Fraudulent Transfers and Obligations: Issues of Current Interest

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FRAUDULENT TRANSFERS AND OBLIGATIONS: ISSUES OF CURRENT INTEREST

GERALD K. SMITH* AND FRANK R. KENNEDY**

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I. Introduction

The law of fraudulent transfers concerns property transferred by a debtor who, but for the transfer, could have satisfied the claims of his, her, or its creditors. If the property was transferred to defeat the creditors' rights, or under circumstances deemed fraudulent, then it is a fraudulent transfer. The creditors' traditional remedy is to "recapture . . . the property from the fraudulent grantee or from a subgrantee who took gratuitously or paid value with notice." But, according to Professor Glenn, it is generally not possible to recover from those who aided, participated in, or conspired to effect the fraudulent transfer because the general creditor plaintiff has no property interest in the assets of the debtor. However, Professor Glenn views the rule as different after judgment: "The meddling outsider becomes liable under principles that are easy to understand, but they do not

1. The creditor's right . . . is to realize upon all property that is capable of conversion into money or distribution. In other words, the creditor should be able to reach whatever is available to the debtor. Now, the kind of wrongdoing that is known as a fraudulent conveyance consists of putting realizable assets beyond the reach of the creditor's process, whatever form that process may take.


3. 1 Glenn, supra note 1, § 56, at 77. "The grievance asserted under the theory of fraudulent conveyance is that property has been put beyond the reach of process normally available to creditors; hence all persons involved in the wrongdoing are responsible for the property, and its proceeds or value." Id. § 57.
flow directly from the Statute of Elizabeth or any modern substitute.”

4. Id. § 56. Professor Glenn cited chapters 6 and 13 of his treatise in support of his observation. However, only chapter 6 contains any relevant discussion, and it does not support his general statement.

The Statute of Elizabeth, it will be recalled, gave a queer sort of *qui tam* action in which the recovery went, one half to the Crown and the other half to the party aggrieved. But those aspects of the Act simply sloughed off as time went along, although there were strange survivals in one or more of our States. Apart from that, however, the notion that an action lies in tort is so discredited, that one may venture upon a generality. It may safely be said, then, that there is no tort cause of action, when a transfer is made before the creditor obtains judgment; and it only remains to notice the exceptions, actual or apparent.

. . . . But an exception which proves the rule, is made where the transfer takes place after the aggrieved creditor has obtained judgment, or procured a warrant of attachment. We then have a “rescue”, to the injury of a man who, by judgment or attachment, has acquired the right to subject the debtor’s assets to his claim; and so in that case an action lies.

An extension of this idea, however, is not so easy to justify. It has been held that a tort action lies when the fraudulent transfer was made on the eve of judgment or attachment, and in view of that event. The cases which go so far seem to overlook the fact that the creditor is sufficiently protected by the Statute of Fraudulent Conveyances, and does not really stand in need of a tort action.

*Id.* § 74, at 122-24 (footnotes omitted). Professor Glenn cited Schwenn v. Schwenn, 166 N.W. 171 (Wis. 1918), as one authority that supports the no-tort-action proposition. However, *Schwenn* held to the contrary when a single creditor was defrauded. Professor Glenn also cited a student-written case critique of *Schwenn*. It succinctly capitalized the state of the law in 1918 as follows:

The weight of authority is that an unsecured general creditor cannot maintain an action against third persons conspiring with the debtor fraudulently to dispose of the debtor’s property. Since such a creditor has no lien upon or interest in the property of his debtor, he has lost only a possibility of realization, and this injury is too remote and speculative. Nor can the creditor be said to be damaged in law, for he still has his debt, and has open to him the privilege of securing judgment and then enforcing any of the remedies of the judgment creditor. The result of allowing such actions would be to subject the fraudulent transferee to liability for all the debts of his transferor, however large the debts, and however small the value of the property transferred, for the action would be equally available to every creditor.

Recent Decision, 18 COLUM. L. REV. 363 (1918) (citations omitted) (emphasis added). Neither the Uniform Fraudulent Conveyance Act (UFCA), promulgated in 1918, nor its 1984 revision, the Uniform Fraudulent Transfer Act (UFTA), departs from providing creditors with the remedy of recovery of the fraudulently transferred property. However, the UFTA also provides for a money judgment in the amount of the value of the asset transferred as an alternative remedy, apparently at the election of the creditor. *See generally* Williams, *supra* note 2, at 116-26. Section 550(a)(1) of the Bankruptcy Code, 11 U.S.C. § 550(a)(1) (1988), and § 8(b)(1) of the UFTA, 7A U.L.A. 662 (1985), expressly allow recovery from those who do not receive the fraudulently transferred property but who nonetheless benefit from it. *See infra* notes 67-88 and accompanying text. This is a significant change, but probably reflects the rule under prior law. *E.g.* Mack v. Newton,
By the time of the revised edition of Professor Glenn's famous treatise, there was a clear-cut basis for recovery from those who aided, participated in, or conspired to effect an intentionally fraudulent transfer. Section 870 of the Restatement of Torts, promulgated in 1939, assigned liability to anyone who intended the consequences of his or her acts. This rule was more clearly expressed in 1977 in section 870 of the Second Restatement of Torts, which provided that "[o]ne who intentionally causes injury to another is subject to liability to the other for that injury, if his conduct is generally culpable and not justifiable under the circumstances." The section was intended to serve as a guide for determining when liability should be imposed for harm that was intentionally inflicted, "even though the conduct does not come within the requirements of one of the well established and named intentional torts."

One of the problems with a rule that does not impose liability on those who aid and abet or participate in an intentionally fraudulent transfer is that there is no disincentive not to do so. The only remedy is against the transferee, and that is a remedy to recover the property transferred or its value. Professor Carlson made this point in his criticism of existing fraudulent conveyance law:

One fact about the fraudulent conveyance law remedy that must be strongly emphasized is that the debtor is not rendered more liable to his creditor because he has made a fraudulent conveyance. Only third parties are prejudiced. Furthermore, liability of third parties, under existing law, is limited to the property actually received (or its value).

The recent decision of the Supreme Court of Georgia in Kesler v. Veal, which reversed a Georgia Court of Appeals decision, discusses this issue. In a case involving an intentional fraudulent transfer, the court of appeals affirmed a jury verdict setting aside a transfer of real

737 F.2d 1343, 1356-58 (6th Cir. 1984). The new language encompasses transfers that would create resulting trusts. Under the Restatement of Trusts, if the debtor pays for property and the title is in the name of a third party, a resulting trust for the benefit of the debtor can be imposed. Restatement (Second) of Trusts § 440 (1957). Creditors of the debtor then can reach the property to satisfy their claims. Id. § 407(3). Both the Bankruptcy Code and the UFTA avoid this unnecessary step by allowing recovery from anyone who benefits from the transfer.

5. Restatement of Torts § 870 (1939); cf. Restatement (Second) of Torts §§ 766, 744(b) (1977).
7. Id. cmt. a.
property and awarding actual and punitive damages against the transferee. The supreme court reversed on the basis that the legislature did not intend that the transferee should be liable for damages in addition to disgorging the property received.\textsuperscript{10}

One concern of the courts in refusing to extend liability to those who aid and abet or participate in a fraudulent transfer is that innocent persons might be subjected to liability in connection with constructively fraudulent transfers.\textsuperscript{11} However, rather than precluding all claims, it would be better to limit liability to those aiding and abetting or participating in transfers intended to hinder, delay, or defraud creditors. Another concern is whether the legislature intends to limit the remedy to recovery of the property transferred (or its value); the fraudulent transfer statutes do not address the liability of third parties. This was the rationale of the Supreme Court of Georgia in \textit{Kesler v. Veal}. However, the fraudulent transfer statutes only deal with transfers or obligations. The statutes do not purport to allow or limit liability under tort law or other statutory provisions.

Fraudulent transfer law developed gradually over the centuries, undergoing significant formulations in the Statute of 13 Elizabeth\textsuperscript{12} and its famous restatement in \textit{Twyne's Case}.\textsuperscript{13} A major event along the way was the promulgation of the Uniform Fraudulent Conveyance Act (UFCA) in 1918.\textsuperscript{14} Thirty years later, section 67d of the Bankruptcy Act was conformed to the language of the UFCA with the passage of the Chandler Act Amendments.\textsuperscript{15} About thirty years after that, the pace quickened with the rewriting of the Bankruptcy Act's fraudulent transfer provisions as part of the work of the Commission on the Bankruptcy Laws of the United States. The proposed Bankruptcy Act of 1973\textsuperscript{16} recommended changes that were adopted in the Bankruptcy Reform Act of 1978.\textsuperscript{17} Thereafter, in an interesting turnabout, the UFCA was conformed to the Bankruptcy Code with the promulgation of the Uniform Fraudulent Transfer Act (UFTA)\textsuperscript{18} in 1984.\textsuperscript{19}

\begin{enumerate}
\item\textsuperscript{10} Id. at 215.
\item\textsuperscript{11} \textit{See} Elliott \textit{v. Glushon}, 390 F.2d 514 (9th Cir. 1967).
\item\textsuperscript{12} An Act Against Fraudulent Deeds, Alienations, &c., 13 Eliz., ch. 5 (1570) (Eng.).
\item\textsuperscript{13} 76 Eng. Rep. 809 (Star Chamber 1601).
\item\textsuperscript{14} 7A U.L.A. 427 (1985).
\item\textsuperscript{15} Chandler Act, ch. 575, § 67d, 52 Stat. 840, 877-78 (1938) (repealed 1978).
\item\textsuperscript{18} 7A U.L.A. 639 (1985).
\item\textsuperscript{19} \textit{See} id. prefatory note, at 639-42.
\end{enumerate}
What had been a rivulet of fraudulent transfer and obligation cases over the centuries has now become a torrent, and this torrent will become a raging river in the decade of the 1990s, fed in part by litigation arising out of the leveraged buyout (LBO) craze of the 1980s.

This Article is an attempt to identify and explore developing issues in the law of fraudulent transfers and obligations. The issues chosen for discussion include claims resulting from the avoidance of fraudulent transfers and whether they share pari passu with the claims of unsecured creditors; how courts are resolving who is a transferee for purposes of liability; the liability of those who benefit from or participate in fraudulent transfers; the time to file suit under the Bankruptcy Code; the “safe harbor” for LBOs; and the recent enactment of a fraudulent transfer act for the benefit of the FDIC that primes the rights of the bankruptcy trustee under the Bankruptcy Code.

II. THE TREATMENT OF FRAUDULENT OBLIGATIONS

The UFCA assimilated the treatment of fraudulent obligations to the treatment of fraudulent transfers, and the UFTA, section 67d of the Bankruptcy Act, and section 548 of the Bankruptcy Code, which are patterned on the UFCA, have followed suit. It is sometimes asserted or assumed that an obligation is a transfer; but it is not. Equating obligations and transfers is appropriate only if an obligation is secured by a transfer. In such a case both the obligation and the transfer may be voidable because they arise from the same set of fraudulent circumstances.

The classic remedy for a fraudulent transfer is avoidance of the transfer because it impedes the collection of a creditor’s claim.20 The successful suitor in a fraudulent transfer action is permitted to levy on the transferred property as if the transfer had never occurred. The transfer often is not voidable, however, by virtue of the fact that the property has disappeared or has come into the hands of a bona fide purchaser who is protected by a savings clause found in every fraudulent transfer law. In such an eventuality the creditor is authorized to recover the value of the property fraudulently transferred from the transferee or any subsequent transferee who is not protected by virtue of its standing as a good faith transferee for value or successor to a protected transferee.

Section 550(a) of the Bankruptcy Code authorizes the trustee to

20. “[T]he branch of law which we are to examine . . . simply confers upon the creditor, or a representative of creditors such as a trustee in bankruptcy, the right to disregard the conveyance and treat the affected asset as though the transfer had not been made.” 1 GLENN, supra note 1, § 2, at 3.
recover from the initial transferee or any unprotected transferee "the
property transferred, or, if the court so orders, the value of such prop-
erty."21 The value of the property is typically determined as of the
time of the transfer.22 If the property has increased in value after
the transfer, section 550(d) of the Bankruptcy Code recognizes that the
transferee is entitled to be reimbursed or otherwise protected to the
extent the transferee has improved the value of the property without
being compensated. The implication of this provision is that any ad-
ventitious increases in the value of the property transferred accrues to
the estate. Section 8(b) of the UFTA23 authorizes a creditor to recover
the value of the property transferred up to the amount of the creditor's
claim. Under section 8(c) the value is determined as of the time of the
transfer but is subject to adjustment as the equities may require.24

Subdivisions (d) and (h) of section 502 of the Bankruptcy Code
contain an implication that when a transfer is avoided pursuant to sec-
tion 550, the transferee has a claim for the value of the property sub-
ject to the avoided transfer.25 The implication is strongest when the
transfer avoided was a nonfraudulent preference26 and is weakest when
the transferee was chargeable with having an actual intent to de-

fraud.27 Nevertheless, there is judicial authority for allowing even a
transferee with fraudulent intent to assert a claim against the debtor's
estate for value returned to the estate.28 Section 548(c) of the Bank-

22. United States v. Fernon, 640 F.2d 609, 611 (5th Cir. Unit B Mar. 1981); Hamil-
24. Id. § 8(c).
25. Section 502(d) conditions the transferee's claim on the disgorgement of the
property transferred or the value for which the transferee is liable. 11 U.S.C. § 502(d)
(1988). Section 502(h) converts the transferee's claim into a prepetition claim for the
purposes of determining its allowability and priority. Id. § 502(h). Precursors of
§ 502(d) in the Bankruptcy Act generated controversy because of overweening construc-
tion. See James A. MacLachlan, Bankruptcy § 143, at 133-36 (1956); id. § 268, at 310-
11.
26. See, e.g., Katchen v. Landy, 382 U.S. 323 (1966); Keppel v. Tiffin Sav. Bank,
197 U.S. 356 (1905). These cases applied § 57g of the Bankruptcy Act, which is the pred-
ecessor of § 502(d) of the Bankruptcy Code.
27. The relevant case law is not extensive or illuminating. See, e.g., In re Spotless
Tavern Co., 4 F. Supp. 752, 755 (D. Md. 1933) (disallowing a fraudulent mortgagee's
claim for cash advanced to the debtor under the Bankruptcy Act); see also Barnard v.
Seaman, 211 N.W. 473, 474 (Minn. 1926) (denying reimbursement to a transferee guilty
of actual fraud under the UPCA); James A. McLaughlin, Note, Application of the Uni-
form Fraudulent Conveyance Act, 46 Harv. L. Rev. 404, 433-35 (1933) (opining that
under the UPCA actually fraudulent transferees should be denied reimbursement).
28. See Misty Management Corp. v. Lockwood, 539 F.2d 1205 (9th Cir. 1976).
[The modern view is that a transferee guilty of fraudulent behavior may nev-
ertheless prove a claim against the bankrupt estate, once he returns the fraud-
Bankruptcy Code and section 8(d) of the UFTA recognize that to the extent value has been given, a good faith transferee or obligee has a lien against the property transferred or a right of setoff against the amount of the liability imposed as a result of the fraudulent transaction.

<ul>
<li>Id. at 1214 (citations omitted); In re Moody, 131 F. 525, 530 (N.D. Iowa 1904) (stating that the trustee is not entitled to avoid a transfer while retaining the consideration received).</li>
<li>31. William B. Tanner Co., Inc. v. United States (In re Automated Business Sys., Inc.), 642 F.2d 200, 203 (6th Cir. 1981) (excusing from liability a transferee that, without fraudulent intent or knowledge of the debtor-transferor's fraudulent intent, accepted a transfer as payment of its claim, although payment was made from funds provided to the debtor for another purpose); Carr v. DeMusis (In re Carr), 34 B.R. 653, 657-58 (Bankr. D. Conn. 1983) (avoiding redemption of debtor's mortgaged property from strict foreclosure by third mortgagee on payment by junior lienholder of $9,022 under § 548(a)(2)(A)), aff'd, 40 B.R. 1007 (D. Conn. 1984) (avoiding a transfer to the redeemer for 31% of the debtor's equity and refusing to grant a lien to the final transferees for lack of good faith); Gillman v. Preston Family Inv. Co. (In re Richardson), 23 B.R. 434, 449 (Bankr. D. Utah 1982) (granting a lien to a bidder at a constructively fraudulent foreclosure sale for the amount of the bid plus interest from the date of sale).</li>
<li>In Carr the court reasoned that because the value of debtor's equity was $30,000, the transfer to the redeeming lienholder was constructively fraudulent, but the court allowed the redemptioner, who was in good faith, a lien for the amount it paid on redemption. The officers and attorney for the redeeming lienholder who acquired the property from the redemptioner on payment of its $231 judgment lien were denied a lien for their outlay because they were found not to be good faith transferees.</li>
<li>The Carr case is criticized by Professor Vern Countryman in Vern Countryman, The Trustee's Recovery in Preference Actions, 3 BANKR. DEV. J. 449, 466 (1986), for not allowing the officers and attorney to retain their interests because they gave value in good faith and therefore the redemption by their transferor was not voidable. Thus, the court did not need to resort to § 550(b) at all.</li>
<li>"As a matter of equity, the transferee is normally entitled to a credit for those proceeds of [a] sale [which violated a bulk transfer statute] traceable to funds held by the Trustee." Ross v. Rodolpho (In re Villa Roel, Inc.), 57 B.R. 835, 839 (Bankr. D.D.C. 1985) (citing Murdock v. Plymouth Enter., Inc. (In re Curtina Int'l, Inc.), 23 B.R. 969, 980 (Bankr. S.D.N.Y. 1982)). The transferee was denied credit in the Villa Roel case, however, because the debtor's estate had no assets. In Verco Industries v. Spartan Plastics (In re Verco Industries), 704 F.2d 1134 (9th Cir. 1983), the court was presented with the problem of fashioning an appropriate remedy for the trustee when the parties to a bulk transfer failed to comply with the notice requirements of Uniform Commercial Code (UCC) Article 6, but the debtor in possession had received cash, property, an assumption of indebtedness, and a promissory note from the transferee. The debtor was allowed to retain the property that had never been delivered to the purchaser and the right to recover on the purchaser's promissory note, but the purchaser's claim under § 502(h) for the loss resulting from the avoidance was recognized as an appropriate set-
Although sections 544 and 548 of the Bankruptcy Code authorize the trustee to avoid a transfer or an obligation, section 102(5) negates any implication that the trustee may not avoid both a transfer that secures or is otherwise related to an obligation and the obligation itself.\textsuperscript{32} Section 7(a)(1) of the UFTA\textsuperscript{33} likewise authorizes a creditor to obtain avoidance of a fraudulent transfer or obligation. The question has been raised, frequently of late, in court opinions and commentary whether subordination of the claim underlying a voidable lien is an appropriate remedy for a complainant creditor. There is no provision in the UFTA comparable to either section 102(5) of the Bankruptcy Code or section 510(c), the Bankruptcy Code's provision that authorizes equitable subordination of a claim or interest. Moreover, it has frequently been held that an individual creditor is not authorized by the Bankruptcy Code to obtain relief in the form of subordination of another creditor's claim.\textsuperscript{34} The court is nevertheless authorized by section 7(a)(3)(iii) of the UFTA\textsuperscript{35} to grant any other relief the circumstances may require. This provision has been liberally construed,\textsuperscript{36} and subordinating the claim of one creditor to the claim of another when both creditors are before the court is not incompatible with the policy of the UFTA. Indeed, the avoidance of a creditor's claim accomplishes

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off against the liability on the note. \textit{Id.} at 1137-39. Professor Countryman appropriately raised the question of why the purchaser should not have been allowed a claim for his loss against the debtor's estate without regard to the setoff against the note. Countryman, \textit{supra}, at 482.

Section 8(a) of the UFTA insulates any "person who took in good faith and for a reasonably equivalent value" from avoidance under § 4(a) (1) (i.e., a good faith purchaser from a party who made a transfer or incurred an obligation with actual intent to hinder, delay, or defraud). \textit{Unif. Fraudulent Transfer Act} § 8(a), 7A U.L.A. 662 (1985).

Transferees for less than fair consideration but without actual fraudulent intent were accorded liens pursuant to § 9(2) of the UFCA in Goodhope \textit{v.} Overgaard, 227 N.W. 380 (S.D. 1929) (questioned by McLaughlin, \textit{supra} note 27, at 433).

32. Section 102(5) states that the word "or" is not to be read as exclusive when it appears in the Bankruptcy Code. 11 U.S.C. § 102(5) (1988). Sections 544 and 548 allow the trustee to avoid either transfers or obligations. \textit{Id.} §§ 544(a), 548(a).


the same result vis-a-vis all other creditors.\textsuperscript{37} It seems clear, however, that equitable subordination in a UFTA proceeding must not result in a detrimental change in the relative priority of a creditor not before the court with respect to the creditors who are parties to the proceeding.

Equitable subordination is appropriate when a defendant’s conduct is directed toward a particular creditor who was misled by the defendant’s conduct.\textsuperscript{38} A fraudulent transfer, however, typically is not directed toward or detrimental to only one creditor or even to only a group of creditors. The importation of equitable subordination into the panoply of remedies available to a defrauded creditor, however, enables the court to modify the relief accorded in light of competing considerations. Thus, the lien to which a transferee is entitled for the consideration that the transferee gave in a constructively fraudulent transfer conceivably may be required to share its priority with secured creditors whose equities are entitled to equal treatment. Instead of allowing the claim of a creditor whose security interest is avoided as constructively fraudulent to compete pari passu with other creditors, however, the court may subordinate the claim of the erstwhile secured creditor.\textsuperscript{39}

\begin{footnotesize}
\begin{enumerate}
\item See, e.g., Miller v. Borton (\textit{In re} Bowman Hardware & Elec. Co.), 67 F.2d 792, 795 (7th Cir. 1933) (subordinating the claim of a creditor who induced the debtor to deny its indebtedness to that creditor when the debtor was negotiating with another creditor who relied on the debtor’s misrepresentation in extending credit); Cambridge Meridian Group, Inc. v. Connecticut Nat’l Bank (\textit{In re} Erin Food Servs., Inc.), 117 B.R. 21, 26-28 (Bankr. D. Mass. 1990) (apparently subordinating security interests for loans aggregating $61,741,000 to the claims of unsecured creditors to the extent of $5,827,541, which represented the amount that the debtor diverted from financing the debtor’s operations and needs; citing the reference in § II of the New Hampshire Fraudulent Conveyance Statute to “rules of law and equity” in support of allocating loans “between those that are fully secured and prioritized, and loans in fact used for an unsecured purpose”) (discussed in Ellen J. Pollock, \textit{Secured Lenders Can Lose Place in Line}, \textit{Wall St. J.}, June 20, 1991, at B4); see also \textit{In re} Process-Mainz Press, Inc., 236 F. Supp. 333, 346-49 (N.D. Ill. 1964) (finding that a lender who financed a buyout, taking the debtor’s assets and a pledge of the debtor’s stock as security, and who thereafter assumed control of the debtor’s financial affairs, manipulating them for its own benefit, was a fraudulent transferee of the mortgaged assets; and subordinating the lender’s claims to the claims of unsecured creditors on determination by the court that the lender “was not a secured creditor but in substance the owner” of the corporate debtor in view of its “control, domination, spoliation, ownership and breach of fiduciary duty’’), rev’d on jurisdictional
\end{enumerate}
\end{footnotesize}
In *Murphy v. Meritor Savings Bank (In re O'Day Corp.)*\(^{40}\) the court held, after an extended evidentiary hearing on the trustee and a secured creditor's motions, that the trustee had stated grounds for relief under sections 4 and 5 of the UFCA against the bank that financed a leveraged buyout.\(^{41}\) The trustee argued that it would be anomalous to avoid the liens and then permit the bank to participate in the recovered assets as an unsecured creditor.\(^{42}\) The bank countered that it was entitled, as an unsecured creditor, to a pro rata share of the estate or, at worst, to participate as a subordinated creditor under section 510 of the Code.\(^{43}\) After disagreeing with the bank and agreeing with the trustee, the court elaborated on the reasons why the bank's claim as an unsecured creditor should be subordinated pursuant to section 510 of the Code.\(^{44}\) The court found no fraudulent intent on the part of the bank, however, and explicitly declined to annul the obligations incurred by the debtor or to order disgorgement of the payments received after the LBO.\(^{45}\) A mortgage to the bank that secured an antecedent debt independent of the LBO was sustained.\(^{46}\)

At least one state has expressly listed "equitable subordination" in section 10 of its version of the UFTA as one of the "principles of law and equity" that supplement the Uniform Act.\(^{47}\)

In *Max Sugarman Funeral Home, Inc. v. A.D.B. Investors*\(^{48}\) Cir-

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42. *Id.* at 411.
43. *Id.* at 412.
44. *Id.*
45. *Id.* at 413.
46. *Id.* at 410, 413.
48. 926 F.2d 1248 (1st Cir. 1991).
cuit Judge Cyr, writing for the First Circuit, declared that section 510(c) of the Bankruptcy Code, which authorizes equitable subordination of a claim, could not be employed to avoid security interests given to insiders of a corporate debtor as fraudulent transfers.\textsuperscript{49} After subordination orders entered by the bankruptcy court were vacated on the ground that only allowed claims can be subordinated, however, the court held that the series of liens given the insiders were fraudulent transfers.\textsuperscript{50} The opinion did not preclude the possibility that the insiders might still file claims pursuant to sections 502(d) and (h) and that these claims might yet be allowed and subordinated to unsecured claims rather than utterly disallowed.

III. TRANSFEREE DEFINED

Neither the Bankruptcy Code nor the UFTA defines transferee. The courts have had a difficult time determining who is a transferee for purposes of liability under section 550 of the Bankruptcy Code. The courts have dealt with this problem only minimally under the UFTA.\textsuperscript{51} The problem arises typically when the fraudulent transfer is a deposit of money to a bank account or a payment to brokers or agents for the benefit of third parties. Several approaches have evolved as to when the one receiving money is liable as a transferee. Judge Easterbrook found that transferee status requires “dominion over the money or other asset, the right to put the money to one’s own purposes.”\textsuperscript{52} Other courts have hinged transferee status on whether the transferee had notice that the transaction was suspect,\textsuperscript{53} whether the recipient had a direct business relationship with the transferor,\textsuperscript{54} and whether the transferee was liable under common-law agency principles.\textsuperscript{55}

\textsuperscript{49} Id. at 1253-54.
\textsuperscript{50} Id. at 1255.
\textsuperscript{51} See Kennedy, supra note 36, at 662-65.
\textsuperscript{52} Bonded Fin. Servs., Inc. v. European Am. Bank, 838 F.2d 890, 893 (7th Cir. 1988). Judge Easterbrook’s approach was cited favorably by the district court in Lowry v. First National Bank (In re Robinson Brothers Drilling, Inc.), 97 B.R. 77, 81 (W.D. Okla. 1988), aff’d, 892 F.2d 850 (10th Cir. 1989). Easterbrook’s definition also was utilized in Nordberg v. Societe Generale (In re Chase & Sanborn Corp.), 848 F.2d 1196, 1200 (11th Cir. 1988).
\textsuperscript{53} See Huffman v. Commerce Sec. Corp. (In re Harbour), 845 F.2d 1254, 1258 (4th Cir. 1988).
Under the Bankruptcy Act of 1898, a transferee had to have ownership of or the beneficial interest in transferred assets before it could be required to return them. Appellant, Kaiser Steel Resources, Inc. (Kaiser), in Kaiser Steel Resources, Inc. v. Jacobs (In re Kaiser Steel Corp.), argued that Congress changed the Bankruptcy Act of 1898 by enacting section 550(a) of the Bankruptcy Code. Section 550(a) expressly permits recovery from the initial transferee regardless of whether the initial transferee is the owner of the fraudulently transferred property either legally or beneficially. In attempting to defeat liability, stockbrokers, who had received funds from Kaiser in redemption of customer stock, argued that they were not initial transferees. The bankruptcy court concluded that the brokers were liable as agents for undisclosed principals. The district court reversed, holding that agency principles were inapplicable because the broker (Schwab) had “no contractual relationship” with Kaiser, the debtor. Kaiser’s brief to the Tenth Circuit argued not only in support of the bankruptcy court’s ruling but also that the stockbrokers had sufficient control.

60. The bankruptcy court reviewed numerous cases interpreting Section 550, and explained how they have employed, in essence, centuries-old agency principles. Its analysis ties into the Fourth Circuit’s holding in Columbia Data Products that the initial transferee is the one who has “a direct business relationship with the debtor.” 892 F.2d at 28. That entity is generally a disclosed principal in “conduit” cases, but it may be the agent for an undisclosed principal.

The blunt fact is that brokers are agents; more to the point, they are agents for undisclosed or partially disclosed principals; and, as such, they are governed, at least in part, by the common law.

1. (1) Kaiser’s shareholders had the right to sue Kaiser in contract to get the $22 they were promised for each share of common stock they turned in. At the least, the Kaiser merger created a quasi-contractual obligation enforceable by and rescindable against the shareholders. See United States v. Neidorf, 522 F.2d 916, 918 (9th Cir. 1975), cert. denied, 423 U.S. 1087 (1976) (fraudulent conveyance action alleging dividends and stock transactions rendered company insolvent; shareholder liability is based on quasi-contract). Schwab had the right to sue, in contract, to enforce the merger as agent for its undisclosed customer principals. Schwab, dealing with Kaiser as an agent for partially disclosed principals, can likewise be sued. Restatement (Second) of Agency § 321 (1958); Port Ship Service v. International Ship Management, 800 F.2d 1418 (5th Cir. 1986) (agent liable for debts of partially disclosed principals).

(2) The remedy Kaiser seeks in this suit, a return of the $22 per share taken by its shareholders, is akin to the remedy of rescission. Cf. Pinter v. Dahl, 486 U.S. 622, 108 S. Ct. 2063, 2076 n.18 (1988) (Securities Act remedy is
over the funds to result in initial transferee liability. The later argument was premised on the following: Schwab, for all intents and purposes, was a stockholder to the outside world, including Kaiser; Schwab’s customer agreements gave it broad rights over the cash received on behalf of its customers; Schwab had even greater control


An agent who has received things from another for a disclosed or partially disclosed principal in a transaction conducted by him has a duty to return them or their proceeds if the other rescinds the transaction for a cause existing at the time of their receipt, to the extent that the agent has not, before notice of rescission and in good faith, changed his position.

Restatement (Second) of Agency § 339, pp. 97-98 (1958) (emphasis added). Rescission predicated on fraud may be obtained from an agent with no privity to the fraudulent agreement. Pinter v. Dahl, 108 S. Ct. at 2079 n.23 (citing Gordon v. Burr, 506 F.2d 1080 (2d Cir. 1974) (stock purchaser suit for rescission against broker)).

An agent for a partially disclosed principal cannot escape liability on "mere conduit" grounds. Insurance Brokers Service, Inc. v. Marsh & McLennan, 665 F. Supp. 649, 651 (N.D. Ill. 1987). And there is no change of position when an agent, like Schwab, only credits its principals' accounts and maintains a lien on the money. Restatement (Second) of Agency § 339, Comment f. .

(3) Kaiser's cause of action need not fit precisely into a rescission or contract niche for agency principles to apply. Restatement (Second) of Agency § 321, Comment b is clear:

Separate liability of agent. Unless agreed otherwise, the agent is subject to separate liability and may be sued individually without the joinder of the principal.

Agents acting for undisclosed or partially disclosed principals are liable for statutory violations, as well as torts and contract breaches. Powers v. Coffeyville Livestock Sales Co., Inc., 685 F.2d 311 (10th Cir. 1981) (auctioneer liability for violation of UCC, interpreted in light of common law agency). See also cases supplementing federal securities law analysis with common law agency rules, e.g., In re Atlantic Financial Management, Inc., 784 F.2d 29 (1st Cir. 1986); Marbury Management, Inc. v. Kohn, 629 F.2d 705, 712-16 (2d Cir.), cert. denied, 449 U.S. 1011 (1980); Paul F. Newton & Co. v. Texas Commerce Bank, 630 F.2d 1111, 1118-19 (5th Cir. 1980).

Schwab kept its principals' identities to itself; it benefitted by doing so; it has the means to collect in turn from those principals; it should be held responsible for the legal obligations flowing from its choices, whether Kaiser's suit lies in contract, tort, or statute.

Appellant's Opening Brief at 22-25, Kaiser I, 913 F.2d 846 (10th Cir. 1990) (footnotes omitted).

61. Id. at 14-15.
62. Id. at 16.
over cash received for Kaiser stock bought on the margin; Schwab had the right to use the cash credited to its customer accounts; Schwab had total control over the Kaiser cash for a week; and Schwab had more control than a bank. As will be seen in Part VI, Kaiser's arguments went unanswered and unresolved.

IV. LIABILITY OF THOSE BENEFITTED AND PARTICIPANTS IN FRAUDULENT TRANSFERS

The position taken by Professor Glenn, the preeminent authority on the subject of fraudulent transfers, may have been responsible for the hesitancy of courts to develop theories of recovery against those

63. Id. at 17-18.
64. Id. at 18-19.
65. Id. at 19-21.
66. The Seventh Circuit concluded in Bonded Financial that its bank had no dominion and control because "the Bank did not even acquire a valuable right to offset its loan against the funds in [the check payee's] account," and did not acquire dominion "until [the payee told it] to debit the account to reduce the loan." 838 F.2d at 893, 934. The court indicated initial transferee dominion and control would exist if the bank had the right to take and use the money upon receipt merely because of offset rights or a customer instruction.

Schwab, in contrast, had more than inchoate, common-law offset rights. Unlike the bank in Bonded Financial, Schwab had the right to take and use the Kaiser money pursuant to broad customer written authorization, especially to the extent its customers had purchased their Kaiser stock on margin, and pursuant to industry practice and SEC rules. Schwab had the express right to take the Kaiser money, its collateral, to repay any margin loans, and could even hold it to ensure funds would be available to cover other customer purchase obligations.

The difference between banking and brokerage is most prominent in the several days just after funds are received for a customer's accounts. The bank in Bonded Financial received money directed to a specific customer and a specific account; it was not able to use the money for a week before crediting that account and allowing the customer to withdraw it.

Schwab received Kaiser's money directed simply to "Schwab." Neither Kaiser nor DTC knew how many customers, if any, Schwab had. Some brokers disbursed all the money, and some kept most for their arbitrage account—only the brokers knew for sure. And until the brokers reconciled their books and credited their customers, with no required deadline to do so, the customers could not withdraw the money. The customer could not use the money in the interim; but under SEC rules, the broker could use the money to make a lot more money. Under Bonded Financial, which this Court found provides "sound guidance," and in light of all five types of rights and powers described above, Schwab had sufficient dominion and control to be an initial transferee, responsible to return the cash it received and used, and take up the burden of collecting from its customers.

Id. at 21-22.
who assist in making fraudulent transfers. Whatever the reason, those who assist fraudulent transfers but do not necessarily receive any direct benefit from the transfer have remained largely outside the reach of creditors’ remedies. What cases there are have reached differing results. Several cases simply state, as did Professor Glenn, that there can be no recovery from one who aids, participates in, or conspires to effect a fraudulent transfer. Other courts have permitted recovery. In Atlanta Shipping Corp. v. Chemical Bank the Second Circuit held that there is no aider and abettor liability under the New York fraudulent conveyance statute, but that there is aider and abettor liability under New York common law if funds are wrongfully diverted.

In Elliott v. Glushon the Ninth Circuit refused to recognize conspiracy liability under section 67d of the Bankruptcy Act. The Ninth

67. See Lowell Staats Mining Co. v. Philadelphia Elec. Co., 878 F.2d 1271, 1276 n.1 (10th Cir. 1989); FDIC v. Porco, 552 N.E.2d 158, 159-60 (N.Y. 1990). In Mack v. Newton, 737 F.2d 1343 (5th Cir. 1984), a bankruptcy trustee sought to assert claims against the debtor’s former principals on the theory that they had conspired to divert the debtor’s assets. The trustee argued that the transfers were made both without adequate consideration and with the intent to hinder, delay, or defraud creditors. The court rejected these claims for the most part, reasoning that neither federal law (i.e., §§ 67d(6) and 70e(2) of the Bankruptcy Act) nor state law (i.e., the Texas Fraudulent Conveyance Act) authorized a claim against someone who did not receive either directly or indirectly any benefit from the transfer. Id. at 1356-62; see also Menner v. Slater, 83 P. 35, 35 (Cal. 1905); Gilmore v. Tucker, 148 Cal. Rptr. 86 (Cal. Dist. Ct. App. 1978) (text available on LEXIS) (holding that a plaintiff cannot recover on a conspiracy claim unless the defendants committed a separate wrong that caused the plaintiff to suffer damages).

68. See, e.g., McElhanon v. Hing, 728 P.2d 256, 261-64 (Ariz. Ct. App. 1985) (holding that an attorney who drafted transfer documents knowing that the consideration for the transfer was inadequate, that the debtor would be rendered insolvent, and that the debtor intended to defraud creditors may be held liable for conspiring to commit a fraudulent conveyance, vacated en banc in part on other grounds, 728 P.2d 273 (Ariz. 1985), cert. denied, 481 U.S. 1030 (1987); Dalton v. Meister, 239 N.W.2d 9, 17-18 (Wis. 1976).

69. 818 F.2d 240 (2d Cir. 1987).

70. Id. at 250-51. The Second Circuit affirmed the district court, which had held that there was no aiding and abetting liability under the fraudulent conveyance statute.

The fourth cause of action contains a claim against Chemical for aiding and abetting a fraudulent conveyance. We do not believe it possible to state such a claim. In a fraudulent conveyance action, the plaintiff attacks the conveyance seeking to reclaim the property conveyed. The appropriate relief is to void the conveyance. An aiding and abetting claim against someone other than a transferee is meaningless in these circumstances. That aspect of the fourth cause of action alleging that Chemical aided and abetted a fraudulent conveyance is dismissed.


71. 390 F.2d 514 (9th Cir. 1967).
Circuit declined to follow its earlier decision in *Brainard v. Cohn* in which the court held that all conspiring parties "are as one who received the property, and each joint tort-feasor has the burden of bearing the entire loss." In *Elliott*, however, the Ninth Circuit limited *Brainard* to situations in which the defendants have "intermixed" the fraudulently transferred property with identical property so that identifying the fraudulently transferred property is impossible. Also, the court ruled that section 67d is designed to cancel fraudulent transfers, not "to render civilly liable all persons who may have contributed in some way to" making a fraudulent transfer. The court was concerned about how far a contrary rule would lead.

It is also significant that the term "fraudulent transfer" as used in the [Bankruptcy] Act includes a great many transactions which do not constitute "actual" fraud; no intent to defraud need be found so long as the prescribed statutory criteria are met. Thus there is affirmative justification for rejecting a rule under which all persons having a hand in transactions later held void under the Act would be civilly liable. Limiting recovery in the manner suggested by the appellee Glushon protects innocent persons from civil liability, while at the same time preserving the assets of the bankrupt's estate.

The Fifth Circuit followed *Elliott* in *Mack v. Newton* and rejected conspiracy liability under both the Bankruptcy Act and the Texas fraudulent conveyance statute. The Fifth Circuit noted that *Elliott* had been followed in the First, Second, and Eighth Circuits and that no court had disagreed with *Elliott*. *Mack* is, perhaps, no more than the product of Professor Glenn's persuasiveness. In *Mack* the Fifth Circuit relied on the Texas Supreme Court's decision in *Estate of Stonecipher v. Estate of Butts*. In *Estate of Stonecipher* the Texas Supreme Court, in language reminiscent of Professor Glenn, stated the following in regard to actions in civil conspiracy:

72. 8 F.2d 13 (9th Cir. 1925).
73. Id. at 15.
74. *Elliott*, 390 F.2d at 515-16.
75. Id. at 516.
76. Id. at 516-17 (footnote omitted).
77. 737 F.2d 1343 (5th Cir. 1984).
78. Id. at 1356-62.
79. Id. at 1358 (citing Robinson v. Watts Detective Agency, Inc., 685 F.2d 729, 737-38 (1st Cir. 1982), cert. denied, 459 U.S. 1105, and cert. denied, 459 U.S. 1204 (1983); Klein v. Tabatchnick, 610 F.2d 1043, 1048 n.4 (2d Cir. 1979); Jackson v. Star Sprinkler Corp., 575 F.2d 1223, 1234 (8th Cir. 1978)). The Ninth Circuit had also reaffirmed its holding in *Elliott*. Id. (citing Gough v. Titus (In re Christian & Porter Aluminum Co.), 584 F.2d 326, 339 (9th Cir. 1978)).
80. 591 S.W.2d 806 (Tex. 1979).
[A] general creditor has no right in or lien upon property of the debtor and therefore suffers no damages if the debtor’s property is conveyed to others to evade payment. The damage sustained by the creditor in being deprived of an opportunity to make a levy and this damage is too remote. The loss suffered is not of a right, but of a chance to secure a right.81

Recent decisions, however, indicate that the law is changing. Several courts have recognized a shareholder’s right to recovery against those who aid and abet fraudulent transfers made by a corporation on the theory that they aid and abet a breach of fiduciary duty.82 Although in Mack the Fifth Circuit stated that Texas law does not allow an action for civil conspiracy,83 a recent Texas Court of Appeals decision suggests that relief may be permitted for what is in effect a conspiracy to effect a fraudulent transfer under a constructive fraud theory.84 Furthermore, one bankruptcy judge has interpreted Mack to allow recovery from anyone who benefits from a fraudulent transfer, 81. Id. at 808 (citing Le Gierse v. Whitehurst, 18 S.W. 510 (Tex. 1886)). 82. See Samuel M. Feinberg Testamentary Trust v. Carter, 652 F. Supp. 1066, 1082-84 (S.D.N.Y. 1987) (holding that greenmailers may be held liable as aiders and abettors to target company’s management); Heckmann v. Ahmannson, 214 Cal. Rptr. 177, 182-83 (Ct. App. 1985) (holding that corporate “greenmailers” could be liable for proceeds received in failed takeover bid as aiders and abettors to a breach of fiduciary duty committed by the incumbent management); Gilbert v. El Paso Co., 490 A.2d 1050, 1056-58 (Del. Ch. 1984) (holding that a hostile corporate raider that withdrew its original tender offer upon reaching an agreement with the incumbent management, which included golden parachute arrangements, could be liable in civil conspiracy for aiding and abetting a breach of the incumbent management’s fiduciary duty), aff’d, 575 A.2d 1131 (Del. 1990). 83. Mack v. Newton, 737 F.2d 1343, 1356 (5th Cir. 1984). 84. In Speed v. Eluma International, Inc., 757 S.W.2d 794 (Tex. Ct. App. 1988), the directors and shareholders of a corporation attempted a bulk sale of the company’s assets. The corporation’s creditors, however, obtained a court order enjoining the sale. One of the directors, who owned the land on which the company operated, then claimed that the company was in default on its lease and foreclosed on his landlord’s lien. At the foreclosure sale the original buyer purchased the company’s assets for the same price agreed upon in the thwarted bulk sale agreement. Id. at 795. The Texas Court of Appeals found sufficient evidence to support a verdict of constructive fraud. Id. at 798. It ruled that the directors had perpetrated a sham transaction in order to breach an equitable duty owed to the company’s creditors. The court defined constructive fraud broadly to include the breach of a “legal or equitable duty which . . . the law declares fraudulent because of its tendency to deceive others, to violate confidence, or to injure public interests.” Id. at 796. The court held the directors personally liable for damages and noted that the purchaser of the company’s assets also could have been held personally liable for damages. Id. Although the court based the purchaser’s liability on the idea that it was “merely a continuation” of the original debtor company, its decision could be interpreted as relying on an aider and abettor or civil conspiracy theory of recovery.
not just those who directly receive the property transferred.\textsuperscript{85} This is consistent with section 550(a) of the Bankruptcy Code, which expressly allows recovery from "the entity for whose benefit such transfer was made."\textsuperscript{86}

In view of the change in the statutory language, decisions like \textit{Ellliott v. Glushon}, based on the more limited language of the Bankruptcy Act, have lost their former authority. It is no longer true that Congress has limited the trustee's action "to recovery against persons who have 'received' the property in question." Fraudulent conveyances are now like preferential transfers, as to which actions would always lie against the persons who benefitted from them, as well as those who were the recipients of such transfers.\textsuperscript{87}

Recent cases, relying on section 550(a), have allowed personal recoveries from the stockholders of closely held corporations if the stockholders benefit from a fraudulent transfer received by the corporation.\textsuperscript{88} Thus, despite Professor Glenn, the law is evolving.

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{85} Ossen v. Bernatovich (\textit{In re National Safe Northeast, Inc.}, 76 B.R. 896, 904 (Bankr. D. Conn. 1987).
\item \textsuperscript{87} Pereira v. Checkmate Communications Co. (\textit{In re Checkmate Stereo & Elecs., Ltd.}, 9 B.R. 585, 620 (Bankr. E.D.N.Y. 1981) (citations omitted), aff'd, 21 B.R. 102 (E.D.N.Y. 1982).
\item \textsuperscript{88} In Tavormina v. Weiss (\textit{In re Behr Contracting, Inc.}, 79 B.R. 84 (Bankr. S.D. Fla. 1987), a corporate debtor transferred $68,000 within a year of bankruptcy to American Dream Realty & Mortgage, Inc., a corporation owned wholly by a man named Weiss who also was a director of the debtor corporation. The bankruptcy court held that § 550(a)(1) enabled recovery of the transfer both from American Dream and from Weiss. As the court reasoned: "It is undisputed that American Dream is fully owned by Weiss and has no assets or liabilities. As such, the court concludes that the transfer was for the benefit of Weiss and therefore, recoverable from him." \textit{Id.} at 87 (citing 11 U.S.C. § 550(a)(1) (1988)). In Ossen v. Bernatovich (\textit{In re National Safe Northeast, Inc.}, 76 B.R. 896 (Bankr. D. Conn. 1987), the court held that $48,000 transferred from the debtor, which was owned wholly by Bernatovich, to another corporation also owned wholly by Bernatovich could be recovered from Bernatovich himself. \textit{Id.} at 904. As the court explained: "Bernatovich, as the sole stockholder of both the debtor and ATM, was in a position that enabled him to manipulate transactions between the two corporations for [his] benefit." \textit{Id.} And in Ohio Corrugating Co. v. Security Pacific Business Credit, Inc. (\textit{In re Ohio Corrugating Co.}, 70 B.R. 920 (Bankr. N.D. Ohio 1987), an LBO case, the court held that a corporation which did not even exist at the time of the transfer could be sued on the theory that it was "an entity for whose benefit the transfer was made under section 550(a)(1)." \textit{Id.} at 924. Also, the court concluded that the sole stockholder of this newly formed corporation could be sued but cautioned that some additional evidence is needed beyond the fact of sole ownership. The court stated, "Plaintiff must prove that SHEPPARD [the sole stockholder] acted other than in the normal course of business of DPAC I, DPAC II, or OHIO CORRUGATING [the corporations] and must submit appropriate evidence as to SHEPPARD's individual liability." \textit{Id.} at 925. There is also authority that the intended benefit need not have been received by the
\end{enumerate}
\end{footnotesize}
A significant development in recent years was the enactment of the Racketeer Influenced and Corrupt Organizations Act (RICO) in 1970.\textsuperscript{69} Under certain circumstances RICO, and its state law counterparts,\textsuperscript{60} allow recovery from those who participate in or assist fraudulent transfers.\textsuperscript{61} Although judicial reception of the RICO statute has been chilly, this is largely because of its misuse.\textsuperscript{92} Courts should not be hostile to its use, however, if a transfer is made with the express intent to hinder, delay, or defraud creditors under circumstances that violate defendant. See Merrill v. Dietz (\textit{In re} Universal Clearing House Co.), 62 B.R. 118, 127 (D. Utah 1986) (allowing recovery from an individual who requested that the debtor write a check directly to one of the individual’s creditors); Hayley v. Sorani (\textit{In re} Richmond Produce Co.), 118 B.R. 753, 759 (Bankr. N.D. Cal. 1990) (“[R]ecovery of an avoided transfer may be ordered under 11 U.S.C. § 550(a)(1) even though the entity did not actually receive a benefit as a result of the transfer.”).


90. Similar legislation has been adopted in a number of states. E.g., ARZ. REV. STAT. ANN. §§ 13-2301 to -2317 (1989 & Supp. 1991); FLA. STAT. ANN. chs. 895.01 to .09 (Harrison 1991 & Supp.).

91. The RICO statute defines “racketeering activity” by referring to various criminal acts, the so-called predicate acts. 18 U.S.C. § 1961(1) (Supp. II 1990). The list of activities includes criminal bankruptcy fraud, best defined by 18 U.S.C. § 152:

Whoever, either individually or as agent or officer of any person or corporation, in contemplation of a case under title 11 by or against him or any other person or corporation, or with intent to defeat the provisions of title 11, knowingly and fraudulently transfers or conceals any of his property or the property of such other person or corporation;

\ldots

Shall be fined not more than $5,000 or imprisoned not more than five years, or both.

18 U.S.C. § 152 (1988). Section 1962(d) of RICO makes it unlawful for anyone to conspire to commit racketeering activities, \textit{id.} § 1962(d), and § 1964 authorizes the Attorney General to institute civil proceedings against anyone who violates § 1962. In addition, § 1964 creates a private cause of action for anyone who suffers injury to “business or property by reason of a violation of section 1962,” and a plaintiff can recover triple damages under the statute. \textit{id.} § 1964(c).

section 152 of Title 18, the definition of criminal bankruptcy fraud.\textsuperscript{93} Under RICO a plaintiff can proceed against those who conspired in or aided and abetted the fraudulent conduct because there is a specific conspiracy provision within RICO.\textsuperscript{94} It requires that the participants agreed to violate section 1962(a), (b), or (c) of RICO. Thus, assuming the elements of a RICO claim are otherwise met, a fraudulent transfer—that is, a knowing and fraudulent transfer of property made with the intent to defeat the provisions of Title 11, or in contemplation of a case under Title 11—gives rise to joint and several liability against those who participated in the fraudulent conduct.

The trustee in bankruptcy clearly has standing to bring a RICO claim if the debtor is an entity because the entity can be separated from the individuals involved in the fraud.\textsuperscript{95} The claim is an asset of


\textsuperscript{94} Id. § 1962(d). The general rules as to criminal conspiracy are similar and require:

an agreement between two or more persons to commit a crime . . . and an overt act by one of them in furtherance of the agreement. The government must prove beyond a reasonable doubt that the defendant knew of the conspiracy and that he voluntarily became a part of it. The existence of a conspiracy may be proved by circumstantial evidence and may be inferred from concert of action.


\textsuperscript{95} In Wooten v. Loshbough, 951 F.2d 768 (7th Cir. 1991), the court ruled as follows:

The company's claim against the defendants for what they did to it is a corporate asset now vested in the trustee so that he can liquidate it for the benefit of the company's creditors—including Wooten—in accordance with their legal entitlements in bankruptcy. Wooten is seeking to jump the queue—to bypass bankruptcy—to wrest this valuable corporate asset from the trustee by suing the defendants directly. To allow her to do this would upset the priorities established by the bankruptcy law—which gives a low priority to a judgment creditor, who despite the apparent connotation of the term is just another unsecured creditor until by executing the judgment he obtains a judicial lien. \textit{Id.} at 770 (citing Linsey v. Federal Land Bank (\textit{In re Lindsey}), 823 F.2d 189, 191 (7th Cir. 1987); Barnett v. Stern, 93 B.R. 962, 975-77 (N.D. Ill. 1988), rev'd, 909 F.2d 973 (7th Cir. 1990)); cf. Whalen v. Carter, 954 F.2d 1087 (5th Cir. 1992) (denying RICO standing to plaintiffs as shareholders but finding standing for limited partners to assert RICO claims against general partners and third parties); Mid-State Fertilizer Co. v. Exchange Nat'l Bank, 877 F.2d 1333 (7th Cir. 1989) (denying standing to shareholders and creditors who sued individually because RICO claims can be brought only by the entity directly injured by a fraudulent transfer); Ocean Energy II, Inc. v. Alexander & Alexander,
the estate under Bankruptcy Code section 541(a)\textsuperscript{96} and derivative suits by stockholders are automatically stayed under section 362(a).\textsuperscript{97} However, establishing the trustee's standing is more problematic if the debtor is an individual because the debtor is involved in the fraud. In \textit{Barnett v. Stern}\textsuperscript{98} an individual involved in various fraudulent transfers filed bankruptcy. The court held that the individual's trustee had standing to prosecute a RICO claim.\textsuperscript{99} The court did not find, however, that the cause of action belonged to the estate under either section 541 (because the debtor was \textit{in pari delicto} and therefore could not bring the claim outside of bankruptcy\textsuperscript{100}) or section 544 (the court interpreted section 544 as limited to "avoidance claims"\textsuperscript{101}) of the Bankruptcy Code.\textsuperscript{102} Instead, the court distinguished cases that had followed the Supreme Court's decision in \textit{Caplin v. Marine Midland Inc.}, 988 F.2d 740 (5th Cir. 1989) (setting forth a two-part test for shareholder RICO standing based on derivative suit analysis). \textit{But see} Feltman v. Prudential-Bache Sec., 122 B.R. 466 (S.D. Fla. 1990) (holding that the Chapter 11 trustee of sham corporations created by a convicted embezzler to hide the proceeds of his crimes could not assert RICO claims because the debtor corporations were \textit{in pari delicto} with the embezzler's fraud).

96. 11 U.S.C. § 541(a) (1988); see \textit{Wooten}, 951 F.2d at 770.
98. 93 B.R. 962 (N.D. Ill. 1988), \textit{rev'd on other grounds}, 909 F.2d 973 (7th Cir. 1990).
99. In \textit{Barnett} the debtor was an individual who had fraudulently transferred personal assets to a trust prior to filing a Chapter 7 petition. Two creditors initiated a RICO claim against third parties for their involvement in the prepetition fraudulent transfers. The court held that the bankruptcy trustee, not the creditors, had standing to pursue RICO claims which concerned prepetition fraudulent activity. \textit{Id.} at 967-72. In \textit{Kremen v. Blank}, 55 B.R. 1018 (D. Md. 1985), however, the court held that the trustee has standing to challenge only postpetition RICO violations. The court reasoned as follows:

\begin{quote}
Plaintiff argues that property conveyed by the Debtor in an effort to defraud his creditors prior to the filing of his Petition remains the property of the Estate. It is true that, like an unsecured general creditor, the trustee has standing to overturn fraudulent conveyances. 11 U.S.C. § 544(a)(b). Property fraudulently conveyed reverts to the estate. However, a general creditor without a lien has no legal right or interest in a Debtor's property prior to obtaining a judgment of fraudulent conveyance. \textit{Van Royen v. Lacey}, 262 Md. 94, 277 A.2d 13 (1971). A trustee has no greater interest than an unsecured creditor in property conveyed prior to the Debtor's voluntary filing of a bankruptcy petition.
\textit{Id.} at 1021.
\end{quote}

100. \textit{Barnett}, 93 B.R. at 969.
101. \textit{Id.} at 969-70.
102. \textit{Id.} At least one court has held that although a RICO claim is not estate property if the debtor participated in the fraud, it is assertable by the trustee under § 544. \textit{Lumbard v. Maglia}, Inc., 621 F. Supp. 1529, 1541-42 (S.D.N.Y. 1985) (holding that the trustee can bring a RICO claim under § 544 even if the debtor participated in the challenged wrongdoing).
Grace Trust Co., which held that a bankruptcy trustee does not have standing to assert damage claims that belong to creditors. In the Caplin case the creditors whose claims were being asserted were debenture holders who had claims against the indenture trustee for breach of its fiduciary duty. The Barnett court relied on "common sense," the principle of equitable distribution, and a series of alter-ego cases in distinguishing Caplin and finding RICO standing. However, all but one of the alter-ego cases cited by the court allowed a debtor corporation to pierce its own corporate veil, and thus the decisions are based on the idea that the alter-ego claims became property of the estate under section 541 of the Bankruptcy Code. The one alter-ego case that directly supports the Barnett court's holding is Koch Refining v. Farmers Union Central Exchange, Inc. In Koch the Seventh Circuit interpreted Caplin only as denying standing to the trustee if the trustee is asserting the personal claims of a specific creditor. Thus, the Koch court stated that "allegations that could be asserted by any creditor could be brought by the trustee as a representative of all credi-

The question was settled, for all practical purposes, under the Act by Caplin v. Marine Midland Grace Trust Co., where the Supreme Court held that a trustee had no standing to bring an action on behalf of certain creditors (bondholders) against an indenture trustee. Because of the reach of the doctrine of Moore v. Bay... Caplin was widely understood to prohibit trustees from raising creditor damage actions generally, including alter ego claims. Since such a veil-piercing action was not a claim which the corporation could bring in its own behalf under state law, and thus was not property of the estate under Section 70a, there was no way for the trustee to argue that standing existed by virtue of this alternate route either.
The Caplin court determined, also, that Section 70e, whereby the trustee could assert the rights of creditors of the estate, was limited to avoidance of transfers or obligations. The court was concerned with, among other things, the subrogation problems which would be raised when estate creditors, some of whom could not have recovered under state law, attempted to participate in the trustee's recovery.
Richard L. Epling, Trustee's Standing to Sue in Alter Ego or Other Damage Remedy Actions, 6 BANKR. DEV. J. 191, 192-93 (1989).
106. Barnett, 93 B.R. at 967-72; see also St. Paul Fire & Marine Ins. Co. v. Pepsico, Inc., 884 F.2d 688 (2d Cir. 1989) (finding that an alter-ego claim was a generalized claim and could be pursued only by the trustee because the claim is property of the estate); S.I. Acquisition, Inc. v. Eastway Delivery Serv., Inc. (In re S.I. Acquisition, Inc.), 817 F.2d 1142 (5th Cir. 1987) (ruling that if state law does not specifically forbid a corporation from piercing its own corporate veil, then common sense, judicial economy, and the bankruptcy process indicate that the trustee should have standing to bring third party claims and pierce its debtor's veil).
108. Id. at 1347 n.11.
tors.109 The Koch court, however, ultimately based its holding that the trustee had standing to pursue an alter-ego claim on the same rationale as the other alter-ego cases cited in the Barnett decision.110 Thus, the legal authority supporting the Barnett decision is somewhat dubious.

The Eighth Circuit has taken a different view of the matter. In Mixon v. Anderson (In re Ozark Restaurant Equipment Co.)111 the Eighth Circuit held that an alter-ego claim belonged to the creditors and not the debtor corporation. Therefore, the alter-ego claim was not property of the bankruptcy estate.112 The Eighth Circuit, relying on the legislative history underlying section 544, also held that section 544(a) does not allow the trustee to assert creditors’ claims.113 Based on the work of the Commission on the Bankruptcy Laws of the United States, the sponsors of the Bankruptcy Reform Act of 1978 originally proposed a version of section 544 that contained an additional subsection expressly overruling Caplin.114 Congress did not adopt this proposal,115 and in Ozark Restaurant Equipment the Eighth Circuit found

109. Koch, 831 F.2d at 1348-49.
110. Id. at 1343-47.

Virtually all of these recent cases find that standing lies in Section 541 by discovering a right of action under state law permitting a corporation to maintain an alter ego action against its own stockholders and other insiders; in effect, this action permits a corporation to pierce its own veil. Surprisingly, Koch Refining v. Farmers Union Central Exchange, Inc., suggested that standing might also be found by inference in Section 544(a). However, the court, in a very hazy opinion, then proceeded to disclaim that notion. The court in Koch then relied on reasoning that was similarly adopted by the Fourth and Fifth Circuits. It examined underlying state law (Indiana and Illinois) and concluded that since those states did not expressly prohibit a corporation from maintaining an alter ego action, the cause of action must belong to the corporation and pass to the trustee as property of the estate.

Epling, supra note 104, at 196 (footnotes omitted).
111. 816 F.2d 1222 (8th Cir.), cert. denied, 404 U.S. 848 (1987).
112. Id. at 1224-28.
113. Id. at 1227-30.
114. This proposal was based on § 4-604(b)(2) of the Commission’s Proposed Bankruptcy Act of 1973:
The Trustee may, when in the best interest of the estate, enforce any claim which any class of creditors has against any person and if necessary for that purpose, the court may stay any other pending action on such claims. If the trustee brings an action on such a claim, he shall give notice to all creditors who could have brought an action on the claim if the trustee had not done so. Any judgment entered for or against the trustee on such claim shall be binding on all such creditors and any recovery by the trustee shall be for the benefit only of such creditors after the deduction of all expenses incurred by the trustee in effecting such recovery.115

115. See Epling, supra note 104, at 193-95.
this inaction determinative. The court declined to distinguish Caplin even though the claims in Caplin were claims that belonged to specific creditors, rather than claims that all creditors could assert.\textsuperscript{116}

A further roadblock to RICO fraudulent transfer claims are several cases which have indicated that the RICO claims of creditors are too speculative or are not ripe until the fraudulent transfer claims of the trustee are resolved. Only then will the extent of the injury be known. The Second Circuit addressed this issue in Banque de l'Amerique del Nord v. Rhoades\textsuperscript{117} and concluded that although RICO does not impose any special standing limitations on creditors, any RICO plaintiff must suffer injury in fact.\textsuperscript{118} Therefore, the overlap between the creditors' RICO claim and the trustee's fraudulent transfer claim "does not present a question of [the creditors'] standing to bring a civil RICO claim, but rather presents the question of which and how much in damages [the creditors'] can recover under that RICO claim."\textsuperscript{119} On the damages issue the court stated:

\begin{quote}
[S]hould the bankruptcy trustee ultimately recover all the fraudulently transferred assets, [the creditors'] injury could be significantly reduced; conversely should the assets never be recovered, or should the bankruptcy court order the claim abandoned, [the creditors'] injury would be much more severe.

Trebling and attorney's fees aside, congress intended the basic award under civil RICO to compensate the plaintiff for injury to "his property or business." 18 U.S.C. § 1964(c) (1984). As in other areas of the law, this compensation takes the form of awarding damages sufficient to place the plaintiff in the same financial position he would have occupied absent the illegal conduct.

Yet, at this time, it is impossible to determine the amount of damages that would be necessary to make plaintiff [creditors] whole, because it is not known whether some or all of the fraudulently transferred funds will be recovered by the [debtor] corporation.\textsuperscript{120}
\end{quote}

Although in Barnett the Seventh Circuit held that the trustee has standing to assert RICO claims, in dictum the court concurred with the Second Circuit's conclusion that the judgment creditors' damage claims were speculative and premature because "it remains to be seen whether they will be able to satisfy their claims from the bankruptcy estate."\textsuperscript{121}

\textsuperscript{116} Ozark Restaurant Equipment, 816 F.2d at 1227-29.

\textsuperscript{117} 859 F.2d 1096 (2d Cir. 1988), cert. denied, 490 U.S. 1007 (1989).

\textsuperscript{118} Id. at 1100 (citing Sedima v. Imrex Co., 473 U.S. 479 (1985)).

\textsuperscript{119} Id. at 1101.

\textsuperscript{120} Id. at 1106.

\textsuperscript{121} Barnett v. Stern, 909 F.2d 973, 977 n.4 (7th Cir. 1990). In L'Europeenne de Banque v. La Republica de Venezuela, 700 F. Supp. 114 (S.D.N.Y. 1989), the plaintiff, a
V. Time to File Suit

Section 546 of the Bankruptcy Code limits the time within which avoidance actions can be initiated to two years following the appointment of a trustee.122 Some courts and commentators have difficulty with this provision because they feel it is too open-ended in Chapter 11 cases, where the norm is to continue the debtor in possession and a trustee may never be appointed. In such cases the time to initiate an avoidance action does not expire until some indefinite time in the future when the case is closed or dismissed.123 Even the confirmation of a plan is irrelevant to the time period within which to commence an action. In Korvettes, Inc. v. Sanyo Electric, Inc. (In re Korvettes, Inc.)124 Judge Lifland became the first judge to try to correct this problem. Not satisfied with section 546(a), he simply rewrote it:

It is thus my view that the longer of confirmation or two years from the reorganization filing date should be the appropriate period for the bringing of preference actions for statute of limitations purposes. Stated differently, a debtor in possession should be able to bring preference actions until a reorganization case is confirmed, no matter how long that process naturally takes. If, however, a case is confirmed in less than two years, the debtor may bring these actions until the two-year period has elapsed, so long as it has provided in the confirmation documents that preference actions may be brought post-confirmation. A formulation crafted in the alternative is indeed proper as the statute of limitations under former Bankruptcy Act Section 11(e) was constructed in this manner. Pursuant to Act Section 11(e), a trustee could bring preference actions for the longer of two years from the date of the bankrupt’s adjudication in bankruptcy or any applicable federal or state statute of limitations, so long as that federal or state statute had not expired before the adjudication. A fortiori, the Chapter 11 debtor in possession should be able to bring preference

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corollary of banks, brought a RICO claim against third parties for looting the assets of a Venezuelan bank that had contracted with the consortium. Id. at 116. Citing Rhoades, the court held that the plaintiff’s RICO claim was not ripe because the Venezuelan bank was still in liquidation proceedings that could result in a reduction of the plaintiff’s damages. Id. at 118-19; see also Lincoln House, Inc. v. Dupre, 903 F.2d 845, 847-48 (1st Cir. 1990) (upholding the district court’s dismissal of a RICO fraudulent transfer claim filed during the pendency of plaintiff’s claim for breach of contract against defendant because the RICO injury was contingent upon plaintiff winning the contract claim); Wooten v. Loshbough, 738 F. Supp. 314, 316-17 (N.D. Ind. 1990) (holding that personal injury judgment creditor of corporation who sued third parties under RICO for looting corporate assets lacked standing because the injury to the judgment creditor was indirect and the amount of her damages too speculative), aff’d, 951 F.2d 768 (7th Cir. 1991).

123. Id. § 546 (a)(2) (1988).
actions for the longer of two years from the date of the filing of a Chapter 11 petition or entry of an order of confirmation.\textsuperscript{128}

The district court reversed Judge Lifland, however, holding that the statute was clear and that the court could not ignore it merely because the court disagreed with it.\textsuperscript{129} The case law, until about the middle of 1990, other than Judge Lifland’s brief misadventure, solidly supported the proposition that section 546(a) means what it says: The two-year statutory limitation begins to run when a trustee is appointed under one of the named sections; otherwise, avoidance actions can be brought at any time until the case is closed or dismissed. Unfortunately, in 1990 and 1991, four more courts jumped the tracks.\textsuperscript{130} Two of these were inspired by the Tenth Circuit’s decision in Zilkha Energy Co. \textit{v. Leighton},\textsuperscript{128} but the other acted before Zilkha.\textsuperscript{129}

By its terms, section 546(a)(1) does not apply to debtors in possession. The Tenth Circuit’s holding to the contrary is based upon section 1107(a) of the Code, which gives a debtor in possession all the rights and powers of a trustee subject to any limitations imposed upon a Chapter 11 trustee.\textsuperscript{130} Because section 546(a)(1) imposes a two-year limitation period upon Chapter 11 trustees, the court concluded that because of section 1107(a) this limitation also applies to debtors in possession. Hence, the court held that the two-year period begins to run from the date of the filing of the petition because that is the date the debtor in possession is "appointed."\textsuperscript{131}

It is well settled that "when the express language of a statute is clear, a court will not adopt a different construction absent clear legislative history contradicting the plain meaning of the words."\textsuperscript{132} The

\begin{footnotes}
\footnote{125. Id. at 222-23 (citation omitted).}
\footnote{128. 920 F.2d 1520 (10th Cir. 1990).}
\footnote{129. The \textit{Lill} decision is dated May 21, 1990, prior to the Tenth Circuit’s decision in \textit{Zilkha}, which is dated December 10, 1990.}
\footnote{130. 11 U.S.C. § 1107(a) (1988).}
\footnote{131. \textit{Zilkha}, 920 F.2d 1523-24.}
\footnote{132. United States \textit{v. Holroyd}, 732 F.2d 1122, 1125 (2d Cir. 1984); \textit{see United States v. Ron Pair Enters., Inc., 489 U.S. 235, 242 (1989); United States \textit{v. Oregon, 366 U.S. 643, 648 (1961); Ex Parte Collett, 337 U.S. 55, 61 (1949) (“This canon of construction has received consistent adherence in our decisions.”); Gemsco, Inc. \textit{v. Walling, 324 U.S. 244, 260 (1945); Helvering \textit{v. City Bank Farmers Trust Co., 296 U.S. 85, 89 (1935) (“We are not at liberty to construe language so plain as to need no construction, or to refer to}}
Zilkha opinion cited no legislative history supporting the result it reached. This omission was undoubtedly due to the total absence of any legislative history in the briefs and supplemental briefs of the parties to the court.\(^{133}\) If the court had examined the legislative history and the historical antecedents of sections 546(a) and 1107(a), it could not have concluded that Congress intended section 546(a)(1) to apply to debtors in possession.

The legislative history begins not with section 546 of the Bankruptcy Reform Act of 1978 but with section 77B, the corporate reorganization statute enacted in 1934.\(^{134}\) Section 77B(b)(10) provided for the tolling of all periods of time prescribed by the Bankruptcy Act and of all other statutes of limitations during the pendency of the reorganization.\(^{135}\) The Chandler Act amendments of 1938,\(^{136}\) which repealed section 77B and added Chapters X, XI, and XII, contained similar suspension provisions. For example, section 261 of Chapter X provided that “the running of all periods of time prescribed by this Act in respect to commission of acts of bankruptcy, the recovery of preferences, and the avoidance of liens and transfers shall be suspended while a proceeding under this chapter is pending and until it is finally dismissed.”\(^{137}\)

The Chandler Act Amendments of 1938 also added section 11e, which required a “receiver or trustee . . . within two years subsequent to the date of adjudication [to] institute proceedings . . . upon any claim against which the period of limitation fixed by Federal or State law had not expired at the time of the filing of the petition in bankruptcy.”\(^{138}\) In Herget v. Central National Bank & Trust Co.\(^{139}\) the Supreme Court applied section 11e to an action by a liquidating trustee to recover a preference under section 60 of the Act,\(^{140}\) and the statute

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Committee reports where there can be no doubt of the meaning of the words used.”); Caminetti v. United States, 242 U.S. 470, 485 (1917).

133. The Zilkha case was only marginally, if at all, an avoidance action. The claim asserted by the reorganized debtor was to recover mistaken royalty overpayments made to the defendants on oil and gas leases before the debtor filed bankruptcy. 920 F.2d at 1521-22. The reorganized debtor cast one of the claims as a strong arm claim, brought under § 544(a)(1), to avoid the fact that the state statute of limitations had run. Id. at 1522. Appellants’ and appellees’ briefs contained no reference to legislative history.

135. Id. § 77B(b)(10), 48 Stat. at 915.
137. Id. ch. X, § 261, 52 Stat. at 902. To the same effect, see § 391 (Chapter XI) and § 516 (Chapter XII) of the Chandler amendments. Id. ch. XI, § 391, 52 Stat. at 914; id. ch. XII, § 516, 52 Stat. at 928.
138. Id. ch. III, § 11e, 52 Stat. at 849.
139. 324 U.S. 4 (1945).
140. Id. at 9.
was later applied to a fraudulent conveyance as well.¹⁴¹ Later decisions made clear, however, that section 11e’s two-year time period was to be applied consistently with the tolling provisions of the reorganization chapters described above.

In Davis v. Security National Bank¹⁴² the trustee’s preference action would have been untimely under section 11e unless the time during the Chapter X case was excluded. In holding that the action was timely, the court rejected an argument very similar to the one that is the foundation for the Zilkha decision:

Appellee argues that the appellant trustee is barred because the Chapter X trustee might have proceeded to recover the alleged preferential payment. To be sure, the Chapter X trustee had all of the powers of a trustee in bankruptcy [but] there is nothing in the Act which even remotely suggests that the Chapter X trustee is required to exercise all of the powers of a general trustee in bankruptcy.¹⁴³

Similarly, the court in Liman v. Bank of Nova Scotia¹⁴⁴ held that section 11e did not bar a preference complaint filed nearly seven years after the original Chapter XI petition, but within two years of an order that terminated the attempted reorganization and directed that bankruptcy proceed.¹⁴⁵ As in Davis, the court rejected the argument that because the reorganization trustee could have recovered the preferential payment, the liquidating trustee should be barred:

The fact is the reorganization trustee did not (for reasons best known to that trustee) exercise his discretion to seek recovery of the alleged preferential payment during the pendency of the reorganization effort. The reorganization trustee may not have been aware of the possibility of any such action against defendant who had been paid in full by the Chase Manhattan Bank. As another leading text writer has said: "Such recovery . . . may be had during the Chapter X administration, but § 261 [11 U.S.C. § 661] recognizes the possibility that either no such action will be taken or the pertinent facts will not be discovered before the dismissal of the reorganization proceeding, and it accordingly suspends the running of the various periods of time involved."

One purpose of §§ 661 and 791 seems plain. They suspend the running of all statutes of limitations affecting claims provable under Chapters X and XI by the creditors of the debtor so as to allow for unfettered consideration by the creditors of any plan of reorganization or arrangement. The other purpose of §§ 661 and 791 seems equally obvious. They suspend the running of the time within which a trustee

¹⁴². 447 F.2d 1094 (9th Cir. 1971).
¹⁴³. Id. at 1097-98 (citations omitted).
¹⁴⁵. Id. at 63.
in bankruptcy must proceed to recover a preference (after the hypothetical date of adjudication set by §§ 778(a)(2) and 638) during the pendency of a Chapter XI or X proceeding so that the rights of creditors to an equal share of the estate in any ensuing bankruptcy proceeding may be protected.146

In summary, prior to the enactment of the 1978 Bankruptcy Reform Act, section 11e gave liquidating trustees two years within which to initiate preference and fraudulent conveyance actions. However, this period was tolled during the pendency of a reorganization case. This was true even though the trustee or debtor in possession had the power under Chapters X, XI, and XII to initiate preference and fraudulent conveyance actions. It was against this background that the Commission on the Bankruptcy Laws of the United States commenced its work in the early 1970s.

The Commission’s section 7-201(b) provided, as to the debtor, that “the debtor shall have all the rights and exercise all the powers of the trustee under subdivision (a) and under this chapter, subject to such limitations and conditions as the administrator or the court may prescribe.”147 As indicated in Note 2 to the Commission’s proposed section:

Subdivision (b), is derived from §§ 188, 342, and 444 of the [Bankruptcy] Act. . . . Until a trustee or receiver is appointed, the debtor has all the rights and powers of a trustee appointed under [the reorganization chapter]. These rights and powers are, however, subject to the control of the administrator and the court. Under prior reorganization law, section 188, 342, and 444, granted the debtor the title and vested the debtor with the rights, subject to the duties, and all the powers of a trustee “subject, however, at all times to the control of the judge and to such limitations, restrictions, terms, and conditions as the judge may from time to time prescribe.”148

The House and Senate versions of section 7-201(b) were enacted as section 1107(a) of the Bankruptcy Code. The relevant legislative history is found in the House and Senate Reports, which state:

This section places a debtor in possession in the shoes of a trustee in every way. The debtor is given the rights and powers of a chapter 11 trustee. He is required to perform the functions and duties of a chapter 11 trustee (except the investigative duties). He is also subject to any limitations on a chapter 11 trustee, and to such other limitations and conditions as the court prescribes . . . .149

146. Id. at 66 (citations omitted).
147. 1973 COMMISSION REPORT, supra note 16, at 68.
148. Id. at 236.
There is nothing in this language—other than the reference to the “limitations on a chapter 11 trustee”—to suggest that Congress intended in any way to impose a statute of limitations on preference and fraudulent conveyance actions commenced by debtors in cases in which trustees are not appointed.

The Commission also incorporated the extension provisions of section 11e of the Bankruptcy Act in its proposed section 4-102(a),\textsuperscript{150} which later became section 108. However, the Commission neglected to include, probably through oversight, the judicial construction given section 11e by \textit{Herget}. The Senate rectified this omission by adding a limitation on avoidance actions in subdivision (c) to its version of section 546, which, with changes not relevant here, ultimately became section 546(a)(1).\textsuperscript{151} The legislative history states simply: “Subsection (c) adds a statute of limitations to the use by the trustee of the avoiding powers. The limitation is two years after his appointment, or the time the case is closed or dismissed, whichever occurs later.”\textsuperscript{152}

Because section 103(b) makes section 546(a)(1) applicable to reorganization cases\textsuperscript{153} and because the tolling provisions of Chapters X, XI, and XII of the Bankruptcy Act were not carried over into Chapter 11 of the Code, the Code departs from prior reorganization law. It is clear that if a trustee is appointed, the two-year limitation period on preference and fraudulent conveyance actions in a reorganization begins to run when the trustee is appointed, and that such claims are barred when a case is closed or dismissed. Clearly Congress eliminated the tolling provisions as to the trustee. It concluded that the trustee must initiate suit within the two-year period, but that was the only change. It is equally clear that Congress did not intend to go further and eliminate the tolling provisions that have existed since the first corporate reorganization statute that allowed the debtor to remain in possession. Nor did Congress intend to overrule prior case law. The Supreme Court has repeatedly emphasized its reluctance “to accept arguments that would interpret the [Bankruptcy] Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history.”\textsuperscript{154}

\begin{itemize}
\item 150. 1973 \textit{COMMISSION REPORT, supra} note 16, at 68.
\end{itemize}
Clearly, section 1107(a) gives a debtor in possession the powers of a trustee. The issue is whether the time limitation in section 546(a)(1), which by its terms applies only to trustees, also applies to debtors in possession. Courts which have found that the time limitation does apply to debtors in possession have unilaterally instituted a dramatic reversal of prior reorganization law that can be explained only by a misinterpretation of section 1107(a) and the relevant legislative history.

Section 1107(a) was not created out of whole cloth in 1978. Similar language was used in the reorganization chapters of the Bankruptcy Act, and that language basically was carried over into Chapter 11. The analogous sections in these earlier statutes had nothing whatsoever to do with the time to sue. The only change in 1978 was to make the powers of the debtor in possession, which had been subject to limitations imposed by the court, subject to the limitations imposed under Chapter 11 as well.

The 1978 Code added additional references to "limitations," but it did not change the meaning of the word "limitations" as it was used in section 1107(a)'s predecessors. It was a limitation on the power of a trustee to sue, not a statute of limitations or a prescription of the time within which to sue. The time within which to sue was found in another section of the Bankruptcy Act—section 11e—and it was tolled in reorganization cases. Section 546(a)(1) operates the same way, with only one significant change: The time within which a trustee must sue runs even while the reorganization case is pending, but the change applies only to a trustee. The prior reorganization rule as to a debtor in possession remains the same; there simply is no time limitation running while the debtor in possession administers a Chapter 11 reorganization. Until 1990, no court had held otherwise.

Prior to 1990 courts held time and again that section 546(a)'s two-year limitation applied only to trustees appointed pursuant to one of the sections enumerated in the statute. This "prevailing view" was
summarized in *Collier on Bankruptcy* as follows:

Note that the two year limitation period runs from the appointment of a trustee under section 702, 1104, 1163, 1302, or 1202. Thus, if a debtor in possession is serving in a case under chapter 11 and no trustee has been appointed, the two year period arguably would not begin to run unless and until a trustee is appointed. The better view is that section 1107(a), which gives the debtor powers of a trustee and subjects the debtor in possession to the limitations placed on a trustee, does not equate service of the debtor in possession with the appointment of a trustee for the purposes of section 546(a).158

Moreover, section 546(a) escaped the Bankruptcy Amendments and Federal Judgeship Act of 1984 unchanged.159 At the time Congress was considering the 1984 amendments there were at least two reported decisions which held that section 546(a)(1) does not apply to debtors in possession.160 This is some evidence that the Zilkha construction does not square with congressional intent.161

In *Lill v. Bricker (In re Lill)*,162 however, the court, without any discussion or authority, reached the same conclusion that the Zilkha court did.163 And after Zilkha the courts in *Sparmal Enterprises, Inc. v. Moffit Realty Corp. (In re Sparmal Enterprises, Inc.)*164 and *Construction Management Services, Inc. v. Manufacturers Hanover Trust*

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Sales Corp. *(In re Alithochrome Corp.)*, 53 B.R. 906, 909 (Bankr. S.D.N.Y. 1985) ("Alithochrome properly argues that that two year statute of limitations does not apply to preference actions brought by a Chapter 11 debtor in possession.").


158. 4 *COLLIER ON BANKRUPTCY* ¶ 546.02, at 546-10 to -11 (Lawrence P. King et al. eds., 16th ed. 1991) (footnote omitted); see id. at 546-11 n.9 ("Section 546(a)(1) is inapplicable to debtors in possession; thus a debtor in possession may commence a suit to recover a preference more than two years after the filing of the petition.").


161. *See Korvettes, Inc. v. Sanyo Elec., Inc. (In re Korvettes, Inc.)*, 67 B.R. 730, 733 (S.D.N.Y. 1986); *Choice Vend, 49 B.R. at 721 ("It may be presumed Congress was aware of this interpretation and desired no change."); see also Air Transp. Ass'n of Am. v. Professional Air Traffic Controllers Org., 667 F.2d 316, 321 (2d Cir. 1981) ("[Courts] can presume that Congress is aware of settled judicial constructions of existing law, and that it intends to retain those remedies that it has left in place." (citation omitted)).


163. *Lill* was decided before Zilkha. Thus, the court had no authority and cited none; it relied on its own two sentence analysis of the interplay between § 546(a)(1) and § 1107(a). *Id.* at 546.

Co. (In re Coastal Group, Inc.) chose to ignore the "prevailing view" and follow Zilkha. The most recent pronouncements on the subject, however, considered all four decisions and rejected them. The Zilkha view has been rejected not only because of its inconsistency with the language of the statute and legislative history but for policy reasons that were well summarized by the district court in Korvettes:

As the authorities that have considered the question have recognized, this conclusion is well-grounded in policy. The respective duties of a debtor in possession and a trustee make application of the two year rule inappropriate to constrain a debtor in possession. While a debtor in possession continues the operation of the business, a trustee appointed pursuant to 11 U.S.C. § 704 is responsible for the expeditious liquidation of the estate in order to protect the interest of the creditors. While a trustee's tasks include pursuing preferential transfer claims in furtherance of liquidation of assets, a debtor in possession traditionally will not attack ancillary issues such as preferences until it has dealt with reorganization.

Section 546(a)(1) explicitly provides that trustees have two years from the date of their appointment to bring an action under sections 544 or 548 of the Code. Any contrary interpretation is flatly inconsistent with the language of the statute and with all prior case law interpreting it. If section 546 imposed a two-year limitation upon all claims, it could very easily and simply have said that "an action or proceeding under section 544 . . . may not be commenced after two years from the date of the filing of the petition." That, however, is not what section 546 says.

167. Korvettes, 67 B.R. at 733-34.
168. See, e.g., Edleman v. Gleeson (In re Silver Mill Frozen Foods, Inc.), 23 B.R. 179, 181 (Bankr. W.D. Mich. 1982) ("The statute is clear that the two year limitation runs from the date the trustee is appointed, not the date the case is filed."); 4 COLLIER ON BANKRUPTCY, supra note 158, at 546-11 ("If a trustee is appointed in a case under chapter 11 or in a case converted from chapter 11, he will have two years from the date of his appointment to commence actions pursuant to § 546(a). ")

https://scholarcommons.sc.edu/sclr/vol43/iss4/5
The court in Coastal Group distinguished cases in which trustees had been appointed from those in which no trustee had been appointed. The Zilkha court specifically declined to take a position on that issue but indicated that its conclusion might be different in the case of a subsequently appointed trustee. It did so, both by citing a case in which the court rejected the very argument and by acknowledging that the appointment of a trustee is "a distinguishable circumstance requiring a different analysis."

In Boatman v. E.J. Davis Co. (In re Choice Vend, Inc.), the case cited by the Zilkha court, a voluntary Chapter 11 case was filed on December 21, 1981. A trustee was appointed on February 7, 1983, and a section 547 suit was filed on September 26, 1984. The defendant argued that "the two-year period referred to in § 546(a)(1) starts when a voluntary petition is filed," and hence the trustee's suit was barred. The court flatly rejected the defendant's argument "as unsupported and contrary to the clear language of the statute." If the two year limitation began to run on the date the bankruptcy petition is filed, it would produce wildly and intolerably disparate results in fraudulent conveyance cases because the time available for suits by trustees would vary from one case to the next.

A Chapter 11 debtor normally is more interested in preserving relationships and thus has little incentive to pursue preference and fraudulent conveyance actions. This incentive is further lessened because "the debtor in possession and the debtor who made the preferential transfer being one and the same, there may be no inclination to

169. Coastal Group, 125 B.R. at 731-32.
170. Zilkha Energy Co. v. Leighton, 920 F.2d 1520, 1524 n.11 (10th Cir. 1990).
171. Id. (citing Boatman v. E.J. Davis Co. (In re Choice Vend, Inc.), 49 B.R. 719, 720 (Bankr. D. Conn. 1985)).
172. Id.
174. Id. at 720 & n.1.
175. Id. at 720.
176. Id.; accord One Mktg. Co. v. Addington & Associs. (In re One Mktg. Co.), 17 B.R. 738, 739-40 (Bankr. S.D. Tex. 1982) ("If the statute of limitations is allowed to run before the appointment of an independent trustee, this might harm other creditors.").

Without this approximate two-year period, a trustee who does not immediately determine what potential claims are available for the recovery of assets may forever be barred from asserting those claims if the statute of limitations expires early in the bankruptcy, or potentially before the trustee is even appointed. Such would contravene the broad powers Congress has granted to the trustee under §§ 544, 547 and 548 of the Code to recover property for the benefit of the estate.

seek a return of the preferential transfer.”177

Several courts have held that section 546(a) extends the time for bringing avoidance actions if the state statute of limitations has not yet run at the time the bankruptcy petition is filed.178 However, Judge Abramson held in Lynn v. NCNB Texas National Bank (In re Corland Corp.)179 that section 546 does not extend the running of the state statute of limitations. Judge Abramson’s decision was based, at least in part, on two concerns. First, he noted that the plaintiffs had not cited any cases in which a court had held that section 546(a) extends a state statute of limitations.180 Second, Judge Abramson was concerned that a contrary holding “would render the provisions of 11 U.S.C. § 108(a) meaningless at least in bankruptcy cases filed where trustees are appointed. In such instances, section 546(a) would always control regardless of whether or not the limitations period found in section 108 had expired.”181 In Mahoney, Trocki & Assoc., Inc. v. Kunzman (In re Mahoney, Trocki & Assoc., Inc.)182 the court answered the second concern by pointing out that section 108 does not apply at all because a fraudulent transfer action maintained under section 544(b) is “clearly the creation of the Bankruptcy Code,” and section “‘108(a) refers to pre-filing causes of action belonging to the debtor and not to a cause of action created by the Bankruptcy Code.’”183 Therefore, when the issue next came before him, Judge Abramson reversed himself and held that section 546(a) controls when the state statute has not run prior to the filing of the petition.184

In Pate v. Hunt (In re Hunt)185 Nelson Bunker Hunt and William Herbert Hunt filed Chapter 11 cases on September 21, 1988. Reorgani-

177. One Marketing, 17 B.R. at 739.
178. Dry Wall Supply, 111 B.R. at 936 (“[A]s long as the state law statute of limitations has not run before the debtor’s filing for bankruptcy, the trustee can bring a fraudulent conveyance action as long as he complies with the provisions of § 546(a).”); Mahoney, Trocki & Assoc., Inc. v. Kunzman (In re Mahoney, Trocki & Assoc., Inc.), 111 B.R. 914, 920 (Bankr. S.D. Cal. 1990) (“So long as the statute of limitations has not run at the filing of the petition, the trustee may then utilize the provisions of § 546(a).”); see In re Revco D.S., Inc., 118 B.R. 468, 498 (Bankr. N.D. Ohio 1990) (appendix) (“[T]he weight of authority supports the proposition that as long as the statute of limitations has not run as of the date of the filing of the petition, section 546(a) acts to extend the time to bring the cause of action.”).
180. Id. at 17.
181. Id. at 17-18.
183. Id. at 920 (quoting Andrew v. Coopersmith (In re Downtown Inv. Club III), 89 B.R. 59, 65 (Bankr. 9th Cir. 1988)).
zation plans were confirmed in the cases in December of 1989. Under the plans assets and causes of action were transferred to liquidating trusts. On June 11, 1991, the trustees of the liquidating trusts initiated adversary proceedings in the bankruptcy cases seeking to avoid transfers under sections 544 and 548 of the Bankruptcy Code and to recover the properties transferred or their value. The defendants included the debtors' relatives and "trustees of trusts created for the benefit of the Debtor's children and grandchildren," along with certain corporate, general partnership, and limited partnership entities in which the individual defendants or their trusts had ownership interests.

Motions to dismiss were urged by defendants who asserted that the claims were time barred by state statutes of limitations and section 546(a) of the Bankruptcy Code. The independent trustees had been appointed pursuant to the plans in January 1990, and the fraudulent transfer actions were filed in June 1991. Thus, more than two years had expired between the date of the filing of the bankruptcy cases and the filing of the fraudulent transfer actions, but only one year and six months had expired between the trustees' appointments and the filing of the fraudulent transfer actions. If section 546(a) controlled and the two-year period within which actions under sections 544 and 548 can be brought commenced running at the date of the filing of the Chapter 11 cases, the fraudulent transfer actions were time barred.

Because many millions of dollars worth of properties and cash had been transferred, this was a significant matter but not one of first impression before Judge Abramson. He had decided Mancuso v. Continental Bank National Ass'n (In re Topcor, Inc.) approximately two months earlier. In Topcor Judge Abramson held that section 108 of the Bankruptcy Code does not control the time within which a section 544(b) avoidance claim can be brought and that the time period in section 546(a) does not begin to run upon the filing of the petition but upon the appointment of a trustee.

186. Id. at 440-41.
187. Id. at 440.
189. Id. at 125-26.
190. Id. at 124. In support of his holding, Judge Abramson made the following observations:

Limitations periods are intended to apprise defendants of any adverse claims against them by preventing plaintiffs from sleeping on their rights to the detriment of the defendants. See Crown Cork & Seal Co. v. Parker, 462 U.S. 345, 352, 76 L. Ed. 2d 628, 103 S. Ct. 2392 (1983). The Court notes that this purpose is not unduly frustrated by giving the Trustee two years from the date of his appointment to bring any fraudulent transfer actions. The Court also notes that several compelling reasons support Congress' decision to provide trustees two years to commence any avoidance actions.
In *Hunt* Judge Abramson considered not only *Zilkha* but also its progeny, which at that time included *Sparmal Enterprises* and

The most evident reason for providing trustees two years to bring avoidance actions is to ensure that the trustee has ample time to investigate any potential claims and causes of action for the estate. In *re Dry Wall Supply, Inc.*, 111 B.R. at 936-37. In *Dry Wall Supply*, the Colorado District Court stated that, ""[w]ithout this two year period, a trustee who does not immediately determine what potential claims are available for the recovery of assets may forever be barred from asserting those claims if the statute of limitations expires early in the bankruptcy, or potentially before the trustee is even appointed."" *Id.* at 937. The opportunity to investigate potential claims is not the only consideration in allowing trustees an additional limitations period for filing such actions.

Another reason to provide trustees with a two year limitation period is the way many bankruptcy proceedings progress. Often, a debtor will file a bankruptcy petition under Chapter 11 of the Code, and the case will remain open for years before a Chapter 11 trustee is appointed or the case is converted to Chapter 7. In such instances, unless the court orders otherwise, the creditors of the estate are dependent upon the Debtor in Possession to bring any avoidance claims on their behalf. *Nebraska State Bank v. Jones*, 846 F.2d 477, 478 (8th Cir. 1988) (only trustees, and not creditors, have standing to bring § 544(b) avoidance actions); See also *In re Hansen*, 114 B.R. at 932.

The very nature of Chapter 11 proceedings demonstrates the problems with the *Zilkha* holding that the two year limitations period provided by § 546(a) begins to run from the date the bankruptcy petition is filed. In a Chapter 11 case, the Debtor in Possession is concerned primarily with rehabilitating the company by developing a confirmable plan of reorganization. The Debtor in Possession negotiates with the creditors of the estate regarding the treatment they will receive under the plan, and ultimately, it is the creditors who vote to accept or reject the plan. The Debtor in Possession may decide during this negotiation period to compromise, settle, or abandon any avoidance actions. Therefore, even though both a Debtor in Possession and a trustee have fiduciary responsibilities to the estate, the recovery of preferential transfers is more likely to occur with a trustee.

Furthermore, the Debtor in Possession has less incentive to bring an avoidance action, since the Debtor is the one who made the preferential transfer in the first place. *Perlstein v. Saltzstein (In re AOV Indus., Inc.)*, 62 B.R. 988, 974 (Bankr. D.C. 1986). Therefore, sound policy calls for providing trustees an additional two years from the date of appointment to bring any § 544(b) actions.

The Court also points out that its holding is in accord with the general policy of the Code to provide trustees broad avoidance powers to maximize the value of the estate for the benefit of all creditors. *See American Nat'l Bank of Austin v. MortgageAmerica Corp. (In re MortgageAmerica Corp.)*, 714 F.2d 1266, 1275 (5th Cir.1983). Furthermore, numerous courts have held that each trustee appointed under the enumerated provisions of § 546(a) has two years within which to commence avoidance actions. *Smith v. Moody (In re Moody)*, 77 B.R. 566, 673-74 (S.D.Tex.1987), *aff'd*, 862 F.2d 1194 (5th Cir.1987) (limitations period under § 546(a) runs anew with each successive trustee appointed).

*Id.* at 124-25 (footnote omitted).
Coastal Group. Judge Abramson concluded that the cases were decided wrongly and that "Congress made it perfectly clear that § 546(a)(1) applies only to trustees appointed under specifically enumerated sections of the Code."\textsuperscript{191}

\footnotesize

The decisions relied upon by the Defendants generally begin with a determination that § 546(a) is ambiguous, thereby allowing the courts to construe the statute. Then, the courts generally follow a two-part analysis. First, the courts equate a debtor-in-possession with a Chapter 11 trustee by citing § 1107(a) of the Code. In finding that § 546(a)(1) applies to debtors in possession, the Delaware bankruptcy court emphasized that the debtor-in-possession is subject to any limitations applicable to a Chapter 11 trustee. \textit{In re Coastal Group, Inc.}, 125 B.R. at 732.

Secondly, the courts address the issue of whether a debtor-in-possession is subject to the same two year statute of limitations as an appointed trustee. The Tenth Circuit stated:

We do not believe that Congress intended to limit actions filed by an appointed trustee to two years without making the same restriction apply to a debtor in possession who is the functional equivalent of an appointed trustee. Because of the virtual identity of function between a trustee and a debtor in possession, there would be no reason to create a different limitation period for the filing of actions by the two fiduciaries. Moreover, when the balance of § 546 is considered, it is even more apparent that Congress intended for the word "trustee" to apply to a debtor in possession, for every reference to actions brought by a trustee contained in § 546 obviously applies to actions brought by a debtor in possession. A contrary analysis would deprive § 546 of significance in the majority of recovery actions filed in Chapter 11 cases.

Consequently, we construe § 546(a)(1) to apply to actions filed by a debtor in possession, and we believe the period of limitation begins to run from the date of the filing of a petition for reorganization under chapter 11. We reach that conclusion because the debtor becomes a debtor in possession on that date.

Zilkha, 920 F.2d at 1524. Although it has been followed by a few courts, Zilkha is contrary to the majority of cases that have addressed § 546(a)(1). This Court declines to follow the Zilkha analysis for the reasons set out below.

(b) The Statute is Unambiguous

Initially, this Court finds the wording of § 546(a)(1) unambiguous. If it had intended for the word "trustee" to apply to a debtor-in-possession as the Tenth Circuit Court of Appeals believed, Congress could have made it clear by including the words "debtor-in-possession" or referring to the "date of the petition". [sic] Instead, Congress made it perfectly clear that § 546(a)(1) applies only to trustees appointed under specifically enumerated sections of the Code. Where the statute's language is unambiguous, the inquiry into the meaning of the statute should begin and end with its language, and the Court's sole function is to enforce it according to its terms. \textit{United States v. Ron Pair Enter., Inc.}, 489 U.S. 235, 241 (1989), \textit{citing Caminetti v. United States}, 242 U.S. 470, 485 (1917). This Court agrees with the district court in \textit{Korvettes, Inc. v. Sanyo Elec., Inc. (In re Korvettes, Inc.)}, 67 B.R. 730 (S.D.N.Y. 1986) that:
Also, Judge Abramson found that Zilkha was inconsistent with the Fifth Circuit's decision in MortgageAmerica Corp. v. American Federal Savings and Loan (In re MortgageAmerica Corp),[192] in which the court stated that "the limitations period under section 546(a) should commence consistent with the appointment of the trustee through a written order."[193]

Judge Abramson's opinion is particularly persuasive because of its observations about the distinction between a trustee and a debtor in possession, which of course goes to the heart of the matter.

This Court also disagrees with the Tenth Circuit Court of Appeals' view that § 546(a)(1) should apply to debtors in possession as well as trustees because of the "virtual identity of function between a trustee and a debtor-in-possession." Zilkha, 920 F.2d at 1524. Although many of the powers and duties of a trustee are granted to or imposed upon a debtor-in-possession, they are distinct entities, often operating under different agendas. A debtor-in-possession is concerned primarily with rehabilitating the company by developing a confirmable plan of reorganization. The debtor-in-possession negotiates with the creditors of the estate regarding the treatment they will receive under the plan, knowing that ultimately it is the creditors who vote to accept or reject the plan. The debtor-in-possession may decide during this negotiation period to compromise, settle, or abandon any avoidance actions, or may simply let potential claims lie until after a plan is confirmed.

A Chapter 11 trustee, however, is primarily interested in obtaining the maximum return possible for the estate's creditors. In order to achieve this result, a trustee generally will be more diligent in pursuing any possible avoidance actions. Even though both a debtor-in-possession and a trustee have fiduciary responsibilities to the estate, a trustee is more likely to pursue voidable transfers. Further-

[a]t the time Congress amended the Bankruptcy Code in 1984, several cases had interpreted subsection 546(a)(1)'s two year time bar as starting to run only after a trustee is appointed, and as inapplicable to debtors in possession. Congress' failure to amend subsection 546(a)(1) to include debtors in possession supports the view that that subsection does not apply to them. See Air Transport Association of America v. PATCO, 667 F.2d 316, 321 (2d Cir. 1981) (court can "presume that Congress is aware of settled judicial constructions of existing law ... and that it intends to retain those remedies that it has left in place"), cited in In re Choice Vend, supra, 49 B.R. at 721.

In re Korvettes, 67 B.R. at 733.
Id. at 446-47 (parallel citations omitted) (footnotes omitted).
192. 831 F.2d 97 (5th Cir. 1987) (per curiam).
193. Id. at 98; see also Chapman v. Cardell Cabinets, Inc. (In re Nash Phillips/ Copus-Houston, Inc.), 114 B.R. 466 (Bankr. W.D. Tex. 1990) (holding that for purposes of § 546 a trustee is appointed on the date the order approving the appointment is entered on the docket unless the order indicates a nunc pro tunc appointment).
more, while a trustee is specifically required to investigate the affairs of the debtor and file a statement of the results of such investigation, including any causes of action available to the estate, a debtor-in-possession is not required to perform such duties. Therefore, the Tenth Circuit's conclusion that a debtor-in-possession is the "functional equivalent" of an appointed trustee is theoretically correct, but not in sync with real life.

Furthermore, a debtor-in-possession has less incentive to bring an avoidance action, since the debtor is the one who made the questioned transfer in the first place. This rationale clearly applies in this case. It is doubtful that the Debtors in Possession would have any incentive to bring any of the claims alleged in the Complaints if the Debtors made the alleged transfers to their relatives and affiliates. Therefore, sound policy justifies Congress having provided trustees two years from the date of appointment to bring any avoidance actions, while not limiting all avoidance actions to two years from the petition date. This Court concludes that the Zilkha line of cases are incorrect in holding that the two year limitations period in § 546(a)(1) applies to debtors in possession.194

Turning to the applicability of the state statutes of limitations, Judge Abramson felt that such statutes were relevant only to the issue of whether the claim was time barred prior to bankruptcy. If it was not, then section 546(a) "supersedes the state statute of limitations" and controls "since it provides a specific time within which a § 544 claim can be brought."196 Moreover, Judge Abramson went on to hold that even those fraudulent transfer claims that would have been time barred prior to the filing of the bankruptcy cases were not subject to state statutes of limitations because state statutes of limitations do not run against the federal government.198 Because the United States had an allowable unsecured claim in Hunt and was in a position to set aside the transfers in question, the running of the statute of limitations under the UFCA was not a defense. The UFTA attempts to reverse this rule by providing that the expiration of the prescribed period "bars the right rather than the remedy on expiration of the statutory periods prescribed."197 Under section 544(b) of the Bankruptcy Code, however, the representative of creditors (the trustee or debtor in pos-

195. Id. at 450.
session) steps into the shoes of the United States of America and therefore is not bound by state statutes of limitations.198

Judge Abramson had previously ruled in *Lynn v. NCNB Texas National Bank, N.A. (In re Corland Corp.)*199 that the state statute of limitations controlled, but that section 108(a) of the Bankruptcy Code extended the state limitations period to at least two years after the filing of the bankruptcy case. Judge Abramson had expressly rejected the argument that section 546(a) controlled, concluding that section 546(a) "merely acts as an additional limitation period in respect of a trustee's ability to bring certain avoidance actions."200 However, in *Topcor* Judge Abramson backed off his holding in *Corland*, and at the time of *Hunt*, Judge Abramson was of the opinion that section 546(a) controlled the time limitations on avoidance actions brought under sec-

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198. The *Hunt* court stated:

Plaintiffs are asserting avoidance actions on behalf of the estate for the benefit of all creditors (including the IRS). See *American Nat'l. Bank of Austin v. MortgageAmerica Corp. (In re MortgageAmerica Corp.*), 714 F.2d 1266, 1275 (5th Cir. 1983) (the trustee in an avoidance action acts for the benefit of all creditors). It is well settled that the United States is not bound by state statutes of limitation. *United States v. Summerlin*, 310 U.S. 414 (1940). Furthermore, the government utilizes state law in an action to set aside a fraudulent conveyance. Therefore, the question is whether a trustee, or similar party such as Plaintiffs as representatives of the estates in this proceeding, who acquires the status of an actual unsecured creditor for purposes of § 544(b) is immune from state statutes of limitations when utilizing the status of the United States as an unsecured creditor under § 544(b).

Section 544(b) of the Code creates a power of avoidance in a trustee to avoid any transfer that an actual unsecured creditor of the debtor as of the date of the petition could have avoided. For purposes of the dismissal motions, the Court must accept as true Plaintiffs' allegations in the Complaints that the United States of America was an actual unsecured creditor of the Debtors as of the petition date. *Kaiser Aluminum*, 677 F.2d at 1050. Furthermore, § 544(b) permits a trustee to "stand in the shoes of a creditor" to assert any state law claims that a creditor may have. *Kupetz v. Wolf*, 845 F.2d 842, 845 (9th Cir.1988). Therefore, this Court concludes that Plaintiffs are not barred by the applicable state statutes of limitations since they acquired the status of the United States pursuant to § 544(b) of the Code. *United States v. Gleneagles Investment Co., Inc.*, 565 F.Supp. 556, 583 (M.D. Pa. 1983), aff'd sub. nom., *United States v. Tabor Court Realty Corp.*, 803 F.2d 1288 (3d Cir. 1986), cert. denied, *McClellan Realty Co. v. United States*, 483 U.S. 1005 (1987) (trustee's claim asserted on behalf of the United States was not barred by the state statute of limitations since the trustee was empowered to assert the rights of the United States as a creditor). Finally, if a transfer is avoidable at all by any creditor, it is avoidable in full for all creditors. *Abramson v. Boedeker*, 379 F.2d 741, 748 n.16 (5th Cir. 1967), cert. denied, 389 U.S. 1006 (1967).


200. Id. at 17.
tions 544(a), 548, and 550(a). Thus, he concluded that the language of section 108(a) controls only those causes of action owned by the debtor prior to bankruptcy. Section 108(a) provides that if the applicable state law sets a time “within which the debtor may commence an action, and such period has not expired before” the bankruptcy petition is filed, the trustee can bring the action before the latter of the end of the applicable state law time period or two years after the case is filed. Clearly, section 108(a) relates only to actions that may be initiated by the debtor. Fraudulent transfer actions under state law or section 548 of the Bankruptcy Code, which only the trustee can bring, are not actions that could be commenced by the debtor prior to the filing of the bankruptcy case. Thus, Judge Abramson recognized the error he had made in Corland, corrected his position in Topcor, and reemphasized the correct rule in Hunt.

VI. Bankruptcy Code Section 546(e): A Safe Harbor for Leveraged Buyouts?

It has been less than ten years since the Gleneagles case lit up the corporate firmament. In the six years that have passed since the Third Circuit’s affirmance of most of the district court’s rulings in its three Gleneagles decisions, much has taken place in the world of fraudulent transfers and LBOs. Although some courts have been reluctant to apply fraudulent transfer law to LBOs, it is now well accepted that the UFCA, UFTA, and section 548 of the Bankruptcy Code apply to LBOs. In adversary proceedings that arose in the Kai-

ser Steel Chapter 11 case, however, the Tenth Circuit recently closed the door to recovery in bankruptcy from stockholders who are stockbrokers or represented by stockbrokers.

The Kaiser Steel litigation involved an LBO merger approved in January, 1984, and effective in February, 1984. On the effective date of the merger Kaiser's stockholders were required to tender shares to Kaiser's disbursing agent in exchange for cash and preferred stock of the new company. Because Kaiser was listed on the New York Stock Exchange, most of its stock was in the possession of a clearing agency that received the cash and preferred stock from the disbursing agent. The clearing agency in turn transferred the cash and preferred stock to the accounts of its participants, which included brokers and other financial intermediaries. Eventually the beneficial owners of the Kaiser stock received the LBO proceeds.


208. The Tenth Circuit capsulized the process as follows:

Most of the common stock was in the possession of Depository Trust Com-
Kaiser filed a Chapter 11 case in 1987 and initiated an adversary proceeding seeking to recover $162 million in cash and preferred stock distributed under the LBO plan. The initial lawsuit named as defendants the “street name shareholders” of the Kaiser stock. A second action was filed after discovery from the initial broker defendants disclosed the names of the beneficial owners of Kaiser stock. The second action asserted the same fraudulent conveyance theories but joined as defendants a large number of the beneficial owners. The district court withdrew the reference of the adversary proceedings and consolidated the cases with other adversary proceedings related to Kaiser’s LBO.

Before the withdrawal of the reference, several brokers moved for summary judgment on the basis that as to shares not beneficially owned, the brokers were “mere conduits” rather than initial transferees and were therefore not liable under section 550(a)(1) of the Bankruptcy Code. Also, the brokers interjected section 546(e), which was enacted shortly before the Kaiser LBO. Their defense was that section 546(e) exempts settlement payments from recovery in section 544(b) and section 548(a)(2) actions. Therefore, as a matter of law the brokers were not liable because the benefits of the LBO were received by the brokers as settlement payments.

Bankruptcy Judge Matheson denied the brokers’ motion for summary judgment but was reversed by the district court on the grounds that the brokers were mere conduits and section 546(e) precluded recovery. The Tenth Circuit affirmed but solely on the ground that the distributions to the stockbrokers were settlement payments exempt

pany (“DTC”), a securities clearing agency acting as depository. After the merger, DTC tendered the [Kaiser stock] certificates to Bank of America [the disbursing agent] and received the payments of LBO consideration [the cash and preferred stock]. DTC then transferred these payments to the accounts of its participants, including brokers and other financial intermediaries. These intermediaries, in turn, either disbursed the payments to their customers who were the beneficial owners of Kaiser Steel stock or retained the payments if they themselves were the beneficial owners. Some shares were exchanged through securities clearing agencies other than DTC, and since DTC stopped handling trades of Kaiser Steel shares prior to the effective date of the LBO, some financial intermediaries and beneficial owners were required to tender their shares directly to Bank of America.

Kaiser II, 952 F.2d at 1235-36.


210. See id. at 521-22.


212. See Kaiser Steel Resources, 110 B.R. at 519-21, 521-22.
from recovery as fraudulent conveyances under section 546(e).\(^{213}\)

In *Kaiser II* the Tenth Circuit dealt with the remaining issue, whether section 546(e), which provides that "the trustee may not avoid a transfer that is a . . . settlement payment . . . made by or to a . . . stockbroker, financial institution, or securities clearing agency,"\(^{214}\) protected the beneficial owners of the Kaiser stock. The opinion summarized Kaiser's arguments on appeal as follows:

First, it maintains that these payments are not "settlement payments." Second, it insists that even if the payments are settlement payments, payments made "by or to" one of the enumerated entities are protected under section 546(e) *only* to the extent the recipient is a participant in the clearance and settlement system (i.e., a stockbroker, financial institution, clearing agency, or some other participant). Settlement payments received by an "equity security holder," according to Kaiser, are not protected.\(^{215}\)

The court observed that "settlement payment" encompasses all types of payments in light of the broad definition under section 741(8) and that it is necessary to interpret settlement payment "as it is plainly understood within the securities industry."\(^{216}\) The court recognized that two opportunities for a settlement arise in a typical securities trade and that these settlements involve two corresponding sets of guarantees. The first, the so-called "street-side settlement," occurs between brokers and the clearing agency, and the second, the "customer-side settlement . . . occurs between the broker and its customer."\(^{217}\)

Kaiser argued that the term "settlement payment" in section 546(e) only applies to routine purchases and sales of securities, and not to an "extraordinary securities transaction" like an LBO.\(^{218}\) However, the Tenth Circuit observed that neither section 546(e) nor section 741(8) is limited on its face to routine purchases and sales of securities.

\( ^{213} \) Kaiser *I*, 913 F.2d 846 (10th Cir. 1990). This holding did not determine whether the ultimate recipients of the LBO proceeds, the beneficial owners of the Kaiser stock, would have to disgorge the proceeds. That issue was resolved by the Tenth Circuit approximately four months later in *Kaiser II*. In *Kaiser I* the Tenth Circuit did not reach the issue because it held that brokers acting on behalf of third parties were protected by § 546(e). The *Kaiser II* court noted that as a result of *Kaiser I*, "Kaiser . . . abandoned all claims against the appellants [brokers] in this case insofar as they acted in conduit/financial intermediary capacities. Therefore, all appellants remaining before us are shareholders or brokers that beneficially owned the Kaiser Steel shares tendered in connection with the LBO." *Kaiser II*, 952 F.2d at 1236.


\( ^{215} \) *Kaiser II*, 952 F.2d at 1236-37.

\( ^{216} \) *Id.* at 1237 (citing McCarthy v. Bronson, 111 S. Ct. 1737, 1740 (1991); Shell Oil Co. v. Iowa Dept' of Revenue, 488 U.S. 19, 25 (1988)).

\( ^{217} \) *Id.* at 1237-38.

\( ^{218} \) *Id.* at 1239.
The court apparently believed that the term “settlement payment” is broad enough to include payments received in transactions other than routine purchases and sales of securities. The court relied primarily on the fact that section 362(b)(6) excepts from the automatic stay a setoff by a . . . stockbroker . . . of any mutual debt and claim under or in connection with . . . securities contracts, as defined in section 741(7) . . . that constitutes the setoff of a claim against the debtor for a margin payment . . . or settlement payment . . . arising out of . . . securities contracts against cash, securities, or other property held by or due from such . . . stockbroker . . . to margin, guarantee, secure, or settle . . . securities contracts.\(^{219}\)

The court reasoned that if Congress had intended what Kaiser argued, Congress would have used the same language in section 546(e) that it used in section 362(b)(6).\(^{220}\) However, the settlement payment in section 546(e) is narrower than the “settlement payment . . . arising out of . . . securities contracts” in section 362(b)(6) because the language in section 362(b)(6) indicates that Congress intended to expand the settlement payment exception from the stay to include loans of securities in addition to purchases and sales of securities. Therefore, if any conclusion can be drawn from the use of the phrase “arising out of . . . securities contracts” in section 362(b)(6), it is that a “settlement payment” alone, which is what Section 546(e) addresses, does not include payments that arise from loans of securities. Thus, the Kaiser II court improperly adopted a broad definition of settlement payment for purposes of section 546(e).\(^{221}\)

Also, the court concluded that an LBO is a securities transaction.

While the leveraged buy out may not be a “routine” securities trade, at least as viewed by Kaiser, we cannot deny what in substance took place here. The LBO was a securities transaction, varying only in form from the various other ways in which a shareholder’s equity interest can be sold. The former Kaiser Steel shareholders effectively sold their equity interests to the new investors in exchange for money and a continuing stake in the new entity as preferred shareholders. In settlement of that transaction, the Kaiser Steel shareholders tendered their shares and received payment. These payments were “settlement payments.”\(^{222}\)


\(^{220}\) Kaiser II, 952 F.2d at 1239 (citing Gozlone-Peretz v. United States, 111 S. Ct. 840, 846-847 (1991) (stating that if particular language is used in one section of a statute but omitted in another, Congress is presumed to have acted “intentionally and purposely in the disparate inclusion or exclusion” ) (quoting Russello v. United States, 464 U.S. 16, 23 (1983))).

\(^{221}\) See id. at 1239-40.

\(^{222}\) Id. (citing Kaiser I, 913 F.2d 846, 850 (10th Cir. 1990)).
A student commentator, in a recent article analyzing *Kaiser I*, disagreed with the Tenth Circuit's interpretation of the relevant Bankruptcy Code provisions and proposed a "framework . . . to serve as a guide as to the scope and applicability of sections 546(e) and 741(8)."\(^{223}\)

Settlement implies some sort of connection to an exchange or trade, and because Congress considered section 546(e) within the context of insulating the workings of the securities markets (the trading or exchanging of securities), that should also be the contextual framework in which the scope of "settlement payment" is examined.

In determining, then, whether or not a particular flow of funds between a customer and a broker is indeed a "settlement payment" for purposes of section 546(e), the proper question should be: "Is this generally the type of transfer whose protection is necessary to the smooth working of the securities markets?" Where LBO payments to public shareholders are concerned, the answer to that question is "No." The inviolability of payments to shareholders is simply not basic to the operation of the clearance and settlement systems. Those systems will be only incidentally affected, if at all, if former shareholders are required to return payments they received in an LBO. Neither the system of guarantees nor the solvency of participants in the chain is threatened by a legal order in which payments to the shareholders by their brokers are subject to recovery by a trustee in bankruptcy. Thus, while the flows of funds to and between financial intermediaries in the clearance and settlement chain must be protected in order to insure the stability of those systems, funds flowing from the intermediaries to the shareholders do not require protection, and section 546(e) should therefore not apply.\(^{224}\)

The Tenth Circuit found comfort in the "symmetry of treatment" that its decision accorded to those stockholders who sold their stock before the LBO tender date and those who tendered their shares pursuant to the LBO plan.\(^{225}\)

[T]hose shareholders who tendered their shares one day after the LBO and received the LBO consideration are treated just the same under the Code as shareholders who sold their shares in the market one day prior to the LBO and received a settlement payment reflecting the market value of the LBO consideration. Neither type of investor will be forced to disgorge . . . \(^{226}\)

However, these are entirely different situations. The consideration in

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224. *Id.* at 66-67.
225. *Kaiser II*, 952 F.2d at 1240 n.10.
226. *Id.* at 1240.
the LBO flowed from the target corporation (the debtor) and constitutes a fraudulent transfer because there was no reasonable equivalent value returned to the target corporation. The securities traded one day before the LBO are entirely different. Someone in the market place purchased these securities and paid with consideration that flowed from that purchaser, not the target of the LBO. There is no basis at all for setting aside these pre-LBO transactions, and little more than the court's desire for symmetry can explain the court's reasoning. No public policy is served by excepting from avoidance profits enjoyed by those who waited on a further rise in the market just to reach a symmetry with those who took their profits early.

Nonetheless, the court believed that a "symmetry of treatment" was justified not only by "the plain notion of 'settlement' " but also by Congress's decision to promote "finality," "‘speed and certainty in resolving complex financial transactions.'"227 Furthermore, it found its earlier Kaiser I decision consistent with section 546(e)'s goal of protecting " 'the nation's financial markets from the instability caused by the reversal of settled securities transactions.'"228 These concerns seem beside the point, however, because Kaiser limited its prayer for recovery to the beneficial owners. A recovery from the beneficial owners would have had no impact on the nation's financial markets, other than perhaps to dampen the enthusiasm for LBOs, nor would it have slowed down any complex financial transactions. Nonetheless, the court somehow concluded that its holding was "supported by Congress' policy of promoting the health of the clearance and settlement system, which by all accounts is one of the fundamental aims of the 546(e) exemption."229

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229. Kaiser II, 952 F.2d at 1240 n.10. The SEC's brief in Kaiser I asserted this improbable threat to the securities market: If brokerage customers are forced to return LBO payments they might not pay the brokers, who will fail and cause a ripple effect that would cripple the market. Brief of the Securities and Exchange Commission at 30-35, Kaiser I, 913 F.2d 846 (10th Cir. 1990). One commentator analyzed the SEC's brief as follows:

Recognizing the improbability of the above scenario, the SEC then goes on to make two other arguments in favor of § 546(e)'s applicability. The first is a plain meaning argument: The section says what it says and should therefore be applied. Contrary to the SEC's assertion, the section is far from clear, and because of the import of a decision either way in this area, it seems judicially irresponsible not to consider the role the provision was intended to play in the
Also, the Tenth Circuit held that those brokers who were beneficial owners of Kaiser shares were exempted from avoidance recovery by the "clear" reference to stockbrokers in section 546(e).230 Kaiser argued that these brokers acted as equity security holders, who are not exempted from avoidance recovery in section 546(e), and not as stockbrokers because a stockbroker is not a stockbroker unless it acts for a customer.231 The court held, however, that the plain language of the statute protects all stockbrokers regardless of the nature of their ownership. "Certainly, we cannot say that the clear application is absurd, given the fact that disruption in the securities industry—an inevitable result if leveraged buy outs can freely be unwound years after they occurred—is also a harm the statute was designed to avoid."232 In conclusion, the court stated that it was "not convinced [its holding] leaves the trustee remediless by way of a suit for damages, or some similar device, against specific individuals or institutions for unlawful acts."233

context of the securities markets. "It says what it says" should not carry a great deal of weight at all, much less the day.

The second argument the SEC presents is that to find shareholders liable in general would undermine investor confidence in the market and increase market volatility. Therefore, § 546(e) should be read to insulate shareholders. This argument essentially asserts that investors should not be required to examine the validity of the transactions they effect in the marketplace. In today's world, a rule which promotes shareholder passivity and ignorance does not seem to further any compelling purpose.

Capital formation and investor confidence should not be significantly affected by a legal environment that requires an investor to look before he or she leaps. Shareholders reap the benefits of these buyouts in the form of large premiums when they approve the transaction. They should similarly be exposed to some of the risks. If fairness dictates that some shareholders should be exempted, then a way should be found to do that. But bending a relatively specific bankruptcy provision to serve as a blanket exemption in the name of investor confidence is both unwarranted and ill-advised.

Garfinkel, supra note 207, at 67 n.69.

231. Id. at 1240 n.11. Section 101(54) defines a stockbroker as a "person . . . with respect to which there is a customer . . . and . . . that is engaged in the business of effectuating transactions in securities." 11 U.S.C. § 101(54)(A)-(B) (Supp. II 1990) (emphasis added).
233. Id. As explained in Kaiser's petition for certiorari, while the Kaiser decisions may not have left Kaiser remediless, they did have a substantial adverse impact.

The increased cost and risk and reduction of monies available to fund retiree trusts is clear and immediate for Kaiser's creditors and retirees. The Tenth Circuit concluded its decision with the point that Kaiser could still sue specific individuals or institutions for unlawful acts. (App. A at 26A). Kaiser has done so, pursuing and settling various claims, including one with the officers and directors who held a $25 million insurance policy that decreased with each dollar spent by defense counsel, for $17 million. The retiree medical
In determining whether stockbrokers *qua* stockbrokers were liable for LBO payments, the Tenth Circuit in *Kaiser I* determined that the phrase "settlement payment" included the receipt of proceeds from an LBO. In *Kaiser II* the question was not whether the payments could be recovered from the stockbrokers *qua* stockbrokers, but whether the payments could be recovered from the beneficial owners of Kaiser stock, who in some cases were brokers. Kaiser took the position that

[section 546(e) of the Bankruptcy Code, far from literally and unambiguously precluding collection from beneficial shareowners . . . does not preclude that collection at all. Equity security holders, defined in Bankruptcy Code § 101(16), are not among the parties enumerated in § 546(e) to be exempt from fraudulent conveyance recovery. Stockbrokers themselves are not within the scope of the statute when they are also equity security holders.]

In its Brief the SEC conceded that Congress did not intend to create a safe harbor for LBOs by acknowledging that the "by or to" language in section 546(e) was discussed only "in the context of payments between brokers and payments between brokers and clearing agencies." The SEC also recognized that "protecting individual shareholders would not necessarily further the exact purpose that led to the enactment of Section 546(e)" and that "the hearings focused upon the system of guarantees through which the clearance and settlement process operates."

In the Congressional hearings on the 1982 amendment to section 546(e), Commissioner Bevis Longstreth testified for the Securities and Exchange Commission. He described the pending amendments as "technical, clarifying, and minor substantive amendments to the new

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trust has already exhausted all the net litigation proceeds it has received to date, on benefits payments costing about $400,000 a month. Kaiser is still pursuing claims against accountants and an investment banker, but recognizes that comparative negligence statutes and judgment reduction requirements of the directors and officers' settlement may well reduce any collection from them. Kaiser has claims against the Jacobs Group, including a $14 million "greenmail" claim; $33 million of its claims against the Jacobs Group are for monies distributed for their shares, however.


236. Id. at 15-16.

Bankruptcy Code." He stated that "[i]n brief, the Commission's position is that the preference, fraudulent transfer and stay provisions can be interpreted to apply in harmful and costly ways to customary methods of operation essential to the securities industry." One of the problems he noted was the fact that there were express provisions that protected the commodities industry, but none that protected the securities industry. Commissioner Longstreth was concerned that this omission would give rise to an unfortunate inference that no protection was intended for the securities industry.

The Commission was particularly concerned that the preference, fraudulent transfer, and automatic stay provisions could have an adverse impact on the national clearance and settlement system. The Commission's view was that the Bankruptcy Code created three problems. First, the elimination of the reasonable cause to believe requirement from the preference provisions increased the number of securities transactions subject to preference avoidance. The solution was to apply the commodities exemption, then in section 764(c), to the securities industry as well as the commodities industry.

The second problem noted by the Commission was a fraudulent conveyance problem,

which is a problem closely analogous to the one arising under Section 547 and exists under Section 548 of the code related to fraudulent transfers. Section 548 establishes another class of transfers by the debtor which, in order to achieve equity among creditors, can be avoided by the trustee. These include, among others, transfers of any property of the debtor made within 1 year before the bankruptcy where the debtor received less than "a reasonably equivalent value" in exchange and was then insolvent or thereby became insolvent. Unfortunately, however, section 548(d)(2)(B) provides that a "commodity broker . . . that receives a margin payment . . . takes for value."

Once again, this language by emphasizing that a commodities margin payment is not subject to the trustee's avoiding powers, creates the inference that a functionally identical securities margin payment is subject to avoidance as a fraudulent transfer.


239. Id. at 239.

240. To extend the protections afforded the commodities industry to the securities industry, Congress repealed § 764(c) in 1982. Act of July 27, 1982, Pub. L. No. 97-222, § 17(c), 96 Stat. 240. Congress then added what is now § 546(e) to the Code and changed the definitions in § 741 to include securities margin and settlement payments. Id. §§ 4, 6, 96 Stat. at 236, 237.

241. Hearings, supra note 238, at 240. Jack Nelson, President of National Securities Clearing Corporation, stated that "the new uncertainty regarding fraudulent transfers
The solution suggested and enacted was to extend the special treatment accorded commodities margin payments to securities margin and settlement payments.\textsuperscript{242}

A third problem was created by the automatic stay.

[The stay] would force a clearing agency or broker to obtain explicit judicial permission to close out the open securities positions of an insolvent broker or customer. Once a broker or customer is insolvent, the clearing agency—to take one example—will receive no further mark-to-market or clearance fund payments, even if the market continues to move against the insolvent broker's net securities position.

At this point, the clearing agency can limit its loss exposure by closing out that net position. The automatic stay would prevent such a step until court permission could be obtained, by which time mounting losses may have rendered the agency itself insolvent, or at least resulted in further losses.

The proposed amendments would extend and clarify section 362(b)(6) and other related provisions to make it clear that, in general, neither securities nor commodities brokers and clearing agencies can be stayed from exercising their rights to apply margin payments to close out open positions of brokers and customers.\textsuperscript{243}

In response to Congressman Butler's question as to whether there was a need for an amendment, Commissioner Longstreth said:

I think the answer—part answer—is that in the hashing out that


\textsuperscript{243} Hearings, supra note 238, at 241. In its prepared statement, id. at 242-62, the Securities and Exchange Commission made its concerns about the automatic stay perfectly clear:

I should add parenthetically that while one or even a few days' price movement may not seem like problems of unacceptable magnitude, in times of market volatility substantial sums can be involved. Thus, in the case of major brokerage firms, losses resulting from net securities positions could run to millions of dollars on any single day. If such losses are suffered by a clearing agency and, due to the operation of the automatic stay, are dramatically increased and must be absorbed by the solvent participants in the system, they could result in a chain reaction of insolvencies and chaos in the securities markets.

\textit{Id.} at 258 (footnote omitted).
led to the code, the problems to which I have alluded were recognized as problems to the commodities industry and solutions to these problems are embedded in the code, but another industry closely linked and very similar, if not indistinguishable in this area, was left out. That would be bad enough without the negative inference, but you have got the negative inference that is a powerful one, given a code that is painfully detailed and carefully built word upon word, so that inferences can easily be drawn, negative or positive, by omissions.\textsuperscript{244}

In \textit{Kaiser I} the court concluded that the 1982 amendment to section 546(e) expanded the market protection “beyond the ordinary course of business to include margin and settlement payments to and from brokers, clearing organizations, and financial institutions.”\textsuperscript{245} Prior to the 1982 amendments, the predecessor of subsection (e), section 764(c) of the Bankruptcy Reform Act of 1978,\textsuperscript{246} protected only “the ordinary course of business in the [commodities] market.”\textsuperscript{247} Kaiser argued that the court in \textit{Kaiser I} was incorrect in concluding that Congress intended to extend market protections beyond the ordinary course of business.

The “expansion” took the form of allowing, for the first time, the prompt liquidation of an insolvent’s securities and commodities contracts, unfettered by any stay, to minimize losses if the market were to move sharply in the wrong direction. 11 U.S.C. §§ 555, 556. The other provisions only “clarified” the existing Code protections, and gave the same protections to participants in the securities market. H.R. Rep. No. 97-420, 97th Cong., 2d Sess. 2 (1982), \textit{reprinted in} 1982 U.S. Code Cong. & Admin. News 583-87. (“The new § 546(e)) reiterates the provisions of current § 764(c). The new section also encom-

\textsuperscript{244} \textit{Id.} at 264-65. Theodore H. Focht, General Counsel for the Securities Investor Protection Corporation, concurred that there was an ambiguity that needed clarification. The proposed amendment to section 546 of the Bankruptcy Code would prevent a trustee from avoiding a transfer which is a deposit made by or to a commodities broker, forward contract merchant, stockbroker, or securities clearing agency.

The word “deposit” is undefined. It is, in my view, too ambiguous a word and might be used to defeat a trustee’s attempt to recover a preferential transfer that should be recovered.

The committee report, I believe, could clarify this matter by making it clear that a preferential payment which is neither a margin, mark-to-market or settlement payment, nor a deposit to a clearing fund should continue to be recoverable by a trustee as it is under existing law.

\textit{Id.} at 285.

\textsuperscript{245} \textit{Kaiser I}, 913 F.2d 846, 849 (10th Cir. 1990).
passes both stockbrokers and securities clearing agencies."). Thus, the same ordinary course of business protections were extended from the commodities industry to the securities industry, but the protections themselves were not expanded beyond ordinary course of business transactions.248

Kaiser asserted that there was no evidence reflected anywhere that the 1982 amendments were intended to include transactions like leveraged buyouts, mergers, and dividend payments within the protection of section 546(e). In the absence of any manifest congressional intention to include such payments, Kaiser argued that the statute should not be interpreted to apply beyond the situations mentioned in the legislative history.248


249. The Court does not judicially legislate by interpreting settlement payment only in the context defined by the industry in its publications and testimony to Congress. Rather, it judicially legislates when it interprets beyond Congress' intent, as evidenced by the information Congress considered when enacting the law, into unchartered and unconsidered depths.

The Supreme Court has repeatedly concluded that statutes should not be interpreted to cover situations unmentioned in the legislative history. In Schreiber v. Burlington Northern, Inc., 472 U.S. 1 (1985), for example, the petitioner argued that the proscription of "manipulative acts or practices, in connection with any tender offer" in Section 14(e) of the Securities Exchange Act covered fully disclosed acts which manipulated the price of the takeover target's stock. The Court said, "[n]owhere in the legislative history is there the slightest suggestion that § 14(e) serves any purpose other than disclosure, or that the term 'manipulative' should be read as an invitation to the courts to oversee the substantive fairness of tender offers; the quality of any offer is a matter for the marketplace." Id. at 11-12. The Court refused to broaden the scope of the statute beyond the context evidenced in the legislative history to an unconsidered context.

Similarly, in United States v. American Trucking Associations, 310 U.S. 534 (1940), the Court refused to give the ICC the power to regulate the qualifications and hours of service of employees, other than those employees concerned with the safety of operations. It said, "We are especially hesitant to conclude that Congress intended to grant the Commission other than the customary power to secure safety in view of the absence in the legislative history of the Act of any discussion of the desirability of giving the Commission broad and unusual powers over all employees." Id. at 546-47. See also Heppner v. Alyeska Pipeline Service Co., 665 F.2d 868 (9th Cir. 1981), where the court held that personal injury actions unrelated to the special environmental risks created by the trans-Alaskan pipeline were not within the scope of the Trans-Alaska Pipeline Authorization Act. The Court said that "[a]n explicit denial in the legislative history of the distant possibilities included within [the statutory language's] sweep is not required. Instead we need only see if the purpose of the Act, as revealed by the legislative history, confirms that the language
In Kaiser I the court recognized that “Kaiser’s position that section 546(e) was only intended to insulate from avoidance routine securities transactions is not without merit.”250 The court did not, however, respond to Kaiser’s position that the statute should not be broadened beyond the intent manifested in the legislative history, except to state that “we will not interpret the term ‘settlement payment’ so narrowly as to exclude the exchange of stock for consideration in an LBO.”251

Also in Kaiser II, Kaiser argued that in order to be exempt from preference avoidance section 546(e) settlement payments had to be made by or to the enumerated entities. The enumerated entities include “a commodity broker, forward contract merchant, stockbroker, financial institution, or securities clearing agency,”252 but do not include an “equity security holder.”253

Congress addressed and intended to protect only the brokers and clearing agencies who stand behind the obligations of an insolvent customer or broker to make settlement payments. The broker on behalf of the customer and the clearing agency on behalf of the broker interpose themselves between the customers wishing to buy and sell securities. The counterpart of a bankrupt customer, the beneficial holder of the security sold to or brought from the bankrupt customer, is likely unidentifiable. The clearing agencies net out stock positions and cash in their broker members’ accounts each day. On the date when a bankrupt’s broker settled his sale of a particular stock, the broker could well have had no change in the number of that company’s shares in its account at the clearing agency, or a decrease. It could have had no change or a decrease in its cash account as well, should not be read too broadly.” 665 F.2d at 873.

Of the many transactions in which publicly traded companies and their street name and beneficial shareholders can engage, Congress only addressed securities contracts, those that were open and those that had been settled when a brokerage company or its customer filed bankruptcy, in the Bankruptcy Code provisions bearing to any degree on this case. The “ripple effect” of a customer or broker insolvency on the financial stability of clearing agencies and other brokers applies only in the “securities contract” context. Only with securities contracts do the clearing agencies and brokers guarantee consumption. A corporate merger payment like Kaiser’s is not within the scope of risks Congress intended to protect. The Court does not judicially legislate by restricting statutory language to the context Congress addressed.

Id. at 11-13 (footnote omitted).


due to other transactions. Collection from customer counterparts to trades, if they could somehow be identified, was never contemplated because the brokers and clearing agencies were the true trading partners.254

 Furthermore, because a stockbroker by definition must be acting for a customer,255 section 546(e) clearly cannot insulate a payment to a stockbroker in its capacity as an equity security holder.256

 The Tenth Circuit responded that “the statute is clear. The statute exempts payments made ‘by or to’ a stockbroker, financial institution, or clearing agency. Again, unless there is some reason to believe the clear application is absurd or otherwise unreasonable, we can leave our inquiry at that.”257 However, this did not answer Kaiser’s assertion that the Code definition of stockbroker requires a transaction in securities done on behalf of a customer.258

254. Id. at 14-15.
255. 11 U.S.C. § 101(54) (Supp. II 1990) (“[S]tockbroker means person . . . with respect to which there is a customer . . . .”).
256. For the relevant legislative history, see Hearings supra note 238.
257. Kaiser II, 952 F.2d at 1240 (quoting 11 U.S.C. § 546(e) (Supp. II 1990)). The Bankruptcy Code sponsor’s statements about the reason for including payments “by” as well as “to” the enumerated parties, the insertion of the words “by or,” and the deletion of the phrase “made by a clearing organization” indicate that the Code’s sponsors intended to bring these payments under § 764(c).

Mr. MATHIAS. “Am I correct in my understanding of the Senator’s [Mr. DeConcini’s] statement that the intent of section 764 and section 548(d)(2) is to provide that margin payments and settlement payments previously made by a bankrupt to a commodity broker, forward contract merchant and by or to a clearing organization are nonavoidable transfers by the bankrupt’s trustee?”

MR. DECONCINI. “Yes.”

124 CONG. REC. 34018 (1978) (emphasis added).
258. The opinion did address the issue further in a footnote:

It is difficult to imagine, for instance, how Congress could recognize that a settlement payment may be made by a stockbroker to its customer (whether that customer is bankrupt or not), see Appellant’s Opening Brief at 16 (citing reference in legislative history to “settlement payment owed to a customer”), and not realize that section 546(e), which on its face protects settlement payments by a stockbroker, is likely to be read by a court to protect settlement payments by a stockbroker to its customer.

Further, Kaiser’s claim that § 546(e) does not protect brokers trading on their own account is clearly wrong. Kaiser argues that such brokers are “equity security holders” and not “stockbrokers.” It notes as well that “stockbrokers” must have “customers.” 11 U.S.C. § 101(54)(A). However, the definition of “stockbroker” was intentionally fashioned to include dealers who “effect[] transactions in securities . . . with members of the general public, from or for such person’s own account,” 11 U.S.C. § 101(54)(B) (emphasis added), and “customer,” as used in the Code is a term of art, broadly defined in § 741(2) to “include anybody that interacts with the [broker] in a capacity that concerns securities transactions.” S.Rep. No. 989, 95th Cong., 2d Sess. 100 (1978), re-
On the key issue of whether a settlement payment, which is not defined in the Code, includes consideration paid to shareholders for their stock in connection with a LBO, the court concluded that it did. The court unequivocally stated that “we must interpret the term ‘settlement payment’ as it is plainly understood within the securities industry.” But the court did not do so!

“Settlement” is a word with meaning “in the securities trade”; it is not all-encompassing. Rather, in the numerous industry publications cited by the Tenth Circuit, “settlement” is defined as the completion of a securities transaction, which in turn is defined as a “trade”. Neither the Bankruptcy Code provision nor a single industry publication which any of the parties has unearthed applies the word “settlement” to one-time mandatory redemptions or cash mergers where corporate assets are distributed to shareholders, rather than a market trade where shares and money are exchanged between buyers and sellers. Moreover, the understanding of settlement payment “in the securities trade” is evidenced by Kaiser’s uncontroverted affidavit from a securities industry expert, stating that the “mandatory redemption of Kaiser common stock as part of the leveraged buyout was not a ‘settlement payment’ as that term is commonly used in the se-


Kaiser II, 952 F.2d at 1240 n.11.

259. Section 546(e) refers to § 741(8) for the meaning of settlement payment. However, as Kaiser pointed out in its brief in Kaiser II, this is a nondefinition.

As Gertrude Stein might say, “a settlement payment is a settlement payment is a settlement payment.” But litigation is settled, debts are settled, trades are settled, and settlement payments are made. When a brokerage customer is delinquent on amounts due to a broker, and enters into a settlement agreement to pay monthly installments before or after litigation, are the payments to the broker settlement payments exempt from preference or fraudulent conveyance attack? Are payments pursuant to a pre-bankruptcy workout agreement to a bank, a “financial institution,” settlement payments which are likewise insulated? What if the debt arises out of the financing of a stock purchase? See In re Edelsberg, 101 B.R. 386, 389 (Bankr. S.D. Fla. 1989) (garnishment on debt for stock purchases not settlement payment). The Third Circuit said the definition of settlement payments is “extremely broad,” but breadth does not stretch to infinity. There are hybrids of Gertrude Stein’s roses; there are hybrids of settlement payments. When the term is used in a statute, it must be limited to the context Congress addressed. That context was simply and only “securities contracts,” trades guaranteed by brokers and clearing agencies.


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ties trade."

VII. THE FDIC’S FRAUDULENT TRANSFER ACT UNDER F.I.R.R.E.A.

As a legislative expression of outrage at the frauds perpetrated by the participants in the activities that precipitated the dramatic decline of the savings and loan industry, Congress has enacted a special fraudulent transfer law for the benefit of the victims of that decline. Sometimes identified as part of the Crime Control Act of 1990, subparagraph (17) of section 1821(d) of Title 12 authorizes the Federal Deposit Insurance Corporation, or another appointee of the Comptroller of the Currency or the Director of the Office of Thrift Supervision, to act as a conservator or receiver for any insured depository institution in avoiding a fraudulent transfer made or obligation incurred by an "institution-affiliated party" or a debtor of the institution. Sec-


262. Congressman Charles E. Schumer, sponsor of the law, gave this brief account of relevant history:

Since a year ago last August, when the [Financial Institutions Reform, Recovery, and Enforcement Act of 1989] became effective, the losses from failed financial institutions have ballooned. Reports of criminal activity and grossly excessive behavior that led to the dramatic decline of the savings and loan industry have proliferated. Title XXV responds to the public outcry to put to justice those who defrauded the savings and loan industry by providing Federal regulating agencies, Federal prosecutors, and law enforcement agencies with additional tools to combat fraud and abuse affecting financial institutions.

Subtitle B of the legislation, which is aimed at protecting assets from wrongful disposition, expands the authority of the Attorney General, conservators, receivers or liquidating agents and Federal banking agencies to enjoin the dissipation of assets wrongfully obtained.

Subtitle B further expands the power of conservators, receivers or liquidating agents to void fraudulent transfers . . .


264. 12 U.S.C. § 1821(d)(17) (Supp. II 1990). The statute provides as follows: (A) In general

The Corporation, as conservator or receiver for any insured depository institution, and any conservator appointed by the Comptroller of the Currency or the Director of the Office of Thrift Supervision may avoid a transfer of any interest of an institution-affiliated party, or any person who the Corporation or conservator determines is a debtor of the institution, in property, or any obli-
tion 1821(d)(17) contains an extraordinary and questionable grant of superiority for the rights it creates over "any rights of a trustee or any other party (other than any party which is a Federal agency) under Title 11." The statute is not well drafted and presents several troublesome issues apart from those involving its relationship to the Bankruptcy Code and other legislation dealing with fraudulent transfers.

First, the legislation contains its own statute of limitations; it applies only to transfers and obligations incurred within five years of the date the FDIC or other agency as conservator or receiver is appointed. It has been held, however, that section 1821(d)(17) applies retroactively to transfers made before its enactment. A transfer or

gation incurred by such party or person, that was made within 5 years of the date on which the Corporation or conservator was appointed conservator or receiver if such party or person voluntarily or involuntarily made such transfer or incurred such liability with the intent to hinder, delay, or defraud the insured depository institution, the Corporation or other conservator, or any other appropriate Federal banking agency.

(B) Right of recovery

To the extent a transfer is avoided under subparagraph (A), the Corporation or any conservator described in such subparagraph may recover, for the benefit of the insured depository institution, the property transferred, or, if a court so orders, the value of such property (at the time of such transfer) from-

(i) the initial transferee of such transfer or the institution-affiliated party or person for whose benefit such transfer was made; or

(ii) any immediate or mediate transferee of any such initial transferee.

(C) Rights of transferee or obligee

The Corporation or any conservator described in subparagraph (A) may not recover under subparagraph (B) from-

(i) any transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith; or

(ii) any immediate or mediate good faith transferee of such transferee.

(D) Rights under this paragraph

The rights under this paragraph of the Corporation and any conservator described in subparagraph (A) shall be superior to any rights of a trustee or any other party (other than any party which is a Federal agency) under Title 11.

Id.

265. Id. § 1821(d)(17)(D).

266. Id. § 1821(d)(17)(A).

267. FDIC v. Yemelos, 778 F. Supp. 329 (E.D. La. 1991). In Yemelos the court noted that the Supreme Court has not resolved tensions between two lines of decisions dealing with the retroactive application of statutes but, relying principally on Bradley v. School Board, 416 U.S. 696 (1974), the court decided in favor of retroactivity because, frankly, it yields the result which the Court finds to be the just, logical, and proper decision in this instance, and because the Court believes that Congress, in enacting the statute, intended that the statute be applied retroactively to enable the FDIC to protect its solvency so that it is available to pro-
obligation must be made or incurred "with the intent to hinder, delay, or defraud the insured depository institution" in order to be voidable. The absence of any language or legislative history suggesting that Congress intended to render voidable a constructively fraudulent transfer or obligation of the kind described in section 548(a)(2) of the Bankruptcy Code, sections 4(a)(2) and 5 of the UFTA and sections 4, 5, and 6 of the UFCA predictably has generated dispute about whether such a transfer or obligation is vulnerable to avoidance under section 1821(d)(17).

The dispute has arisen in at least four reported cases. The most explicit consideration of this issue appears in In re Colonial Realty Co., 134 B.R. 1017 (Bankr. D. Conn. 1991), aff'd, Civ. No. 3:91-200X, 1991 WL 288833 (D. Conn. Dec. 30, 1991), in which the court read the statute as not applicable to constructively fraudulent transfers. Id. at 1022. Thus, the court suggested, the statute "excludes the most commonly brought fraudulent conveyance actions." Id. The bankruptcy court's decision upholding the applicability of the automatic stay to the FDIC's § 1821(d)(17) action against a Chapter 7 debtor was affirmed by the district court on appeal, without reference to the standard applicable in avoiding transfers under the statute. Colonial Realty, 1991 WL 288833 at *9.

In FDIC v. Cafritz, 762 F. Supp. 1503 (D.D.C. 1991), the court ruled that the FDIC had made a sufficient showing to justify the issuance of a temporary restraining order and the appointment of a trustee pending a determination on the merits. Id. at 1510. The court found that the FDIC had made a prima facie case of actual fraud under § 1821(d)(17) without deciding whether state or federal law applies under the statute and rejected the defendants' argument that only direct, as distinguished from circumstantial, evidence could be considered by the court in determining whether a fraudulent conveyance had occurred. Id. at 1506-07.

In Resolution Trust Corp. v. Cruce, 783 F. Supp. 1309 (D. Kan. 1992), the court followed Cafritz in sustaining the issuance of a preliminary injunction. Id. at 1313-14. Without ruling on whether state law governs the voidability of challenged transfers under § 1821(d)(17), the court examined the transactions under Kansas law and found that evidence of three badges of fraud—insolvency of the transferor, lack of consideration "for the most part" for the transfers, and an insider relationship with the transferor—was "enough indices of fraud . . . even under Kansas Law, to present fair grounds for litigation." Id.

In FDIC v. Owen, Civ. No. 5:91-00389, 1991 WL 173325 (D. Conn. Sept. 3, 1991), the court sustained the issuance of a preliminary injunction and the seizure of vehicles because the FDIC had shown that while in default on several loans, the debtor conveyed collateral to his relatives, and his testimony in regard to these transactions lacked credibility. Id. at *14-*19.
Second, the statute does not indicate when an unperfected or undiscovered transfer or obligation is deemed to occur for the purpose of computing the period of limitations.273 By explicitly conferring superiority on the rights created by the statute over the rights of a trustee or any other party under Title 11, however, section 1821(d) appears to leave the claims of individual creditors under nonbankruptcy law intact. The same is true of the bankruptcy trustee’s power under section 544(b) of the Bankruptcy Code. Such creditors or the trustee thus would be able to avoid unperfected or undiscovered transfers or obligations under state law or the Bankruptcy Code. The argument in favor of recognizing the continued validity of individual creditors’ rights is particularly strong in cases concerning transfers and obligations that are not voidable by the conservator or receiver under section 1841(d)—i.e., cases in which the transfer or obligation is only constructively fraudulent and cases involving transfers or obligations that occurred prior to the commencement of the five year period of limitations prescribed in section 1821(d)(17)(A).

Another problem with section 1841(d) is that it does not specify how the proceeds of any recovery from a transferee are to be distributed. Thus, employees, suppliers, tort claimants, and other creditors of the depositary institution, some of whom may have contributed substantially to the value of the property fraudulently transferred, may or may not be entitled to share in the recovered proceeds, although their equities may be at least as strong as the beneficiaries of the recovery based on the statute.

In the recent case of Board of Governors of the Federal Reserve System of the United States v. MCorp Financial, Inc.,274 the Supreme Court displayed a troubling insensitivity to the need for a balancing approach when the policies of the bankruptcy laws and the protection of creditors’ interests conflict with the exigencies of administrative regulation under the banking laws and related statutes. The Court held that the automatic stay does not preclude the Board of Governors from continuing ongoing administrative proceedings against a bank holding company in Chapter 11.275 Nevertheless, the Court was careful to point out that the administrative proceedings in question had not yet eventuated in any order affecting the bankruptcy court’s control of the debtor’s property and that “if and when judicial proceedings are commenced to enforce such an order, then it may well be proper for the Bankruptcy Court to exercise its concurrent jurisdiction under 28

275. Id. at 463-64.
U.S.C. § 1334(b).”

In In re Colonial Realty Co. a Connecticut bankruptcy court did not hesitate to invoke its concurrent jurisdiction over a section 1821(d)(17) fraudulent transfer action brought by the FDIC in the United States District Court for the Southern District of Florida. The FDIC argued that the automatic stay does not apply to proceedings instituted by the FDIC under § 1821(d)(17) and that it should not be bound by the stay or any ruling of the bankruptcy court based on the stay. The bankruptcy court disagreed and entered an injunction against the continuation of the action by the FDIC. The district court affirmed in the following unequivocal language:

Inasmuch as Congress has not explicitly stated that the FDIC is exempt from the automatic stay and there is no other authority for such an exception, I simply cannot accept the position of the FDIC so that it may, without prior bankruptcy court approval, decide that any action it wishes to bring to recover fraudulent conveyances complies with 18 U.S.C. section 1821(d)(17). Were the FDIC allowed to circumvent the automatic stay for such purposes, certainly every bankruptcy case involving a debtor to an insolvent depository institution in receivership—a very large number of cases—would degenerate into chaos, as the FDIC and other creditors compete and race for assets around the world and as the trustee seeks to intervene, as suggested by the FDIC, in every action it believes the FDIC should be prevented from continuing.

We have no evidence that Congress intended any such irrational and destructive result or that it intended to remove the process of

276. Id. at 464.
278. Id. at 1020-21.
279. Id. at 1019-20.
280. Id. at 1025. The bankruptcy court pointed out that although § 1821(d)(17)(D) grants the FDIC rights superior to those of the bankruptcy trustee, this grant does not immunize the FDIC from application of the automatic stay. A secured creditor likewise enjoys superiority to the rights of the trustee but remains subject to the stay. Moreover, “[t]he automatic stay provisions do not constitute a ‘right’ of a trustee, but a congressionally-mandated restraint that springs into existence upon the filing of a bankruptcy case.” Id. at 1021. General Counsel for the FDIC and RTC announced that § 1821(d)(17) “was added to ensure that the special powers given to a conservator/receiver of a failed financial institution and FDIC/RTC corporate may not be utilized by a bankruptcy trustee under 11 U.S.C. section 544(b), and to provide that the claims of a conservator/receiver and/or FDIC/RTC corporate are superior to the claims of a bankruptcy trustee.” Alfred J.T. Byrne, Basic Issues Affecting the FDIC and the RTC in Bankruptcy Cases, 65th Annual Meeting of the National Conference of Bankruptcy Judges 7-39, 7-42 (1992).
recovering assets from the administrative oversight of the bankruptcy courts.\textsuperscript{282}

VIII. CONCLUSION

The UFCA, UFTA, and the Bankruptcy Code have all assimilated the treatment of fraudulent obligations to the treatment of fraudulent transfers. When property that has been fraudulently transferred is no longer recoverable, the transferee has been subjected to an obligation to pay for its value, typically measured as of the time of the transfer. If the transfer is avoided and the property is recovered, the Bankruptcy Code contains implications that the transferee has a claim for the value of the property disgorged. The courts generally have declined to allow a claim on behalf of a transferee who is found guilty of intentional fraud, but there is authority to the contrary. Good faith transferees or obligees are accorded a lien against the fraudulently transferred property to the extent they gave value for the property. Equitably subordinating the claim of a fraudulent transferee pursuant to section 510(c) of the Bankruptcy Code has been recognized as appropriate in a number of recent cases. Although equitable subordination may be useful in fashioning relief in particular circumstances, it probably has limited utility as a remedy against fraudulent transferees and obligees.

It is sometimes difficult to determine who is a transferee in a fraudulent transaction when the defendant argues that it was merely a conduit. In \textit{Bonded Financial Services, Inc. v. European American Bank},\textsuperscript{283} Judge Easterbrook required that a defendant have "dominion over the money or other asset, the right to put the money to one's own purposes," in order to be a transferee.\textsuperscript{284} The \textit{Kaiser Steel} cases, however, complicated the definition of transferee. The bankruptcy court held that stockbrokers who had received funds from the debtor in redemption of customer stock are liable as transferees because they act as agents for undisclosed principals.\textsuperscript{285} The district court reversed, however, holding that agency principles do not apply.\textsuperscript{286} The Tenth Circuit affirmed on the basis that section 546(e) of the Code precludes

\textsuperscript{282} \textit{Id.} at *6-*7.
\textsuperscript{283} \textit{838} F.2d 890 (7th Cir. 1988).
\textsuperscript{284} \textit{Id.} at 893.
\textsuperscript{286} \textit{Kaiser Steel Resources}, 110 B.R. at 522-23.
any recovery from stockbrokers. The Tenth Circuit did not reach the correctness of the district court’s ruling in favor of the stockbrokers grounded on a lack of contractual relationship between the stockbrokers and the corporate debtor.

The law of fraudulent transfers allows recovery from transferees of property or its value when the property has been transferred to defeat creditors’ rights. Professor Glenn’s treatise, *Fraudulent Conveyances and Preferences*, has been influential in deterring the recognition of any liability in tort for aiding and abetting a fraudulent transfer. Nonetheless, a judicial willingness to impose liability on those who aid and abet fraudulent transfers is emerging. Such liability has not been predicated on the law of fraudulent conveyances but on implications derived from the law governing fiduciary relationships and from recently enacted statutes, including the Bankruptcy Code and the RICO Act. Courts have no difficulty finding that the bankruptcy trustee has standing to assert RICO claims if the debtor is an entity. However, individual debtors are another matter because they are *in pari delicto*. *Barnett v. Stern* recognized that the trustee in bankruptcy has standing to represent all creditors in proceedings under the Act against persons involved in prepetition fraudulent transfers. In distinguishing *Caplin v. Marine Midland Grace Trust Co.*, the court relied on cases that allowed the trustee to pursue alter-ego causes of action. However, RICO’s effectiveness has been limited by several cases which have indicated that RICO claims brought by creditors are too speculative or are not ripe until the fraudulent transfer claims of the trustee are resolved.

Section 546(a) of the Bankruptcy Code requires trustees to bring actions to avoid fraudulent transfers within two years of their appointment or before the closing or dismissal of the case. The debtor in possession appears not to be subject to a time limitation as long as the case is pending. With the exception of Bankruptcy Judge Lifland’s opinion in *Korvettes, Inc. v. Sanyo Electric (In re Korvettes, Inc.)*, the courts applied the statute as it was written until 1990, when four courts, including the Tenth Circuit in *Zilkha Energy Co. v. Leigh-

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288. See supra notes 3-4 and accompanying text.
289. 93 B.R. 962 (N.D. Ill. 1988), rev’d on other grounds, 909 F.2d 973 (7th Cir. 1990).
292. See supra notes 117-21 and accompanying text.
rewrote the statute and subjected debtors in possession to the
two-year statute of limitations. Under pre-Code law a liquidating
trustee was given two years within which to bring avoidance actions, but
the statute of limitations was tolled during the pendency of a reorgani-
zation case. The tolling provisions of the Bankruptcy Act applicable in
reorganization cases were not incorporated into the Bankruptcy Code,
but there is no evidence that Congress intended to deny the benefit of
tolling to debtors in possession. In view of the duties and incentives
operating when a debtor is retained in possession, the Zilkha interpre-
tation of section 546(a) is seriously objectionable on policy grounds.

It was held in the Gleneagles case that state statutes of limitations on
fraudulent transfer actions are not operative against the fed-
eral government. According to the prevailing view, if the applicable
state period of limitations has not expired when a debtor files bank-
ruptcy, section 546(a) extends the limitations period. A potential con-
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section 546(e). It is unfortunate that the court refused to consider the legislative history of the statute in construing the undefined term "settlement payment."

Congress added section 1821(d)(17) to Title 12 as a special fraudulent transfer law for the FDIC and other conservators of insured depository institutions who pursue property and its proceeds fraudulently disposed of by those responsible for the "dramatic decline of the savings and loan industry." The statute grants superiority for the rights it creates over the trustee's rights under the Bankruptcy Code. Section 1821(d)(17) is not well drafted, however, and appears not to reach constructively fraudulent transfers. It has a five-year statute of limitations but has been construed to have a retroactive application. The District Court of Connecticut in In re Colonial Realty Co. held that the statute does not preclude applicability of the automatic stay and upheld an injunction issued by the bankruptcy court against the FDIC's pursuit of its new remedy, notwithstanding its statutory superiority.

302. Id. at *6-*7.