

MEMORANDUM

To: Richard T. Cassidy
Chair, Committee on Scope and Program
Uniform Law Commission

Date: January 9, 2012

From: Edwin E. Smith
Chair, Committee on Choice of Law for Fraudulent Transfer

Re: Report of the Committee on Choice of Law for Fraudulent Transfer

The Committee on Choice of Law for Fraudulent Transfer (the “Study Group”) believes that it has completed its work and respectfully submits this report, which describes the Study Group, the meetings that it held, and the conclusions that it reached.

I. The Study Group. The Study Group was formed by action of the Committee on Scope and Program at its meeting on July 8, 2011, approved by the Executive Committee on July 11, 2011. As stated in the minutes of the July 8 meeting, the Study Group was charged with evaluating the following proposal:

to study whether or not it is feasible to draft a law on choice of law for fraudulent transfers when a given transaction is challenged. The study could look at revising or amending the Uniform Fraudulent Transfer Act [“UFTA”], which does not contain any choice of law rule, or it could study the feasibility of drafting a stand-alone statute. A study committee would also need to determine what other areas of the law beyond commercial law are impacted.

The roster of the Study Group’s members and observers is enclosed with this memorandum.

II. Meetings. The Study Group met by conference call three times: on September 30, 2011, October 17, 2011, and November 18, 2011. Observers were invited to participate in meetings after the first. This memorandum was circulated in draft form for approval by the members, and for comment by observers, before its submission.

Background for the Study Group’s deliberations was provided by the memorandum dated June 1, 2011, by Professor Kenneth Kettering to the Committee on Scope and Program, which proposed that the Committee institute this project. That memorandum, as revised for publication, has been publicly available since August 31, 2011, having been posted on the Social Science Research Network website and linked to by the Study Group’s page on the ULC website. A copy of that memorandum, as revised for publication, is enclosed with this memorandum.

III. Conclusions. The Study Group reached the following conclusions. These conclusions represent the unanimous view of the members and were not materially qualified by views expressed by participating observers except as noted.

1. *General recommendation.* The Study Group recommends that a drafting committee be formed to prepare a uniform law on conflict of laws for fraudulent transfer.¹ All participants acknowledge that the conflict of laws issue does not arise with sufficient frequency to make statutory resolution a matter of urgency. However, the object is desirable, a rule on the subject should be fairly easy to formulate, and the benefits of having the rule would, the Study Group believes, justify the costs of a drafting project.

Whether the benefits of having the rule would justify the costs of a drafting project was not without some controversy. One observer believes that the frequency with which the issue arises is not sufficient, on balance, to warrant a drafting project. However, others expressed the view that the issue does not arise with frequency because parties and courts have not focused on the issue, even in circumstances in which different candidate jurisdictions have differing substantive law rules.² A few stated that they have encountered the issue in practice, either in the context of a bankruptcy case involving a debtor with multiple locations or in planning, defending or challenging transfers to an asset protection trust.

2. *Form of implementation.* The Study Group recommends that the new uniform law take the form of an amendment to the UFTA, though the drafting committee should be empowered to prepare it as a stand-alone uniform law if the drafting committee deems that preferable.

3. *Enactability.* The Study Group does not perceive any likelihood of organized opposition to enactment of such a uniform law. No contention has been made that codification of a rule on this subject would be undesirable in principle, nor does the Study Group perceive any reason for any constituency to oppose the particular rule that it has tentatively formulated. On the other hand, the only constituency to favor enactment thus far is the legal community, particularly transactional lawyers who desire certainty on the subject for planning purposes. The interest of the legal community in enactment is not particularly strong. On balance, the Study Group estimates that there is a reasonable likelihood of enactment, especially if the uniform law is cast in the form of an amendment to the UFTA and the uniform conflict of laws rule is accompanied by provisions relating to evidentiary matters (as discussed in paragraph 5 below)..

4. *Drafting considerations.* The Study Group recommends that the drafting committee consider drafting the new uniform law generally to choose the substantive fraudulent transfer law (*i.e.*, excluding conflict of laws rules) of the debtor's home jurisdiction at the time the challenged transfer is made or the challenged obligation is incurred. "Home jurisdiction" means place of business (or, if more than one place of business, chief executive office) in the case of an organization, and domicile in the case of an individual. The foregoing definition is almost identical to the general rule for determining the "location" of a debtor under Article 9 of the

¹ In ordinary usage the terms "conflict of laws" and "choice of law" are often treated as synonymous. This report employs the former term, because the latter term might be misunderstood to contemplate a rule allowing the parties to a transfer to choose the fraudulent transfer law applicable to the transfer. Such a rule would be highly undesirable.

² In one very recent case in the bankruptcy court for the Southern District of New York, considered one of the country's most sophisticated commercial bankruptcy districts, the court had to raise the issue *sua sponte* because it was not recognized or briefed by the parties. *In re Trinsum Group, Inc.*, No. 08-12547 (AJG), 2011 WL 5966123 (Bankr. S.D.N.Y. Nov. 29, 2011).

Uniform Commercial Code, which is the key determinant of which jurisdiction’s law governs perfection and priority of a security interest.³

The foregoing definition is arguably comparable to that of the term “center of main interest” used in Chapter 15 of the Bankruptcy Code, the UNCITRAL Model Law on Cross-Border Insolvency and the European Union’s Insolvency Regulation. However, because the use of the term “center of main interest” has created considerable uncertainty in litigation, especially as that term is used in the European Union’s Insolvency Regulation (in the context of court jurisdiction, not conflict of laws), it would be undesirable to use that term in this setting, and care will need to be taken to avoid a similar uncertainty.

The “debtor’s home jurisdiction” conflict of laws rule has the advantage of being a relatively stable rule that does not depend upon other factors—*e.g.*, the law chosen in the transfer agreement, the location of the majority of creditors of the transferor, or the situs of the transferred property—that may not be as readily ascertainable by a third party who extends credit to or otherwise has a claim against the debtor. The Study Group recognizes that the “debtor’s home jurisdiction” may in some circumstances not be readily apparent but believes that in most circumstances it would be.

The foregoing recommendation is proposed principally with constructive fraud in mind, and it must be subject to carveouts if applied to claims of actual fraud. At a minimum it would have to accommodate the different conflict of laws rules set forth in sections 2-403(2) and 6-103 of the Uniform Commercial Code, which apply to transactions that are susceptible to fraudulent transfer attack on a theory of actual fraud. It may be inadvisable to codify a conflict of laws rule applicable to actual fraud claims at all, at least if the actual fraud claim is not effectively redundant of a constructive fraud claim.

No member or observer dissented from this recommendation. However, several observations were made.

- One observer suggested that it may be possible and desirable to elaborate on this rule in such a way as to minimize the effect of dispute over the location of the debtor’s home jurisdiction, or of eve-of-transfer relocation by the debtor, by using supplemental “content-based” rules that would (for example) select the substantive law most favorable to creditors from among the jurisdictions that are contenders for being the debtor’s home jurisdiction. Two observers opposed that suggestion. One maintained that such a content-based rule would create excessive *ex ante* uncertainty and is unnecessary because

³ U.C.C. § 9-307(b) (2011) (general rule for determining the debtor’s “location”); *id.* § 9-301(1) (stating the baseline rule that perfection and priority of a security interest are governed by the law of the jurisdiction in which the debtor is “located”). The “debtor’s home jurisdiction,” as tentatively defined by the Study Group, differs slightly from Article 9’s general definition of the debtor’s “location,” in that the Study Group locates an individual at his or her “domicile,” while Article 9 looks to his or her “principal residence.” Further study may warrant use of the Article 9 term, thus making the identity complete. The Study Group does not suggest that the drafting committee, if appointed, follow the special Article 9 debtor location rule for a “registered organization” in U.C.C. § 9-307(e). *See also* Hertz Corp. v. Friend, 130 S. Ct. 1181 (2010) (defining a corporation’s “principal place of business” for purposes of diversity jurisdiction to be its “nerve center,” in terms that appear indistinguishable from the Article 9 concept of “chief executive office,” though the Supreme Court did not draw that analogy).

the risks of uncertainty of the debtor's home jurisdiction, and of debtor forum-shopping by relocation, are minimal. Another opposed the specific content-based rule proposed on the ground that creditors are not always "good guys."

- One observer suggested that a situs rule might be more appropriate if the transfer is of real rather than personal property.
- One observer suggested that there may be a need for an "escape hatch" if the substantive law determined by the baseline conflict of laws rule were either very aggressive or very lenient.

No specific proposals were made. The Study Group believes that, while it generally favors a "debtor's home jurisdiction" conflict of laws rule, further consideration and refinement by the drafting committee are necessary and desirable. The Study Committee does not by its recommendation intend to fetter the drafting committee.

5. *Evidentiary rules.* The Study Group recommends that the drafting committee be empowered also to amend the UFTA to clarify the evidentiary presumptions and burdens of proof that apply under it. Courts in states that have enacted the UFTA have differed materially on such matters, and those nonuniformities would seem to be best addressed by clarifying the substantive rules of the UFTA on the subject. One observer suggested that this might well be the most useful part of the project. These rules might provide uniformity on virtually all matters other than the statute of limitations, bringing more certainty to the subject. The Study Committee has not formulated a recommendation as to the substance of those evidentiary rules.

6. *Other issues.* The Study Group recommends that the drafting committee be required to receive prior authorization from the Committee on Scope and Program before pursuing any other amendments to the substantive rules of the UFTA.

Respectfully submitted.

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Enclosures