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MEMORANDUM

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To: Uniform Law Commission   Date: May 28, 2013

From: Edwin E. Smith, *Chair, Drafting Committee*
        Kenneth C. Kettering, *Reporter, Drafting Committee*

Re: <u>Amendments to the Uniform Fraudulent Transfer Act: 2013 Annual Meeting Draft</u>

This memorandum accompanies the Annual Meeting Draft of amendments to the Uniform Fraudulent Transfer Act ("UFTA"), which is to be considered at the ULC's 2013 Annual Meeting. The first reading of the amendments will take place at that meeting. It is hoped that the amendments will be ready for final approval by the ULC at its annual meeting in 2014.

The Annual Meeting Draft contains the entire Official Text, Comments and Prefatory Note to the UFTA as it was originally promulgated in 1984. They are marked to show the amendments.

Purpose and Nature of the UFTA. The UFTA codifies a doctrine that historically has been known as the law of fraudulent conveyance. That doctrine sets the limits of a debtor's right to deal with his property as against his creditors. A simple example of the operation of the UFTA would be to unwind a debtor's eve-of-bankruptcy gifting of property to a favored relative, or to a straw man to hold for the debtor's own benefit. Fraudulent conveyance law is not limited to such blatant attempts to shield assets from creditors, however. It applies to transactions that thwart creditors in more subtle ways. The doctrine is of very general applicability. It applies equally to business debtors and to consumer debtors. It is of great age: the core operative language of the UFTA is carried forward from the English Statute of 13 Elizabeth, which was enacted in 1571. The doctrine is often employed by the debtor's bankruptcy trustee in a later bankruptcy proceeding, but it is equally applicable if the debtor never goes bankrupt. The UFTA has been enacted by 43 states, the District of Columbia and the U.S. Virgin Islands. The UFTA replaced the very similar Uniform Fraudulent Conveyance Act, which was promulgated in 1918 and remains in force in two states.

Nature of the Amendments. The current amendments are the first since the UFTA was promulgated in 1984. The Drafting Committee's mandate extends only to a small number of narrowly-defined issues. Hence the amendments are in no way a comprehensive revision. Nor are they responsive to any single guiding theme. The principal features of the amendments are listed on pages 5-6 of the Annual Meeting Draft under the heading "Prefatory Note (2014)."

Major Issues for the Conference. The Drafting Committee welcomes input on all aspects of the amendments, but particularly invites input on the following issues.

1. Choice of Law. The UFTA currently has no choice of law provision. The common-law choice of law principles that courts have applies in respect of transfers governed by the UFTA, or by comparable law in jurisdictions that have not enacted the UFTA, are diverse, and they are generally vague and unpredictable. The need for a clear choice of law rule for transactions of this nature was the principal impetus for this amendment project.

The proposed choice of law rule is Section 10 of the current draft, which appears on page 45 and is followed by a long Reporter's Note. The Drafting Committee had little difficulty agreeing on a single simple general rule: namely, that the fraudulent conveyance law applicable

to a transfer should be the law of the jurisdiction in which the debtor is located when the transfer is made. The Drafting Committee also had little difficulty in agreeing that an escape hatch is necessary in the event that the general rule points to a jurisdiction whose fraudulent conveyance law is substantially debased. Such a jurisdiction can be called an "asset haven" for short.

Discussion in the Drafting Committee has centered on defining that escape hatch. The discussion can be grouped around the following three issues, on which the Drafting Committee particularly invites input:

(a) Should the escape hatch be stated in the statutory text, or relegated to the comments?

(b) Should the escape hatch apply only to non-U.S. jurisdictions, or should it also apply to U.S. jurisdictions?

(c) Should the standard for invoking the escape hatch be "conflict with a fundamental public policy of the forum state," or should a more concrete standard be used?

2. Title of the Act. The Drafting Committee is considering recommending that the title of the UFTA be changed so as to eliminate the word "fraudulent." One possible alternative would be "Uniform Voidable Transfer Act." This proposal is not motivated by the minor revisions to the Act that are made by these amendments. Rather, the word "fraudulent" in the title of the Act is a misleading description of the Act as it presently stands. That is because fraud is not a necessary element of a claim under the Act. The misleading association of the Act with common-law fraud has demonstrably led to confusion in the courts. The only plausible justification for the Act's present title is historical. Yet the original Act jettisoned the historical name "fraudulent conveyance" in favor of the name "fraudulent transfer," in order to eliminate the misleading imputation that the Act is applicable only to real estate. A further change would continue the ULC's tradition of prizing accuracy over inertia.

For further discussion, see the "Reporter's Introductory Note" on page 1 of the draft.

3. Section 8(a). The *prima facie* elements of a claim for avoidance of a transfer of property under the UFTA are set forth in Sections 4 and 5. Section 8 provides a menu of defenses. One of those defenses, Section 8(a), is anomalous because the parallel provisions of the Bankruptcy Code unaccountably contain no similar defense. Different members of the Drafting Committee have different intuitions about the fairness of the Section 8(a) defense, and three radically different ways of dealing with Section 8(a) have been seriously discussed: (a) retain it as it is, (b) amend it to narrow its application substantially, or (c) delete it.

Section 8(a) appears on page 36 of the current draft. A Reporter's Note pertaining to Section 8(a), which includes an example of its operation, begins on page 38.

Respectfully submitted.

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