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Attorney

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Of Counsel

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LIVE WEBCAST

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What You Need to Know About Fraudulent Conveyance Law

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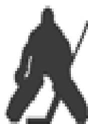

Michael Goldman & Associates, LLC
Certified Public Accountant
Certified Valuation Analyst, Certified Fraud Examiner

MIchael Goldman & Associates, LLC is a consulting practice focused on supporting stressed or distressed situations including insolvency, fraud, and litigation. The firm typically is referred into troubled situations by lawyers or lenders and provides services for plaintiffs, defendants, debtors, and creditors. Our variety of experience helps to provide a fresh perspective to the cases we assist in.

Horwood Marcus & Berk Chartered is recognized as a premier middle market business firm in Chicago, with a flexible team-building approach, access to a vast network of professionals and an unyielding commitment to service excellence. The firm combines the practice breadth and resources of a large commercial firm with the entrepreneurial atmosphere and creativity of a boutique.

The firm boasts depth and expertise in an array of legal areas: business law and planning; mergers, acquisitions and dispositions; banking, finance and securities; restructuring and creditors rights; state and local tax planning and litigation; real estate; zoning; commercial litigation; corporate and real estate financing and workout; estate and asset protection planning; probate; and trusts and estates litigation. Similarly, HMB serves clients in a myriad of industries throughout the country.

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What You Need to Know About Fraudulent Conveyance Law

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Brief Speaker Bios:

Mark Radtke

Mark Radtke is a member of Shaw Gussis Fishman Glantz Wolfson & Towbin LLC. He concentrates his practice in corporate reorganization, creditors' rights, bankruptcy and commercial litigation involving contract disputes, the Uniform Commercial Code, lien rights, employment issues, fraud, fiduciary duties and corporate governance. Mr. Radtke has represented debtors, trustees, assignees, committees, financial institutions, secured and unsecured creditors, interest holders, and both business entities and individuals in a variety of insolvency and commercial matters. Mr. Radtke has been a member of the American Bankruptcy Institute since 2002 and currently serves as the Co-Chair of the Young and New Members Committee.

In 1998, Mr. Radtke became a Certified Public Accountant in Illinois, though he is not currently licensed to practice public accounting. He is a graduate with high honors from Chicago-Kent College of Law, where he was an Executive Articles Editor for the Chicago-Kent Law Review and was elected to the Order of the Coif, a national honor society for scholastic achievement in law. Illinois Super Lawyers magazine has selected Mr. Radtke as an "Illinois Rising Star" in the 2008, 2009, 2010 and 2011 issues of Chicago Magazine. He has authored and co-authored articles and chapters on bankruptcy-related topics in various publications and has spoken on bankruptcy-related topics at regional and national conferences. Mr. Radtke is admitted to practice law in the State of Illinois; the United States District Courts for the Northern District of Illinois, Central District of Illinois and Eastern District of Michigan; and the United States Court of Appeals for the Seventh Circuit.

Michael Goldman

Michael Goldman is a Certified Public Accountant, a Certified Fraud Examiner, a Certified Valuation Analyst, and Certified in Financial Forensics. He has been qualified as an expert witness in both federal and state courts in the areas of Insolvency, Forensic Accounting, Business Valuation, Business Management, Accounting, and internal Control. Michael has served as a court-appointed examiner, and has worked as a forensic accountant for bankruptcy trustees, secured lenders, unsecured creditors, company owners, and the management teams of companies. He has performed forensic accounting in shareholder disputes, marital dissolution, commercial damages, bank fraud, embezzlement, skimming, and personal damage cases.

MIchael has authored chapters about insolvency or investigation of fraud in books published by the Association of Certified Fraud Examiners, the American Bankruptcy Institute, Westlaw, and Aspen Law and Business. He has also had articles published in numerous professional journals for both lawyers and accountants.

MIchael has a Bachelor of Arts degree from Rice University and a Master of Management degree from the J. L. Kellogg Graduate School of Management at Northwestern University. He currently teaches a course in Entrepreneurship at the Lake Forest Graduate School of Management.

Brief Speaker Bios:

George Spathis

George Spathis is of counsel at the Chicago law firm of Horwood Marcus & Berk Chartered. George is a seasoned trial lawyer with extensive experience in the area of bankruptcy litigation, having represented bankruptcy trustees, secured creditors, creditors committees, assignees and receivers in an array of complex litigation matters in a myriad of industries, and having counseled clients on issues relating to insolvency and dealing with businesses in distress. He has prosecuted and defended large fraudulent conveyance actions in Federal Courts throughout the country, and has authored and published numerous articles on the topic.

Prior to joining Horwood Marcus & Berk, George was a partner at Shaw Gusiss Fishman Glantz Wolfson and Towbin, a boutique commercial bankruptcy firm in Chicago. He is a Member of the American Bankruptcy Institute and the Turnaround Management Association.

George is a 1990 graduate of the Chicago-Kent Law School, with High Honors, and is a Member of its Order of the Coif. He served as an Executive Articles Editor for the Law Review and was elected to the inaugural class of the Kent Legal Scholars.

► *For more information about the speakers, you can visit:* http://www.knowledgecongress.org/speakers_2012_Fraudulent_Conveyance.html

Summary

Typically regarded as a collection resource for judgment creditors chasing “judgment proof” debtors, fraudulent conveyance laws are being invoked with vastly greater frequency and broader reach. Entities and individuals experiencing financial distress, as well as those who deal with such entities and individuals, regularly (and often unknowingly) walk a fine line that expose them to protracted and expensive litigation and potentially substantial adverse judgments.

In a two-hour live webcast, a panel of distinguished experts will discuss the following:

- A concise overview of applicable federal and Uniform state laws that govern fraudulent conveyance
- An overview of the elements of claims based upon alternative theories of actual and constructive fraud
- Emphasis on the principle elements involved: the “badges of fraud,” insolvency at the time of transfer, and the “reasonable equivalence” of value
- APractical litigation experiences, strategies and tips for asserting and defending against fraudulent conveyance discussion of recent developments in the law claims
- Case studies and real-life application of fraudulent conveyance laws and recognizing and avoiding exposure in cases premised upon constructive fraud

Featured Speakers:

SEGMENT 1:

Mark Radtke
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Shaw Gussis Fishman Glantz Wolfson & Towbin LLC

SEGMENT 2:

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Michael Goldman
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SEGMENT 3:

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SEGMENT 1:

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Introduction

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SEGMENT 1:

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Attorney
Shaw Gussis Fishman Glantz Wolfson & Towbin LLC

AGENDA: What You Need to Know About Fraudulent Conveyance Law – Part 1

- Overview of Fraudulent Conveyance Law
- Elements: Actual and Constructive Fraud (Bankruptcy Code and UFTA)
- Recent Developments

SEGMENT 1:

Mark Radtke
Attorney
Shaw Gussis Fishman Glantz Wolfson & Towbin LLC

Policy Considerations

- Actual Fraudulent Transfers
  - Bad Intent
- Constructively Fraudulent Transfers
  - Bad Economics; Intent Irrelevant
- Statutes Cover Both *Transfers of Property* and *Incurrence of Obligations*

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Statutorily Based

- Federal: Bankruptcy Code (11 U.S.C. § 548)
  - Section 548(a)(1)(A): Actual Fraud
  - Section 548(a)(1)(B): Constructive Fraud
- State: Uniform Fraudulent Transfer Act
  - Generally Analyzed Same as Federal Statute
  - Key Difference Is Look-Back Period: 2 Years vs. Up to 6 Years
  - Section 544 Enables Suit Under State Law
- Pleading Standards

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Actual Fraud

- Section 548(a)(1)(A) of the Bankruptcy Code provides that:

  The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred, 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…

- Generally focus on debtor, but heightened scrutiny for "insiders" and transferee's intent is imputed to debtor

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Badges of Fraud

- The transfer or obligation was to an insider;
- The debtor retained possession or control of the property transferred after the transfer;
- The transfer or obligation was not disclosed or concealed;
- Before transfer was made or obligation incurred, the debtor sued or threatened with suit;
- The transfer was of substantially all the debtor's assets;
- The debtor absconded;
- The debtor removed or concealed assets;
- The value of the consideration received by the debtor was not reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;
- The debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;
- The transfer occurred shortly before or shortly after a substantial debt was incurred; and
- The debtor transferred the essential assets of the business to a lien holder who transferred the assets to an insider of the debtor.

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Constructive Fraud

- Components of Constructive Fraud
  - Transfer of an interest of the debtor in property or any obligation incurred; and
  - Debtor voluntarily or involuntarily:
    - (1) Received less than reasonably equivalent value in exchange; and
    - (2) (A) Was insolvent or rendered insolvent; or
    - (B) Was left with unreasonably small capital; or
    - (C) Incurred debts that would be beyond the debtor's ability to pay as such debts matured; or
    - (D) Benefitted "insider" under an employment contract and not in the ordinary course of business.
- Measured at Date of Transaction; No Hindsight Permitted

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Insolvency Defined

- Condition where the sum of an entity's debts are greater than the value of its assets at "fair valuation." *11 U.S.C. § 101(32)(B)*
  - *Includes contingent assets and contingent liabilities*
- Fair valuation
  - "Going concern" vs. liquidation or distressed value
  - Determine what willing buyer would pay in an arm's length transaction for the debtor's entire package of assets and liabilities

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Undercapitalization

- Debtor may be technically solvent, but insufficient liquidity to conduct business makes bankruptcy or liquidation likely, if not imminent
- Thus, undercapitalization occurs when net working capital is maintained at unreasonably low levels (measured against industry peers) for a sustained period of time
- "Net Working Capital" represents operating liquidity and is calculated by subtracting current liabilities from current assets

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Inability to Pay Debts

- Requires contemporaneous intent or belief that subsequent creditors would not be paid as claims come due
- Intent can be inferred by facts and circumstances showing debtor could not have reasonably believed it would pay maturing obligations
- Not commonly litigated component; therefore less precedential authority

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Reasonably Equivalent Value

- Not Defined or Reduced to Mathematical Formula
- Depends on Circumstances:
  - Fair Market Value
  - Prevailing Economic Forces
- Measured From Creditor's Perspective as of Date of Transaction
- Quantifiable Indirect Benefits Considered

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Who Can Sue?

- Bankruptcy Code
  - Bankruptcy Trustee
  - Debtor in Possession
  - Creditors Committees
  - Plan Trustees
  - Any Creditor, if claim is abandoned
- UFTA
  - Any Creditor

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Who Can Be Sued?

- Avoidance (§ 548)
  - The party to the transaction
- Recovery (§ 550)
  - Initial Transferee
  - Entity for Whose Benefit Transfer Was Made
  - Immediate or Mediate Transferees of Initial Transferees

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Defenses to Avoidance

- Transferees who transact in good faith and for value (and can prove it) can lien or retain interest transferred or enforce an obligation incurred to the extent of the value that they gave (548(c) & (d))
- Transfers to certain qualified charities are not avoidable (548(a)(2))
- Other defenses under 546, 548 and 550

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What Can Be Recovered?

- Property or, if the court orders, the value of such property (§ 550(a)(2))
- Immediate or Mediate Transferee's Defenses to Recovery (§ 550(b))
  - Take for value, including satisfaction of antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; OR
  - Be an immediate or mediate good faith transferee of such transferee

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Recent Developments

- *Stern v. Marshall* (Supreme Court: Limits of bankruptcy court's constitutional power to enter final judgment)
- *TOUSA* (11th Circuit: Invalidating liens by subsidiaries to secure the new credit facilities of parent)
- *Paloian v. LaSalle Bank, N.A.* (7th Circuit: Contingent assets and contingent liabilities must be accounted for)
- *Boyer v. Crown Stock Distribution, Inc.* (7th Circuit: Not in clear just because debtor stayed in business for more than a year after transaction)
- *Chicago Tribune* (Strategies for skirting defenses under § 546)

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Introduction

Michael Goldman is a Certified Public Accountant, a Certified Fraud Examiner, a Certified Valuation Analyst, and Certified in Financial Forensics. He has been qualified as an expert witness in both federal and state courts in the areas of Insolvency, Forensic Accounting, Business Valuation, Business Management, Accounting, and internal Control. Michael has served as a court-appointed examiner, and has worked as a forensic accountant for bankruptcy trustees, secured lenders, unsecured creditors, company owners, and the management teams of companies. He has performed forensic accounting in shareholder disputes, marital dissolution, commercial damages, bank fraud, embezzlement, skimming, and personal damage cases.

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Outline

1. *varying methods of valuation*
2. *the art and science of valuing assets*
3. *determining insolvency*

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Accepted Methods of Valuation

- Income Approach
  - Conversion of expected future economic benefits (income, cash flow, etc.) to present value.
- Market Approach
  - Comparison of subject company to historical transactions from private databases or public markets
- Asset Approach
  - Build-up of appraisals of the existing individual assets and liabilities of the company.

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Income Approach

- Theoretically the most correct approach, widely used in financial markets and well accepted in court proceedings
- Requires evaluation of financial markets and assessment of market, industry, and specific company risks.
- Based on expectations and projections of the future. Difficult to use in start-ups, high-growth companies, or situations in extreme flux.
- Results are highly sensitive to the facts used and assumptions made.

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Market Approach

- Market is the final arbiter of value, most judges and juries are familiar with market methods (think of shopping for a new house)
- Often difficult to find sufficiently comparable companies
- Adequate information about companies being used for comparison is usually not available
- Need to be able to focus on specific factors that drive or detract from value

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Asset Approach

- Easy to understand
- Valuation of intangible assets, contingent liabilities may be considered speculative.
- Piece-by-piece approach is of questionable relevance when valuing a going concern operation.
- Least relevant method when valuing companies with high-growth potential, significant intellectual property, important contractual rights, or significant goodwill.

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Overlap of Methods of Valuation

- The three methods overlap somewhat – the market value of a business is based on its benefit stream, the assets are valued in large part based on market prices and the benefits they can generate, and the value of a benefit stream is dependent on market conditions.

- In theory, the three methods should give similar results. If not, they must be reconciled and the differences must be understood.

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The art and science of Valuation

- The value of a company is dependent on the assets in place and the benefit streams being generated at the time of the valuation. Since we are talking about distressed companies, those assets likely are not generating enough cash to pay the liabilities that are encumbering them.
- In healthy companies, a large component of the value is often the company's growth prospects and anticipated profitability. In a distressed company, growth and profitability are often non-existent or negative.

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Inherent conflict

- The valuation of a company should be premised upon its future earning capacity, free of impact of specific distress or past mismanagement.
- See, e.g., Consolidated Rock Products Co., v. Du Bois, 312 U.S. 510, 526 (1941)
- However, the more speculation (as to future results) a valuation contains, the more it needs to be discounted (i.e. lower valuation) and the more the valuation is likely to be ruled inadmissible by the court.

Value is hard to discern and often a point of contention

Would you have invested?

Microsoft Corporation, 1978

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Value is determined by the market and by identification of risk

- The risks potentially impacting a company's anticipated benefit stream are evaluated by considering factors such as the quality of the management team and operations, the company's ability to execute on its business plans, financial strength and ability to finance its planned activities, the probability of survival, political factors, industry factors, competitive factors, the longevity of customers, and the size of the market.
- These often include factors that led to the company's distress. To the extent that success factors are missing or impaired, the company's value will be lower.

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Problems in Valuing Distressed Companies

- Management is often in denial or clueless, and possibly committing fraud
- Cost-of-capital models are for going concern entities. Distressed firms have severely restricted access to capital and often only at vulture prices.
- There are often considerable disagreements as to whether the declines can be reversed
- Context is particularly significant when valuing distressed companies

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Characteristics of companies in decline

- Declining working capital, sales, margins, and profits.
- Increased aging of receivables, payables, and inventory
- Disruptions in operations due to shortages, quality problems, etc. lead to increasing customer dissatisfaction
- Mismatch between strategic needs and available capital
- Low employee morale, high or key turnover
- Lack of timely and accurate information
- Management is more reactive than proactive

These would all negatively impact the analysis of value

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Insolvency defined:

- The Code defines "insolvent" as a condition where the sum of an entity's debts are greater than the value of it's assets at "fair valuation." 11 U.S.C. § 101(32)(B)
- Fair valuation generally contemplates a "going concern" value rather than liquidation or distressed value, and is intended to estimate the price that a willing buyer would pay in an arm's length transaction for the debtor's entire package of assets and liabilities

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Determining Insolvency

- The balance sheet is the starting point, not the end point of the analysis. Book value does not equal "fair value"
- Accounting has archaic rules that can often keep significant value (such as Coke's secret formula) off of the balance sheet.
- Incompetent or fraudulent accounting practice can often make the balance sheet look much healthier than it actually is.
- Defendants in avoidance actions often see value that is highly subjective as to both existence and amount.
- Adjust every element of the balance sheet, including assets or liabilities not recorded or improperly stated, to fair value for every time period under consideration.

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Inability to pay debts

- In determining a debtor's insolvency for purposes of avoiding a transfer under § 548(a), the ability to pay debts as they mature is irrelevant if the insolvency is clearly demonstrated under the balance sheet test
- Since balance sheet solvency is often arguable, inability to pay debts is often used as a supplemental or alternative argument.

Ability to pay debts as they become due

- A company can appear solvent on the balance sheet, but still not be able to pay its bills as they become due. Evidence of this includes:
  - Aged accounts payable, Cash consistently overdrawn, Checks being held before mail
  - Vendors accepting steep compromises for either more immediate payment or more security
  - Churning of vendors, vendors constantly being replaced
  - Difficulty sourcing required materials, being forced to pay COD or CIA
  - Decreases in gross margin due to higher sourcing costs, decreases in both quality and quantity of inventory due to availability restrictions
  - Excess labor costs due to spurts in production when materials arrive sporadically
  - Significant delay in routine required payments that generate slow responses to non-payment, such as trust fund taxes and pension obligations.
  - Large amounts of cancelled customer orders or product returns
  - Management acting reactively instead of proactively
  - Higher than normal stress levels in employees, significant turnover in management ranks
  - Lawsuits filed for non-payment
  - Internal chaos

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Unreasonably Small Capital

- The concept of unreasonably small capital is intended to show that a debtor is or was likely to become insolvent at a future time. The key issue is will or did the busineass have sufficient cash flow to execute its business plan.
- Arguing unreasonably small capital is usually based on arguing the reasonableness of management's plans and projections, and is therefore significantly more speculative than the other two solvency tests.

Case Study #1 – Medical Practice

- Issue was fraudulent conveyance in the purchase of a specialty medical practice.
- Two competing expert valuations of the practice based on the exact same set of facts – one came in at $80,000 (asset method) and the other was in excess of $5 million (income method)
- Points of contention were whether or not significant goodwill existed (it did) and whether that goodwill belonged to the debtor corporation (it did not) or the doctor personally.
- Key factors were in determining what drove the income and the value of the practice, and who was able to benefit from the resulting income streams and value. Was it the practice itself, or the doctor's personal reputation that was generating income?
- In deposition the doctor defeated himself by clearly describing the goodwill as his personal goodwill and not related to the bankrupt medical practice. He strongly argued that he was the reason that patients came to his practice, it was the strength of his reputation that generated referrals and not the practice name, location, equipment, etc.

Case Study #2 – Retail Company

- Retail company was arguably insolvent for 30 months prior to its bankruptcy filing. Book value was negative for 18 months prior to filing.
- There were inaccuracies in the financial statements – store costs that should have been expensed were capitalized, inventory was improperly accounted for and potentially overstated.
- Defendants claimed there was considerable unrecorded goodwill in the stores' name and even more unrecorded value in the leases, which they claimed were all at below market rates.
- Facts showed that this was the chain's second bankruptcy and that nobody bought either the name or the leases in either asset sale. Profitability was less than at comparable stores in comparable markets, indicating lack of goodwill or better-than-market advantages.
- Company demonstrated repeated inability to pay its obligations as they became due since shortly after its inception.

Case Study #3 – Manufacturer

- Debtor may have been insolvent on a balance sheet basis for 4 years prior to filing:
  - Accounts receivable and inventory were both consistently overstated on the balance sheet
  - Accounts payable and warranty costs were both consistently understated on the balance sheet
  - Fixed assets never generated a profit in place and were very expensive to move, yielding very little going concern or liquidation value.
  - $4 million of capitalized software development costs for a customized system that was never implemented sat on the balance sheet as an asset for 3 years before being written off. Most of these costs were internal labor that were probably ineligible for capitalization under proper accounting procedures.

- Inability to pay debts as they became due:
  - Company was in work-out with its bank for 7 continual years and violated virtually every covenant and restructuring agreement it ever agreed to. Transgressions continued on a quarter-by-quarter basis.
  - On-going pattern of vendor compromises and conversion of short-term payables to long-term notes (which were also not paid). In-between compromises the payables aged significantly.
  - Continual inability to collect accounts receivable within terms, generating on-going liquidity shortfalls
  - 5 consecutive years of large negative EBITDA. Even the income from cancellation of debt was not sufficient to make EBITDA positive.

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Certified Valuation Analyst, Certified Fraud Examiner

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Introduction

George Spathis is of counsel at the Chicago law firm of Horwood Marcus & Berk Chartered. George is a seasoned trial lawyer with extensive experience in the area of bankruptcy litigation, having represented bankruptcy trustees, secured creditors, creditors committees, assignees and receivers in an array of complex litigation matters in a myriad of industries, and having counseled clients on issues relating to insolvency and dealing with businesses in distress. He has prosecuted and defended large fraudulent conveyance actions in Federal Courts throughout the country, and has authored and published numerous articles on the topic.

Prior to joining Horwood Marcus & Berk, George was a partner at Shaw Gusiss Fishman Glantz Wolfson and Towbin, a boutique commercial bankruptcy firm in Chicago. He is a Member of the American Bankruptcy Institute and the Turnaround Management Association.

George is a 1990 graduate of the Chicago-Kent Law School, with High Honors, and is a Member of its Order of the Coif. He served as an Executive Articles Editor for the Law Review and was elected to the inaugural class of the Kent Legal Scholars.

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Overview:

- Litigations experiences, strategies and tips
- Case studies and application of fraudulent conveyance laws
- Recognizing and avoiding exposure in cases premised upon constructive fraud

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Section 541 defines **"Property of the Estate"** broadly to include tangible and intangible property, legal and equitable interests, as well as causes of action….

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The Source of Avoidance Powers

The Code confers standing upon Debtors to pursue fraudulent conveyance actions on behalf of their creditors holding allowable unsecured claims who, ***but for*** the commencement of the Debtors' bankruptcy cases, could have challenged the Debtors' pre-petition transfers **under applicable law.**

11 U.S.C. § 544(b)(1)

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Based on information that is known or knowable

"[T]he job of the valuation expert is to look at the information that's available and use that available information in an appropriate fashion to predict what's likely to take place in the future…[I]n general, looking at the currently available data and projecting the future returns consistent with that data is what's required…."

Hon. Eugene R. Wedoff, Chief Judge
United States Bankruptcy Court, N.D. IL

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Measured from the Creditors' Perspective

"The purpose of [Section 548] is estate preservation; thus, the question whether the debtor received reasonably equivalent value must be determined from the standpoint of creditors….The touchstone is whether the transaction conferred realizable commercial value on the debtor reasonably equivalent to the realizable commercial value of the assets transferred."

Mellon Bank, N.A. v. Metro Communications, Inc., 945 F.2d 635, 646-47 (3d Cir. 1991)

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In re: McCook Metals, LLC

- Struggling privately held aluminum sheet manufacture picked expensive antitrust fight with industry heavyweight, Alcoa
- Litigation settled through agreement to divest Longview, WA smelting plant, ensuring McCook access to critical raw material
- With outlook for McCook bleak, Members formed new LLC to buy the Longview plant; McCook was repaid for expenses incurred, but received no membership interest in new LLC
- After McCook (and later, Longview) failed, Trustee sought to avoid transfer under § 548 as actually and constructively fraudulent, and recover value from controlling member

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In re: McCook Metals, LLC

- A corporate opportunity qualifies as "an interest in property," the transfer of which may be avoided under section 548.

- Reimbursement to McCook of the $7.8 million in expenses it incurred in pursuing the opportunity was not a substitute for the value of the opportunity.

- Majority member plainly and predictably stood in a position to directly benefit from the transfer, and thus was an entity for whose benefit the transfer was made (to the extent of membership interest)

Baldi v. Lynch, et al., (In re McCook Metals, LLC), 319 B.R. 570 (Bankr. N.D. Ill. 2005)

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Cornerstone Center

- two member, single asset entity that developed strip mall
- one member's financial struggles prevented him from infusing his share of capital to meet needs of LLC facing "perfect storm"
- short term loan between members secured by interest in Membership interest in the property; default and "foreclosure" ensued
- after Member's personal bankruptcy, Trustee sought to avoid the transfer of the Membership interest as both actually and constructively fraudulent
- vastly different opinions regarding the value of the 50% interest in the LLC

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Cornerstone Center

- The code applies to involuntary transfers

- Bankruptcy schedules did not paint a pretty picture, but still did not adequately prove insolvency at the time of transfer

- valuation turned, in large part, on the appropriate discounting of a non-controlling membership interest in LLC

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In re Trailmobile Trailer, LLC

- Carefully crafted corporate restructuring isolated risk of volatile manufacturing division in new stand-alone LLC
- LCC enjoyed banner years, paid all its trade debts, but never made accrual for looming subordinated debt
- After major industry downturn forced liquidation, Creditors' Committee sought to recover $10 M in distributions to members under tax sharing agreement

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In re Trailmobile Trailer, LLC

- Insolvency can take extremely subtle form
- Where LLC elects flow through taxation, the obligation to pay taxes falls on the members
- LLC (its creditors) received no value from tax distributions to members
- extreme risks of maintaining a “business as usual” attitude through financially precarious times

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ABC NACO v. Matrix Metals

- Struggling publicly traded rail supply company facing Bank mandate to substantially pay-down debt; bows to pressure, chases recovery
- Hires Investment Banking firm to market the assets of its healthiest division to select strategic and prospective financial buyers
- Sophisticated insider belatedly matches highest sealed bid, but strategically lowers offering price during due diligence
- Buys assets at “attractive price” and makes $15 M convertible bridge loan to company…which failed within the year
- Debtor sought to avoid the sale as constructively fraudulent

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ABC NACO v. Matrix Metals

- Underscoring the complexity of determining "reasonably equivalent value," the Court held that the $24 million purchase price for complex assets sold through an extensive—but ultimately flawed—marketing process, was not a conclusive proxy for the reasonable value of those assets in this case.

  But, the Court [incorrectly] "collapsed" the separate deals into a single transaction thereby aggregating the consideration to the Debtors.

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In re: CFS, Inc.

- Cornered the market for fresh charged-off credit card debt
- Securitization of loan pools masked failed model; whistle blown on more than $1B in losses
- Trustee sought to avoid purchases under
  § 548 and UFTA as constructively fraudulent

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In re: Commercial Financial Services, Inc.

- "Unusual circumstances" diminished the utility of fair market value and comparable sales as a proxy for value of the subject property

- expert's methodology, which used both information not ordinarily available to prospective buyers of charged-off credit card debt and information commonly considered and reasonably relied upon by such buyers, was admissible.

Sharpe v. Chase Manhattan Bank, NA (In re Commercial Financial Services, Inc.)350 B.R. 559 (Bkrtcy.N.D.Okla.,2005)

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In re: Tiger Petroleum Co.

- Ponzi scheme in OK involving oil and gas

- Sole shareholder destroys records, commits suicide; investors lost millions

- Ch. 7 Trustee sought to avoid distributions under § 548 and UFTA for alleged actual and constructive fraud

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In re: Tiger Petroleum Co.

Regarding actual fraud claim, cannot be transferee in good faith if you knew or should have known of the debtor's scheme….**BUT**

Regarding constructive fraud claim, victims gave "reasonably equivalent value" in exchange for the distributions they received in Ponzi scheme case because distributions did not exceed amount of investor's initial cash investment in the debtor, which established the amount of investor's restitution claim and precluded finding that debtor's estate was depleted.

In re Tiger Petroleum Co., 319 B.R. 225 (Bankr. N.D. Okla. 2004).

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Fifth Third Bank v. Huntley Chevrolet, Inc. et al.,

- One of the Defendants was floor plan lender to the Huntley dealership.

- Huntley paid down its financing by tendering a $150K check drawn on the account of a third party (motorcycle dealership) payable to floor plan lender.

- Fifth Third was the lender to the motorcycle dealership, which defaulted on its loan months thereafter.

- Fifth Third sued to avoid the transfer from the motorcycle dealership to Huntley and then to the floor plan lender under the IUFTA as actual and constructive fraud.

- Under Section 9 of the IUFTA, there is a defense available to a “subsequent transferee” who took in good faith and for value.

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Fifth Third Bank v. Huntley Chevrolet, Inc. et al.,

"Initial Transferee" vs. "Subsequent Transferee"

"[T]he 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."

The term "'transferee' must mean something different from 'possessor' or 'holder' or 'agent' or 'anyone who touches the money.'"

Bonded Fin. Servs., Inc. v. European American Bank, 838 F.2d 890 (7th Cir. 1988).

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