1989), cert. denied, 110 S. Ct. 1476 (1990) (\$2 million transfer that left company insolvent for up to two weeks was not fraudulent transfer when (i) company was winding up its affairs and (ii) company became solvent and able to pay plaintiffs' potential claims within 2 weeks after transfer).

The Third Circuit's decision under the Pennsylvania UFCA identified several criteria to apply in connection with the question of whether a debtor was left with unreasonably small capital following a leveraged buyout (Pennsylvania has since adopted the UFTA). Moody v. Security Pacific Business Credit, Inc., 971 F.2d 1056 (3d Cir. 1992). The Third Circuit noted that the "unreasonably small capital" test of section 5 of the UFCA is distinct from the bankruptcy or balance sheet insolvency test of section 4 of the UFCA and equitable insolvency (i.e., the inability to pay debts as they mature). Id. at 1071-72 ("unreasonably small capital denotes a financial condition short of equitable insolvency"). Thus, a debtor that is solvent under the balance sheet and equity insolvency tests may, nevertheless, successfully avoid transfers made or obligations incurred for less than fair consideration if such transfers or incurrences of

debt leave the debtor with, or occur at a time when the debtor has, unreasonably small capital. This alternative basis for fraudulent transfer liability is extremely fact intensive and is grounded upon a reasonable foreseeability standard. *Id.* at 1073 ("The critical question is whether the parties' [financial] projections were reasonable;" relevant factors include reasonableness of cash flow, net sales, gross margins, net profits and losses, and availability of credit "tested by an objective standard anchored in the company's actual performance;" other contingency factors must be also be considered such as interest rate fluctuations and general economic downturn to develop margin of error). In *Moody*, the Third Circuit affirmed the lower court's findings that the financial projections of the acquirer and the party providing acquisition financing were reasonable considering the company's pre-acquisition financial performance and the existence of other extrinsic factors contributing to the debtor's demise, such as lost sales due to increased competition and buildup of excess inventory due, in part, to mismanagement. *Id.* at 1074-75. Because the court construed the "unreasonably small capital" test as a causal link between the challenged transfer and the debtor's failure, *id.* at 1071, the failed leveraged buyout in *Moody* was found not to be constructively fraudulent. The court found no relationship between the post-acquisition capital structure and the unforeseeable extrinsic economic factors that caused the debtor's demise.

E. Transfers By Persons About To Incur Debts. A transfer of an interest in property or incurrence of debt for less than reasonably equivalent value when the debtor

intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.

may also be avoided as constructively fraudulent under section 548(a)(1)(B)(ii)(III). See generally *Pirrone v. Toboroff (In re Vaniman Int'l, Inc.)*, 22 B.R. 166, 186-88 (Bankr. E.D.N.Y. 1982) (citing *Carpenter v. Roe*, 10 N.Y. 227, 231-32 (1851)). Intent for purposes of that section must occur contemporaneously with the transfer or incurrence; proof of a chronological link between the transfer and subsequently incurred debts will not suffice. 5 *Collier on Bankruptcy*, ¶ 548.05, at 548-30 (Lawrence P. King ed., 15th rev. ed. 1997). It is not necessary, however, to prove knowledge of inability to pay particular debts; general intent is enough. *Lackawanna Pants Mfg. Co. v. Wiseman*, 133 F.2d 482 (6th Cir. 1943).

The UFCA contains a similar provision in section 6, as does the UFTA in section 4(a)(2)(ii).

F. Transfers To Insiders Under Employment Contract. The 2005 Amendments enable a trustee to avoid an insider transfer pursuant to an employment contract if it was made outside the ordinary course of business and the debtor received less than reasonably equivalent value. 11 U.S.C. § 548(a)(1)(B)(ii)(IV). This amendment applies to cases commenced on or after April 20, 2005 and does not require proof of insolvency.

G. Transfers To Insiders Under UFTA. A transfer to an "insider" under section 5(b) of the UFTA (a term broadly defined in UFTA section 1(7) and derived from the definition of that term in section 101(31) of the Code) may be avoided as constructively fraudulent by a creditor whose claim arose before the transfer. *Kroh Brothers Development Co.*

v. United Mo. Bank of Kansas City (In re Kroh Brothers Dev. Co.), 137 B.R. 332 (Bankr. W.D. Mo. 1992) (insider of affiliate held to be insider of debtor; 20% ownership of debtor's stock creates affiliate status; control of corporation not necessary to be insider). Courts will also read the statutes broadly. Browning Interests v. Allison (In re Holloway), 955 F.2d 1008 (5th Cir. 1992) (held, although not expressly mentioned in statute, ex-spouse may be insider; court should focus on "closeness" of relationship between transferee and debtor to determine whether insider status exists). To be avoided, the transfer must be made to an insider, for an antecedent debt, and at a time when the debtor was insolvent, and the insider must have had reasonable cause to believe that the debtor was insolvent. Collusion or some degree of bad faith on the part of the insider is presumed. UFTA § 5(b) thus blurs the distinction between a fraudulent transfer and a bankruptcy preference; it allows an individual creditor to avoid a transfer to an otherwise innocent insider regardless of whether the insider has actually obtained an unfair advantage over other creditors. The avoidance will be solely for the benefit of the plaintiff creditor. Unlike bankruptcy preferences (11 U.S.C. § 547), there is no requirement that the transfer enable the insider to receive more than he would receive in a liquidation of the debtor's assets. The UFTA also does not make available to the insider all of the possible defenses to a preference as enumerated in section 547(c) of the Code.

The defenses that are available to an insider against a UFTA § 5(b) attack are enumerated in UFTA § 8(e) and (f). Section 8(e) provides that a transfer is not voidable if it results from lawful termination of a lease after a default by the debtor or from enforcement of a security interest in compliance with Article 9 of the Uniform Commercial Code. Foreclosure by an insider on a lien that is not validly perfected may be avoided under UFTA § 5(b). UFTA § 8(f)(1) provides that a transfer is not voidable under section 5(b) to the extent that the insider gave new value to or for the benefit of the debtor after (not contemporaneously with) the transfer, unless the new value was itself "secured by a valid lien." Under UFTA § 8(f)(2), a transfer is not voidable "if made in the ordinary course of business or financial affairs of the debtor and the insider." This corresponds to the preference defense provided by section 547(c)(2) of the Code; but UFTA § 8(f)(2), unlike section 547(c)(2) of the Code, does not require that the transfer be made in payment of a debt incurred in the ordinary course of business, or that it be made according to ordinary business terms. UFTA § 8(f)(3) also protects a transfer to an insider if it was made "pursuant to a good-faith effort to rehabilitate the debtor" and "secured present value given for that purpose as well as an antecedent debt of the debtor."

The key ramifications of UFTA § 5(b) are as follows: (i) creditors may have a new ground to attack transfers to insiders in non-bankruptcy cases; (ii) a powerful new weapon may be put in the hands of government agencies, particularly the Internal Revenue Service, enabling them to attack virtually all payments from business organizations to insiders, in or out of bankruptcy. This is of special concern; even in a state that adopts UFTA § 9(c), the one year limitation may not apply to the federal government; although Comment (1) of UFTA § 9 states that the UFTA rejects the result in United States v. Gleneagles Inv. Co., 565 F. Supp. 556, 583 (M.D. Pa. 1983) (Pennsylvania's six-year statute of limitations on fraudulent transfer actions does not bar untimely action by United States), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987), the UFTA may not effectively avoid that result; and (iii) trustees in bankruptcy might acquire important new

powers to attack transfers to insiders: the UFTA, made available by section 544(b) of the Bankruptcy Code, can be used when a preference action under section 547 would not be viable.

Even in jurisdictions that have not adopted the UFTA, such as New York, transfers to insiders in exchange for what would otherwise be considered fair consideration, e.g., the discharge of an antecedent debt owed to the insider, may be treated as constructive fraudulent transfers if a non-insider was the transferee. See Orlando Food Corp. v. PFP Food Importers, Inc., No. 91-3552, 1992 WL 403425 (E.D.N.Y. Dec. 18, 1992) (transfer to officer, director, or shareholder of insolvent corporation in exchange for discharge of antecedent debt lacks good faith and does not constitute fair consideration). Cf. Lippe v. Bairnco Corp., 218 B.R. 294, 303 (S.D.N.Y. 1998) aff'd Lippe v. Bairnco Corp., 99 Fed. Appx. 274 (2d Cir. 2004) (even if trustee had standing to assert aiding and abetting a breach of fiduciary claim against professionals, claim dismissed because, "[u]nder New York law, a non-transferee may not be held liable for a fraudulent transfer unless it has dominion and control over the transferred assets or unless it benefits in some way from the conveyance," and there was no such allegation that the professionals exercised dominion and control over the transferred assets or that they benefited from the transfer); Brenner v. Phillips, Appel & Walden, Inc., No. 93 Civ. 7838, 1997 U.S. Dist. LEXIS 11539, at *14 (S.D.N.Y. July 22, 1997) (summary judgment granted in favor of corporate officers and directors on claim that they violated New York's Uniform Fraudulent Conveyance Act because plaintiffs failed to prove that corporate officers and directors were either transferees or beneficiaries of the alleged fraudulent transfer).

V. Transfers To General Partners By Insolvent Partnerships

Pursuant to section 548(b) of the Code, the trustee of a partnership debtor may avoid any transfer made to a general partner or incurred by a general partner that was made or incurred on or within one year of the filing of the petition, provided the debtor was insolvent at the time of the transfer or obligation or was rendered insolvent as a result of it.¹⁴ See Scherer v. Leslie Fay Sales (In re Jercyn Dress Shop), 516 F.2d 864, 867 (2d Cir. 1975); Berisford, Inc. v. Stroock & Stroock & Lavan (In re 1634 Assoc.), 157 B.R. 231 (Bankr. S.D.N.Y. 1993) (§ 548(b) encompasses indirect as well as direct transfers to general partner of partnership). The trustee need not prove that the transfer was made for less than reasonably equivalent value; the insolvency of the partnership at the time of or as a result of the transfer is the critical factor.

An interesting standing issue is presented in cases involving insolvent real estate partnerships with nonrecourse secured debt. Does the nonrecourse secured creditor have standing to assert fraudulent transfer claims against partners of an insolvent partnership for receiving distributions that the secured creditor could not reach directly? The Second Circuit has held that a nonrecourse secured creditor may have standing if the creditor can demonstrate that the alleged transfer caused a decline in the value of its collateral, thereby depriving the creditor from obtaining equitable relief for waste. Travelers Ins. Co. v. 633 Third Assoc., 973 F.2d 82, 85-88 (2d Cir. 1992).

¹⁴ The 2005 Amendments extend the one-year statutory reachback period to two-years for cases commenced on or after April 20, 2006.

The corresponding provision of the UFCA is section 8; the UFTA contains no similar provisions because it treats partnerships like other entities.

VI. Leveraged Buyouts

A. Leveraged Buyouts As Fraudulent Transfers.

In a leveraged buyout, the purchaser uses the value of the target corporation as security in financing the cost of the acquisition. If this is done by simply causing the target to grant a lien on its assets to a lender (which may be a bank or other outside financing source, or even the acquiring shareholders themselves), to secure financing for the purchaser, the grant of such a security interest may constitute a fraudulent transfer if the target is thereby rendered insolvent or undercapitalized. Rationale: the purchaser, not the target, has received the consideration for the interest thus granted. As discussed in IV.B.11., supra, a transfer solely for the benefit of a third party normally will not be for reasonably equivalent value. The installation of new management does not, in itself, constitute reasonably equivalent value. United States v. Gleneagles Inv. Co., 565 F. Supp. at 576, aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987).

There is more than one way that a court may value the assets of a target corporation to determine whether the leveraged buyout left the target undercapitalized. Even when the remaining unencumbered assets of the target corporation are sufficient under a fair market value analysis to prevent the target from being insolvent or undercapitalized as a result of the leveraged buyout, the risk that the transfer will be found fraudulent may still exist. Rather than placing a fair market value upon the assets of the target, a court may use the "forced sale value"--the amount which could be received for the property from an immediate sale, if the seller had to sell but the buyer was under no compulsion to buy. The discrepancy between the two methods of valuation will be substantial if the valued assets are illiquid and thus subject to a large discount in a forced sale. As a result, transfers which might seem completely feasible in an open market can still be at risk when subject to a fraudulent transfer analysis. See Join-In Int'l (U.S.A.) Ltd. v. New York Wholesale Distributors Corp. (In re Join-In International (U.S.A.) Ltd.), 56 B.R. 555 (Bankr. S.D.N.Y. 1986); Barr v. Weber (In re Carousel Candy Co.), 38 B.R. 927, 937 (Bankr. E.D.N.Y. 1984) ("it is appropriate, in the determination of the question of insolvency, to value doubtful or contingent claims at less than face value."); Much and O'Dea, LBO's And The Risks Of Fraudulent Conveyance, Nat'l L.J., Nov. 3, 1986 at 36, col. 1. But see Moody v. Security Pacific Business Credit, Inc., 971 F.2d 1056, 1067 (3d Cir. 1992) (following majority rule of cited cases and applying going concern asset valuation for purposes of UFCA where bankruptcy not clearly imminent); Ohio Corrugating Co. v. DPAC, Inc. (In re Ohio Corrugating Co.), 91 B.R. 430 (Bankr. N.D. Ohio 1988) (applying going-concern values to debtor's assets in determining whether LBO rendered debtor insolvent).

Another method for determining whether the target corporation was left undercapitalized as a result of the buyout is to examine the cash flow of the target, as projected at the time of the buyout. In Credit Managers Ass'n of Southern California v. Federal Co., 629 F. Supp. 175 (C.D. Cal. 1985), the parent corporation sold all of the stock of its wholly owned subsidiary to a holding company organized by the management of the target corporation for the purpose of acquiring the stock of the target. The price for the shares was the book value of the

target corporation. The acquisition was financed by borrowing against the assets of the target. In addition, the target repaid an unsecured loan of the parent corporation with the proceeds of a loan that it obtained by pledging both its personal and real property. Subsequently, the target corporation experienced several unforeseen setbacks, including an employee strike, which interrupted business for two months. Unable to recover from the setbacks, the target corporation shut down approximately 17 months after the buyout, and executed an assignment of its assets for the benefit of its creditors. The assignee challenged the initial acquisition of the stock of the target on the grounds that the transfer was fraudulent, and sought to set aside the leveraged buyout. The court held that the purchase of stock was neither a fraudulent transfer nor an unlawful distribution to shareholders. To support its finding that the target was not left with unreasonably small capital as a result of the acquisition, the court relied heavily upon the testimony of the officials of the lender which, after the acquisition, loaned the target the money used to refinance the unsecured loan of the parent corporation. Among the factors considered by the court were the sales forecast of the target, the gross profit margin, the inventory turnover, and the average age of accounts receivable. The combination of these factors resulted in a projection of positive cash flow, and as a result, the court found that the target was adequately capitalized after the transfer.

The rejection by the court in Credit Managers of fraudulent transfer liability because of a projection of positive cash flow at the time of the acquisition was viewed favorably by at least one commentator. See Carlson, Leveraged Buyouts In Bankruptcy, 20 Ga. L. Rev. 73, 95, 121 (1985). The author argued that there should be a valid defense against fraudulent transfer attack, even when the target corporation was left insolvent as a result of the acquisition, provided that the lender had a good faith belief that the target would have sufficient cash flow to cover the debt service of the loan, and further provided that the lender was not an insider of the borrower. Under this analysis, fraudulent transfer liability would be limited in the leveraged buyout context to those transfers made in anticipation of probable liquidation. See also Baird and Jackson, Fraudulent Conveyance Law And Its Proper Domain, 38 Vand. L. Rev. 829, 854 (1985) (fraudulent transfer law should only be applicable when "there is little chance that creditors would find the transfer in their interest," and should never apply "to arms-length transactions, even if it appears after the fact that the debtor's actions injured the creditors.").

Positive cash flows and other financial factors contained within pre-transaction projections of post-transaction performance were considered significant in the Third Circuit's decision holding that a failed leveraged buyout did not result in fraudulent transfer liability. Moody v. Security Pacific Business Credit, Inc., 971 F.2d 1056 (3d Cir. 1992). Prior to the leveraged buyout, the target company was profitable, had a record of increased annual sales and positive cash flows. As in any leveraged buyout, the acquisition financing left the target highly leveraged, but solvent under the balance sheet bankruptcy insolvency test. Id. at 1065-69. The remainder of the opinion primarily addresses the question of whether the target was left with unreasonably small capital following the leveraged buyout. To resolve this issue, the Third Circuit reviewed several findings of the district court and applied a reasonable foreseeability standard to pre-transaction financial projections in order to determine whether a causal relationship existed between the capital structure of the target after the leveraged buyout and the subsequent financial failure.

The acquirers and the financial institution providing acquisition and working capital financing performed independent financial projections based, in part, on the target's historical performance. *Id.* at 1060. Both parties concluded that the target would produce sufficient cash flow to service the acquisition debt and working capital financing, and that post-acquisition working capital would be sufficient. For approximately six months after the leveraged buyout, the company's sales, gross profits and cash flows tracked projections. *Id.* at 1061. The company subsequently faced a precipitous decline in performance attributable to a shrinking market for its products, increased foreign and domestic competition, general downturn in the economy and a buildup in inventory caused by mismanagement. The company responded by stretching out payments to trade creditors, shutting down operations, and, ultimately, liquidating its business. The company never exceeded its credit limits on its working capital line of credit and the lender never refused to make advances. The Third Circuit in Moody declined to impose liability based on the unreasonably small capital test for a constructive fraudulent transfer, primarily because of the objective reasonableness of the parties' projections and the availability of working capital credit.

The Third Circuit noted that "unreasonably small capital denotes a financial condition short of equitable insolvency." *Id.* at 1070. Thus, even if parties to a leveraged buyout can demonstrate that the target was solvent under both the bankruptcy and equity insolvency tests, transfers made in connection with the transaction may still be vulnerable to attack as fraudulent transfers under the unreasonably small capital standard. From a plaintiff's perspective, pleading the unreasonably small capital element is important to preserve an independent ground for a constructive fraudulent transfer. Defendants, on the other hand, must be prepared to defend against this type of claim based on the reasonableness of pre-transaction projections in light of historical performance and reasonably foreseeable circumstances that might adversely affect the acquired entity.

The test for reasonable foreseeability under Moody constitutes more than a comparison of projections with historical performance--"parties must also account for difficulties that are likely to arise, including interest rate fluctuations and general economic downturns, and otherwise incorporate some margin for error." *Id.* at 1073. Although the adequacy of capitalization approach adopted in Moody is factually intensive and somewhat uncertain in application, the Third Circuit's decision attempts to identify a class of failed leveraged buyouts that should not fall within the purview of constructive fraudulent transfer remedies, namely, transactions for which financial failure is not a reasonably foreseeable result of capital structure, but rather a result of unpredictable extrinsic circumstances that may affect any business, regardless of capital structure. See also Kaiser v. Wood County Nat'l Bank & Trust Co. (In re Loyal Cheese Co.), 969 F.2d 515, 519 (7th Cir. 1992) (secured transaction held not to leave debtor with unreasonably small capital; debtor operated historically with small capital, produced net profits at time of loan, and debtor's demise attributable to government program cutback, not increased loan payments).

The Credit Managers case is of further significance because the court stated that only those who were creditors at the time of the transfer should have the right to challenge a leveraged buyout as fraudulent, a position at odds with the literal language of UFCA § 5, under which this particular transfer was challenged.

Finally, the Credit Managers case is noteworthy because of dicta suggesting that fraudulent transfer law should not be broadly applicable to leveraged buyouts. For a discussion of the impact of this case upon future leveraged buyouts, see Kornberg, Leveraged Buyout On Fair Terms Is Not A Fraudulent Conveyance, *The Bankruptcy Strategist*, Aug. 1986, at 3.

The reluctance of the Credit Managers court to apply fraudulent transfer law to leveraged buyouts was rejected by the Third Circuit in United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), *aff'g* United States v. Gleneagles Inv. Co., 565 F. Supp. 556 (M.D. Pa. 1983), *cert. denied*, 483 U.S. 1005 (1987). The Third Circuit held that the broad language of the UFCA "extends to any 'conveyance' which is defined as 'every payment of money . . . and also the creation of any lien or encumbrance.'" *Id.* at 1297. The court cautioned against excluding particular types of transactions, such as leveraged buyouts, from fraudulent transfer law merely because those transactions are innovative or complicated. "If the UFCA is not to be applied to leveraged buy-outs, it should be for the state legislatures, not the courts, to decide." *Id.* In its discussion of the applicability of fraudulent transfer law, the Third Circuit also took exception to portions of the analysis contained within the Baird and Jackson article, *supra*, that broadly proscribed application of fraudulent transfer law to leveraged buyouts. The court demolished Baird's and Jackson's premise that "creditors can protect themselves from undesirable leveraged buy-outs by altering the terms of their credit contracts." *Id.* at 1297, n.2. According to the court, such a premise ignores major creditors, such as municipalities, who become creditors involuntarily and not "by virtue of a contract." *Id.* For a discussion of the effect of fraudulent transfer laws after the Tabor Court Realty Corp. case, see Kirby, McGuinness, and Kandel, Fraudulent Conveyance Concerns In Leveraged Buyout Lending, 43 *Bus. Law.* 27 (1987); Murdoch, Sartin and Zadek, Fraudulent Conveyances And Leveraged Buyouts, 43 *Bus. Law.* 1 (1987); Cook, Axelrod and Frankel, The Judicially Created "Innocent Shareholder" Defense To Constructive Fraudulent Transfer Liability In Failed Leveraged Buyouts, 43 *S.C. L. Rev.* 777 (1992).

The same court that decided the Credit Managers case reaffirmed its reluctance to apply fraudulent transfer law to leveraged buyouts despite the earlier decision to the contrary in Tabor Court Realty Corp. See Kupetz v. Continental Illinois Nat'l Bank & Trust Co., 77 B.R. 754 (C.D. Cal. 1987), *aff'd sub nom.* Kupetz v. Wolf, 845 F.2d 842 (9th Cir. 1988). Kupetz involved a typical leveraged buyout in which the purchaser obtained the funds to finance the acquisition of the target corporation from a bank, in exchange for a personal guaranty and a pledge of the assets of the target corporation. The sellers of the target were unaware of the finance transaction or its leveraged nature. When the target's business deteriorated and the target filed a chapter 11 petition, the trustee sued to set aside the purchase and recover the payments made to the sellers. The court held that the sellers "had nothing to do with the financial structuring of the purchase worked out by [the purchaser] and should not be held responsible for any damage this financing caused later acquired creditors of [the target]." Kupetz, 77 B.R. at 760.

The Kupetz court interpreted the Tabor Court Realty Corp. case as holding only that a leveraged buyout that involved an "intentionally fraudulent conveyance" was subject to fraudulent transfer laws, leaving unanswered the broader issue of whether such laws should be applied to "buyouts entered in the ordinary course." *Id.* at 760 n.5.

The Ninth Circuit affirmed the lower court's holding, and declined, on the facts before it, to apply fraudulent transfer law to avoid the leveraged buyout in the absence of an intentional scheme to defraud creditors. See Kupetz v. Wolf, 845 F.2d 842 (9th Cir. 1988). The court found no evidence that the sellers intended to defraud creditors and, indeed, emphasized that the sellers had apparently taken care to select a purchaser that appeared financially stable and that was backed by a major financial institution. Although recognizing that fraudulent intent was not a necessary predicate for fraudulent transfer liability, the court stated that it would not "utilize constructive intent to frustrate" an apparently legitimate leveraged buyout, nor was it "appropriate to utilize constructive intent to brand most, if not all, LBOs as illegitimate." Id. at 848. See also Lippi v. City Bank, 955 F.2d 599 (9th Cir. 1992) ("courts' treatment of LBOs will depend on whether the transactions were 'above board' in all relevant aspects or were intentionally fraudulent;" the court concluded that courts may allow recovery from selling shareholders "where there is evidence that the parties knew or should have known that the [LBO] would deplete the assets of the company.").

Though Kupetz, Moody, and Kaiser arguably show an apparent move by a few courts away from the Tabor Court Realty Corp.'s broad application of fraudulent transfer law to leveraged buyouts, another court followed Tabor in an important case. In Murphy v. Meritor Savs. Bank (In re O'Day Corp.), 126 B.R. 370 (Bankr. D. Mass. 1991), the court held that a leveraged buyout was a fraudulent transfer, finding that the transaction rendered the company insolvent. The court rejected using a "going concern" valuation of the company and instead valued each asset individually. Based on this method, the court also concluded that the company was left with an unreasonably small amount of capital.

In Crowthers McCall Pattern, Inc. v. Lewis, 129 B.R. 992 (S.D.N.Y. 1991), the court denied the defendants' motion to dismiss the fraudulent transfer complaint, holding that by "collapsing" the various steps of the leveraged buyout into one integrated transaction, the complaint stated a claim against all of the defendants, including a creditor who made a loan knowing the company would not receive the proceeds but would assume responsibility for the debt. See HBE Leasing Corp. v. Frank, 48 F.3d 623, 635 (2d Cir. 1995). Cf. Aluminum Mills Corp. v. Citicorp N. Am., Inc. (In re Aluminum Mills Corp.), 132 B.R. 869, 883-84 (Bankr. N.D. Ill. 1991) (refusing to dismiss complaint that alleged LBO to be fraudulent transfer).

In Wieboldt Stores, Inc. v. Schottenstein, 94 B.R. 488 (N.D. Ill. 1988), certification for immediate appeal granted, 1989 WL 51068 (N.D. Ill. 1989), interlocutory review denied, No. 89-8038 (7th Cir. July 13, 1989), the court, ruling on motions to dismiss filed by all of the defendants, held that fraudulent transfer law is generally applicable to leveraged buyout transactions, but that "a debtor cannot use these laws to avoid any and all LBO transfers." Id. at 500. The court "collapsed" certain individual transfers which comprised the leveraged buyout so that the debtor's former insider shareholders and the lenders who financed the leveraged buyout could be liable as the recipients of a fraudulent transfer. Id. at 502. The court, however, was not "willing to 'collapse'" the individual transactions which comprised the leveraged buyout in order to find that the non-insider public shareholders received the debtor's property in the leveraged buyout. Id. at 503. See generally, M. Cook & G. Zimmerman, Collapsing Leveraged Buyouts In Fraudulent Transfer Suits: Courts Separated By The Same Analysis, 6 M&A and Corp. Gov. L. Rep. 940 (1991). The court therefore granted the non-

insider public shareholder's motions to dismiss the plaintiff's complaint but denied the motions to dismiss filed by the insider shareholders and LBO lenders. In a later proceeding, the district court dismissed all third party plaintiffs' complaints for contribution against all third-party defendants (e.g., the parties who acquired control of the board after the leveraged buyout, lenders who secured financing for the tender offer, shareholders who tendered their shares, and the accountants who provided the financial information for the tender offer and leveraged buyout). Wieboldt Stores, Inc. v. Schottenstein, 111 B.R. 162, 173, (N.D. Ill. 1990) entry of final judgment denied, No. 87-8111, 1990 WL 60679 (N.D. Ill. April 24, 1990). The court held that the Bankruptcy Code did not expressly or implicitly create a right to contribution or indemnity, id. at 168, but refused to dismiss third-party claims for negligent misrepresentation and breach of contract against the acquirer's financial advisors. Id. at 175, 176.

The Bankruptcy Court for the District of Colorado adopted the reasoning of the Tabor Court Realty Corp. decision when it rejected an argument made by a defendant in a fraudulent transfer suit that leveraged buyouts should not be encompassed within fraudulent transfer laws. Kaiser Steel Corp. v. Jacobs (In re Kaiser Steel Corp.), 87 B.R. 154 (Bankr. D. Colo. 1988). Unimpressed with the suggestion that a law should not be applied to prohibit types of transactions that were not yet envisioned at the time the law was drafted, the court stated that "[s]uch an argument is at odds with much which has transpired in Anglo-American jurisprudence." Id. at 160. It is the job of the legislatures and not the courts to decide whether certain transactions should be excluded from the broad statutory language. The court recognized the Kupetz Ninth Circuit decision, but only in a chain citation for the general proposition that leveraged buyouts were not insulated from fraudulent transfer laws. Id. at 161. See also Ohio Corrugating Co. v. Security Pacific Bus. Credit, Inc. (In re Ohio Corrugating Co.), 70 B.R. 920, 925 (Bankr. N.D. Ohio 1987) (finding that fraudulent transfer law encompassed leveraged buyouts, court stated that "[i]f it had been intended that fraudulent conveyance law be applied only to situations where the debtor attempts to place his property out of the reach of creditors, the constructive fraud provisions would have been unnecessary since, theoretically, the actual fraud provisions would cover those situations.").

Leveraged buyouts are still potentially voidable under the UFTA. Indeed, because "assets" do not include property to the extent encumbered by a valid lien under UFTA § 1(2)(i), a leveraged acquisition that left a corporation with little or no unencumbered property would be even more readily subject to attack than under present law. For a brief overview of fraudulent transfer problems in leveraged acquisitions, see L. King & M. Cook, Creditors' Rights, Debtors' Protection and Bankruptcy 326-468 (Matthew Bender 3d ed. 1997).

B. Effect Of Section 546(e).

1. Actual Fraud Exception

Section 546(e) excludes from a trustee's fraudulent transfer attack "margin payments" and "settlement payments" by or to a broker or financial institution¹⁵ unless the

¹⁵ The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, enacted April 20, 2005 (the "2005 Amendments"), makes section 546(e) applicable to settlement payments by or to financial participants (defined in section 101(22A)). The amendment applies to bankruptcy cases filed on or after October 17, 2005.

payments were made with actual intent to hinder, delay, or defraud creditors under section 548(a)(1). 11 U.S.C. § 546(e); In re Manhattan Inv. Fund Ltd., 310 B.R. 500, 513 (Bankr. S.D.N.Y. 2002) (held; section 546(e) was inapplicable when payments were made as part of Ponzi scheme under section 548(a)(1)(A)), leave to appeal denied, 288 B.R. 52 (S.D.N.Y. 2002). A securities broker that innocently received funds on behalf of its customers in exchange for their stock in an LBO transaction was thus exonerated in Kaiser Steel Corporation v. Charles Schwab & Co., 913 F.2d 846 (10th Cir. 1990).

2. Leveraged Buyouts

The Tenth Circuit also extended the protection of section 546(e) to the selling shareholders in an LBO. Kaiser Steel Corp. v. Pearl Brewing Corp. (In re Kaiser Steel Corp.), 952 F.2d 1230 (10th Cir. 1991), cert. denied, 112 S. Ct. 3015 (1992). After finding section 546(e) to be unambiguous on its face and refusing therefore to delve into murky legislative history, the court concluded that "those shareholders who tendered their shares one day after the LBO and received the LBO consideration are treated just the same under the Code as shareholders who sold their shares in the market one day prior to the LBO and received a settlement payment reflecting the market value of the LBO consideration. Neither type of investor will be forced to disgorge the payment several years later." Id. at 22. The court viewed its decision as consistent with Congressional policy to promote finality, speed and certainty in the securities markets. Id. at 22 n.10. See also Lowenschuss v. Resorts Int'l, Inc. (In re Resorts Int'l, Inc.), 181 F.3d 505, 514-16 (3d Cir. 1999) (payments to shareholders in LBO are settlement payments for purposes of section 546(e); funds transferred to shareholder who had tendered shares as part of merger but who had also demanded appraisal could not be recovered as fraudulent transfer; although no clearing agency was involved, wiring of funds from debtor to Chase Manhattan Bank which forwarded the funds to Merrill Lynch which in turn paid shareholder satisfied requirement of section 546(e) that settlement payment be made by "financial institution"), cert. denied, 528 U.S. 1021 (1999); In re Hechinger Inv. Co. of Del., 274 B.R. 71, 86-88, 95-98 (D. Del. 2002) (applying In re Resorts Int'l; held, disbursing agent in LBO qualified as "financial institution" under section 546(e), and payments made to disbursing agent were thus unavoidable as fraudulent transfers; section 546(e) also pre-empted unjust enrichment claim against shareholders, officers, and directors for proceeds received from LBO because unjust enrichment effectively acts as avoidance claim). Other courts, however, have declined to extend section 546(e) protection to certain LBO transactions. See, e.g., Wieboldt Stores, Inc. v. Schottenstein, 131 B.R. 655, 663-65 (N.D. Ill. 1991) (Section 546(e) did not prevent recovery from selling shareholders because Congress intended only to protect brokers and clearing agencies); Munford v. Valuation Research Corp. (In re Munford, Inc.), 98 F.3d 604, 610 (11th Cir. 1996) ("regardless of whether the payments [to shareholders] qualify as settlement payments, section 546(e) is not applicable since the LBO transaction did not involve a transfer to one of the listed protected entities") cert. denied, 118 S. Ct. 738, and cert. denied, 118 S. Ct. 739 (1998); Jewel Recovery, L.P. v. Gordon, 196 B.R. 348, 353 (N.D. Tex. 1996) (held, section 546(e) did not protect selling shareholders from avoidance of LBO as fraudulent transfer because transaction was a private stock purchase; section 546(e) "appl[ies] to settlement payments in the clearance and settlement process in the public market" (emphasis added)); Zahn v. Yucaipa Capital Fund, 218 B.R. 656, 675 (D.R.I. 1998) ("The § 546(e) exception applies if the transfers were: (1) 'settlement payments'; and (2) made 'by or to' one of the enumerated entities"; section

546(e) exception inapplicable because transfer of non-publicly traded securities was not a "settlement payment," and even if transfers were settlement payments, they were not made by one of entities named in statute); Brandt v. Hicks, Muse & Co., Inc. (In re Healthco Int'l, Inc.), 195 B.R. 971, 981-83 (Bankr. D. Mass. 1996) (declining to apply section 546(e) to LBO because transfers were from debtor to selling shareholders, neither of which was stockbroker, financial institution, or securities clearing agency; "section 546(e) would not govern even if [stockbroker, financial institution, or securities clearing agency] acted as an intermediary"); In re Grand Eagle Cos., Inc., 288 B.R. 484, 493-95 (Bankr. N.D. Oh. 2003) (creditors' committee challenged LBO involving purchase of privately held stock as fraudulent transfer; held, section 546(e) did not preclude challenge); In re OODC, LLC, 321 B.R. 128, 144-45 (Bankr. D. Del. 2005) (held, section 546(e) inapplicable to LBO because transaction was asset sale, not stock sale, and payments were made to shareholders through selling companies, not through commodity broker, forward contract merchant, stockbroker, financial institution, or securities clearing agency; "Consequently, the instant case does not implicate the settlement and clearing systems for stock sales in any way").

3. Judicial Construction of Settlement Payments

The Third, Ninth, and Tenth Circuits have defined "settlement payments" broadly to determine section 546(e)'s applicability. In re Bevill, Bresler & Schulman Asset Mgmt. Corp., 878 F.2d 742, 751-52 (3d Cir. 1989) ("Section 741(8) ... gives an extremely broad definition of 'settlement payment' ... [I]t is clear that 'settlement payment' does not only mean payment of cash to the dealer by the purchaser, but also encompasses transfer of the purchased securities to the purchaser from the dealer"); Jonas v. Resolution Trust Corp. (In re Comark), 971 F.2d 322, 326 (9th Cir. 1992) (reverse repo participant delivered additional securities to debtor as additional margin for purchase price; debtor returned additional securities to reverse repo participant upon withdrawing from transaction; held, return of additional securities fell within broad definition of "settlement payment" and was thus unavoidable as preference under section 546(e)); Wyle v. Howard, Weil, Labouisse, Friedrichs Inc. (In re Hamilton Taft & Co.), 114 F.3d 991, 993 (9th Cir. 1997) ("[W]e have broadly construed the term 'settlement payment' to 'include[] a transfer of securities that completes a securities transaction'" (quoting In re Comark, 971 F.2d at 326)); In re Kaiser Steel Corp., 952 F.2d at 1237-1240 (held, definition of "settlement payment" is "extremely broad"; exchange of stock for consideration in LBO was "settlement payment" under section 546(e)); PHP Liquidating, LLC v. Robbins, 291 B.R. 592, 596 (D. Del. 2003) (held, stock redemption payments made by debtor and cleared through stockbrokers were settlement payments under section 546(e)); but see KSC Recovery, Inc. v. First Boston Corp. (In re Kaiser Merger Litig.), 168 B.R. 991, 1000-01 (D. Colo. 1994) (held, definition of "settlement payment" does not extend to "money paid to equity shareholders before a proposed LBO in exchange for (1) an irrevocable proxy to vote their stock in favor of the LBO; and (2) an option to purchase shares of preferred stock that [shareholders] would receive only if the LBO were consummated" (emphasis in original)); Weinman v. Fid. Capital Appreciation Fund (In re Integra Realty Res., Inc.), 198 B.R. 352, 360 (Bankr. D. Colo. 1996) (held, stock distribution in spinoff was not a settlement payment when stock recipients gave no consideration for the exchange); In re Adler Coleman Clearing Corp., 263 B.R. 406, 478-485 (S.D.N.Y. 2001) ("Though the courts agree that the § 546(e) definition of 'settlement payment' is to be read broadly, the term 'is not boundless'"; held, payments made as part of criminal conduct and

outside ordinary course of business were not "settlement payments" or "margin payments"); In re Grafton Partners, L.P., 321 B.R. 527, 538-39, 540-41 (B.A.P. 9th Cir. 2005) (held, non-public trade in illegally unregistered securities not a "settlement payment") appeal docketed, No. 05-55485 (9th Cir. Apr. 8, 2005); Enron Corp. v. Bear Stearns Int'l Ltd. (In re Enron Corp.), 323 B.R. 857, 876-77 (Bankr. S.D.N.Y. 2005) (held, transaction by debtor to acquire its own shares was not settlement payment when state law would render transaction void; "If [state] law was violated, the payment cannot be a settlement payment because the transaction is void and there is no settlement obligation to discharge nor any securities transaction to complete"; protection under section 546(g) would also be precluded); In re Healthco Int'l, Inc., 195 B.R. at 983 (held, one-time payment to shareholder in LBO and complete liquidation of stock interest was not "settlement payment," particularly without guaranty by securities clearing agency). The district court in Adler Coleman Clearing Corp. identified five considerations for determining whether a transaction qualifies as a "settlement payment" under section 546(e), including whether:

- (1) the transactions have long settled by means of actual transfers of consideration, so that subsequent reversal of the trade may result in disruption of the securities industry, creating a potential chain reaction that could threaten collapse of the affected market;
- (2) consideration was paid out in exchange for the securities or property interest as part of settlement of the transaction;
- (3) the transfer of cash or securities effected contemplates consummation of a securities transaction;
- (4) the transfers were made to financial intermediaries involved in the national clearance and settlement system;
- (5) the transaction implicated participants in the system of intermediaries and guarantees which characterize the clearing and settlement process of public adverse impacts on the functioning of the securities market if any of those guarantees in the chain were involved.

In re Adler Coleman Clearing Corp., 263 B.R. at 479-80 (citations omitted). The Fifth Circuit, however, has limited the scope of section 546(e) by limiting the definition of "stockbroker." Wider v. Wootton, 907 F.2d 570, 572-73 (5th Cir. 1990) (held, transferee was not a "stockbroker" under 11 U.S.C. § 101(46) (1984) when transfers and purchase of securities were part of Ponzi scheme).

4. Third Parties and Forward Contracts

Section 546(e) protection has also been extended to include a stockbroker's payment to a third party under a reverse repurchase agreement. Wyle v. Howard, Weil, Labouisse, Friedrichs Inc. (In re Hamilton Taft & Co.), 114 F.3d 991, 993 (9th Cir. 1997) (held, stockbroker's payment to third party, at direction of debtor pursuant to reverse repurchase agreement, was settlement payment within the meaning of section 546(e), despite possible application of section 546(f)¹⁶, intended to augment section 546(e) rather than supersede it).

¹⁶ Section 546(f) excludes from a trustee's attack settlement payments "made by or to a repo participant or financial participant, in connection with a repurchase agreement" 11 U.S.C. § 546(f). The Bankruptcy Code, as

Section 546(g) similarly excludes from a trustee's attack payments by a debtor party to a swap agreement¹⁷, even when a creditor (also party to the swap agreement) attaches money a third party owed to the debtor. See, e.g., In re Interbulk, 240 B.R. 195, 201-02 (Bankr. S.D.N.Y. 1999) (debtor owed swap participant money under swap agreement; creditor swap participant attached money third party owed debtor in order to settle amounts due under swap agreement; held, creditor's attachment was transfer under section 546(g), in connection with swap agreement).¹⁸ Margin payments and settlement payments made by or to a forward contract merchant¹⁹ are also exempt from a trustee's avoidance power under section 546(e). See, e.g., In re Olympic Natural Gas Co., 294 F.3d 737, 740-41 (5th Cir. 2002) (parties entered natural gas trading contract providing for single net payments as settlement of each month's trading; held, payments made under contract were insulated from trustee's attack because contract was forward contract, and payments debtor made to contract party were thus settlements payments made to forward contract merchant under section 546(e)).

amended by the 2005 Amendments, defines a "repurchase agreement" to mean "an agreement ... which provides for the transfer of one or more certificates of deposit, mortgage related securities ... , mortgage loans, interests in mortgage related securities or mortgage loans, eligible bankers' acceptances, qualified foreign government securities ... , or securities that are direct obligations of, or that are fully guaranteed by, the United States or any agency of the United States against the transfer of funds by the transferee of such certificates of deposit, eligible bankers' acceptances, securities, mortgage loans or interests, with a simultaneous agreement by such transferee to transfer to the transferor thereof certificates of deposit, eligible bankers' acceptance, securities mortgage loans, or interests of the kind described in this clause, at a date certain not later than 1 year after such transfer or on demand, against the transfer of funds" and related agreements. 11 U.S.C. § 101(47)(A) (2005). The term "repurchase agreement" does not include "a repurchase obligation under a participation in a commercial mortgage loan." Id. at § 101(47)(B). This definition applies to cases commenced on or after October 17, 2005.

¹⁷ The 2005 Amendments, applicable to cases filed on or after October 17, 2005, define "swap agreement" in 11 U.S.C. § 101(53B) to mean "any agreement, ... which is -- (I) an interest rate swap, option, future, or forward agreement ...; (II) ... foreign exchange or precious metals agreement; (III) a currency swap, option, future, or forward agreement; (IV) an equity index or equity swap, option, future, or forward agreement; (V) a debt index or debt swap, option, future, or forward agreement; (VI) a total return, credit spread or credit swap, option, future, or forward agreement; (VII) a commodity index or a commodity swap, option, future, or forward agreement; or (VIII) a weather swap, weather derivative, or weather option" and similar and related agreements.

¹⁸ The Interbulk court ultimately held that the attachment was not entitled to protection under section 546(g) because section 546(g) required that the transfer be "under" and "in connection with" a swap agreement, but the attachment there was only "in connection with" a swap agreement. In re Interbulk, 240 B.R. 195 at 202-03. The 2005 Amendments, however, clarify that section 546(g) applies to transfers "under or in connection with any swap agreement," thus overruling Interbulk. 11 U.S.C. § 546(g) (2005) (emphasis added). An attachment like the one in Interbulk would likely be insulated under section 546(g) for a case commenced on or after the October 17, 2005 effective date of the 2005 Amendments.

¹⁹ A "forward contract" means "a contract (other than a commodity contract) for the purchase, sale, or transfer of a commodity ... or any similar good, article, service, right, or interest which is presently or in the future becomes the subject of dealing in the forward contract trade, or product or byproduct thereof ..." and related agreements. 11 U.S.C. § 101(25) (2005). The Bankruptcy Code, as amended by the 2005 Amendments, thus defines a "forward contract merchant" as "a Federal reserve bank, or an entity the business of which consists in whole or in part of entering into forward contracts as or with merchants in a commodity ... or any similar good, article, service, right, or interest which is presently or in the future becomes the subject of dealing in the forward contract trade." Id. at § 101(26).

C. Preventing Fraudulent Transfer Liability.

The best way to assure that a leveraged acquisition will not be voidable as a fraudulent transfer is to structure the transaction appropriately. One straightforward method is to have the acquirer(s) purchase the target's assets, rather than its shares, and to secure financing for the transaction with a lien against the assets transferred. If the target receives an adequate price for the assets, it will not have made a fraudulent transfer. A bankruptcy court has recognized this distinction in holding that fair consideration exists in a leveraged asset acquisition, even though the court found that the acquisition vehicle was left with unreasonably small capital. Ferrari v. Barclay's Business Credit, Inc. (In re Morse Tool, Inc.), 148 B.R. 97, 134-135 (Bankr. D. Mass. 1992). The chapter 7 trustee argued that the asset sale structure was in reality a leveraged buyout in which the secured financing permitted the debtor to obtain nothing more than the control of its stock. Id. at 104. The bankruptcy court rejected the trustee's characterization holding that "[t]he Trustee's proposed analysis, by focusing narrowly on only one of the buyout transactions, takes it out of context and ignores the economic reality of what actually occurred." Id. at 134. Another bankruptcy court decision appears to take the opposite approach by holding that leveraged acquisitions structured, in part, as asset sales may not be immune to a fraudulent transfer attack if the court chooses to collapse the asset sale with other related components of an acquisition to construct the equivalent of a leveraged buyout. See, e.g., CPY Co. v. Ameriscribe Corp. (In re Chas. P. Young Co.), 145 B.R. 131, 137 (Bankr. S.D.N.Y. 1992) (asset sale to acquisition company is subject to fraudulent transfer claims against noteholders of seller that received sales proceeds). Although acquisition structure may be helpful in defending against subsequent fraudulent transfer claims, it is not clear that this factor will necessarily be dispositive in any given case. Alternatively, the acquirer(s) may secure financing for the transaction by pledging the stock thereby acquired. Other possibilities include partial financing, with the lender buying a minority interest itself while covenanting to resell it to the true acquirer.

Somewhat less secure are methods that employ a lien granted by the target, but which attempt to demonstrate that the transaction lacks one or more of the elements of a fraudulent transfer. These involve documentation by valuation and financial experts that, at the time of the transaction, the target was not insolvent, nor was it rendered insolvent by the transaction; that the transaction did not leave it undercapitalized; and that the transaction did not require it to incur debts beyond its ability to pay as they matured. Projections showing continued solvency and adequate capitalization would also be appropriate. In addition, similar valuation opinions should be obtained for a subsidiary or sibling corporation if the structure of the leveraged buyout includes either secured or unsecured guaranties by the affiliate corporation.

More difficult to establish, but still potentially useful as part of a defense against a fraudulent transfer action, some form or combination of forms of consideration to the target can be provided. These include provision for a right of subrogation to the lender's claims; guaranties by the acquirer(s) and by parties related to the acquirer(s); and opportunities made available to the target by the acquisition (other than the mere installment of new management), such as access to new supplies, new markets, and better financing terms. See, e.g., Mellon Bank v. Metro Communications, Inc. (In re Grant Street Nat'l Bank), 945 F.2d 635 (3d Cir. 1991) (expanded credit line and "synergy" created by LBO held to be reasonably equivalent value). Thus, fair consideration may exist when the transferor (e.g., the target assuming and securing its

new shareholder's obligations) receives an indirect benefit corresponding in value to the property it has transferred. See generally Carl, Fraudulent Transfer Attacks On Guaranties In Bankruptcy, 60 Am. Bankr. L.J. 109 (1986). In Barr & Creelman Mill & Plumbing Supply Co. v. Zoller (In re Dolomite 3 Corp.), 109 F.2d 924 (2d Cir. 1940), a shipbuilding corporation organized a subsidiary (the debtor in the case) to build a particular ship. Both corporations filed reorganization petitions. The subsidiary's trustee claimed that it had been fraudulent for the subsidiary, shortly before bankruptcy, to pay \$6,000 to a supply company for materials furnished to the parent (though used by the subsidiary). The court noted, among other things, that the subsidiary might in fact have received fair consideration indirectly because the payment might have reduced the subsidiary's debt to its parent--e.g., for the materials the parent provided to the subsidiary. Judge Swan, in a concurring opinion, also emphasized this point. Id. at 928.

The court in Rubin v. Manufacturers Hanover Trust Co., 661 F.2d 979, 991 (2d Cir. 1981), noted that fair consideration exists when "the consideration given to the third person has ultimately landed in the debtor's hands, or if the giving of the consideration to the third person otherwise confers an economic benefit upon the debtor" roughly equivalent to property transferred by the debtor. In Rubin, the court found that fair consideration might exist when the debtor, an issuer of money orders, had given liens on its property to a bank lender in return for the latter's grant of credit to several check-cashing businesses (some of which were at least partially owned by the debtor or its affiliates). The check-cashing businesses were among the most important retailers of the debtor's money orders; the court noted that, since the bank's credit to the affiliates encouraged the debtor's sale of money orders, the economic benefit to the debtor might be equivalent to the value it had given in granting the liens to the bank. Although it vacated a district court judgment for the lender, the Second Circuit Court of Appeals remanded for consideration, inter alia, of whether the total economic benefit indirectly received by the debtor was sufficient to constitute fair consideration for the granting of the liens. Id. at 994. See also Klein v. Tabatchnick, 610 F.2d 1043, 1047 (2d Cir. 1979) ("[b]enefit to a debtor need not be direct; it may come indirectly through benefit to a third person"); United States v. Gleneagles Inv. Co., 565 F. Supp. 556, 576 (M.D. Pa. 1983) (suggesting in dictum that loan proceeds trickling down to guarantors would be a direct benefit), aff'd sub nom. United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987).

Other economic benefits may also exist. A financially strong parent is a good source of financial and other support to a subsidiary, while a weak parent may impair a subsidiary's credit and even make it subject to liquidation. See, e.g., Coquillette, Guaranty Of And Security For The Debt Of A Parent Corporation By A Subsidiary Corporation, 30 Case W. Res. L. Rev. 433, 442, 452 (1980). Subsidiary guaranties may be further insulated from fraudulent transfer attack by either paying the subsidiary a fee for issuing its guaranty, limiting the maximum liability on the guaranty to an amount that would not render the subsidiary insolvent, or making a commitment to provide working capital to the subsidiary.

A second approach to structuring the leveraged acquisition may be available when there is an identity of interest between parent and subsidiary. The court may treat them as a single entity, so that the agreement becomes a simple two-sided transaction between borrower and lender. Under this analysis, the funds advanced to the parent will be fair consideration for the pledge by the subsidiary, providing that the relative amounts are not disproportionate.

The Fifth Circuit adopted this approach in Mayo v. Pioneer Bank & Trust Co., 270 F.2d 823 (5th Cir. 1959), cert. denied, 362 U.S. 962 (1960). The president and sole shareholder of a construction corporation had obtained a personal loan from a bank and deposited the proceeds in the corporation's account. Subsequently, he caused the corporation to repay the bank on his obligation. When the corporation filed a bankruptcy petition shortly thereafter, its bankruptcy trustees attempted to avoid the repayment to the bank as fraudulent, claiming it had been made to satisfy another person's (*i.e.*, the shareholder's) debt, and therefore lacked fair consideration. Rejecting this attack, the court held that "[t]here was such a degree of identity and commingling of affairs between Twin City [the corporation] and Gray [its sole stockholder] that the corporation and its sole stockholder cannot be regarded as separate legal entities. . . ." Id. at 830. This was not the usual case where a transfer was made to pay the obligation of another, and the court readily found that fair consideration for the debtor's payment existed. Id.

The Second Circuit subsequently affirmed a similar holding by a district court in McNellis v. Raymond, 287 F. Supp. 232 (N.D.N.Y. 1968), aff'd in relevant part, 420 F.2d 51 (2d Cir. 1970). This case involved transactions between a lender, a father, a son, and the corporation they controlled. The father and son were adjudged bankrupt, and their trustee attempted to recover payments made by the son to the lender to repay loans previously made to the corporation. The district court, citing Mayo, held that there was such an identity between the son and the corporation "that they cannot be regarded as separate entities insofar as [the son's] obligation to repay the loans is concerned." 287 F. Supp. at 239. The court also found an indirect benefit to the son sufficient to support a finding of fair consideration, even if the transaction were viewed as three-sided, because the loans to the corporation enabled him to postpone his own bankruptcy. Id.

The court in Biggs v. United States Nat'l Bank of Omaha, 11 B.R. 524 (D. Neb. 1980), found fair consideration in a case involving a cross-stream transfer. The debtor corporation, National Auto Supply, Inc., was owned and managed by the same person as another corporation, National Auto Centers. National Auto Centers executed the lease for business premises occupied by both, and executed a series of notes to the defendant bank naming itself as sole obligor. National Auto Supply, however, made all payments both on the lease and the loans. When it filed a bankruptcy petition, it included its affiliate, National Auto Centers, on its list of creditors. The trustee attempted to set aside payments made by National Auto Supply to the bank on National Auto Centers' notes as fraudulent, but the court found fair consideration. Because National Auto Centers engaged in no business activities apart from executing the lease and the notes, while National Auto Supply occupied the same premises and paid all obligations on the lease and the notes, the court held that "the total identity of interest between the [debtor] and National Auto Centers justifies treating these two corporations as a single entity." Id. at 528.

VII. Liability Of Transferees

A. Initial Transferees. When a trustee avoids a fraudulent transfer, section 550(a) of the Code permits the trustee to "receive, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property" from the transferee. The "trustee's right to recover from the initial transferee is absolute." Schaffer v. Las Vegas Hilton Corp. (In re Video Depot, Ltd.), 127 F.3d 1195, 1197-98 (9th Cir. 1997). An "initial transferee is

exposed to stricter liability than a subsequent transferee because an initial transferee is in the best position to evaluate whether the conveyance is fraudulent." Id. at 1199. When creditors seek to recover the value of the property transferred, their recovery is not necessarily limited to the value of the property at the time of the transfer. U.S. v. Verduchi, No. 05-1950, 2006 WL 51410, at *5 (1st Cir. Jan. 10, 2006). The court may make an equitable adjustment to a creditor's recovery from an initial transferee. Id. (debtor transferred home to son as gift before bankruptcy; son gave mortgage on home in exchange for \$196,000; held, recovery from son for fraudulently transferred home was not limited to value of home at time of transfer under Rhode Island's version of UFTA; U.S. government could recover \$196,000 from transferee when federal tax lien was subordinate to mortgage). The Ninth Circuit has held that the trustee's recovery was not limited to the amount of unsecured claims paid on the distribution date of a chapter 11 plan, even when creditors had been paid in full. In re Acequia, Inc., 34 F.3d 800 (9th Cir. 1994) (2-1). It reasoned that recovery under section 550(a) was not limited to the creditors' rights, but had to benefit the estate, which included reimbursement of the estate's costs in pursuing the litigation. The Code does not specifically define the word "transferee," but § 550(a)(1) provides that, under certain circumstances, the trustee may recover fraudulently transferred property from "the initial transferee of such transfer or the entity for whose benefit such transfer was made." 11 U.S.C. § 550(a)(1). Generally, a financial intermediary or conduit, such as a clearinghouse bank, would not be a "transferee" of the debtor's property, because the conduit does not have control over the property. See Schaffer v. Las Vegas Hilton Corp. (In re Video Depot, Ltd.), 127 F.3d 1195, 1198 (9th Cir. 1997) ("it is widely accepted that a transferee is one who, at a minimum, has 'dominion over the money or other asset, the right to put the money to one's own purposes'") (quoting Danning v. Miller (In re Bullion Reserve of North America), 922 F.2d 544, 548 (9th Cir. 1991) ("transferee" must have dominion over property)); Nordberg v. Societe Generale (In re Chase & Sanborn Corp.), 848 F.2d 1196, 1199-1200 (11th Cir. 1988) (bank was mere conduit that had no control over funds); Bonded Fin. Servs., Inc. v. European Am. Bank, 838 F.2d 890, 893 (7th Cir. 1988) ("minimum requirement of status as a 'transferee' is dominion over the money or other asset, the right to put the money to one's own purposes"). Accord Christy v. Alexander & Alexander of New York, Inc. (In re Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey), 130 F.3d 52, 56-57 (2d Cir. 1997) ("We think the wording of section 550(a) is not so plain as to compel, or persuasively argue for, the principle that every conduit is an initial transferee. The statutory term is 'transferee'—not 'recipient'—and is not self-defining. Numerous courts have recognized the distinction between the initial recipient—that is, the first entity to touch the disputed funds—and the initial transferee under section 550 Indeed, if couriers and other mere conduits were deemed 'initial transferees,' some surely unintended consequences would ensue") (citations omitted), cert. dismissed, 118 S. Ct. 2295 (1998); In re First Security Mortgage Co., 33 F.3d 42, 43-44 (10th Cir. 1994) (bank was not an initial transferee because it held funds "only for the purpose of fulfilling an instruction to make the funds available to someone else"); Bailey v. Big Sky Motors, Ltd. (In re Ogden), 314 F.3d 1190 (10th Cir. 2002) (escrow company disburses escrow account funds belonging to creditor Big Sky to debtor based upon debtor's misrepresentations; escrow company demands that debtor replace funds; debtor replaces funds with funds generated from Ponzi scheme; escrow company disburses Ponzi generated funds to Big Sky; held, escrow company did not exert dominion and control over funds; section 550(b)(1) defense not available to Big Sky who must repay funds to the estate). Additionally, "[a] subsequent transferee cannot be an entity for whose benefit the initial transfer was made [under § 550(a)(1)], even if the subsequent transferee

actually receives a benefit from the initial transfer." Danning, 922 F.2d at 598; In re Cohen, 300 F.3d 1097, 1106 (9th Cir. 2002) (wife purchased cashier's check with own funds payable to creditor, with husband designated as purchaser on check; "as a matter of law . . . [husband] was not the remitter of cashier's check . . . [but] simply the courier of an instrument"; creditor was first to exercise "dominion" over the check and thus strictly liable to trustee under sections 548 and 550).

In addition, several circuit courts have recently held that a principal who directs a debtor-corporation to issue a certified check to pay for a personal debt is not an initial transferee. See Schaffer v. Las Vegas Hilton Corp. (In re Video Depot, Ltd.), 127 F.3d 1195, 1199-1200 (9th Cir. 1997) (debtor purchased cashier's check to pay its president's gambling debts to defendant; debtor was listed as purchaser on check, such that legal control over the funds passed directly from debtor to defendant; court held that debtor's president was not an initial transferee because his control over debtor's business operations did not, in itself, compel a finding that principal had dominion and control over funds transferred from debtor to defendant; instead, defendant was initial transferee); Bowers v. Atlanta Motor Speedway, Inc. (In re Southeast Hotel Properties L.P.), 99 F.3d 151, 156 (4th Cir. 1996) ("Many principals presumably exercise de facto control over the funds of the corporations they manage. They can choose to cause their corporations to use those funds appropriately or inappropriately. The distinction is only relevant to the question whether the principal's conduct amounted to a breach of duty to the corporation.' . . . [W]e agree with those courts that have held that the dominion and control test as set forth in Bonded requires legal dominion and control over the funds transferred. To hold that a party needs only physical dominion and control over the funds to constitute an 'initial transferee' is to hold every agent or principal of a corporation to be the initial transferee when he or she effects a transfer of property in his or her representative capacity.") (emphasis in original) (citations omitted); Rupp v. Markgraf, 95 F.3d 936, 943 (10th Cir. 1996) (principal stockholder of corporate debtor instructed bank to issue cashier's check to principal's own creditor; cashier's check purchased with corporate debtor's funds; held, neither bank nor principal was initial transferee of funds; thus, funds were recoverable from either the creditor, as initial transferee, or the principal, as entity for whose benefit transfer was made).

When the initial recipient manifests control over funds, however, it is an initial transferee and any action brought against a mediate or immediate transferee must be brought under section 550(a)(2), not under 550(a)(1). See Barber v. Citizens Nat'l Bank of Macomb (In re KZK Livestock, Inc.), 191 F.3d 456 (7th Cir. 1999) (summary judgment affirmed in favor of bank when debtor sought to recover funds from bank under section 550(a)(1) when debtor's funds were deposited into an account owned individually by one of its principals, transferred by that individual into an account owned by a non-debtor corporation of which he was a principal and ultimately paid to defendant bank; held, regardless of intent of individual and directions given to transfer the funds to bank, there were four days during which individual could manifest control over funds while in his account; he could have changed his mind and spent money rather than transfer funds; bank not initial transferee of funds. The court further followed the holding in Bonded Fin. Servs., Inc. v. European American Bank, 838 F.2d 890 (7th Cir. 1988), that phrase "entity for whose benefit" an initial transfer is made in section 550(a)(1) does not include an entity which actually receives money as bank did in this case.)

The Second Circuit has held that an insurance broker, having recommended the purchase of insurance to a law firm that was then insolvent and soon after a chapter 11 debtor, was not an "initial transferee" within the meaning of § 550(a), when the broker transferred the premium payment from the policyholder to the insurance company. Christy v. Alexander & Alexander of New York, Inc. (In re Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey), 130 F.3d 52 (2d Cir. 1997), cert. denied, 118 S. Ct. 2295 (1998). After determining that "[e]very court of appeals to consider this issue has squarely rejected a test that equates mere receipt with liability, declining to find 'mere conduits' to be initial transferees," the court "join[ed] the other circuits" in adopting the "mere conduit" test for determining who is an initial transferee under § 550(a)(1). Id. at 57-58. The Second Circuit held that "a commercial entity that, in the ordinary course of its business, acts as a mere conduit for funds and performs that role consistent with its contractual undertaking in respect of the challenged transaction, is not an initial transferee within the meaning of § 550(a)(1)." Id. at 59. The court concluded that the insurance broker was a mere conduit because it had "no discretion or authority to do anything else but transmit the money" from the debtor to the insurer, and that "there can be no question" that it "was acting only to channel the funds" to the insurer. Id. at 59. The Sixth Circuit in Taunt v. Hurtado (In re Hurtado), 342 F.3d 528 (6th Cir. 2003), followed this reasoning, holding that once legal title to the funds at issue has passed, the transferee can no longer be deemed a mere conduit, but stressed the fact-intensive nature of the inquiry: the defendant was liable as an initial transferee because she "had control over the [funds] for a number of years, exercising control to write checks ...," and the debtor transferors would have no "legal recourse ... if she had chosen to use the funds for her own benefit." Hurtado, 342 F.3d at 535. Recently, the Second Circuit addressed the issue again, holding "initial" transferees of a fraudulent transfer are strictly liable and unable to rely on any asserted good faith defense. In re Red Dot Scenic, Inc., 351 F.3d 57 (2d Cir. 2003) (debtor's purchasing shareholder paid personal debt with checks drawn on debtor's corporate account; held, recipient of checks was initial transferee "and was therefore required to return the funds regardless of any potential good faith defense;" purchasing shareholder was not initial transferee because "he exercised no control over funds at issue once they were transferred from [debtor's] account."); Reily v. Kapila (In re Internat'l. Mgmt. Assoc.), 399 F.3d 1288, 1292 (11th Cir. 2005) (no initial transferee liability under § 550(a) if no benefit received from transfer; "unquantifiable advantage is not the sort of "benefit" contemplated by 11 U.S.C. § 550(a).").

B. Good Faith Defense. Section 548(c) of the Code provides that, "except to the extent a [fraudulent] transfer ... is voidable under 544, 545 or 547" a transferee "has a lien on" the property transferred by the debtor to the extent that the transferee "takes for value and in good faith."

1. If the transfer is also voidable as a preference under Code § 547, "by the terms of [548(c)]," the fraudulent transfer defendant "cannot benefit from the § 548(c) defense." Roosevelt v. Ray (In re Roosevelt), 220 F.3d 1032, 1035, 1037-38 (9th Cir. 2000) ("Since the conveyance of the . . . property is avoidable as a § 547 preference transfer, [debtor's wife] cannot benefit [as a good faith transferee] from the § 548(c) defense.").

2. The presence of good faith depends upon whether the "transaction carries the earmarks of an arms-length bargain." Bullard v. Aluminum Co. of Am., 468 F.2d 11, 13 (7th Cir. 1972) (citation omitted). To show good faith, the transferee must show "(1) an

honest belief in the propriety of the activities in question; (2) no intent to take unconscionable advantage of others; and (3) no intent to, or knowledge of the fact that the activities in question will hinder, delay, or defraud others." Southern Indus., Inc. v. Jeremias, 66 A.D.2d 178, 183, 411 N.Y.S.2d 945, 949 (App. Div. 2d Dept 1978). The Second Circuit has broadly defined good faith, finding a lender has no fiduciary duty to its borrower or other creditors. Sharp Int'l Corp. v. State Street Bank & Trust Co. (In re Sharp Int'l Corp. & Sharp Sales Corp.), 403 F.3d 43, 52 (2d Cir. 2005) (Sharp raised new funds from its Noteholders to pay off its debt to a bank, the bank "gave no warnings and blew no whistles, ignored inquiring calls from the Noteholders, preserved Sharp's line of credit when it had the right to foreclose and pull the plug, and gave [the borrower] its needed consent to the new indebtedness. . . . One could say that [the bank] failed to tell someone that his coat was on fire; or one could say that it simply grabbed a seat when the music stopped. The moral analysis contributes little. Whatever [the bank] knew about [management's] fraud, [it came] by that information through diligent inquiries that any other lender could have made. Sharp fails to identify any duty on [the bank's] part to precipitate its own loss in order to protect lenders that were less diligent."); see generally M. Cook & A. Pustilnik, Key Creditors' Rights Decision, The Bankruptcy Strategist, July 2005 (analyzing In re Sharp Int'l Corp.). The Seventh Circuit reached the same result in B.E.L.T., Inc. v. Wachovia Corp., 403 F.3d 474, 476 (7th Cir. 2005), ("Illinois, like most other states, does not require business ventures to do good turns for their rivals."); In re Actrade Financial Technologies Ltd., 337 B.R. 791, 810 (Bankr. S.D.N.Y. 2005) (following Sharp and applying its rule to the Bankruptcy Code, dismissed intentional fraudulent transfer claim because no specific allegation was made that defendant "was complicit with or had knowledge of an intentional scheme to defraud creditors") (Groppe, J.).

3. Knowledge by the transferee of the insolvency of the debtor at the time of the transfer may refute a claim of good faith on the part of the transferee. Meeks v. Red River Entm't of Shreveport (In re Armstrong), 285 F.3d 1092 (8th Cir. 2002) (held, casino had not acted in good faith when it accepted payment from financially troubled debtor; record showed that it had failed to check true extent of debtor's assets and liabilities; it had previously increased his credit line, with actual knowledge of a tax lien having been filed against him; casino also ignored borrowing of funds by debtor's friend for him to keep gambling; casino also knew of a tax lien asserted against debtor's bank account; moreover, the casino had acknowledged in its files that debtor was in "over his head"; bankruptcy court had found as a matter of fact that debtor had actually intended to hinder, delay or defraud his creditors, but that casino was insulated from liability as "good faith" transferee; district court and Eighth Circuit found that casino had acted in bad faith, reversing the bankruptcy court's decision as "clearly erroneous."); Torcise v. Community Bank of Homestead (In re Torcise), 116 F.3d 860, 869 (11th Cir. 1997) (held, any error in failing to submit good faith defense jury instruction on actual fraud claim against bank was harmless because evidence would not have supported finding that bank acted in good faith when bank had knowledge of debtor's fraud and insolvency and had control over the disposition of the debtor's receivables); Jahn v. Fassnacht (In re A. Fassnacht & Sons), 826 F.2d 458, 463 (6th Cir. 1987) (in context of alleged preferential transfer, transfer not executed in bad faith when no evidence that transferee had any knowledge of imminent insolvency); United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986) (transferee lacks good faith when it knows debtor would receive no consideration and would be rendered insolvent as result of transfer), cert. denied, 483 U.S. 1005 (1987). See Redwood Raevine Corp.

v. Hayes (In re Hannover Corp.), 310 F.3d 796, 800 (5th Cir. 2002) (held, independent third party unaffiliated with debtors acted in good faith when it accepted payments from debtors on contract that had been negotiated at arms-length; transferee's "state of mind" important; no way of learning of debtor's insolvency; knew of SEC suit from newspapers; but "undertook its own investigation, contacting the SEC and the . . . court . . . receiving assurances . . . from the . . . court . . ."); Atlanta Shipping Corp. v. Chemical Bank, 818 F.2d 240, 249 (2d Cir. 1987) (lender with knowledge of debtor's poor financial condition does not lack good faith if it knows loan proceeds will repay creditor indebtedness and not adversely affect debtor's balance sheet); Sharp Int'l Corp. v. State Street Bank & Trust Co. (In re Sharp Int'l Corp. & Sharp Sales Corp.), 403 F.3d 43, 55 (2d Cir. 2005) (secured lender was not liable for aiding and abetting management's breach of fiduciary duty, and not liable for receiving a \$12 million loan repayment from a closely held borrower it correctly suspected of engaging in massive fraud, because it did not participate in the fraud itself.).

4. Good faith "should be measured objectively," and "if the circumstances would place a reasonable person on inquiry of a debtor's fraudulent purpose, and a diligent inquiry would have discovered the fraudulent purpose, then the transfer is fraudulent." Jobin v. McKay (In re M & L Business Machine Co.), 84 F.3d 1330, 1338 (10th Cir. 1996), cert. denied, 117 S. Ct. 608 (1996) (citation omitted) (investor in Ponzi scheme not entitled to claim good faith when he should have known of the fraudulent intent); Warfield v. Byron, 436 F.3d 551, 560 (5th Cir. 2006) (finding strong likelihood investor in Ponzi scheme could not establish good faith under objective standard because of his "failure to inquire about [Ponzi scheme] more closely, in light of the abundant suspicious information he possessed about the people, the scheme, and the previous schemes"). Thus, "[t]he personal good faith of the [transferee] will not avail him as a defense if he acted with full knowledge of facts and circumstances which put him on inquiry." Chorost v. Grand Rapids Factory Showrooms, Inc., 77 F. Supp. 276, 281 (D.N.J. 1948), aff'd, 172 F.2d 327 (3d Cir. 1949). See Sherman v. Third National Bank (In re Sherman), 67 F.3d 1348, 1355 (8th Cir. 1995) (held, transferees lacked good faith under section 548(c) of Code when "they were aware of sufficient facts concerning the debtor's precarious financial situation to place [them] on inquiry notice of debtor's insolvency and looming bankruptcy.") (emphasis added). See also Stoebner v. Lingenfelter, 115 F.3d 576, 579 (8th Cir. 1997) (defendant-transferee failed to carry "the substantial burden necessary" to warrant judgment as a matter of law on his "'good faith for value' defense," where defendant "presented little more than his personal background to demonstrate that he acted in good faith"; defendant's "scant offer of proof barely challenged" trustee's "voluminous evidence" that debtor received no value for payments it made to defendant).

5. Conscious disregard of facts that would put one on notice to investigate facially suspect transactions negates a good faith defense. Huffman v. Commerce Security Corp. (In re Harbour), 845 F.2d 1254, 1258 (4th Cir. 1988) (initial transferee, who was mother of ultimate transferee and close friend of debtor transferor, and who held funds for no longer than one day, was not good faith transferee when she failed to investigate transaction which she knew had no apparent business purpose).

6. Transfers made to one in a fiduciary capacity toward the debtor may be scrutinized with particular care. Burroughs v. Fields, 546 F.2d 215, 218 (7th Cir. 1976)

(good faith of corporate officer and director transferee was lacking when he should have been on notice as to corporation's shaky financial condition at time of transfer).

7. A transferee who coerces the debtor into signing a third mortgage lacks good faith under section 548(c). Reaves v. Sunset Branch, Nat'l Bank of South Dakota (In re Reaves), 8 B.R. 177, 182 (Bankr. D.S.D. 1981).

8. One court held that a finding of actual intent to defraud under section 548(a)(1) "precludes the possibility of a [section] 548(c) lien because good faith does not exist where there is actual intent to defraud." Consove v. Cohen (In re Roco Corp.), 21 B.R. 429, 436 (B.A.P. 1st Cir. 1982) (court apparently so held because of intrafamily nature of transaction), aff'd, 701 F.2d 978 (1st Cir. 1983); see, e.g., Dean v. Davis, 242 U.S. 438, 445 (1917) (when debtor's transferee brother-in-law, who knew the facts, "cooperated in the [debtor's] fraudulent purpose").

9. A defendant's failure to raise the § 548(c) lien offset may constitute a waiver. Buncher Co. v. Official Committee of Unsecured Creditors of Genfarm LP IV, 229 F.3d 245, 253 (3d Cir. 2000) (affirming defendant "waived the lien issue by failing to raise it in the Bankruptcy Court."); United States v. Westley, 7 Fed.Appx. 393, 401, 406 (6th Cir. 2001) (distribution of corporation's assets to its shareholders constituted fraudulent transfer, but government's failure to respond to bankruptcy court's order to file a proof of claim and a request for dischargeability barred it from challenging debt's dischargeability thereafter); Nicolaci v. Anapol, 387 F. 3d 21, 27 (1st Cir. 2004) (common-law right of indemnity does not apply to fraudulent transfer claim asserted by chapter 7 trustee against debtor's former shareholders based on pre-petition stock purchase transaction.).

10. Affirmative defense under section 548(c) is based upon "value given" and "good faith" rather than the impact of the transaction upon the estate. In re Fin. Federated Title & Trust, Inc., 309 F.3d 1325, 1332-1333 (11th Cir. 2002) (defendant allegedly received fraudulent transfers as part of Ponzi scheme not barred as a matter of law to demonstrate value of services rendered to debtor and whether those services were rendered in good faith; defendant's services deepened debtor's insolvency and may have been part of fraudulent transfer; however, services provided did constitute value; upon remand, court must determine whether those services represented reasonable equivalent value to the payments defendant received); Securities and Exchange Commission v. Res. Dev. Int'l, LLC, 487 F.3d 295, 302 (5th Cir. 2007) (held, good faith defense failed because defendants could not show they exchanged reasonably equivalent value for transfer from "debtor."); Warfield v. Byron, 436 F.3d 551, 560 (5th Cir. 2006) ("The primary consideration in analyzing the exchange of value for any transfer is the degree to which the transferor's net worth is preserved"; held, investor in Ponzi scheme could not argue his broker services to Ponzi scheme were reasonably equivalent value for transfers received under UFTA: "It takes cheek to contend that in exchange for the payments he received, the ... Ponzi scheme benefited [sic] from his efforts to extend the fraud by securing new investments").

C. Subsequent Transferees. Under section 550(a)(2), once a transfer has been avoided under applicable provisions of the Code, the trustee may recover the property or its

value from the immediate or mediate transferee. See, e.g., Consove v. Cohen (In re Roco Corp.), 701 F.2d 978 (1st Cir. 1983) (debtor's redemption of president/director/sole stockholder's shares held fraudulent; return of payments ordered); In re Int'l Admin. Services, Inc., 408 F.3d 689, 706-07 (11th Cir. 2005) ("once the plaintiff proves that an avoidable transfer exists[,] he can then skip over the initial transferee and recover from those next in line. . . . Certainly, the plaintiff can pursue the initial transferee, but the plaintiff is not obligated to do so."). Section 550(d) provides that the trustee is entitled to only a single satisfaction. E.g., In re Prudential Lines of Florida Leasing, Inc., 478 F.3d 1291, 1301 (11th Cir. 2007) (trustee settled \$10 million fraudulent transfer suit against multiple defendants for \$3.9 million; after settlement, trustee filed fraudulent transfer suit against additional party to recover difference; held, subsequent suit did not violate section 550(d); "[s]ection 550(d) limits the trustee to a 'single satisfaction': no more and no less.").

If an immediate or mediate transferee takes "for value, . . . in good faith, and without knowledge of the voidability of the transfer avoided," the trustee may not recover the property or its value from such immediate or mediate good faith transferee, 11 U.S.C. § 550(b)(1), or from a subsequent good faith transferee, 11 U.S.C. § 550(b)(2). See Max Sugarman Funeral Home, Inc. v. A.D.B. Investors, 926 F.2d 1248 (1st Cir. 1991) (even if property was acquired for value, lack of good faith enables trustee to recover such property). The good faith requirement "is intended to prevent a transferee from whom the trustee could recover from transferring [sic] the recoverable property to an innocent transferee, and receiving a retransfer from him, that is, 'washing' the transaction through an innocent third party." H.R. Rep. No. 595, 95th Cong., 2d Sess. 376, reprinted in 1978 U.S.C.C.A.N. 5963, 6332. See Davis v. Cook Constr. Co. (In re SLF News Distributions, Inc.), 649 F.2d 613 (8th Cir. 1981) (held, defendant in fraudulent transfer action, that had released mechanic's lien in exchange for \$10,000 certified check without knowledge that funds came from insolvent debtor rather than from entity on whose property it held lien, was protected good faith secondary transferee, from which trustee could not recover \$10,000); Kuhn v. Nance (In re Nance), 26 B.R. 105 (Bankr. S.D. Ohio 1982) (debtors fraudulently transferred property to defendants for less than fair value, and defendants later sold property at profit; held, trustee could not recover property from subsequent good faith transferees, but could recover profit earned by defendants); see also Carr v. Demusis (In re Carr), 34 B.R. 653 (Bankr. D. Conn. 1983) (grossly inadequate price prevented immediate transferee from establishing good faith), aff'd, 40 B.R. 1007 (D. Conn. 1984). But see Burtrum v. Laughlin (In re Laughlin), 18 B.R. 778 (Bankr. W.D. Mo. 1982) (after transfer to initial transferees was voided under applicable state law, bankruptcy court permitted trustee to (1) recover property from subsequent good faith transferees or (2) recover value of property, less amount already paid for property by good faith transferees; court apparently construed "value" in section 550(b)(1) to mean "fair market value"). In Fargo Biltmore Motor Hotel Corp. v. Metropolitan Fed. Bank (In re Fargo Biltmore Motor Hotel Corp.), 45 B.R. 568 (Bankr. D.N.D. 1984), the court issued a preliminary injunction preventing a foreclosing creditor from transferring property to a good faith transferee pending the resolution of a Durrett-type avoidance proceeding.

Although a subsequent transferee is not obligated to inquire into voidability, he may not ignore indications that the transfer may be fraudulent in order to avoid knowledge of the voidability of the transfer. Sherman v. Third National Bank (In re Sherman), 67 F.3d 1348, 1357 (8th Cir. 1995) (transferee with knowledge of at least three badges of fraud with respect to

transfer of property held to have had knowledge of voidability of transfer; "if transferee possesses knowledge of facts that suggest a transfer may be fraudulent, and further inquiry . . . would reveal facts sufficient to alert him that the property is recoverable, he cannot sit on his heels, thereby preventing a finding that he has knowledge."); Bonded Fin. Servs., Inc. v. European Am. Bank, 838 F.2d 890, 898 (7th Cir. 1988) (failure to make inquiry did not permit court to attribute to transferee knowledge of voidability of transaction; "'Knowledge' is a stronger term than 'notice'. A transferee that lacks information necessary to support an inference of knowledge need not start investigating on his own."); Bressman v. Bressman (In re Bressman), 327 F.3d 229 (3d Cir. 2003) (held, law firms were "good faith" transferees who took "for value . . . and without knowledge of the voidability of the transfer avoided"; counsel could keep legal fees received in good faith from debtor's fraudulently transferred assets); In re First Independence Capital Corp., 181 Fed.Appx. 524 (6th Cir. 2006) (subsequent transferee found not to have "knowledge" that transfer may be fraudulent when other legitimate explanations for the transfers existed and inquiry would be fruitless since "the party seeking to use the funds for his own benefit was also the only party to whom the bank could make inquiry").

Under section 550(e), a good faith transferee who is liable for property transferred retains a lien on the property to the extent of the lesser of the cost, to the transferee, of any improvements made after the transfer, or the increase in value of the property as the result of such improvements. Section 550(e) prevents a windfall addition to the estate of the cost of post-transfer improvements to the property by the subsequent transferee. Beck v. Amato (In re Amato), 10 B.R. 120, 123 (Bankr. S.D. Fla. 1981).

VIII. Enjoining Anticipated Fraudulent Transfers

A creditor who learns of the debtor's intent to transfer property fraudulently may seek a temporary restraining order and preliminary injunction enjoining the transfer. See, e.g., Republic of the Philippines v. Marcos, 806 F.2d 344 (2d Cir. 1986) (preliminary injunctions are proper to prevent defendant from making judgment uncollectible), cert. denied, 481 U.S. 1048 (1987). It is unusual, however, for a court to grant the application if the creditor does not have a lien on the specific property about to be transferred. See Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc., 527 U.S. 308 (1999) (5-4) (unsecured creditor suing to collect debt held not entitled to preliminary injunctive relief under Fed. R. Civ. P. 65 to prevent debtor's asserted dissipation of assets prior to judgment); Credit Agricole Indosuez v. Rossiyskiy Kredit Bank, 94 N.Y.2d 541 (2000) (reasoning that under New York law "a general creditor has no legally recognized interest in or right to interfere with the use of the unencumbered property of a debtor prior to obtaining judgment."); Martin v. James B. Berry Sons' Co., 83 F.2d 857, 861 (1st Cir. 1936) ("[a] creditor without such lien cannot obtain an injunction to prevent the debtor from disposing of his property, although he has reason to apprehend that such disposition may be fraudulent."); but see Federal Deposit Ins. Corp. v. Bell, 106 F.3d 258, 265 (8th Cir. 1997) (affirming, inter alia, district court's grant of injunctive relief under Arkansas Fraudulent Transfer Act in favor of bank, as judgment creditor, to protect the judgment entered in favor of bank and prevent defendants from "transferring or encumbering certain assets"), reh'g and suggestion for reh'g en banc denied, (1997). Several Circuits have held that a preliminary injunction is appropriate when equitable relief is sought. Rubin v. Pringle (In re Focus Media), 387 F.3d 1077, 1084 (9th Cir. 2004) (held, when legal and equitable claims for relief are made in the

bankruptcy and fraudulent transfer context, preliminary injunction is appropriate), cert. denied, 161 L. Ed. 2d 482, 125 S. Ct. 1674, 2005 U.S. LEXIS 2497, 73 U.S.L.W. 3555 (U.S. 2005); see also United States v. Oncology Assocs., P.C., 198 F.3d 489, 497 (4th Cir. 1999) (upholding issuance of a preliminary injunction when equitable relief was sought); CSC Holdings, Inc. v. Redisi, 309 F.3d 988 (7th Cir. 2002) (same). Courts are also likely to enjoin a proposed fraudulent transfer if it can be shown that the debtor would be acting with actual fraudulent intent. See, e.g., Green v. Drexler (In re Feit & Drexler, Inc.), 760 F.2d 406, 416 (2d Cir. 1985) (injunction issued to prevent transfer of property of defendant who repeatedly and intentionally attempted to hide assets).

The amount of harm an injunction may potentially cause the defendant is also an important factor. If the injunction is structured to create only a minimal interference with the defendant's activities, the creditor will be more likely to obtain the requested relief while the court and all parties in interest have an opportunity to investigate further the possibility of fraudulent activity. See Unsecured Creditors' Comm. of DeLorean Motor Co. v. DeLorean (In re DeLorean Motor Co.), 755 F.2d 1223 (6th Cir. 1985) (creditors sued to have assets of nondebtor entity made part of bankruptcy estate on theory that assets were fraudulently diverted to nondebtor entity; when owner of both entities attempted to sell nondebtor entity, court permitted sale but enjoined owner from disposing of proceeds, pending further investigation of creditors' allegations).

The burden of proof is on the creditor to show the fraudulent nature of the transfer, as well as the usual preliminary injunction requirements of irreparable harm and likelihood of success on the merits. The requirements for the Resolution Trust Corporation to obtain a preliminary injunction to enjoin a fraudulent transfer are less stringent than for other types of creditors. See Resolution Trust Corp. v. Cruce, 972 F.2d 1195, 1198-1200 (10th Cir. 1992) (RTC need not show irreparable injury, only some showing of injury; 18 U.S.C. § 1821(d)(19); RTC need only show "fair ground for litigation" rather than substantial likelihood of success on merits, even when relaxed injury standard applies). The creditor will generally be required to furnish a bond to cover the debtor's damages in the event the debtor is wrongfully enjoined. See Fed. R. Civ. P. 65.

IX. Remedies Against Entities That Facilitate Fraudulent Transfers

Courts have applied various remedies against a person who facilitates a fraudulent transfer. Possible remedies include avoidance of a lien or underlying obligation. The Code provides that "[t]he trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor. . . ." 11 U.S.C. § 548(a). See also UFCA § 9(1) and § 10; UFTA § 7(a). For example, in United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1986), cert. denied, 483 U.S. 1005 (1987), the court's remedy in the case of an intentionally and constructively fraudulent transfer was to set aside the mortgages given to the asset-based lender. See also In re Process-Manz Press, Inc., 236 F. Supp. 333 (N.D. Ill. 1964) (court voided liens and subordinated claims of secured lender that advanced money for corporation to purchase and redeem shares, which transaction rendered corporation insolvent), rev'd on other grounds, 369 F.2d 513 (7th Cir. 1966), cert. denied, 386 U.S. 957 (1967); Chemical Bank v. Coan, No. 99-7427, WL 99815 (2d Cir. Feb. 2, 2001) (Conn. statute provides that a court may avoid the

fraudulent transfer and impress a constructive trust on the transferee); In re Carlson, 263 F.3d 748 (7th Cir. 2001) (debtor attorney fraudulently concealed interest in contingency fee by transferring fee to partner under practice merger agreement and ordered to show cause why debtor and partner should not be disciplined for professional misconduct).

In addition to voiding the lien or underlying obligation, a court may order the equitable subordination of the lender's claim. Section 510(c) of the Code provides that the court may

(1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim . . . or

(2) order that any lien securing such a subordinated claim be transferred to the estate.

11 U.S.C. § 510(c)(1) and (2).

In Murphy v. Meritor Sav. Bank (In re O'Day Corp.), 126 B.R. 370 (Bankr. D. Mass. 1991), the court subordinated the lender's claims. This was a particularly severe remedy because the court found only a constructively fraudulent transfer. Equitable subordination has traditionally been used in cases of extremely inequitable or egregious conduct.

In Berquist v. First National Bank (In re American Lumber Co.), 5 B.R. 470 (D. Minn. 1980), the bank dominated and controlled the debtor to the extent of ensuring that its advances to the debtor were used solely for the purpose of protecting property on which the bank had a lien. Finding that the bank's advances were fraudulent transfers that disadvantaged other creditors of the debtor, the court ordered that the debtor's obligations to the bank were subordinated to the claims of other creditors. See Holt v. FDIC (In re CTS Truss, Inc.), 868 F.2d 146, 148-49 (5th Cir. 1989) (Fifth Circuit's criteria for equitable subordination as summarized in Benjamin v. Diamond (In re Mobile Steel Co.), 563 F.2d 692, 703 (5th Cir. 1977) -- "(1) whether the claimant engaged in fraudulent or inequitable conduct; (2) whether the conduct resulted in injury to creditors or gave an unfair advantage to the claimant; and (3) whether equitable subordination would be inconsistent with the bankruptcy law" (emphasis added) . . . may be deceptively broad. The courts have actually confined equitable subordination of claims to three general categories of cases: those in which a fiduciary of the debtor misuses his position to the disadvantage of other creditors; those in which a third party, in effect, controls the debtor to the disadvantage of others; and those in which a third party defrauds other creditors."); Boyajian v. DeFusco (In re Giorgio), 862 F.2d 933, 939 (1st Cir. 1988) (holding that creditor's claim would not be equitably subordinated absent showing of any particular inequity vis-à-vis other creditors).

X. Distinction From Preference

A preference voidable under section 547 of the Code is not the equivalent of a fraudulent transfer. Nicklaus v. Peoples Bank & Trust Co., 369 F.2d 683 (8th Cir. 1966). A preference is an infraction of the rule of equal distribution among all creditors; a fraudulent

transfer goes further, and by it the debtor seeks through deceitful means to secure a personal advantage out of what in law should belong to creditors and not to the debtor. 5 Collier on Bankruptcy, ¶ 547.01, at 547-9 (Lawrence P. King ed., 15th rev. ed. 1997). Preferences do not attempt to remove assets beyond creditors' reach, but merely favor one creditor or group of creditors over others; they are payments honestly owed. Fraudulent transfers, on the other hand, harm creditors in general by wrongfully depleting the estate. D.R. Cowans, Bankruptcy Law and Practice § 10.9(c), at 351 (1994). But see IV.G., supra.

**FRAUDULENT TRANSFERS:
STATUTORY CROSS-REFERENCE**

<u>Operative Voidable Transfers</u>	<u>UFTA</u>	<u>UFCA</u>	<u>Bankruptcy code (11 U.S.C.)</u>
1. Transfer with actual intent to hinder, delay, or defraud creditors	§4(a)(1) [Defense: §8(a)] (good faith buyer for equivalent value)	§7	§548(a)(1)(A)
2. Transfer by insolvent debtor	§5(a) [Defense: §8(e)] (§(e)(1) (lease termination); and §8(e)(2) (enforcement of Article 9 security interest))	§4	§548(a)(1)(B)(i)-(ii)(I)
3. Transfer by business debtor with unreasonably small capital	§4(a)(2)(i) [Defense: §8(e)]	§5	§548(a)(1)(B)(i)-(ii)(II)
4. Transfer by debtor about to incur debts	§4(a)(2)(ii) [Defense: §8(e)]	§6	§548(a)(1)(B)(i)-(ii)(III)
5. Insider transfers	§5(b) [Defense: §8(e); §8(f)(1) (subsequent new value); §8(f)(2) (ordinary course of business); §8(f)(3) good faith rehabilitation]	--	§548(a)(1)(B)(i)-(ii)(IV) [Extraordinary insider transfers for unfair value under employment contract; applies to cases commenced on or after April 20, 2005]

Statute of Limitations

§9 --
[later of 4 years or 1 year after transfer should
have been discovered: actual intent (§9(a));
4 years: constructive intent
(§9(b)); and
one year: insider transfer
(§9(c)).]

§546(a)(1)(A)-(B):
two years from order
for relief, or one year
from
election/appointment
of first trustee if that
occurs within first two
years of case.

Key Definitions

<u>Term</u>	<u>UFTA</u>	<u>UFCA</u>	<u>Bankruptcy Code (11 U.S.C.)</u>
"Claim"	§1(3)	--	§101(5)
"Creditor"	§1(4)	§1,¶4	§101(10)
"Debt"	§1(5)	§1,¶4	§101(12)
"Insider"	§1(7)	--	§101(31)
"Transfer"	§1(12)	§1,¶2 (defines "conveyance")	§101(54)
"Insolvency"	§2	§2	§101(32) (defines "insolvent")
"Value"	§3	§3 (defines "fair consideration")	§548(d)(2)(A) (defines "value")

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