

**PROPOSED AMENDMENTS TO CHAPTER 726
THE FLORIDA UNIFORM FRAUDULENT TRANSFER ACT**

EXECUTIVE SUMMARY

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Summary Overview:

Under Florida law, an exempt organization¹ that accepts a charitable contribution from a donor is subject to the risk of having to return the contribution if the donor is subsequently deemed to have made a fraudulent transfer under the Florida Uniform Fraudulent Transfer Act (“FUFTA”).

FUFTA actions have the potential to cripple, even bankrupt, innocent and unassuming Exempt organizations that accept charitable contributions, and spend or allocate charitable contributions which, many years later, become the subject of a “clawback” action. Few exempt organizations, if any, have cash reserves sufficient to return large contributions arising out of unexpected clawback claims without a significant financial crisis.

This proposal seeks to amend FUFTA to protect an innocent exempt organization from having to return a charitable contribution under FUFTA if the organization accepts the contribution in good faith. The current law, if interpreted as it has been by one federal appeals court in an Illinois case², places exempt organizations in a worse position than before they received the charitable contribution. This proposal seeks to clarify that the Florida legislature did not intend FUFTA to apply to innocent exempt organizations, and to avoid the serious public policy and constitutional issues that arise if it were to apply.

Under FUFTA, a defense to a “clawback” action exists for a person that exchanges value in return for the transfer. Unlike typical businesses for-profit, exempt organizations do not, and cannot, exchange value when they accept from a charitable contribution from a donor. Exempt

¹ For purposes of this proposed amendment, the term “exempt organization” shall collectively refer to any and all organizations that are qualified as exempt from federal income taxation under the provisions of ss. 501(c)(3) or 501(c)(4) of the Internal Revenue Code of 1986, as amended.

² Scholes v. Lehmann, 56 F.3d 750 (7th Cir. 1995).

organizations provide services and goods to the public. While these services are offered to the public free of cost, these services have a typical exchange value.

Where a for-profit business accepts a transfer, both parties to the transaction receive an item of value, and an item of value exists. However, it should be pointed out, in many for profit transactions, the value is transitive or intangible. A \$1,000 bottle of wine is of no lasting value. Neither is a concert, a movie, a haircut, or any number of services or entertainments. But none of these give rise to clawback rights under FUFTA. On the other hand, if FUFTA is interpreted as it was in Scholes v. Lehmann, the Illinois case, exempt organizations are in a worse position than other entities that receive transfers in the ordinary course of business and provide services of far greater and more lasting value than a bottle of wine, a haircut or a concert. This distinction gives rise to serious issues under the constitutional guarantees of equal protection of law and due process. These constitutional issues were not addressed in the appeal in the Scholes because they were not raised at trial.

Proposed Revisions:

The proposed revisions to FUFTA are the joint efforts of Girls Incorporated of Sarasota County. (“Girls Inc.”), a Florida corporation not for profit and an exempt organization, and Jewish Family and Children’s Services of Sarasota-Manatee, Inc. (“JFCS”), also a Florida corporation not for profit and a tax-exempt organization (we will use the term “exempt organization” for non-profit tax exempt organizations under Sections 501(c)(3) and 501(c)(4) of the Internal Revenue Code. Each, along with other exempt organizations, is the subject of clawback claims arising out of contributions made by another exempt organization that was connected to the Arthur Nadel Ponzi scheme in Sarasota, Florida.

This proposal would amend Chapter 726.105, Florida Statutes, “Transfers fraudulent as to present and future creditors” to include an exception exempt organizations that have accepted, in good faith, and without knowledge, contributions, pledges, and others transfers that are subsequently challenged as not having been made for “reasonably equivalent value” under the “clawback” provision of FUFTA, as set forth in detail below. This proposal would make it clear that the services that exempt organizations deliver have a legally recognized value under FUFTA in the same way that traditional goods and services of transitive or intangible worth have recognized value.

The proposals do not involve a major overhaul of the statute but instead are directed at specific areas where reform is necessary.

A history of the law in this field is attached as Appendix A.

PURPOSE OF THE AMENDMENTS: THE NEED FOR REVISIONS

Unfortunately, dozens of other suits against charitable and religious organizations have arisen since the time Scholes was decided. Suits of this type will undoubtedly continue to arise. Justice Posner's interpretation of UFCA resulted in, and will continue to result in every case like it if adopted by other courts, a *per se* judgment against exempt organizations. By virtue of its status as a exempt organization, the Scholes decision holds that exempt organizations do not exchange the traditional type of "consideration" that occurs in ordinary business transactions—and thus, exempt organizations cannot exchange reasonably equivalent value as it is defined by Fla. Stat. § 726.105.

The Scholes decision and its interpretation of FUFTA ignore the unique nature of charitable contributions. That is, exempt organizations are incapable of exchanging reasonably equivalent value in exchange for the receipt of a charitable contribution. Unlike private gifts, charitable contributions cannot inure to the benefit of the recipient charity. Instead, contributions are provided to exempt organizations with the understanding that they will be used to provide necessary goods or services to the objects of an organization's charitable mission.

As a result of Scholes, exempt organizations are, and will continue to be, subject to the risk of being deprived of their property without due process and equal protection of the laws. It is important to note that the exposure is not limited to Ponzi schemes. It extends to any unpaid creditor who obtains a judgment and seeks to "claw back" a contribution made to an innocent exempt organization. The specter of this kind of liability will have a substantial adverse impact on all exempt organizations, and ultimately will impact the entire public sector.

Proposed Revisions

The revisions proposed are simple:

(1) Present subsections (9),(10),(11),(12), and (13) of section 726.102, Florida Statutes, are redesignated as subsections (10),(11),(12),(13), and (14) respectively, and a new subsection (9) is added to that section to read:

726.103 Definitions. – As used in ss. 726.101-726.112:

(9) "Exempt organization" shall mean any and all organizations that are qualified as exempt from federal income taxation under the provisions of ss. 501(c)(3), or 501(c)(4) of the Internal Revenue Code of 1986, as amended.

(2) Subsection (1) of section 726.109, Florida Statutes, is amended to read:

726.109 Defenses, liability, and protection of the transferee. -

- (1) A transfer or obligation is not voidable under s. 726.105(1)(a) against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee. An exempt organization that, in good faith, accepts a charitable contribution from a person for its exempt purpose or purposes, shall be deemed to have exchanged reasonably equivalent value.

Section 3. This act shall take effect upon becoming a law.

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