THE BUSINESS LAW SECTION OF THE FLORIDA BAR
SUPPORT FOR PROPOSED AMENDMENTS TO CHAPTER 726 – FRAUDULENT TRANSFERS.

Summary

The proposed bill enacts as Florida law the amendments (the "Amendments") to the Uniform Fraudulent Transfer Act ("UFTA") promulgated by the National Conference of Commissioners on Uniform State Laws ("NCCUSL") in the summer of 2014. Florida adopted the UFTA in 1988, which is found in Chapter 726, Florida Statutes (the Florida Uniform Fraudulent Transfer Act or "FUFTA.") Although the Amendments to the FUFTA are minor, the Amendments include a change in name to the Uniform Voidable Transactions Act ("UVTA"), discussed more fully below. The Amendment incorporates most of the amendments to the UFTA, with some minor revisions, also discussed more fully below.

The Bankruptcy / UCC Committee of the Florida Bar formed a study group to review the NCCUSL amendments to the UFTA and to draft proposed revisions to the FUFTA which will, if enacted, leave the intent of the FUFTA fully intact while addressing a small number of narrowly-defined issues to better accommodate current practices and conditions. The principal features of the Amendment are listed below.

Enactment Status.

The UVTA has been enacted in nine states and introduced for consideration in seven states as of August 2016.

Statutory Background

Fraudulent transfer law developed as a result of recognition by legislative bodies and the courts that debtors sometimes try to deplete their assets in order to hinder, delay or defraud creditors. Fraudulent transfer law has developed drawing upon the common law, the Bankruptcy Code, the Uniform Fraudulent Conveyance Act and the Uniform Fraudulent Transfer Act.

American fraudulent transfer laws date back to 1571 and the Statute of Elizabeth. That statute allowed the English crown to receive as a penalty one half of property recovered and it prohibited conveyances made "with the intent to delay, hinder or defraud creditors and others of their just and lawful actions." [1] Because such transfers were deemed illegal, it soon became enshrined in common law as a means for creditors to sue to recover the illegally transferred

[1] 15 Eliz. Ch. 5 (1571).

property from the transferee. [2] The law regarding fraudulent transfers has now been codified in most, if not all, states. [3]

Florida adopted the predecessor to the current Uniform Fraudulent Transfer Act in 1923. The act was patterned after the Uniform Fraudulent Conveyance Act, which was promulgated by the NCCUSL in 1918. NCCUSL approved a revised version of the law in 1984 entitled the "Uniform Fraudulent Transfer Act." The UFTA has been adopted by 44 states, including Florida, which adopted the UFTA in 1987.[4] One purpose of the change in title to the act was to reflect that it was applicable to transfers of personal property as well as real estate.

Summary of Changes to Uniform Fraudulent Transfer Act

The UVTA makes the following changes to the UFTA:

1. Change in Title and Style: The title of the Act was changed from the "Uniform Fraudulent Transfer Act" to the "Uniform Voidable Transactions Act." Throughout the Act, the term "fraudulent" was changed to "voidable."

2. Evidentiary Matters: The standard of proof with respect to claims and defenses has been clarified to be a "preponderance of the evidence" in Sections 4, 5, and 8 of the Act.

3. Choice of law: A new choice of law rule is provided in Section 10 of the UVTA.

4. Insolvency: Section 2(c) of the UFTA, which provided a definition of "insolvency" for partnerships, has been deleted. The definition of insolvency has been modified to address liabilities subject to bona fide disputes and the burden of persuasion of insolvency if the transferee is presumed to be insolvent.

5. Defenses: Section 8(a) of the UFTA was amended to provide that reasonably equivalent value must be given to the debtor, and Section 8(b) was amended to be more consistent with the Bankruptcy Code.

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[2] Alces and Dorr, *A Critical Analysis of the New Uniform Fraudulent Transfer Act*, (1985). http://scholarship.law.wm.edu/facpubs; *Bay View Estates Corporation v. Southerland,* 114 Fls. 635, 651, 154 So. 894, 899 (1934).

[3] West's, Florida Statutes Annotated Volume 12B, Chapter 726 (2011)

[4] Florida Statutes Sections 726.101 et seq.

6. Acknowledgment of Series Organizations: A new Section 11 was added that acknowledges series organizations and treats a "protected series" of a "series organization" as a person under the UVTA.

Changes to the Uniform Fraudulent Transfer Act.

A. Change in Title and Style. The title "Uniform Fraudulent Transfer Act" was changed to the "Uniform Voidable Transactions Act." This change in title and terminology is not a change in the law, but rather a clarification of what the intent of Chapter 726 has always been. This change reflects the move from characterizing voidable transfers and obligations as "transfers" to the more appropriate term of "transactions," since Chapter 726 encompasses both transfers made and obligations incurred. Further, the term "fraud" implies common law fraud, or a legal wrong, which is not an element of a claim under Chapter 726, and never has been.

The term "fraud" has also lead to confusion with respect to the standard of proof in courts; some courts have erroneously required a "clear and convincing" evidence standard be met for fraudulent transfers just as is required for pleading fraud.

Further, there has been concern that those who assist with transactions that are characterized as "fraudulent" might be liable under a secondary form of liability (*e.g.*, aiding and abetting or conspiracy.) While the UVTA does not address secondary liability for non-transferees who are involved in a voidable transaction (*e.g.*, as a legal wrong that supports secondary liability, a separate cause of action, unethical, criminal, etc.), the change reflects the fact that fraud is not an element of a fraudulent transfer. The change in evidentiary standard also reflects the position that common law fraud should not be confused with a fraudulent (or voidable) transaction.

The Amendment adopts the changes in style and title as reflected in Section 726.101.

B. Choice of law. Neither the Uniform Fraudulent Transfer Act, nor the Uniform Fraudulent Conveyance Act before it, provided a choice of law provision, leading to a variety of approaches in multi-jurisdictional controversies. Some courts have relied upon the 11 factor test set forth in the Restatement of Conflicts 2nd, which has resulted in considerable uncertainty and inconsistent results. In addition, the lack of clarity has resulted in litigation over the proper choice of law, as well as uncertainty with respect to transactional planning. The UVTA provides a simple rule that is easy to apply; the law applicable to the contested transaction is the law of jurisdiction where the debtor is located at the time of the transfer or obligation. For individual debtors, the UVTA defines the debtor's location as the individual's principal residence. For organizational debtors, the location is defined as the place of business, and in the case where there is more than one place of business, the location is the chief executive office of the business.

The Amendment, which helps provide guidance on an issue that has relatively little

guidance in Florida courts,[5] adds to the uniform text of this provision a clause stating that application of another jurisdiction's voidable transaction law does not impair the protection afforded to an individual's exempt property under Florida's statutory or constitutional laws, including an individual's homestead under the Florida Constitution, to the extent such protection is applicable.[6] The result prescribed by the added clause should follow from the uniform text of

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[5] *See Mukamal v. Nat'l Christian Charitable Foundation (In re Palm Beach Finance Partners)*, Adv. Case No. 11-02940-PGH (Bankr. S.D. Fla. Dec. 10, 2014), ECF No. 100. ("To further complicate matters, the Court notes that in both Florida and the Eleventh Circuit, there is a surprising dearth of case law analyzing choice of law issues in the context of fraudulent transfer actions.7 Indeed, the Court could only locate three such cases, all of which are of limited value to the Court's analysis here: (1) Perkins v. Champagne (In re Int'l Mgmt. Assocs., LLC), 495 B.R. 96 (Bankr. N.D. Ga. 2013); (2) In re Friedlander Capital Mgmt. Corp., 411 B.R. 434; and (3) Alexander v. Delong, Caldwell, Novotny & Bridgers, LLC (In re Terry Mfg. Co., Inc.), 03-32063 WRS, 2007 WL 1560087 (Bankr. M.D. Ala. May 29, 2007) vacated and remanded, 03-32063-WRS, 2008 WL 4493240 (M.D. Ala. Sept. 30, 2008)."); *Steinberg v. A Analyst Ltd.*, No. 04-60898-CIV, 2009 WL 806780, at *11 (S.D. Fla. Mar. 26, 2009). ("The Receiver has not limited his recovery of the alleged fraudulent transfer to causes of action solely under Florida law. The Receiver has asserted causes of action under Florida and "other applicable law." The Receiver's pleadings leave open the possibility that the laws of states other than Florida may apply to the Receiver's recovery of the transfers, and the Receiver has preserved his right to proceed under "other applicable law." This allegation serves to preserve the Receiver's claims against FirstRand in the event the substantive law of some other state governs the Receiver's claims. The Receiver raises the possibility that the law of New York, which provides for a six-year statute of limitation, may be applicable to this action. If New York law applies, the statute of limitations may not have run on the First Redemption.As previously stated, the Court has insufficient information as to whether Florida, New York or the BVI better satisfies the "significant relationship test" of the Restatement (Second) of Conflict of Laws. If it is determined that New York law should apply and, if it is shown that the New York statute of limitations has not run as to the First Redemption, the Receiver's causes of action against FirstRand to recover the First Redemption would be timely, even without application of equitable tolling. Because at the motion to dismiss stage, a complaint may be dismissed on the basis of a statute of limitations defense only if it appears beyond a doubt that plaintiffs can prove no set of facts that toll the statute, FirstRand's motion to dismiss Counts II and III are denied as to other applicable law for the First Redemption.")

[6] *See Havoco of Am., Ltd. v. Hill*, 790 So. 2d 1018, 1028 (Fla.), opinion after certified question answered, 255 F.3d 1321 (11th Cir. 2001). ("The transfer of nonexempt assets into an exempt homestead with the intent to hinder, delay, or defraud creditors is not one of the three exceptions to the homestead exemption provided in article X, section 4. Nor can we reasonably extend our equitable lien jurisprudence to except such conduct from the exemption's protection. We have invoked equitable principles to reach beyond the literal language of the exceptions only where funds obtained through fraud or egregious conduct were used to invest in, purchase, or improve the homestead.");

Republic Credit Corp. I v. Upshaw, 10 So. 3d 1103, 1105 (Fla. Dist. Ct. App. 2009). ("We note that "[t]he transfer of nonexempt assets into an exempt homestead with the intent to hinder, delay, or defraud creditors is not one of the three exceptions to the homestead exemption provided in article X, section 4." Havoco of Am., Ltd. v. Hill, 790 So.2d 1018, 1028 (Fla.2001).");

In re Bifani, 580 F. App'x 740, 747 (11th Cir. 2014). ("Although the state constitution lists only three specific exemptions, Florida courts have "invoked equitable principles to reach beyond the literal language of the excepts" where "funds obtained through fraud or egregious conduct were used to invest in, purchase, or improve the homestead." Havoco, 790 So.2d at 1028; see also Zureikat v. Shaibani, 944 So.2d 1019, 1024 (Fla.Dist.Ct.App.2006) (affirming an equitable lien placed on a homestead where proceeds obtained from fraudulent conduct were used to invest in, purchase, or improve the homestead).")

Hirchert Family Trust v. Hirchert, 65 So. 3d 548, 552–53 (Fla. Dist. Ct. App. 2011) ("We conclude that institution of a constructive trust and/or the placement of an equitable lien over the Kissimmee Property, as the California court did based on Richard Hirchert's constructive fraud emanating from his breach of fiduciary duty, fits within the

the provision, but the Committee deemed it desirable to make the point explicit in order to allay any possible doubt. The choice of law provision only determines which state's voidable transaction law applies, and is not a choice of law provision for the determination of statutory or constitutional exemptions or any other issue.

C. Insolvency. The definition of insolvency under the UVTA is adapted from the definition of the term in the Bankruptcy Code.[7] Insolvency is presumed from proof of a failure generally to pay debts as they become due,[8] however, the UVTA provides that a debt subject to a bona fide dispute should not be included in the calculation of debt. Further, if there is a presumption of insolvency (e.g., the debtor is not paying debts as they come due), the UVTA provides that the burden of persuasion is shifted to the transferee.

The UVTA also removes the unique rule of insolvency as it pertains to partnerships under the UFTA. The Prefatory Note to the UVTA provides that partnership-specific rule was deleted because: (1) the original § 2(c) gave a partnership full credit for the net worth of each of its general partners, which "makes sense only if each general partner is liable for all debts of the partnership, but such is not necessarily the case under modern partnership statutes," and (2) "the general definition of "insolvency" in § 2(a) does not credit a non-partnership debtor with any part of the net worth of its guarantors. To the extent that a general partner is liable for the debts of the partnership, that liability is analogous to that of a guarantor. There is no good reason to define "insolvency" differently for a partnership debtor than for a non-partnership debtor whose debts are guaranteed by contract."

The Amendment adopts the changes to the definition of insolvency and the deletion of the special rule for insolvency as it pertains to partnerships, as reflected in Section 726.103.

D. Evidentiary Matters. There has been a lack of uniformity among the States in applying burdens and standards of proof in fraudulent transfer litigation.[9] The lack of a uniform rule regarding burdens and standards of proof can result in the application of different evidentiary rules and impact the outcome of litigation pertaining to alleged voidable transactions.[10] The UVTA provides uniformity by requiring a creditor prove the elements of a voidable transaction and also places the burden of proving elements of a defense on the transferee. Consistent with the theme that a voidable transaction does not equate to fraud, the burden in each of the foregoing scenarios is a "preponderance of the evidence."

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equitable exception to the homestead protections afforded by the Florida Constitution. Accordingly, although we hold that the Quitclaim Deed is not entitled to full faith and credit, we nevertheless hold that the trial court's order, to the extent it implies that the California *553 court lacks the authority to enforce the order enjoining Appellee to convey the Kissimmee Property, is reversed and this case is remanded to the trial court with instructions to enforce the injunction to convey title to the Kissimmee Property out of comity with California.")

[7] Prefatory Note to the Uniform Voidable Transactions Act.
[8] Id.
[9] *See* Kenneth C. Kettering, *Codifying a Choice of Law Rule for Fraudulent Transfer: A Memorandum to the Uniform Law Commission*, 19 AM. BANKR. INST. L. REV. 319 (2011).
[10] *Id*. at 324.

The Amendment adopts the change in evidentiary matters as reflected in Section 726.109(9). The evidentiary changes do not conflict with how Florida courts have applied the burden and standards of proof in fraudulent transfer cases.[11]

E. Defenses. Several clarifications were made to Section 8 (Section 726.109), dealing with defenses to voidable transactions. The first change requires that a transferee who asserts the good faith defense for taking in good faith and for reasonably equivalent value must provide such reasonably equivalent value to the debtor. Section 8 was also changed to require that any immediate or mediate transferee seeking to use such defense must, like the first transferee, take such property in good faith. Such a defense for transferees applies to recovery of

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[11] *See Wieczoreck v. H & H Builders, Inc*., 475 So. 2d 227, 228 (Fla. 1985). ("In Canal Authority v. Ocala Mfg., Ice and Packing Co., 332 So.2d 321 (Fla.1976), however, this Court stated that "[i]t is rudimentary that proof of fraud must be by clear and convincing evidence." Id. at 327, citing two pre-Rigot decisions from the district courts of appeal. These authorities were, however, expressly overruled in Rigot and consequently are of no precedential value. 245 So.2d at 53.We hereby recede from that portion of the Canal Authority opinion to the extent it announces a rule of law contrary to that expressed in Rigot.");

Beal Bank, SSB v. Almand & Associates, 780 So. 2d 45, 59 (Fla. 2001) ("Preponderance of the evidence" is the generally accepted burden of proof in civil matters. See Seropian v. Forman, 652 So.2d 490, 494 (Fla. 4th DCA 1995); see also Wieczoreck v. H & H Builders, Inc., 475 So.2d 227, 228 (Fla.1985) (holding that the burden of proof in a fraud action is preponderance or greater weight of the evidence), cited in Passaat, Ltd. v. Bettis, 654 So.2d 980, 981 (Fla. 4th DCA 1995). We find no reason to deviate from that standard here. We disapprove Terrace Bank v. Brady, 598 So.2d 225, 228 (Fla. 2d DCA 1992), to the extent it imposes a higher burden of proof.")

See In re Berkman, 517 B.R. 288, 300 (Bankr. M.D. Fla. 2014). ("The ultimate burden of proof on an actual fraudulent transfer claim rests with the party seeking to avoid the transfer to establish by a preponderance of the evidence that the transferor effectuated the transfer in question with actual fraudulent intent to hinder, delay or defraud creditors.43 Similarly, on a constructive fraudulent transfer claim, the party seeking to avoid the transfer must establish by a preponderance of evidence that the transferor received less than reasonably equivalent value in exchange for the transfer").

Mejia v. Ruiz, 985 So. 2d 1109, 1113 (Fla. Dist. Ct. App. 2008) ("The proof required to show that a transfer is fraudulent is the preponderance of the evidence standard. Kapila v. Plave (In re Paul), 217 B.R. 336, 337 n. 2 (S.D.Fla.1997) (citing Wieczoreck v. H & H Builders, Inc., 475 So.2d 227 (Fla.1985))."

Gulf Coast Produce, Inc. v. Am. Growers, Inc., No. 07-80633-CIV, 2008 WL 660100, at *6 (S.D. Fla. Mar. 7, 2008). ("The fraudulent act, the clandestine act of hiding money, is allegedly committed by a defendant and another, to the exclusion of the plaintiff. This is in stark contrast to a common law fraud claim where a plaintiff alleges that a defendant made a material false statement or omission directly to the plaintiff. Under such circumstances, the plaintiff is in a position to plead with the specificity required by Rule 9(b). This Court concludes that despite the use of the word "fraud," a fraudulent transfer claim is significantly different from other fraud claims to which Rule 9(b) is directed. See Nesco Inc. v. Cisco, No. Civ.A. CV205-142, 2005 WL 2493353, * 3 (S.D.Ga. Oct.7, 2005) (finding common law fraud and fraudulent transfer "bear very little relation to each other" since the element of false representation need not be proven in fraudulent transfer cases). Given this lack of access to information on the part of a plaintiff in a fraudulent transfer case, the application of a heightened pleading standard is inappropriate.")

property in addition to a money judgment, thereby more closely following the relevant Bankruptcy Code sections (550(a) and (b)). Section 8 (726.109(5)(b)) was modified to provide an elimination of strict foreclosure from the safe harbor for exercise of remedies under UCC Article 9, because unlike other remedies a secured creditor may exercise under Article 9, strict foreclosure does not contain a requirement of commercial resonableness.

F. Series Organizations. UVTA Section 11 (Section 726.112) provides for rules pertaining to series organizations. Such organizations are recognized in several jurisdictions, (e.g., Delaware and Illinois.) Generally, the operations of a "protected series" are insulated from the operations of other organization and other series within such organization. Under UVTA, each series and the organization are treated as a separate person, despite not being characterized as a separate entity under applicable state law. Because Florida does not currently recognize series organizations, the study group added this non-uniform language to proposed Section 726.112(1)(c): "Law other than ss. 726.101 – 726.115 determines whether and to what extent a series organization and each protected series of the organization is a separate person for purposes other than this Uniform Voidable Transactions Act."

G. Limitations discovery period. There is disagreement among courts around the country as to whether the phrase in §726.110(a), "one year after the transfer or obligation was or could reasonably have been discovered by the claimant," means one year after the transfer or one year after the transfer and its wrongful nature could reasonably have been discovered. The language in the UVTA is unchanged from the UFTA, and of course it applies only to intentionally fraudulent transfers. The great majority of courts hold that the transfer *and* the wrongful nature must be reasonably discoverable for the one-year to begin running. See, e.g., Committee Comment 3 to the UVTA, and the cases cited in *Post-Confirmation Committee for Small Loans, Inc. v. Martin*, No. 1:13-CV-195 (WLS), 2016 WL 1274127 at 7-10 (M.D. Ga. Mar. 31, 2016). However, two courts in Florida have now held that the mere ability to discover the *transfer*, with no way to discover the fraudulent nature, starts the one year running. *Nat'l Auto Serv. Centers, Inc. v. F/R 550, LLC*, No. 2D14-3632, 2016 WL 1238265, at *8 (Fla. 2nd DCA Mar. 30, 2016) (disagreeing with decisions under the UFTA and holding from Hawaii and Washington, and holding further that equitable estoppel is not available to avoid the effect of the statute); *Hill v. Jones*, No. 3:03–cv–1034–J–32, 2004 WL 5694988, at *3 (M.D.Fla. Nov.4, 2004) (Corrigan) (discovery of transfer, not discovery of wrongful nature, starts the one year running). Consistent with the majority rule, and the recommended interpretation in the Official Comments, the proposed Amendments include non-uniform language clarifying that not only the fact of the transfer, but "its wrongful nature," must be reasonably discoverable by the claimant for the one year period to commence running. Arizona's legislature made this change when it enacted the UFTA. Ariz.Rev.Stat. §44-1009(1).

Official Comments.

Further explanation of provisions added or revised by the UVTA may be found in the Official Comments to those provisions. However, as with all other previously adopted uniform

acts, Florida does not officially adopt the Official Comments.

The Official Comments have received negative criticism from members of a study group formed by the Real Property Probate and Trust Law Section of the Florida Bar ("RPPTL study group."), and from the Tax Section. The most common objections to the Official Comments deal with the Official Comments to Section 4 of the UVTA, particularly with respect to (a) "asset substitution" (b) entity formation (c) entity conversion and (d) asset protection trusts.

It is important to recognize that Section 4 of the UFTA (current Chapter 726.105) – which sets forth the standards for determining when a transfer or obligation is voidable as to present or future creditors -- is virtually unchanged. The UVTA does not make any substantive revisions to Section 4, other than to clarify the burden of proof (which is not disputed by the RPPTL study group or the Tax Section). Thus, the enactment of the UVTA in Florida will have absolutely no impact on the current Florida standards for determining when a transfer or obligation is voidable. Nevertheless, the RPPTL study group and the Tax Section urge the wholesale rejection of the UVTA based upon unfounded concerns that courts will use the revised Official Comments – which are NOT adopted in Florida – to interpret Chapter 726 in ways that they believe will impact legitimate tax and estate planning. These concerns are completely misguided.

First, regardless of whether Florida adopts the UVTA, given that Section 726.105 of the Florida Statutes is not being substantively changed, the Official Comments to the UVTA could be referenced and used by the courts as a guide in interpreting the current UFTA, just as the courts may use any article or publication that they may find helpful or persuasive. Thus, the attempt by the RPPTL study group or the Tax Section to torpedo the entire UVTA – based upon Official Comments that are not adopted in Florida – does not prevent the perceived "harm" that they portend.

Second, the RPPTL study group and the Tax Section have expressed concerns merely because the Official Comments to the UVTA expand the comments to include as examples of transactions that ***could be*** subject to a claim under Chapter 726 the following: (a) "asset substitution" (b) entity formation (c) entity conversion and (d) asset protection trusts. However, under current Chapter 726, the definition of "transfer" is broad: "Transfer" means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, lease, and creation of a lien or other encumbrance." This definition, which is virtually unchanged in the UVTA, obviously encompasses any of the transactions provided as an example in the revised Official Comments. But this is nothing new or novel. At the same time, in order to make a claim or challenge any transfer or transaction, under both the current UFTA in Florida, or with the enactment of the UVTA, a creditor has the burden of proof of establishing under Section 726.105(1) that the transfer was made "With actual intent to hinder, delay or defraud any creditor of the debtor." Alternatively, the creditor would have to meet the burden of proof under Section 726.105(1)(b). If any of the transactions that the RPPTL or Tax Sections are concerned about are done for legitimate purposes, and without the intent to "hinder, delay or defraud" creditors

under Chapter 726.105, the transactions will not be subject to avoidance, either under the current UFTA in Florida, or under the proposed UVTA. However, if a creditor is able to prove that the transactions were done with the intent to "hinder, delay or defraud" creditors, or proves that the transaction satisfied the requirements for constructive fraud, the transactions will be equally subject to avoidance under the either the current UFTA in Florida, or the proposed UVTA. Simply put, the enactment of the UVTA in Florida does not change the standard for determining what is, and what is not a voidable transaction, and does not change Florida law in this regard one iota.