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**Indirect Benefits
In
Fraudulent Transfer Cases**



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Submitted for the American Bankruptcy Institute Southwest Conference - 2009

2009 Southwest Bankruptcy Conference

I. Introduction

As a general rule, the debtor's payment of a debt of another is a constructive fraudulent transfer under 11 U.S.C. § 548(a) and the Uniform Fraudulent Transfer Act if the debtor was insolvent or was rendered insolvent by the transfer. *See, e.g., Rubin v. Manufacturers Hanover Trust Co.*, 661 F.2d 979 (2d Cir. 1981); *Pummill v. Greensfelder, Hemker & Gale (In re Richards & Conover Steel, Co.)*, 267 B.R. 602 (B.A.P. 8th Cir. 2001); *McKloskey v. Galva Foundry Co., Inc. (In re Art Unlimited, LLC)*, 356 B.R. 700 (Bankr. E.D. Wis. 2006); *Keith Eickert Power Prods., LLC v. Escada (In re Keith Eickert Power Prods., LLC)*, 344 B.R. 685 (Bankr. M.D. Fla. 2006); *Wessinger v. Spivey (In re Galbreath)*, 286 B.R. 185 (Bankr. S.D. Ga. 2002).

However, if the debtor's payment of the debt of another provided the debtor with an indirect benefit and the value of that benefit was reasonably equivalent to the debtor's payment, then the debtor's payment was not a constructive fraudulent transfer. The cases addressing these claims fall into three categories:

- At one end of the spectrum are the cases in which the debtor's payment was found not to result in any benefit to the debtor. (Part II, below.)
- At the other end of the spectrum are those cases in which the court found a straightforward dollar-for-dollar benefit, usually because the debtor's payment of a debt of a third party also had the effect of reducing the debtor's obligations to that third party. (Part III, below.)
- Finally the cases in the middle of the spectrum must identify the benefit to the debtor from its payment and then determine whether the value of that benefit was reasonably equivalent to the debtor's payment. The benefit in these cases is usually an intangible benefit. (Part IV, below.)

The review of these cases below demonstrates that some courts have been more rigorous than others in their analysis of reasonably equivalent value.

The cases also reflect some divergent views on the burden of proof on these claims. (Part V, below.)

II. Cases Finding That the Debtor's Payment Resulted in No Benefit to the Debtor

Jensen v. Bank of Am. Mortgage Capital Corp. (In re General Mortgage Corp. of Am., Inc.), 399 B.R. 708 (Bankr. M.D. Fla. 2008). The court set aside monthly mortgage payments that debtor had made on account of a debt owed by debtor's principals.

In re Keith Eickert Power Products, LLC, 344 B.R. 685 (Bankr. M.D. Fla. 2006). The wife of the debtor's principal used the debtor's debit card for purchases of expensive clothing. The court found that the clothing was not of benefit to the debtor in its marine engine business.

In re Galbreath, 286 B.R. 185 (Bankr. S.D. Ga. 2002). The debtor signed a note and security agreement to guaranty his corporation's preexisting debt. The court found that the debtor did not receive reasonably equivalent value because his net worth had not been preserved. The debtor's salary and use of car were not reasonably equivalent value because the debtor only became an employee after signing the guaranty.

Brady v. Bestworth-Rommel, Inc. (In re Johnson), 357 B.R. 136 (Bankr N.D. Cal. 2006). The husband-debtor's corporation owed a debt on mechanic's lien. The debt was paid by the wife-debtor. The court found no benefit to the wife-debtor from this payment. (However, the court sustained the defendant's defense under § 550(b)(1).)

Roeder v. Lockwood (In re Lockwood Auto Group, Inc.), 370 B.R. 652 (Bankr. W.D. Pa. 2007). The debtor granted a security interest in a certificate of deposit to secure a loan to the

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debtor's shareholder. The court did not consider that this security interest was part of a refinancing transaction that allowed the debtor to remain in business and found that the debtor received no value for the transfer.

Whitaker v. Volvo Commercial Fin. LLC (In re Gulf N. Transport, Inc.), 323 B.R. 786 (Bankr. M.D. Fla. 2005). The debtor paid the principal's debt on two trucks. The court found that the debtor benefitted from the use of one of the two trucks and that the value of the use was reasonably equivalent to the debtor's payment on that truck. However, the debtor's payments on a second truck were avoided because the debtor did not have use of that truck.

Unencumbered Assets Trust v. Biomar Tech., Inc. (In re Nat'l Century Fin. Enters., Inc.), 341 B.R. 198 (Bankr. S.D. Ohio 2006). The debtor paid the defendant for software licenses used by third parties. The court held that the plaintiff met its burden of showing no direct benefit and then analyzed whether the defendants met their burden of showing indirect benefits to the debtor. The court held that an undocumented promise to the debtor to pay the debts of its subsidiaries was worthless because of that party's own insolvency. The court further found no other "concrete, identifiable" indirect benefit. *See also, Cent. Nat'l Bank of Cleveland v. Coleman (In re B-F Bldg. Corp.)*, 312 F.2d 691, 694 (6th Cir. 1963) ("worthless" demand promissory note issued by insolvent entity did not provide reasonably equivalent value); *Frank v. Kiesel (In re Denison)*, 292 B.R. 150, 154 (E.D. Mich. 2003) ("[A] future return on an investment could constitute 'reasonably equivalent value' for the initial purpose, [but] there must be some 'legitimate and reasonable' chance of return.") (quoting *Mellon Bank, N.A. v. Official Comm. of Unsecured Creditors of R.M.L. (In re R.M.L., Inc.)*, 92 F.3d 139, 152 (3rd Cir. 1996)).

In re R.M.L., Inc., 92 F.3d 139 (3d Cir. 1996). The debtor paid a deposit and fees to the defendant for a failed loan commitment. The court affirmed the trial court's finding that the debtor

received no indirect benefits from these payments. Other creditors had agreed to extend credit terms, but not as a result of the defendant's commitment letter.

Stillwater Nat'l Bank & Trust Co. v. Kirtley (In re Solomon), 299 B.R. 626 (B.A.P. 10th Cir. 2003). The debtors granted two mortgages to secure their previously unsecured guaranty. The court sustained the trial court's finding of no reasonably equivalent value.

Meeks v. Don Howard Charitable Remainder Trust (In re S. Health Care of Arkansas, Inc.), 309 B.R. 314 (B.A.P. 8th Cir. 2004). The debtor made the mortgage payments on behalf of a third party. The court sustained the trial court's finding of no reasonably equivalent value.

III. Cases Finding That the Debtor's Payment Resulted in a Dollar-For-Dollar Benefit to the Debtor

In re Art Unlimited, LLC, 356 B.R. 700 (Bankr. E.D. Wis. 2006). The debtor's payments of the principal's debts did benefit the debtor, where the payment released security that the principal's creditor applied to pay the debtor's debt.

Harker v. Center Motors, Inc. (In re Gerdes), 246 B.R. 311 (Bankr. S.D. Ohio 2000). A creditor of the debtor's auto dealership held the title of a car as security for a debt of the dealership. After the dealership sold the vehicle, the debtor paid the dealership's debt to obtain a title from the creditor so that it could be delivered to the purchaser. The court found that the debtor benefitted from her payment of the debt to the dealership's creditor because of her potential personal liability for failure to deliver title and failure to pay the applicable sales tax. The court further found that this benefit was reasonably equivalent value.

Dowden v. First Sec. Bank (In re Mid-South Auto Brokers, Inc.), 290 B.R. 658 (Bankr. E.D. Ark. 2003). The debtor's principal borrowed funds to purchase a vehicle for the debtor's inventory. The debtor repaid the loan when it sold the vehicle. The court held that the debtor received

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reasonably equivalent value for its payment because the debtor had incurred a debt to the principal when the principal borrowed the funds to purchase the vehicle for the debtor in the first instance.

Schoenmann v. BCCI Constr. Co. (In re NorthPoint Commc'ns Group, Inc.), 361 B.R. 149 (Bankr. N.D. Cal. 2007). The debtor paid an invoice from the defendant on construction debts owed to the defendant and third parties. The court held that the debtor did receive reasonably equivalent value for the payments made on account of the debts to the third parties because the defendant used the payment to pay the debtor's debts to those third parties.

Goldberg v. Countrywide Home Loans, Inc. (In re Seaway Int'l Transport, Inc.), 341 B.R. 333 (Bankr. S.D. Fla. 2006). The debtor made payments on the mortgage on the principal's personal residence. The court found reasonably equivalent value because the mortgage payments were the principal's only compensation.

Lisle v. John Wiley & Sons, Inc. (In re Wilkinson), 196 Fed.Appx. 337 (6th Cir. 2006). The debtor paid for books sold to the debtor's corporation for inventory. Because the payment reduced the debtor's debt to his corporation, the court held there was reasonably equivalent value. The debtor's insolvency at the time of the payment does not suggest otherwise.

IV. Cases Addressing Intangible Benefits

Cordes & Co., LLC v. Mitchell Companies, LLC, 605 F.Supp.2d 1015 (N.D. Ill. 2009). The receivership entities paid the debts of affiliates. The Court held, "Given the apparent close affiliation of the [receivership entities] with [the affiliates], they may have received some indirect benefit such as goodwill or overall synergy of the corporate group as a result of the transfers. However, whether they received such a benefit cannot be determined on this record, and must instead be determined by the trier of fact." *Id.* at 1023. The Court stated:

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Indirect benefits can include a wide range of intangibles such as a corporation's goodwill or increased ability to borrow working capital; the general relationship between affiliates or "synergy" within a corporate group as a whole; or a corporation's ability to retain an important source of supply or an important customer. *See id.* at 578-79; see also *In re Fairchild Aircraft Corp.*, 6 F.3d 1119, 1127 (5th Cir.1993) (corporation's ability to keep affiliated corporation in operation was an indirect benefit constituting reasonably equivalent value); *Mellon Bank N.A. v. Metro Comms., Inc.*, 945 F.2d 635, 646-48 (3d Cir.1991) (indirect benefits of corporate goodwill and ability to obtain credit must be considered in assessing reasonably equivalent value). The Receiver fails to consider this aspect of reasonably equivalent value when arguing that the Receivership Entities received no value in exchange for the wire transfers.

Id. at 1022 (citing *Leibowitz v. Parkway Bank & Trust Co. (In re Image Worldwide, LTD.)*, 139 F.3d 574 (7th Cir. 1998)).

Collins & Aikman Corp v. Valeo (In re Collins & Aikman Corp.), 401 B.R. 900 (Bankr. E.D. Mich. 2009). Debtor brought adversary proceedings against suppliers that sold goods to non-debtor subsidiary and received payment from bank accounts of the debtor. The court held, "[T]here are genuine issues of material fact as to: (1) whether the debtors did in fact receive any value in exchange for the challenged transfers, and (2) if so, whether such value was reasonably equivalent." *Id.* at 906.

Satriale v. Key Bank USA, N.A. (In re Burry), 309 B.R. 130 (Bankr. E.D. Pa. 2004). The debtor made some of the payments on a friend's boat loan, in exchange for which the owner allowed the debtor to use the boat. The court found that the debtor's payments on the owner's loan did indirectly benefit the debtor and that the debtor's payments were reasonably equivalent to the value of the debtor's use of the boat.

Creditors' Comm. of Jumer's Castle Lodge, Inc. v. Jumer (In re Jumer's Castle Lodge, Inc.), 338 B.R. 344 (C.D. Ill. 2006). The debtor transferred assets to its shareholder as part of a sale and refinancing arrangement with a new investor. The court held that when evaluating whether the



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debtor received reasonably equivalent value, all of the value that the debtor received in the transaction had to be considered. The court found that the debtor received more in value than it transferred to its shareholder.

Mellon Bank, N.A. v. Metro Commc'ns, Inc., 945 F.2d 635 (3d Cir. 1991). In a leveraged buy out, the debtor executed a guaranty and granted a security interest to the creditor that financed the acquisition of the debtor. The court stated:

The touchstone is whether the transaction conferred realizable commercial value on the debtor reasonably equivalent to the realizable commercial value of the assets transferred. Thus, when the debtor is a going concern and its realizable going concern value after the transaction is equal to or exceeds its going concern value before the transaction, reasonably equivalent value has been received.

Id. at 647.

The court found that the transaction allowed the debtor to borrow needed working capital, although it agreed that this value of this opportunity was difficult to quantify. The transaction also allowed the debtor and the acquirer synergies of business that enhanced the debtor's value, although again the court observed that this value was difficult to quantify. Ultimately, the court determined that the plaintiff had failed to establish that the transaction left the debtor insolvent, because in valuing the guarantees, plaintiff did not account for the value of other guarantees.

In re Richards & Conover Steel, Co., 267 B.R. 602 (B.A.P. 8th Cir. 2001). The debtor paid the attorney fees for a prepetition unofficial creditors committee that was formed to protect the creditors' interests during liquidation of the debtor's assets. The court held:

As a direct result of the efforts of [the attorneys], Rich-Con maximized its assets by collecting receivables and reducing its debts. Its fiscal situation was improved. Rich-Con received services of [the attorneys] just as it would have if it had hired the firm directly. In this context, it makes no difference who hired the firm and who was ultimately responsible for paying its fees. [The attorneys] transferred value in the form of legal services to Rich-Con.

Id. at 613.

Garrett v. Falkner (In re Royal Crown Bottlers of North Alabama, Inc.), 23 B.R. 28 (Bankr. N.D. Ala. 1982). The debtor- subsidiary paid a debt of its parent. The court distinguished the case in which “the debtor and the third party are so related or situated that they share an ‘identity of interests,’ because what benefits one will, in such case, benefit the other to some degree.” The court then stated, “The ultimate question then becomes one of determining the value of this vicarious benefit and testing it by the measure of ‘reasonably equivalent’ for the property transferred by the insolvent debtor.” *Id.* at 30. (Footnote omitted.) The court continued:

When the consideration for a transfer passes to the parent corporation of a debtor-sub subsidiary making the transfer, as in the case here, the benefit to the debtor may be presumed to be nominal, in the absence of proof of a specific benefit to it. On the other hand, the passing to a subsidiary of the consideration for a transfer by a debtor-parent may be presumed to be substantial, because the subsidiary corporation is an asset of the parent corporation, and what benefits the asset will ordinarily accrue to the benefit of its owner.

(Ultimately the court found that because the funds of the parent and subsidiary were commingled, the plaintiff could not establish that the payment sought to be recovered was a transfer of the debtor.)

Rubin v. Manufacturers Hanover Trust Co., 661 F.2d 979 (2d Cir. 1981). The debtor was in the money order business and executed guarantees of its sales agents’ debts to the defendant. The court vacated the trial court’s finding of reasonably equivalent value, finding that the trial court had not quantified the value of the claimed indirect benefits. The court stated that the trial court “did not attempt to quantify the indirect benefits to either issuer or to compare those benefits with the obligations assumed by the issuers under the guarantees. Without such an analysis, it was impossible for the court to determine whether the estate of either issuer had been conserved[.]” *Id.* at 993. Accordingly the matter was remanded with detailed instructions on how the trial court

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should conduct the analysis of reasonably equivalent value.

Pension Transfer Corp. v. Beneficiaries Under Third Amendment To Fruehauf Trailer Corp. Ret. Plan No. 003., 319 B.R. 76 (D. Del. 2005). The debtor amended its pension plan to increase the retirement benefits to its employees. The court held that this amendment was a transfer and that it did benefit the debtor in retaining employees. However, the court found that because the market cost of employee retention was 0.4% of sales and the cost of debtor's pension plan amendment was 0.8% of sales, the debtor did not receive reasonably equivalent value for its plan amendment.

See also SPC Plastics Corp. v. Griffith (In re Structurelite Plastics Corp.), 224 B.R. 27, 31 (B.A.P. 6th Cir. 1998) (noting that the speculative value of indirect benefits like the opportunity to acquire additional loans or new managerial talent does not constitute fair consideration); *Clark v. Sec. Pac. Bus. Credit (In re Wes Dor, Inc.)*, 996 F.2d 237, 243 (10th Cir. 1993) ("To the extent indirect benefits could be considered . . . the Bank fails to point to any evidence quantifying the amount of such benefits.").

V. Burden of Proof in Indirect Transfer Cases

There is substantial authority that in an indirect transfer case, once the plaintiff has shown that the transfer was for the benefit of a third-party, the burden shifts to the defendant to prove that the debtor received reasonably equivalent value indirectly as a result of the transfer. *See, e.g.:*

First Nat'l Bank in Anoka v. Minn. Utility Contracting, Inc. (In re Minn. Utility Contracting, Inc.), 110 B.R. 414, 419 (D. Minn. 1990).

Braunstein v. Walsh (In re Rowanoak Corp.), 344 F.3d 126, 131-32 (1st Cir. 2003) ("[o]nce the Trustee establishes his prima facie case, he need not affirmatively disprove every other potential theory.").

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In re Richards & Conover Steel, Co., 267 B.R. 602, 614 (B.A.P. 8th Cir. 2001) (“party claiming to have delivered value must quantify it.”).

Commerce Bank of Kansas City, N.A. v. Achtenberg, 1993 WL 476510, *3 (W.D. Mo. 1993) (“[T]he court’s rationale in *Minnesota Utility* is well reasoned and fully supported by other courts and commentators interpreting § 548(a)(2).”).

Leonard v. Mountainwest Fin. Corp. (In re Whaley), 229 B.R. 767, 775 (Bankr. D. Minn. 1999) (where immediate benefit from transfer goes to third party, burden shifts to transferee to show debtor received indirect benefit that was “both tangible and of concrete economic value”).

Leonard v. First Commercial Mortgage Co. (In re Circuit Alliance, Inc.), 228 B.R. 225, 231 (Bankr. D. Minn. 1998) (when trustee establishes transfer was made on account of third party’s debt or obligation, burden shifts to defendant to demonstrate debtor received benefit that was “tangible, of concrete economic value, and reasonably equivalent to what the debtor gave up.”).

Leonard v. Norman Vinitzky Residuary Trust (In re Jolly’s Inc.), 188 B.R. 832, 843 (Bankr. D. Minn. 1995) (once proven that consideration for transfer went directly to third party, defendant seeking shelter of “indirect benefit” defense bears “ ‘intermediate’ burden of production as to the concreteness of the indirect benefit, and its reasonable equivalence in value.”(emphasis in original)).

In re Nat’l Century Fin. Enters., Inc., 341 B.R. 198, 217 (Bankr. S.D. Ohio 2006) (once “a plaintiff has established that consideration for the transfer passed to a third-party, the burden of demonstrating and quantifying reasonably equivalent value for the transfer shifts to the defendant.”).

Dayton Title Agency Inc., v. White Family Co., Inc. (In re Dayton Title Agency, Inc.), 292 B.R. 857 (Bankr. S.D. Ohio 2003).

Wild West World, LLC v. Mainland Valuation Services (In re Wild West World, LLC), 2008 WL 4498803 at *3 n.10 (Bankr. D. Kan. 2008) (The party seeking the shelter of the “indirect



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benefit” defense bears the burden of production as to the concreteness of the indirect benefit and its reasonable equivalence in value.” *quoting In re Jolly’s*, 188 B.R. at 843.)