

## MEMORANDUM

To: Drafting Committee, Advisors and Observers                      Date: January 13, 2013  
From: Ken Kettering  
Re: Compilation of Substantive Nonuniform State Comments to the UFTA

The Drafting Committee's mandate includes authority "to draft, for approval by the Executive Committee, revisions to the comments to [the] provisions of the Uniform Fraudulent Transfer Act." In order to assist the Drafting Committee in evaluating possible revisions to the comments I have prepared this memorandum, with the invaluable assistance of Matt Cursio of Bingham McCutchen LLP.

This memorandum is a compilation of substantive nonuniform comments that have been adopted by states that have enacted the UFTA. The purpose of this compilation is to identify state comments to the official text that may be candidates for adoption at the national level. Hence this compilation does not include state comments that are only of local interest, such as comments referring to local cases confirmed or overruled by UFTA, or comments referring to local statutes thought to be relevant.

This compilation generally does not include state comments that relate to nonuniform changes to the statutory text. However, two nonuniform changes to the statutory text are reflected in the comments compiled here. First, at least two states (Indiana and Pennsylvania) moved to UFTA § 2(b) language stating the intended operation of the presumption created by that provision; the official text relegates that language to Comment 2 to Section 2. Second, at least California and Indiana deleted from the statutory text and moved entirely to the comments the precatory list of badges of fraud that appears in UFTA § 4(b). California later amended its enactment of the UFTA to add the badges of fraud back to the statutory text, but its comments evidently have not been updated. Indiana continues to exclude the badges of fraud from the statutory text.

I relied on Cursio to locate state comments to the UFTA. He provided me with copies of comments from the following states: Alabama, Arkansas, California, Colorado, Maine, New Jersey, North Carolina, Pennsylvania and Tennessee. I was also aware of Indiana comments. Of those, only Alabama, California, Indiana and Pennsylvania appear to have nonuniform comments that meet the criteria described above. The most extensive of these are Pennsylvania's, from which Indiana borrowed liberally. Pennsylvania in turn borrowed some ideas from California, which was the earliest of those three enactments.

The pages following this cover sheet show the substantive nonuniform comments of Alabama, California, Indiana and Pennsylvania, respectively, in the form of blacklined versions of the relevant portions of the official comments. The California, Indiana and Pennsylvania comments were in fact issued as edited versions of the official comments, rather than as freestanding supplements to it. The blacklined text is lightly edited for clarity (e.g., to cite provisions of the UFTA to the official text rather than to the local state statutory code).

It should also be considered whether it would be worthwhile to revise the official comments in other respects, viz.: (a) The original comments, promulgated in 1984, include many references to sections of the Bankruptcy Code, the UCC, and perhaps other statutes, that have changed in numbering (if not in substance) in the meantime. (b) Query the desirability of surveying intervening case law with a view to revising the comments responsively.

Finally, it should be considered whether revision to the Prefatory Note to the UFTA is in order. I have not reviewed the Prefatory Note carefully and comprehensively, but I am aware that some of its language merits attention. For example, it includes the following passage:

[B]oth [the UFTA and the former UFCA] render a transfer made or obligation incurred without adequate consideration to be constructively fraudulent -- *i.e.*, without regard to the actual intent of the parties -- under one of the following conditions:

- (1) the debtor was left by the transfer or obligation with unreasonably small assets for a transaction or the business in which he was engaged;
- (2) the debtor intended to incur, or believed that he would incur, more debts than he would be able to pay; or
- (3) the debtor was insolvent at the time or as a result of the transfer or obligation.

Paragraph (2) is a paraphrase of the constructive fraud rule that appears in UFTA § 4(a)(ii), which declares a transfer or obligation to be fraudulent if the debtor made the transfer or incurred the obligation without receiving reasonably equivalent value in exchange and

(ii) intended to incur, or believed or reasonably should have believed that he [or she] would incur, debts beyond his [or her] ability to pay as they became due.

Section 4(a)(ii) differs significantly from the paraphrase in the above-quoted paragraph (2), in that the former but not the latter includes the phrase “reasonably should have believed.” The inclusion of that language means that Section 4(a)(ii) comprises an objective test (“can the debtor reasonably be expected to pay its debts as they become due?”) as well as a subjective test (“does the debtor believe that he will be able to pay his debts as they become due?”). By contrast, the paraphrase in paragraph (2) is purely subjective. Query what a court would make of the mismatch between these two statements, especially given that “reasonably should have believed” is a decidedly backhanded way of stating the objective test.

Another feature of the Prefatory Note that is probably of less concern but is rather odd relates to its introductory list of reasons why the UFTA was prepared. High on that list is the following:

(2) The Committee on Corporate Laws of the Section of Corporations, Banking & Business Law of the American Bar Association, engaged in revising the Model Corporation Act, suggested that the Conference review provisions of the Uniform Act with a view to determining whether the Acts are consistent in respect to the treatment of dividend distributions.

Nothing further of is heard of this important concern in either the text or the comments. At least one state (Pennsylvania) does include in its nonuniform comments discussion of relationship between UFTA and corporation-law restrictions on dividend distributions.

KCK

**ALABAMA**

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3 1. Alabama’s comments make corrections to the erroneous list of cross-references to  
4 provisions of the UFTA that use the word “value” in Comment 1 to UFTA § 3, as detailed more  
5 fully in the California and Pennsylvania comments.  
6

7 2. Alabama directed that the language shown as deleted below in Comment 5 to UFTA  
8 § 4 should be disregarded, stating “This language is confusing and not properly placed in the  
9 comments.”  
10

11 **SECTION 4. TRANSFERS FRAUDULENT AS TO PRESENT AND FUTURE**  
12 **CREDITORS.**

13 **Comment**  
14

15 (5) Subsection (b) is a nonexclusive catalogue of factors appropriate for consideration by  
16 the court in determining whether the debtor had an actual intent to hinder, delay, or defraud one  
17 or more creditors. Proof of the existence of any one or more of the factors enumerated in  
18 subsection (b) may be relevant evidence as to the debtor's actual intent but does not create a  
19 presumption that the debtor has made a fraudulent transfer or incurred a fraudulent obligation.  
20 The list of factors includes most of the badges of fraud that have been recognized by the courts in  
21 construing and applying the Statute of 13 Elizabeth and § 7 of the Uniform Fraudulent  
22 Conveyance Act. ~~Proof of the presence of certain badges in combination establishes fraud~~  
23 ~~conclusively—i.e., without regard to the actual intent of the parties—when they concur as~~  
24 ~~provided in § 4(a)(2) or in § 5. The fact that a transfer has been made to a relative or to an~~  
25 ~~affiliated corporation has not been regarded as a badge of fraud sufficient to warrant avoidance~~  
26 ~~when unaccompanied by any other evidence of fraud. The courts have uniformly recognized,~~  
27 ~~however, that a transfer to a closely related person warrants close scrutiny of the other~~  
28 ~~circumstances, including the nature and extent of the consideration exchanged. See 1 G. Glenn,~~  
29 ~~Fraudulent Conveyances and Preferences § 307 (Rev. ed. 1940). The second, third, fourth, and~~  
30 ~~fifth factors listed are all adapted from the classic catalogue of badges of fraud provided by Lord~~  
31 ~~Coke in Twyne's Case, 3 Coke 80b, 76 Eng.Rep. 809 (Star Chamber 1601). Lord Coke also~~  
32 ~~included the use of a trust and the recitation in the instrument of transfer that it "was made~~  
33 ~~honestly, truly, and bona fide," but the use of the trust is fraudulent only when accompanied by~~  
34 ~~elements or badges specified in this Act, and recitals of "good faith" can no longer be regarded as~~  
35 ~~significant evidence of a fraudulent intent.~~  
36

37 [End Alabama]  
38

CALIFORNIA

SECTION 2. INSOLVENCY.

Comment

(1) Subsection (a) is derived from the definition of "insolvent" in § 101(29)(A) of the Bankruptcy Code. The definition in subsection (a) and the correlated definition of partnership insolvency in subsection (c) contemplate a fair valuation of the debts as well as the assets of the debtor. As under the definition of the same term in § 2 of the Uniform Fraudulent Conveyance Act exempt property is excluded from the computation of the value of the assets. See § 1(2) supra. For similar reasons interests in valid spendthrift trusts, to the extent they are exempt from the enforcement of a money judgment, and interests in tenancies by the entireties that cannot be severed by a creditor of only one tenant are not included. See the Comment to § 1(2) supra. Since a valid lien also precludes an unsecured creditor from collecting the creditor's claim from the encumbered interest in a debtor's property, both the encumbered interest and the debt secured thereby are excluded from the computation of insolvency under this Act. See § 1(2) supra and subsection (e) of this section.

~~The requirement of § 550(b)(1) of the Bankruptcy Code that a transferee be "without knowledge of the voidability of the transfer" in order to be protected has been omitted as inappropriate. Knowledge of the facts rendering the transfer voidable would be inconsistent with the good faith that is required of a protected transferee. Knowledge of the voidability of a transfer would seem to involve a legal conclusion. Determination of the voidability of the transfer ought not to require the court to inquire into the legal sophistication of the transferee.~~

*[Note: The paragraph deleted above was relocated by California to its version of Section 8 cmt. 1.]*

\* \* \*

(7) Problems of valuation exist in the case of an obligation incurred by a debtor as surety for another. In this situation, the obligation is deemed incurred when the written suretyship agreement, executed by the obligor thereunder is delivered to or for the benefit of the obligee (see[Section 6(e)]). This is the date as of which the solvency or insolvency of the debtor (surety) is to be determined for purposes of [Section 5], and, in determining whether the debtor (surety) incurred the obligation without receiving a reasonably equivalent value in exchange for the suretyship obligation, weight should be given to the likelihood, or lack thereof, as of the time that the suretyship obligation is deemed incurred under [Section 6(e)], that the principal obligation will ultimately be satisfied in whole or in part by the principal debtor. Furthermore, in determining solvency under this section, in placing a fair valuation on the debts of the debtor (surety), appropriate weight should be given to the then prospective likelihood, and the extent thereof, that the debtor (surety) will be called upon to perform under the suretyship agreement, and in placing a fair valuation on the assets of the debtor (surety) at that time, appropriate value should be placed on the rights of the debtor (surety), including subrogation, exoneration, and indemnification. The valuation of these debts and assets of the debtor (surety) should include

1 consideration of such relevant factors as the then prospective ability of the principal debtor to  
2 respond to the exercise of the rights of the debtor (surety).  
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### 5 SECTION 3. VALUE.

#### 6 Comment

7  
8 (1) This section defines "value" as used in various contexts in this Act, frequently with a  
9 qualifying adjective. The word appears in the following sections:

- 10  
11 4(a)(2) ("reasonably equivalent value");  
12 ~~4(b)(8) ("value ... reasonably equivalent");~~  
13 5(a) ("reasonably equivalent value");  
14 ~~5(b) ("present, reasonably equivalent value");~~  
15 8(a) ("reasonably equivalent value");  
16 ~~8(b), (c), (d), and (e) ("value");~~  
17 ~~8(f)(1) ("new value"); and~~  
18 ~~8(f)(3) ("present value").~~  
19

20 *[Note: As noted in the Pennsylvania comments, the definition of "value" in UFTA 3 is germane*  
21 *to the "value received by the debtor". The UFTA also uses "value" in other ways, notably with*  
22 *respect to the "value of the asset transferred by the debtor" in UFTA 8(b) and (c). California's*  
23 *deletion of the references to 8(b) and 8(c) reflect the fact the definition of "value" section 3 is*  
24 *not germane to the word as used in those provisions. Furthermore, section 8(e) does not use the*  
25 *term "value" at all. Section 4(b)(8) uses "value" twice, once in a sense to which the section 3*  
26 *definition is germane and the other time in a sense to which the section 3 definition is not*  
27 *germane. California did not enact the insider preference provision, section 5(b), and hence did*  
28 *not enact section 8(f), which sets forth defenses to an action under section 5(b). However, the*  
29 *official comment's reference to section 5(b) as using the term "present, reasonably equivalent*  
30 *value" is incorrect; neither that nor any similar term is used in section 5(b)]*  
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### 33 SECTION 4. TRANSFERS FRAUDULENT AS TO PRESENT AND FUTURE 34 CREDITORS.

#### 35 Comment

36  
37  
38 (5) Subsection (b) is a nonexclusive catalogue of factors appropriate for consideration by  
39 the court in determining whether the debtor had an actual intent to hinder, delay, or defraud one  
40 or more creditors. Proof of the existence of any one or more of the factors enumerated in  
41 subsection (b) may be relevant evidence as to the debtor's actual intent but does not create a  
42 presumption that the debtor has made a fraudulent transfer or incurred a fraudulent obligation.  
43 The list of factors includes most of the badges of fraud that have been recognized by the courts in  
44 construing and applying the Statute of 13 Elizabeth and § 7 of the Uniform Fraudulent  
45 Conveyance Act. ~~Proof of the presence of certain badges in combination establishes fraud~~  
46 ~~conclusively i.e., without regard to the actual intent of the parties when they concur as~~

1 ~~provided in § 4(a)(2) or in § 5.~~ Proof of actual intent is unnecessary in cases to which [Section  
2 4(a)(2) or Section 5(a) are applicable. The fact that a transfer has been made to a relative or to  
3 an affiliated corporation has not been regarded as a badge of fraud sufficient to warrant  
4 avoidance when unaccompanied by any other evidence of fraud. The courts have uniformly  
5 recognized, however, that a transfer to a closely related person warrants close scrutiny of the  
6 other circumstances, including the nature and extent of the consideration exchanged. See 1 G.  
7 Glenn, Fraudulent Conveyances and Preferences § 307 (Rev. ed. 1940). The second, third,  
8 fourth, and fifth factors listed are all adapted from the classic catalogue of badges of fraud  
9 provided by Lord Coke in *Twyne's Case*, 3 Coke 80b, 76 Eng.Rep. 809 (Star Chamber 1601).  
10 Lord Coke also included the use of a trust and the recitation in the instrument of transfer that it  
11 "was made honestly, truly, and bona fide," but the use of the trust is fraudulent only when  
12 accompanied by elements or badges specified in this Act, and recitals of "good faith" can no  
13 longer be regarded as significant evidence of a fraudulent intent.  
14  
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## 16 SECTION 8. DEFENSES, LIABILITY, AND PROTECTION OF TRANSFEREE.

### 17 Comment

18  
19 (1) Subsection (a) states the rule that applies when the transferee establishes a complete  
20 defense to the action for avoidance based on Section 4(a)(1). The subsection is an adaptation of  
21 the exception stated in §9 of the Uniform Fraudulent Conveyance Act. The insolvency of the  
22 transferor may be a fact from which, in conjunction with other facts, may be inferred fraudulent  
23 intent on the part of the debtor. See the Comments (5) to (8), inclusive, to Section 3439.04,  
24 supra. However, evidence of the transferee's knowledge of the transferor's insolvency at the time  
25 of the transfer or obligation is not relevant on the issue of the transferee's good faith. As used in  
26 this subdivision and in subdivision (d), "good faith" means that the transferee acted without  
27 actual fraudulent intent and that he or she did not collude with the debtor or otherwise actively  
28 participate in the fraudulent scheme of the debtor. The transferee's knowledge of the transferor's  
29 fraudulent intent may, in combination with other facts, be relevant on the issue of the transferee's  
30 good faith of the transferor or of the transferor's insolvency. The person who invokes this  
31 defense carries the burden of establishing good faith and the reasonable equivalence of the  
32 consideration exchanged. *Chorost v. Grand Rapids Factory Showrooms, Inc.*, 77 F. Supp. 276,  
33 280 (D.N.J. 1948), *aff'd*, 172 F.2d 327, 329 (3d Cir. 1949). The requirement of Section  
34 550(b)(1) of the Bankruptcy Code that a transferee be "without knowledge of the voidability of  
35 the transfer" in order to be protected has been omitted as inappropriate. Knowledge of the facts  
36 rendering the transfer voidable would be inconsistent with the good faith that is required of a  
37 protected transferee. Knowledge of the voidability of a transfer would seem to involve a legal  
38 conclusion. Determination of the voidability of the transfer ought not to require the court to  
39 inquire into the legal sophistication of the transferee.  
40

41 *[Note: The second insert above, beginning "The requirement of Section 550(b)(1)...." is a*  
42 *nonuniform relocation of language that appears in Section 2 cmt. 1 of the official text. The first*  
43 *insert above is not in the official text.]*  
44  
45

1 **SECTION 10. SUPPLEMENTARY PROVISIONS.**

2 **Comment**

3  
4 This section is derived from §11 of the Uniform Fraudulent Conveyance Act and §1-103 of  
5 the Uniform Commercial Code. The section adds a reference to "laches" in recognition of the  
6 particular appropriateness of the application of this equitable doctrine to an untimely action to  
7 avoid a fraudulent transfer. See Louis Dreyfus Corp. v. Butler, 496 F.2d 806, 808 (6th Cir.  
8 1974) (action to avoid transfers to debtor's wife when debtor was engaged in speculative  
9 business held to be barred by laches or applicable statutes of limitations); Cooch v. Grier, 30  
10 Del.Ch. 255, 265-66, 59 A.2d 282, 287-88 (1948) (action under the Uniform Fraudulent  
11 Conveyance Act held barred by laches when the creditor was chargeable with inexcusable delay  
12 and the defendant was prejudiced by the delay).

13  
14 Among the remedies preserved by this section are the following:

15  
16 1. The recordation of a lis pendens in an appropriate case.

17  
18 2. The right of the transferee to join all creditors in an action to set aside an alleged fraudulent  
19 transfer or obligation.

20  
21 3. The right of a creditor to institute a class action to set aside an alleged fraudulent transfer or  
22 obligation on behalf of all similarly situated creditors of the transferor.

23  
24 4. The right of a fraudulent transferee to offset against a money judgment any payments  
25 previously made to an aggrieved creditor of the transferor.

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27  
28 [End California]  
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30



1 includes licenses, permits, franchises and contracts, whether or not transferable. In particular, but  
2 without limitation, governmental licenses and permits that contribute to the value of the holder in  
3 general should be deemed “property” of the holder, whether or not transferable, regardless of  
4 whether such items are deemed “property” for other purposes (e.g., regardless of whether such  
5 an item may be the subject of execution, or whether such an item is deemed a withdrawable  
6 privilege, rather than a property right, as against the issuing authority). Note, however, that such  
7 property may have little or no value in certain circumstances (e.g., such items, if nontransferable,  
8 may have no value if the holder is not valued on a going-concern basis). See comment (1) to  
9 section 2, infra.

10  
11 \* \* \*

12  
13 (12) The definition of "transfer" is derived principally from §101(48) of the Bankruptcy  
14 Code. The definition of "conveyance" in § 1 of the Uniform Fraudulent Conveyance Act was  
15 similarly comprehensive, and the references in this Act to "payment of money, release, lease, and  
16 the creation of a lien or incumbrance" are derived from the Uniform Fraudulent Conveyance Act.  
17 While the definition in the Uniform Fraudulent Conveyance Act did not explicitly refer to an  
18 involuntary transfer, the decisions under that Act were generally consistent with an interpretation  
19 that covered such a transfer. See, e.g., Hearn 45 St. Corp. v. Jano, 283 N.Y. 139, 27 N.E.2d 814,  
20 128 A.L.R. 1285 (1940) (execution and foreclosure sales); Lefkowitz v. Finkelstein Trading  
21 Corp., 14 F.Supp. 898, 899 (S.D.N.Y. 1936) (execution sale); Langan v. First Trust & Deposit  
22 Co., 277 App.Div. 1090, 101 N.Y.S.2d 36 (4th Dept. 1950), aff'd, 302 N.Y. 932, 100 N.E.2d 189  
23 (1951) (mortgage foreclosure); Catabene v. Wallner, 16 N.J.Super. 597, 602, 85 A.2d 300, 302  
24 (1951) (mortgage foreclosure).

25  
26 The scope of “transfer” is intended to be quite broad. It includes, for example, transfer  
27 under the UFCA and similar statutes governing the “garden variety” change of title in real estate.  
28 It also includes the more exotic: a settlement agreement, In re Edward Harvey Co., 68 B.R. 851,  
29 858 (Bankr. D. Mass. 1987); a change of a beneficiary of a life insurance policy, Schaefer v.  
30 Fisher, 242 N.Y.S. 308, 314 (N.Y. 1930); a transaction entered into in connection with a  
31 leveraged buyout, United States v. Tabor Court Realty Corp., 803 F.2d 1288 (3d Cir. 1896), cert.  
32 denied, 483 U.S. 1005 (1987); see generally David Gray Carlson, Leveraged Buyouts in  
33 Bankruptcy, 20 GA. L. REV. 73 (1985); and payments of dividends, Consove v. Cohen, 783  
34 F.2d 978, 982 (1st Cir. 1983); Mancuso v. Champion, 119 B.R. 106, 109 (Bankr. N.D. Tex.  
35 1990); Fox v. MGM Grand Hotels, 187 Cal. Rptr. 141 (Cal. Ct. App. 1984). The correlative  
36 concept of “obligations incurred” includes guaranties, Lawrence Paperboard Corp. v. Arlington  
37 Trust Co., 76 B.R. 866, 874-76 (Bankr. D. Mass. 1987), as well as long term contracts for which  
38 the debtor received little benefit, FDIC v. Malin, 802 F.2d 12, 18 (2d Cir. 1986) (divorce  
39 agreement); Wilson v. Holub, 210 N.W. 593, 595 (Iowa 1926) (rescission of a profitable  
40 contract); Larrimer v. Feney, 192 A.2d 351, 353 (Pa. 1963) (payment of usurious interest).

41  
42 In short, almost every economic transaction entered into by a debtor is capable of being  
43 characterized as either a transfer or an obligation incurred. The UFTA provides limitations on  
44 who can avoid these transactions, and which transactions can be avoided in both the standing  
45 areas and in the defenses to the substantive causes of action.

1 **SECTION 2. INSOLVENCY.**

2 **Comment**

3  
4 (1) Subsection (a) is derived from the definition of "insolvent" in § 101(29)(A) of the  
5 Bankruptcy Code. The definition in subsection (a) and the correlated definition of partnership  
6 insolvency in subsection (c) contemplate a fair valuation of the debts as well as the assets of the  
7 debtor. As under the definition of the same term in § 2 of the Uniform Fraudulent Conveyance  
8 Act exempt property is excluded from the computation of the value of the assets. See § 1(2)  
9 supra. For similar reasons interests in valid spendthrift trusts and interests in tenancies by the  
10 entireties that cannot be severed by a creditor of only one tenant are not included. See the  
11 Comment to § 1(2) supra. Since a valid lien also precludes an unsecured creditor from collecting  
12 the creditor's claim from the encumbered interest in a debtor's property, both the encumbered  
13 interest and the debt secured thereby are excluded from the computation of insolvency under this  
14 Act. See § 1(2) supra and subsection (e) of this section.  
15

16 ~~The requirement of § 550(b)(1) of the Bankruptcy Code that a transferee be "without~~  
17 ~~knowledge of the voidability of the transfer" in order to be protected has been omitted as~~  
18 ~~inappropriate. Knowledge of the facts rendering the transfer voidable would be inconsistent with~~  
19 ~~the good faith that is required of a protected transferee. Knowledge of the voidability of a~~  
20 ~~transfer would seem to involve a legal conclusion. Determination of the voidability of the~~  
21 ~~transfer ought not to require the court to inquire into the legal sophistication of the transferee.~~  
22

23 As under the Bankruptcy Code, this valuation is not a liquidation analysis. The "fair  
24 valuation" limitation is almost a modified market price valuation. As stated by Collier with  
25 respect to the identical provision in the Bankruptcy Code:  
26

27 [fair] valuation, in general, will signify the reasonable estimate of what can be realized  
28 from the assets by converting them into, or reducing them to cash, under carefully  
29 guarded if not idealized conditions.  
30

31 1 COLLIER ON BANKRUPTCY ¶ 101.29[4] (15th ed. 1991). See also Emerald Hills Country  
32 Club, Inc. v. Hollywood, Inc., 32 B.R. 408, 420-21 (Bankr. S.D. Fla. 1983); Varon v. Trimble,  
33 Marshall & Goldman, P.C., 33 B.R. 872, 885 (Bankr. S.D.N.Y. 1983).  
34

35 As under the Bankruptcy Code, contingent liabilities are counted at a value discounted by  
36 the probability that they will mature, In re Xonics Photochemical, Inc., 841 F.2d 198 (7th Cir.  
37 1988), even though under the UFCA they were counted at full face value. Chase Manhattan  
38 Bank (N.A.) v. Oppenheim, 440 N.Y.S.2d 829, 831 (N.Y. Sup. Ct. 1981); Marine Midland Bank  
39 v. Stein, 433 N.Y.S.2d 325, 327 (N.Y. Sup. Ct. 1980). The same holds true for contingent assets.  
40 See Mellon Bank, N.A. v. Metro Communications, Inc., 945 F.2d 635 (3d Cir. 1991) (noting that  
41 lower court erred in not counting as an asset the debtor's rights of contribution against other  
42 guarantors of LBO debt).  
43

44 (2) Section 2(b) establishes a rebuttable presumption of insolvency from the fact of  
45 general nonpayment of debts as they become due. Such general nonpayment is a ground for the  
46 filing of an involuntary petition under § 303(h)(1) of the Bankruptcy Code. See also U.C.C. § 1-

1 201(23), which declares a person to be "insolvent" who "has ceased to pay his debts in the  
 2 ordinary course of business." ~~The presumption imposes on the party against whom the~~  
 3 ~~presumption is directed the burden of proving that the nonexistence of insolvency as defined in~~  
 4 ~~§ 2(a) is more probable than its existence. See Uniform Rules of Evidence (1974 Act), Rule~~  
 5 ~~301(a). The 1974 Uniform Rule 301(a) conforms to the Final Draft of Federal Rule 301 as~~  
 6 ~~submitted to the United States Supreme Court by the Advisory Committee on Federal Rules of~~  
 7 ~~Evidence. "The so-called 'bursting bubble' theory, under which a presumption vanishes upon the~~  
 8 ~~introduction of evidence which would support a finding of the nonexistence of the presumed~~  
 9 ~~fact, even though not believed, is rejected as according presumptions too 'slight and evanescent'~~  
 10 ~~an effect." Advisory Committee's Note to Rule 301. See also 1 J.Weinstein & M.Berger,~~  
 11 ~~Evidence 301 [01] (1982). This act elevates language from the official comments to the UFTA~~  
 12 ~~to the text of the statute in order to make clear the effect of the presumption; this change is not~~  
 13 ~~intended to create any variance from the text of the UFTA, and is made in response to existing~~  
 14 ~~academic commentary that suggests that without the elevation, a risk exists for non-uniform~~  
 15 ~~interpretation. See Paul M. Shupack, Confusion in Policy and Language in the Uniform~~  
 16 ~~Fraudulent Transfer Act, 9 CARDOZO L. REV. 811, 830 n.84 (1987).~~

17  
18

19 **SECTION 3. VALUE.**

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21

**Comment**

22 (1) This section defines "value" as used in various contexts in this Act, frequently with a  
23 qualifying adjective. The word appears in the following sections:

24  
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26  
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- 4(a)(2) ("reasonably equivalent value");
- 4(b)(8) ("value ... reasonably equivalent);
- 5(a) ("reasonably equivalent value");
- 5(b) ("~~present, reasonably equivalent value~~");
- 8(a) ("reasonably equivalent value");
- 8(b), (c), (d), and (e) ("value");
- 8(f)(1) ("new value"); and
- 8(f)(3) ("~~present value~~").

33  
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35 **SECTION 4. TRANSFERS FRAUDULENT AS TO PRESENT AND FUTURE**  
36 **CREDITORS.**

37  
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**Comment**

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\* \* \*

(6)

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1 (j) Whether the transfer occurred shortly before or shortly after a substantial debt was  
2 incurred: Commerce Bank of Lebanon v. Halladale A Corp., 618 S.W. 2d 288, 292  
3 (Mo.App. 1981) (when transferors incurred substantial debts near in time to the transfer,  
4 transfer was held to be fraudulent due to inadequate consideration, close family relationship,  
5 the debtor's retention of possession, and the fact that almost all the debtor's property was  
6 transferred).

7  
8 ~~—(7) The effect of the two transfers described in § 4(b)(11), if not avoided, may be to~~  
9 ~~permit a debtor and a lienor to deprive the debtor's unsecured creditors of access to the~~  
10 ~~debtor's assets for the purpose of collecting their claims while the debtor, the debtor's~~  
11 ~~affiliate or insider, and the lienor arrange for the beneficial use or disposition of the assets in~~  
12 ~~accordance with their interests. (k) Whether the debtor transferred the essential assets of the~~  
13 ~~business to a lienor who transferred the assets to an insider of the debtor: Voest-Alpine~~  
14 ~~Trading USA Corp. v. Vantage Steel Corp., 919 F.2d 206 (3d Cir. 1990) (bank forecloses on~~  
15 ~~assets of steel company at 5:00 p.m. on a Friday, and then transfers assets to affiliate of~~  
16 ~~debtor; bank makes loan to affiliate to enable it to purchase at foreclosure sale on almost the~~  
17 ~~same terms as old loan; and new business opens up Monday morning.). The evil targeted by~~  
18 ~~this factor is not hard to identify: collusive and abusive use of a lienor's superior position to~~  
19 ~~eliminate junior creditors while leaving equity holders unaffected. The kind of disposition~~  
20 ~~sought to be reached here is exemplified by that found in Northern Pacific Co. v. Boyd, 228~~  
21 ~~U.S. 482 (1913), the leading case in establishing the absolute priority doctrine in~~  
22 ~~reorganization law. There the Court held that a reorganization whereby the secured~~  
23 ~~creditors and the management-owners retained their economic interests in a railroad through~~  
24 ~~a foreclosure that cut off claims of unsecured creditors against its assets was in effect a~~  
25 ~~fraudulent disposition (id. at 502-05). See Bruce A. Markell, Owners, Auctions and~~  
26 ~~Absolute Priority in Bankruptcy Reorganizations, 44 STAN. L. REV. 69, 74-83 (1991);~~  
27 ~~Frank, Some Realistic Reflections on Some Aspects of Corporate Reorganization, 19 Va.~~  
28 ~~L.Rev. 541, 693 (1933). For cases in which an analogous injury to unsecured creditors was~~  
29 ~~inflicted by a lienor and a debtor, see Jackson v. Star Sprinkler Corp. of Florida, 575 F.2d~~  
30 ~~1223, 1231-34 (8th Cir. 1978); Heath v. Helmick, 173 F.2d 157, 161-62 (9th Cir. 1949);~~  
31 ~~Toner v. Nuss, 234 F.S. 457, 461-62 (E.D.Pa. 1964); and see In re Spotless Tavern Co., Inc.,~~  
32 ~~4 F.Supp. 752, 753, 755 (D.Md. 1933).~~  
33  
34

## 35 SECTION 5. TRANSFERS FRAUDULENT AS TO PRESENT CREDITORS.

### 36 Comment

37  
38 (1) Subsection (a) is derived from § 4 of the Uniform Fraudulent Conveyance Act. It  
39 adheres to the limitation of the protection of that section to a creditor who extended credit before  
40 the transfer or obligation described. As pointed out in Comment (2) accompanying § 4, this Act  
41 substitutes "reasonably equivalent value" for "fair consideration."  
42

43 The classic condition of financial stringency was insolvency. Deming Hotel, 24 N.E.2d at  
44 912. One who has more debts than assets should not give away assets. Creditors are injured.  
45 Insolvency, however, is a term of art that has never acquired a fixed meaning. Legal insolvency,  
46 for example, refers to a balance sheet concept of more debts than assets; equitable insolvency

1 refers to the inability to pay current debts as they became due. As set forth above in the  
2 comments to section 2, the UFTA blends both tests.

3

4

[End Indiana]

5

6

PENNSYLVANIA

SECTION 1. DEFINITIONS.

Comments

(2) The definition of "asset" is substantially to the same effect as the definition of "assets" in § 1 of the Uniform Fraudulent Conveyance Act. The definition in this chapter, unlike that in the earlier Act, does not, however, require a determination that the property is liable for the debts of the debtor. Thus, an unliquidated claim for damages resulting from personal injury or a contingent claim of a surety for reimbursement, contribution or subrogation may be counted as an asset for the purpose of determining whether the holder of the claim is solvent as a debtor under [Section 2], although applicable law may not allow such an asset to be levied on and sold by a creditor. Cf. *Manufacturers & Traders Trust Co. v. Goldman (In re Ollag Construction Equipment Corp.)*, 578 F.2d 904, 907-09 (2d Cir. 1978).

\* \* \*

~~Since this Act~~ This chapter is not an exclusive law on the subject of voidable transfers and obligations (see Comment (8) to § 4 infra. In particular, and without limitation, this chapter does not preclude application of other law, which may include a common law of fraudulent transfer, to render voidable in an appropriate case a disposition of property that does not constitute an "asset" as defined in this chapter. Thus, for example, this chapter does not preclude the holder of a claim that may be collected by process against property generally exempt as to other creditors from obtaining relief from a disposition of such property that hinders, delays or defrauds the holder of such a claim. Likewise, the holder of an unsecured claim enforceable against tenants by the entirety is not precluded by this chapter from pursuing a remedy against a disposition of property held by the entirety that hinders, delays or defrauds the holder of such a claim. Similarly, the holder of a claim secured by a valid lien is not precluded by this chapter from pursuing a remedy against a disposition of the holder's collateral that hinders, delays or defrauds such holder. There are few reported cases in any jurisdiction dealing with fraudulent transfer of property that does not constitute an "asset" as defined in this chapter, and the extent, if any, to which a common law of fraudulent transfers, derived from the principles underlying the Statute of 13 Elizabeth as historically developed, may be appropriately invoked in such circumstances is left to judicial development. Cf. Comment 2(c) to U.C.C. § 9-306 (13 Pa.C.S. § 9306).

Nonbankruptcy law is the law of a state or federal law that is not part of the Bankruptcy Code, Title 11 of the United States Code. The definition of an "asset" thus does not include property that would be subject to administration for the benefit of creditors under the Bankruptcy Code unless it is subject under other applicable law, state or federal, to process for the collection of a creditor's claim against a single debtor.

Property encumbered by a valid lien is excluded from the definition of "asset" only "to the extent" the property is so encumbered. For example, in the case of property encumbered by a lien securing a contingent obligation, such as a guaranty, in general it would be appropriate to

1 value the obligation by discounting its face amount to reflect the probability that the guaranty  
2 will ever be called upon. Likewise, if an obligation is secured by a lien on several items of  
3 property and only one such item is disposed of, it may be appropriate to allocate the obligation  
4 among the items of property subject to the lien for the purpose of determining the "extent" to  
5 which the item disposed of is encumbered for purposes of this definition.

6  
7 \* \* \*

8  
9 (9) The definition of "property" is derived from § 1-201(33) of the Uniform Probate  
10 Code. Property includes both real and personal property, whether tangible or intangible, and any  
11 interest in property, whether legal or equitable. The definition of "property" is intended to be  
12 construed broadly, to include any right or interest that contributes to the value of a person.  
13 Hence, for example, "property" in general includes licenses, permits, franchises and contracts,  
14 whether or not transferable. In particular, but without limitation, governmental licenses and  
15 permits that contribute to the value of the holder in general should be deemed "property" of the  
16 holder, whether or not transferable, regardless of whether such items are deemed "property" for  
17 other purposes (e.g., regardless of whether such an item may be the subject of execution, or  
18 whether such an item is deemed a withdrawable privilege, rather than a property right, as against  
19 the issuing authority). Note, however, that such property may have little or no value in certain  
20 circumstances (e.g., such items, if nontransferable, may have no value if the holder is not valued  
21 on a going-concern basis). See Comment (1) to [Section 2] infra.

## 22 23 24 **SECTION 2. INSOLVENCY.**

### 25 26 **Comments**

27  
28 (1) Subsection (a) is derived from the definition of "insolvent" in § 101(32)(A) of the  
29 Bankruptcy Code. The definition in subsection (a) and the correlated definition of partnership  
30 insolvency in subsection (c) contemplate a fair valuation of the debts as well as the assets of the  
31 debtor. As under the definition of the same term in § 2 of the Uniform Fraudulent Conveyance  
32 Act, exempt property is excluded from the computation of the value of the assets. See the  
33 definition of the term "asset" in Section 1(b) supra. For similar reasons interests in valid  
34 spendthrift trusts and interests in tenancies by the entireties that cannot be severed by a creditor  
35 of only one tenant are not included. See the Comment to the definition of the term "asset" in  
36 Section 1(b) supra. Since a valid lien also precludes an unsecured creditor from collecting the  
37 creditor's claim from the encumbered interest in a debtor's property, both the encumbered interest  
38 and the debt secured thereby are excluded from the computation of insolvency under this  
39 chapter. See the definition of the term "asset" in Section 1(b) supra, and subsection (e) of this  
40 section.

41  
42 Under subsection (a) a person is "insolvent" if, at "fair valuations," debts exceed assets.  
43 By contrast, § 2 of the Uniform Fraudulent Conveyance Act defined a person to be "insolvent"  
44 when "the present fair salable value of his assets is less than the amount that will be required to  
45 pay his probable liability on his existing debts as they become absolute and matured."  
46 Depending on how the previous Act is interpreted, the two definitions may be quite different,

1 and, accordingly, cases construing "insolvency" under the previous Act need not necessarily  
2 have any persuasive force under this chapter. Two possible differences between the two  
3 standards are particularly noteworthy. First, the definition of "insolvency" in the previous Act  
4 mixed terms appropriate to the concept usually referred to as "balance sheet insolvency" (that is,  
5 debts in excess of assets, each valued appropriately) with other terms suggestive of the concept  
6 usually referred to as "equity insolvency" (that is, inability to pay debts as they become due).  
7 Subsection (a) clarifies that "insolvency" is defined solely in the "balance sheet" sense. "Equity  
8 insolvency" concepts are dealt with in [Section 4(a)(2)]. Second, the definition in the previous  
9 Act called for valuation of assets on the basis of their "present fair salable" value. This phrase  
10 too involved a certain degree of inherent contradiction, because "salable" value implies a  
11 liquidation value, and "present" suggests that such liquidation must be prompt, while "fair" value  
12 ordinarily connotes a less stringent and more flexible basis of valuation, not necessarily a  
13 liquidation value. The definition of "insolvency" in subsection (a) does not contain the words  
14 "salable" or "present," thereby removing any possible implication that liquidation is the required  
15 or preferred basis of valuation or that, if liquidation value is appropriate in a particular case, a  
16 prompt liquidation is necessarily appropriate. The definition of "insolvency" in subsection (a) is  
17 consistent with the better-reasoned authorities interpreting the definition of that term in the  
18 previous Act.

19  
20 This chapter does not define "fair valuation," nor does it specify any particular method of  
21 determining "fair valuation" however defined. Different bases of valuation may be appropriate  
22 depending upon the circumstances, and different methods of determining value on any particular  
23 basis may be appropriate depending upon the business engaged in by the debtor and other  
24 factors. For a debtor which is a business enterprise, valuation on the basis of continuation of the  
25 business by the debtor as a going concern ordinarily would be the appropriate basis of valuation  
26 if, at the time as of which the valuation is made, it reasonably would be expected that the  
27 enterprise will continue as a going concern. Particularly in such a case, appropriate values may  
28 be ascribed to goodwill and to nonassignable licenses, franchises, contracts and rights. Often it  
29 would be appropriate not to attempt to determine the value of separate assets and debts, but  
30 rather to determine only the "enterprise value" representing the aggregate difference between the  
31 debtor's assets and debts. Enterprise value should be determined by methods appropriate in the  
32 circumstances. It may be appropriate in many cases to determine enterprise value by multiplying  
33 earnings or cash flow measures by appropriate multipliers, or by discounting reasonably  
34 projected net cash flow at appropriate rates, for example. Even if it is appropriate in a particular  
35 case to value a business enterprise on a liquidation basis, it may be appropriate to value some or  
36 all of the assets on the assumption that they would be sold as one or more smaller going concerns  
37 (in which case the assets so disposed of should be valued in like manner, with appropriate values  
38 ascribed to goodwill and to licenses, franchises, contracts and rights which are assignable or for  
39 which consent to assignment may reasonably be expected; likewise, an "enterprise valuation" of  
40 such assets and related debts may be appropriate).

41  
42 As with valuation of assets, valuation of debts should take into account all relevant  
43 factors. For example, debt due in the future should not be valued at its face amount if the debt  
44 does not bear interest or bears interest at an inappropriately low rate. Rather, the face amount of  
45 such a debt should be discounted to its present value at an appropriate rate to reflect the time  
46 value of money. Likewise, in general, contingent liabilities and assets should be discounted by

1 factors representing the probability that such contingent liabilities or assets will ever be realized  
2 (as well as by factors representing the time value of money with respect to the resulting deferred  
3 payments or collections). For example, if a debtor enters into a written guaranty, the time as of  
4 which financial condition of the guarantor is to be determined for purposes of analyzing whether  
5 its obligation under the guaranty is fraudulent under [Section 4(a)(2) and 5(a)] is the date on  
6 which such guaranty is executed and delivered. See Section 6(5). When evaluating whether the  
7 guarantor is insolvent at such time, in making the "fair valuation of debts," the amount  
8 guaranteed should be discounted to reflect the probability at such time that the guarantor will be  
9 called upon to perform under the guaranty, and in making the "fair valuation of assets,"  
10 appropriate value should be ascribed to the guarantor's rights of reimbursement, subrogation,  
11 contribution, etc. Further adjustment of these contingent debts and assets to reflect the time  
12 value of money would also be appropriate.

13  
14 For a debtor that is a business enterprise, values shown on a balance sheet prepared in  
15 accordance with generally accepted accounting principles ("GAAP") generally would not be fair  
16 valuations as that term is used in this section. Such a balance sheet will have been prepared in  
17 accordance with accounting conventions that do not for the most part purport to reflect fair  
18 valuations (in any sense), nor will such a balance sheet necessarily reflect all of the debtor's  
19 assets and debts as defined in this chapter. For example, asset values under GAAP in most cases  
20 are based on historical costs rather than current fair valuations, and accounting conventions may  
21 ignore or relegate to footnotes certain assets and debts that should be taken into account in  
22 determining fair valuation, such as, for example, valuable contracts and leases, contingent assets  
23 and liabilities, and goodwill arising from operations. In some cases, however, a GAAP balance  
24 sheet may serve as a useful starting point in analyzing whether a debtor is insolvent, given  
25 suitable adjustments to the values of particular line-items and addition or deletion of line-items.

26  
27 This chapter is intended to enable creditors to recapture funds transferred to others in  
28 cases of actual or constructive fraud, as set forth in this chapter. On the other hand, the  
29 Pennsylvania Business Corporation Law ("BCL"), 15 Pa.C.S. §§ 1551, 1553, establishes the  
30 validity of distributions by Pennsylvania business corporations from the corporate law  
31 standpoint, determines the potential liability of directors for improper distributions, and gives  
32 directors the right to obtain contribution from shareholders in certain circumstances. In light of  
33 these diverse purposes, it is not necessary for the standards of this chapter describing the  
34 financial condition a corporation must have so that a distribution will not be constructively  
35 fraudulent under this chapter (set forth in this section and in 12 Pa.C.S. §§ 5104(a)(2) and 5105)  
36 to be identical to the standards of the BCL describing the financial condition a corporation must  
37 satisfy so that such distribution will be valid under the BCL. See also Comment (8) to [Section  
38 4] infra. Cf. Revised Model Business Corp. Act § 6.40, Comment 3 (1991);

39  
40 (6) Neither this chapter nor these comments comprehensively address such evidentiary  
41 and procedural matters as the standard of proof required to establish particular facts, allocation of  
42 the burden of proof and burden of persuasion, and the circumstances in which such burdens may  
43 shift. Certain specific points are addressed. See, e.g., subsection (b), Comment (5) to [Section  
44 4] infra, and Comments (1) and (6) to [Section 8] infra. Except for points specifically addressed,  
45 these matters are left to the courts to determine, giving appropriate consideration to, among other  
46 things, the policy of construing uniform laws to make uniform the laws of those states which

1 have enacted similar uniform laws (as set forth in 1 Pa.C.S. § 1927 and in the transitional  
2 provisions of the act enacting this chapter), the possible desirability of conformity with similar  
3 provisions of the Bankruptcy Code and, to the extent not inconsistent with this chapter, prior  
4 Pennsylvania case law. However, certain cases applying prior Pennsylvania law have stated in  
5 effect (if rephrased in the terms used in this chapter) that if a creditor establishes that the  
6 transferor was in debt at the time of a transfer, the burden shifts to the parties seeking to uphold  
7 the transfer to establish that the transferor received reasonably equivalent value or met the  
8 financial conditions required by 12 Pa.C.S. §§ 5104(a)(2) and 5105. Stinner v. Stinner, 300 Pa.  
9 Super. 351, 446 A.2d 651 (1982); In re Glenn, 108 Bankr. 70 (Bankr. W.D. Pa. 1989). That  
10 principle is an archaism and has not been consistently followed (compare, e.g., In re Joshua  
11 Slocum, Ltd., 103 Bankr. 610 (Bankr. E.D. Pa. 1989), aff'd mem., 121 Bankr. 442 (E.D. Pa.  
12 1989)), and in any event should not be followed in applying this chapter.

### 15 SECTION 3. VALUE.

#### 17 Comments

18  
19 (1) This section defines when "value" is given for a transfer or an obligation. The word  
20 "value" is used in that sense in various places in this chapter, frequently with a qualifying  
21 adjective. The word appears in that sense in the following sections of this chapter:

22  
23 § 4(a)(2) ("reasonably equivalent value");  
24 ~~§ 4(b)(8) ("Value ... reasonably equivalent");~~  
25 § 5(a) ("reasonably equivalent value");  
26 ~~§ 5(b) ("present, reasonably equivalent value")~~  
27 § 8(a) ("reasonably equivalent value");  
28 ~~§ 8(b), (c), (d) and (e) ("value"); and~~  
29 § 8 ("value"); and  
30 § 8(d) ("value")  
31 ~~§ 8(f)(1) ("new value"), and~~  
32 ~~§ 8(f)(2) ("present value").~~

33  
34 The word "value," and similar terms, are also used in other senses elsewhere in this chapter,  
35 including [Sections 8(b) and 8(c)] ("value" in the sense of the value of an asset fraudulently  
36 transferred), and [Sections 2(a) and 2(c)] ("value" and "fair valuation" in the sense of the value of  
37 a person's aggregate assets and debts). This section is not relevant to the meaning of the term  
38 "value" as used in such other senses.

39  
40 The definition in this section of "value," and hence of "reasonably equivalent value," is  
41 purely objective, as is also the case with the definition of "value" in § 548(d)(2) of the  
42 Bankruptcy Code. By contrast, the analogous definition of the term "fair consideration" in § 3 of  
43 the Uniform Fraudulent Conveyance Act required subjective "good faith" on the part of the  
44 transferee, as well as objective "fair equivalen[ce]" in the exchange. The meaning and purpose  
45 of the "good faith" element of the definition of "fair consideration" were never clear. For  
46 example, some courts construed it to mean that a preferential transfer on account of antecedent

1 debt from an insolvent debtor to a knowing recipient (or, perhaps, to a knowing recipient who is  
2 also an insider) is fraudulent because the recipient lacks "good faith." E.g., *Cohen v. Sutherland,*  
3 257 F.2d 737, 742 (2d Cir. 1958) (emphasizing the knowledge of the recipient); *Atlanta Shipping*  
4 *Corp. v. Chemical Bank,* 818 F.2d 240, 249 (2d Cir. 1987) (emphasizing the insider status of the  
5 recipient). Such holdings represent an unwarranted expansion of the scope of fraudulent transfer  
6 law. "If there is in our law one point which is more ungrudgingly accepted than others, it is that  
7 the preferential transfer does not constitute a fraudulent conveyance." 1 G. Glenn, *Fraudulent*  
8 *Conveyances and Preferences* § 289, at 488 (Rev. ed. 1940). See also Clark, *The Duties of the*  
9 *Corporate Creditor to its Creditors,* 90 Harv.L.Rev. 505, 506-16 (1979). Accord, e.g.,  
10 *Pennsylvania Turnpike Commission v. Evans,* 13 D.&C.2d 290, 299 (C.P. Dauphin 1957), *aff'd,*  
11 392 Pa. 110, 139 A.2d 530 (1958); *Berger v. Kraisman,* 376 Pa. 127, 130, 101 A.2d 717, 718  
12 (1954). The definition of "value" in this section removes the uncertainty created by the former  
13 requirement of "good faith" and, accordingly, among other things, clarifies that a preferential  
14 transfer, as such, by an insolvent is not fraudulent under this chapter, regardless of whether the  
15 transferee is an insider or has knowledge of the debtor's financial condition. See also Comment  
16 (2) to [Section 4] *infra*, and Comment (2) to [Section 5] *infra*.  
17

18 (2) Subsection (a) is adapted from § 548(d)(2)(A) of the Bankruptcy Code. See also  
19 § 3(a) of the Uniform Fraudulent Conveyance Act. The definition in subsection (a) is not  
20 exclusive. "Value" is to be determined in light of the purpose of this chapter to protect a debtor's  
21 estate from being depleted to the prejudice of the debtor's unsecured creditors. Consideration  
22 having no utility from a creditor's viewpoint does not satisfy the statutory definition. The  
23 definition does not specify all the kinds of consideration that do not constitute value for the  
24 purposes of this chapter -- e.g., love and affection. See, e.g., *United States v. West,* 299 F.Supp.  
25 661, 666 (D. Del. 1969). Services rendered the debtor may constitute value in an appropriate  
26 case. 1 G. Glenn, *Fraudulent Conveyances and Preferences* § 298b (Rev. ed. 1940).  
27

28 \* \* \*

29  
30 (4) Section 3(a) of the Uniform Fraudulent Conveyance Act has been thought not to  
31 recognize that an unperformed promise could constitute fair consideration. See *McLaughlin,*  
32 *Application of the Uniform Fraudulent Conveyance Act,* 46 Harv.L.Rev. 404,  
33 414 (1933). Courts construing these provisions of the prior law nevertheless have held  
34 unperformed promises to constitute value in a variety of circumstances. See, e.g., *Harper v.*  
35 *Lloyd's Factors, Inc.,* 214 F.2d 662 (2d Cir. 1954) (transfer of money for promise of factor to  
36 discount transferor's purchase-money notes given to fur dealer); *Schlecht v. Schlecht,* 168 Minn.  
37 168, 176-77, 209 N.W. 883, 886-87 (1926) (transfer for promise to make repairs and  
38 improvements on transferor's homestead); *Farmer's Exchange Bank v. Oneida Motor Truck Co.,*  
39 202 Wis. 266, 232 N.W. 536 (1930) (transfer in consideration of assumption of certain of  
40 transferor's liabilities); see also *Hummel v. Cernocky,* 161 F.2d 685 (7th Cir. 1947) (transfer in  
41 consideration of cash, assumption of a mortgage, payment of certain debts, and agreement to pay  
42 other debts). Likewise a transfer in consideration of a negotiable note discountable at a  
43 commercial bank, or the purchase from an established, solvent institution of an insurance policy,  
44 annuity, or contract to provide care and accommodations clearly appears to be for value. On the  
45 other hand, a transfer for an unperformed promise by an individual to support a parent or other  
46 transferor has generally been held voidable as a fraud on creditors of the transferor. See, e.g.,

1 Springfield Ins. Co. v. Fry, 267 F.Supp. 693 (N.D.Okla. 1967); Sandler v. Parlapiano, 236  
2 App.Div. 70, 258 N.Y.Supp. 88 (1st Dep't 1932); Warwick Municipal Employees Credit Union  
3 v. Higham, 106 R.I. 363, 259 A.2d 852 (1969); Hulsether v. Sanders, 54 S.D. 412, 223 N.W. 335  
4 (1929); Cooper v. Cooper, 22 Tenn.App. 473, 477, 124 S.W.2d 264, 267 (1939); Note, Rights of  
5 Creditors in Property Conveyed in Consideration of Future Support, 45 Iowa L. Rev. 546,  
6 550-62 (1960). This chapter adopts the view taken in the cases cited in determining whether an  
7 unperformed promise is value.

8  
9 Accordingly, pursuant to subsection (a), the general rule is that an unperformed promise  
10 may constitute value, and the amount of value to be ascribed to an unperformed promise in a  
11 particular case is a factual question. This general rule is subject to the exception that no value  
12 may ever be attributed to an unperformed promise made otherwise than in the ordinary course of  
13 the promisor's business to furnish support to the debtor or another person. "Support" in this  
14 context refers to housing, feeding, clothing, medical care, recreation, education, travel, burial and  
15 similar services and expenses provided to an individual. "Support" in this context does not refer  
16 to commercial arrangements sometimes loosely referred to as "credit support" or "financial  
17 support" (such as, for example, a guaranty or standby letter of credit provided by one person to  
18 back obligations of another, or a so-called "keep-well" agreement whereby one person, typically  
19 a parent corporation, agrees not to permit the financial condition of another person, typically a  
20 subsidiary corporation, to fail to meet certain minimum requirements).

## 21 22 23 **SECTION 4. TRANSFERS FRAUDULENT AS TO PRESENT AND FUTURE** 24 **CREDITORS.**

### 25 26 **Comments**

27  
28 \* \* \*

29  
30 (2) Subsection (a)(2) is derived from §§ 5 and 6 of the Uniform Fraudulent Conveyance  
31 Act but substitutes "reasonably equivalent value" for "fair consideration." The transferee's good  
32 faith was an element of "fair consideration" as defined in § 3 of the Uniform Fraudulent  
33 Conveyance Act, and lack of fair consideration was one of the elements of a fraudulent transfer  
34 as defined in four sections of the Uniform Fraudulent Conveyance Act. The transferee's good  
35 faith is irrelevant to a determination of the adequacy of the consideration under this chapter, but  
36 lack of good faith may be a basis for withholding protection of a transferee or obligee under  
37 [Section 8] infra. See also Comment (1) to [Section 3].

38  
39 \* \* \*

40  
41 (4) Paragraph (a)(2)(i) is an adaptation of § 5 of the Uniform Fraudulent Conveyance  
42 Act but substitutes "unreasonably small [assets] in relation to the business or transaction" for  
43 "unreasonably small capital." The reference to "capital" in the Uniform Fraudulent Conveyance  
44 Act is ambiguous in that it may refer to, among other things, net worth or to the par value of  
45 stock or to the consideration received for stock issued. The special meanings of "capital" in  
46 corporation law have no relevance in the law of fraudulent transfers. The subparagraph focuses

1 attention on whether the amount of all the assets retained by the debtor was inadequate, i.e.,  
2 unreasonably small, in light of the needs of the business or transaction in which the debtor was  
3 engaged or about to engage (and hence taking into account, among other things, the debtor's  
4 present and prospective debts, and whether the retained assets are sufficiently liquid to enable the  
5 debtor to pay such debts as they become due).

6  
7 In general, the tests of paragraphs (a)(2)(i) and (a)(2)(ii) should be viewed as addressing  
8 slightly different aspects of the same fundamental inquiry: whether the debtor is and, on a  
9 continuing basis, will be able to pay its debts as they become due. By definition, a debtor which  
10 reasonably should be able to pay its debts as they become due on a continuing basis should be  
11 deemed to have adequate assets in relation to its business or transaction, sufficient to satisfy the  
12 test of paragraph (a)(2)(i), and such debtor also should be deemed to satisfy the "reasonably  
13 should have believed" test of paragraph (a)(2)(ii). In evaluating whether a debtor reasonably  
14 should be able to pay its debts as they become due on a continuing basis, it may be useful to  
15 prepare financial projections for the debtor as of the time of such transfer. If such financial  
16 projections show that the debtor will be able to pay its debts as they become due on a continuing  
17 basis, the debtor should be deemed to satisfy paragraph (a)(2)(i), as well as the "reasonably  
18 should have believed" test under paragraph (a)(2)(ii), if such financial projections were  
19 reasonable as of the time of the transfer (and hence, among other things, were based on  
20 assumptions which at such time were reasonable). The debtor should not be responsible as a  
21 matter of hindsight for developments that could not reasonably have been foreseen at the time of  
22 the transfer. "[T]he question the court must decide is not whether [the] projection was correct,  
23 for clearly it was not, but whether it was reasonable and prudent at the time it was made." Credit  
24 Managers Association of Southern California v. Federal Co., 629 F.Supp. 175, 184 (C.D. Cal.  
25 1985). Among other matters, appropriate weight should be given to the likelihood that maturing  
26 debts will be refinanced where, on the basis of the debtor's financial condition and future  
27 prospects and the general availability of credit to debtors similarly situated, it is reasonable to  
28 assume that such refinancing may be accomplished; appropriate weight should be given to the  
29 debtor's ability to pay debts by disposing of fixed assets or other transactions outside the ordinary  
30 course of business; and appropriate allowance should be made for reasonably foreseeable  
31 contingent obligations as they become absolute.

32  
33 The tests stated in subsection (a)(2) should be distinguished from the test stated in  
34 [Section 2(b)], which creates a rebuttable presumption that a debtor is insolvent if such debtor  
35 "is generally not paying his or her debts as they become due." [Section 2(b)], like § 303(h)(1) of  
36 the Bankruptcy Code, is not susceptible to mechanical definition, but usually should be  
37 considered to call for inquiry mainly into the extent to which the debtor is now actually paying  
38 debts presently due. See Comment (2) to [Section 2]. By contrast, the tests stated in subsection  
39 (a)(2) call for inquiry into the debtor's ability (and intentions and beliefs with respect to such  
40 ability) to pay its debts, then existing and thereafter incurred, on a continuing basis now and in  
41 the future.

42  
43 (5) Subsection (b) below is a nonexclusive catalogue of factors appropriate for  
44 consideration by the court in determining whether the debtor had an actual intent to hinder, delay  
45 or defraud one or more creditors. Proof of the existence of any one or more of the factors  
46 enumerated in subsection (b) may be relevant evidence as to the debtor's actual intent but does

1 not create a presumption that the debtor has made a fraudulent transfer or incurred a fraudulent  
2 obligation. The list of factors includes most of the badges of fraud that have been recognized by  
3 the courts in construing and applying the Statute of 13 Elizabeth and § 7 of the Uniform  
4 Fraudulent Conveyance Act. Proof of actual intent is unnecessary in a case in which subsection  
5 (a)(2) or [Section 5(a)] applies. The fact that a transfer has been made to a relative or to an  
6 affiliated corporation has not been regarded as a badge of fraud sufficient to warrant avoidance  
7 when unaccompanied by any other evidence of fraud. The courts have uniformly recognized,  
8 however, that a transfer to a closely related person warrants close scrutiny of the other  
9 circumstances, including the nature and extent of the consideration exchanged. See 1 G. Glenn,  
10 Fraudulent Conveyances and Preferences § 307 (Rev. ed. 1940). See also Comment (12) to  
11 [Section 1]. The second, third, fourth, and fifth factors listed are all adapted from the classic  
12 catalogue of badges of fraud provided by Lord Coke in Twyne's Case, 3 Coke 80b, 76 Eng.Rep.  
13 809 (Star Chamber 1601). Lord Coke also included the use of a trust and the recitation in the  
14 instrument of transfer that it "was made honestly, truly, and bona fide," but the use of the trust is  
15 fraudulent only when accompanied by elements or badges specified in this chapter, and recitals  
16 of "good faith" can no longer be regarded as significant evidence of a fraudulent intent.

17  
18 \* \* \*

19  
20 (8) This chapter, like its predecessor, the Uniform Fraudulent Conveyance Act, does not  
21 purport to cover the whole law of voidable transfers and obligations. Accordingly, nothing in  
22 subsection (b) is intended to affect the application of §§ 2-402(2), 9-205, 9-301, or 6-105 of the  
23 Uniform Commercial Code (13 Pa.C.S. §§ 2402(b), 9205, 9301, 6105). Section 2-402(2) (13  
24 Pa.C.S. § 2402(b)) recognizes the generally prevailing rule that retention of possession of goods  
25 by a seller may be fraudulent but limits the application of the rule by negating any imputation of  
26 fraud from "retention of possession in good faith and current course of trade by a merchant-seller  
27 for a commercially reasonable time after a sale or identification." Section 9-205 (13 Pa.C.S.  
28 § 9205) explicitly negates any imputation of fraud from the grant of liberty by a secured creditor  
29 to a debtor to use, commingle or dispose of personal property collateral or to account for its  
30 proceeds. The section recognizes that it does not relax prevailing requirements for delivery of  
31 possession by a pledgor. Moreover, the section does not mitigate the general requirement of § 9-  
32 301(1)(b) (13 Pa.C.S. 9301(a)(2)) that a nonpossessory security interest in personal property  
33 must be accompanied by notice-filing to be effective against a levying creditor. Finally, like the  
34 Uniform Fraudulent Conveyance Act this chapter does not pre-empt the statutes governing bulk  
35 transfers, such as Article 6 of the Uniform Commercial Code (to the extent, if any, that such  
36 statutes remain in force notwithstanding the recommendation by the National Conference of  
37 Commissioners on Uniform State Laws in 1989 to repeal Article 6). Compliance with the cited  
38 sections of the Uniform Commercial Code does not, however, insulate a transfer or obligation  
39 from avoidance. Thus a sale by an insolvent debtor for less than a reasonably equivalent value  
40 may be voidable under this chapter notwithstanding compliance with the Uniform Commercial  
41 Code. Likewise, this chapter does not pre-empt statutes governing the ability of a business  
42 corporation, partnership, business trust or other entity to make distributions to its shareholders,  
43 partners, beneficiaries or analogous persons; but compliance with such other statutes does not  
44 insulate such distributions from avoidance under this chapter.

1 **SECTION 7. REMEDIES OF CREDITORS.**

2  
3 **Comments**

4 \* \* \*

5  
6 (7) Particularly if a transaction avoided under subsection (a)(1) is an obligation rather  
7 than a transfer, equitable principles should govern what specific remedy or remedies properly  
8 constitute "avoidance" in a particular case. Such remedies should be fashioned in light of the  
9 long-established principle that a transaction fraudulent under this chapter and its predecessors,  
10 even if avoidable by creditors, remains enforceable as between the parties to the transaction.  
11 See, e.g., Smith v. Arrell, 388 Pa. 117, 130 A.2d 167 (1957). Accordingly, even if an obligation  
12 is subject to avoidance under this chapter, it may be inappropriate simply to void or cancel the  
13 obligation, because such an obligation should still rank ahead of equity interests in the debtor. In  
14 many cases the most appropriate remedy will be equitable subordination of the obligation. See,  
15 e.g., In re Crowthers McCall Pattern, Inc., 120 Bankr. 279, 288 (Bankr. S.D.N.Y. 1990).  
16

17  
18 **SECTION 8. DEFENSES, LIABILITY AND PROTECTION OF TRANSFEREE.**

19  
20 **Comments**

21 \* \* \*

22  
23  
24 (2) Subsection (b) is derived from § 550(a) and § 550(b) of the Bankruptcy Code. The  
25 value of the asset transferred is limited to the value of the levyable interest of the transferor,  
26 exclusive of any interest encumbered by a valid lien. See the definition of the term "asset" in  
27 [Section 1(b)] supra.  
28

29 \* \* \*

30  
31 (5) Subsection (e)(1) rejects the rule adopted in Darby v. Atkinson (In re Farris), 415  
32 F.Supp. 33, 39-41 (W.D. Okla. 1976), that termination of a lease on default in accordance with  
33 its terms and applicable law may constitute a fraudulent transfer. Subsection (e)(2) protects a  
34 transferee who acquires a debtor's interest in an asset as a result of the enforcement of a secured  
35 creditor's rights pursuant to and in compliance with the provisions of Article 9 of the Uniform  
36 Commercial Code, except for the provisions of § 9-505(2) (relating to acceptance of collateral as  
37 discharge of obligation). Cf. Calaiaro v. Pittsburgh Nat'l Bank (In re Ewing), 33 B.R. 288, 9  
38 C.B.C.2d 526, CCH B.L.R. ¶ 69,460 (Bk. W.D.Pa. 1983) (sale of pledged stock held subject to  
39 avoidance as fraudulent transfer in § 548 of the Bankruptcy Code), rev'd, 36 B.R. 476 (W.D.Pa.  
40 1984) (transfer held not voidable because deemed to have occurred more than one year before  
41 bankruptcy petition filed). Although a secured creditor may enforce rights in collateral without a  
42 sale under § 9-502 of the Code (13 Pa.C.S. § 9502), the creditor must proceed in good faith  
43 (U.C.C. § 9-103 (13 Pa.C.S. § 9103)) and in a "commercially reasonable" manner (U.C.C. § 9-  
44 502(2) (13 Pa.C.S. § 9502(b))). Subsection (e)(2) and [Section 3(b)] may both apply to  
45 enforcement of a security interest in compliance with Article 9 of the Uniform Commercial  
46 Code. These two provisions are cumulative and do not limit each other.

1  
2 [(7)] As used in this section, "good faith" means that the transferee or obligee acted  
3 without actual fraudulent intent and that the transferee or obligee did not collude with the debtor  
4 or otherwise actively participate in the fraudulent scheme of the debtor. A transferee's or  
5 obligee's knowledge of a transferor's insolvency, in and of itself, is insufficient to support a  
6 finding that the transferee or obligee lacked "good faith" as that term is used in this section. The  
7 transferee's or obligee's knowledge of the transferor's insolvency may, however, in combination  
8 with the transferee's or obligee's knowledge concerning other facts, be relied upon as evidencing  
9 a lack of "good faith" on the part of the transferee or obligee.

10  
11 In the same vein, the requirement of Bankruptcy Code § 550(b)(1) that the transferee be  
12 "without knowledge of the voidability of the transfer" in order to be protected has been omitted  
13 from subsection (b)(2) as inappropriate. Knowledge of the voidability of a transfer would seem  
14 to involve a legal conclusion. Determination of the voidability of the transfer ought not to  
15 require the court to inquire into the legal sophistication of the transferee. *[N.B. This paragraph*  
16 *appears in Comment 1 to Section 2 in the official text.]*

17  
18 Similarly, knowledge on the part of a subsequent transferee that a transfer is made as a  
19 gift or for a nominal consideration between the original transferor and the initial transferee  
20 should not, in and of itself, constitute a basis for finding that the subsequent transferee lacked  
21 "good faith," nor should such knowledge impose any duty on the subsequent transferee to make  
22 inquiry as to whether the original transfer was or was not fraudulent as to the creditors of the  
23 original transferor. *[Citation omitted]*

24  
25  
26 [End Pennsylvania]  
27  
28