

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re:

CASE NO. 01-21082

RENITA L. LOPEZ,

Debtors.

DECISION & ORDER

KENNETH W. GORDON, as Trustee,

Plaintiffs,

V.

AP #02-2164

DONALD MATTICE,

Defendants.

BACKGROUND

On March 28, 2001, Renita L. Lopez, formerly Renita Mattice, (the "Debtor") filed a petition initiating a Chapter 7 case. On the Schedules and Statements required to be filed by Section 521 and Rule 1007, the Debtor indicated that she had \$26,596.00 of unsecured debt.

On May 3, 2002, the Debtor's Chapter 7 Trustee commenced an Adversary Proceeding against her former spouse, Donald Mattice ("Mattice") which alleged that: (1) the Debtor transferred her interest in 6 Stal-Mar Circle, Rochester, New York ("Stal-Mar Circle") to Mattice in connection with their divorce proceeding and in accordance with a July 2000 Separation Agreement (the "Separation Agreement"); (2) at the time of the transfer the

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Debtor's interest had a fair market value of \$14,858.91, representing one-half of the \$96,900.00 fair market value of the property less \$67,182.18 due on the first mortgage; and (3) the Debtor did not receive "fair consideration" in exchange for the transfer of her interest to Mattice, so the transfer was an avoidable fraudulent conveyance under Article 10 of the New York Debtor and Creditor Law (the "DCL") and Section 544 of the Bankruptcy Code.

On July 31, 2002, Mattice interposed an Answer to the Trustee's Complaint which: (1) generally denied the allegations of the Complaint as to the transfer being an avoidable fraudulent conveyance; (2) asserted that at the time of the transfer the fair market value of Stal-Mar Circle was no more than \$88,000.00; and (3) asserted that Mattice had provided fair consideration for the transfer pursuant to the Separation Agreement in that he: (a) assumed certain joint marital debt; (b) transferred other property to the Debtor; and (c) accepted the transfer in part as satisfaction of antecedent debt owed to him by the Debtor.

On March 17, 2003, after several pretrial conferences were conducted by the Court and the parties attempted to settle the Adversary Proceeding, the Trustee filed a Motion for Summary Judgment along with a Memorandum of Law (collectively, the "Motion

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for Summary Judgment"). The Motion asserted that:¹ (1) the parties now agreed that the fair market value of Stal-Mar Circle at the time the Debtor transferred her interest to Mattice was \$88,000.00, so that the value of her interest should be found to have been \$10,408.91; (2) Mattice assumed sole responsibility for the payment of two joint credit card accounts with aggregate balances of \$11,764.80 (the "Assumed Debt") at the time of the execution of the Separation Agreement; (3) the Assumed Debt had not been fully paid by Mattice at the time of the filing of the Debtor's bankruptcy petition; and (4) the unfulfilled promise by Mattice to satisfy the Debtor's liability on the Assumed Debt did not constitute fair consideration under the DCL because: (a) under Section 272(a) of the DCL, fair consideration requires that the transferee act in good faith and either convey property or discharge an antecedent debt in exchange for the transfer, and the property conveyed or antecedent debt discharged must be a fair equivalent value; and (b) the agreement by Mattice to be solely

¹ Mattice alleged that his waiver of a potential enhanced earnings award was additional consideration. The evidence indicated that although the Debtor had enrolled in college in the Fall of 1997, it was not until May 2002, almost two years after the August 2, 2000 Judgment of Divorce, that she received her Bachelor of Science degree. At the pretrial conferences and trial calendar calls the Court indicated that, absent the Trustee providing appropriate precedent, it did not believe there would have been any basis for a New York State matrimonial court to grant an enhanced earnings award based upon those facts, so that Mattice's waiver of any right to such an award did not provide an element of fair consideration.

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responsible for the Assumed Debt did not constitute a conveyance of property or the satisfaction of an antecedent debt.

On April 21, 2003, Mattice interposed Opposition to the Motion for Summary Judgment which included a Crossmotion for Summary Judgment (collectively, the "Crossmotion for Summary Judgment"), which asserted that: (1) in determining the fair market value of Stal-Mar Circle for purposes of a DCL analysis of fair consideration, the Court should deduct a hypothetical seven percent cost of sale, so that the value of the Debtor's transferred interest should be found to have been \$7,328.91; (2) as stated in the Separation Agreement, Mattice provided fair consideration for the transfer of the Debtor's interest in Stal-Mar Circle in that he: (a) forgave a \$1,300.00 loan due him from the Debtor; (b) paid \$1,000.00 to the Debtor's attorney for her attorney's fees; (c) promised to be solely responsible for and indemnify the Debtor in connection with the Assumed Debt; (d) agreed to be solely responsible for a \$1,200.00 joint debt for the purchase of a furnace for Stal-Mar Circle (the "Furnace Debt"); and (e) conveyed an automobile to the Debtor with a value of \$1,370.00; (3) Mattice's promise to be solely responsible for and indemnify the Debtor in connection with the Assumed Debt had a value of one-half of the Assumed Debt or \$5,882.40, because at the time of the transfer Mattice: (a) was gainfully employed as a painter; (b) had

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no debt other than the Assumed and Furnace Debts; and (c) had sufficient projected income and assets to be able to pay the Assumed and Furnace Debts, including a fee ownership interest in Stal-Mar Circle after the transfer; (4) the value of Mattice's promise to be solely responsible for the Assumed and Furnace Debts, along with his forgiveness of debt, cash payments and transfer of the vehicle, exceeded the value of the Debtor's interest in Stal-Mar Circle; (5) since the execution and delivery of the Separation Agreement, Mattice had paid the Furnace Debt in full and made significant payments on the Assumed Debt which had a current aggregate balance of \$8,137.59; (6) the Debtor's estate was not diminished when she transferred her interest in Stal-Mar Circle to Mattice in exchange for the consideration provided by Mattice; (7) by agreeing to be solely responsible for and indemnify the Debtor in connection with the Assumed and Furnace Debts, Mattice provided fair consideration to the extent of one-half of those Debts by having forgone the right of contribution and reimbursement that he would have had against the Debtor in the event that he paid the Debts in full; and (8) there was no credible evidence that the Debtor's transfer of her interest in Stal-Mar Circle pursuant to

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the Separation Agreement and as a part of a divorce action was made with the actual intent to hinder, delay and defraud creditors².

On April 22, 2002, the Trustee filed a Reply in support of the Motion for Summary Judgment (the "Reply"), which asserted that: (1) Mattice had withdrawn his claim that his waiver of an enhanced earnings award constituted an element of fair consideration; (2) the Court should not find that a cost of sale factor reduces the fair market value of property transferred in connection with a DCL analysis of fair consideration; (3) in the event that the Court were to find that payments made by Mattice on the Assumed Debt constituted fair consideration or a credit against any recovery in connection with an avoidable fraudulent conveyance, the only payments that should be considered are those which reduced the outstanding balance of the Assumed Debt on the date of the transfer by more than fifty percent; (4) on the date of the filing of the Debtor's petition, Mattice had failed to fulfill his promise to pay the Assumed Debt in full, so that the Debtor's estate had in fact been diminished; and (5) the Debtor's unfulfilled promise to pay the Assumed Debt is not fair consideration under the DCL.

In a May 12, 2003 letter to the Court, the Trustee asserted that even though Mattice had now paid the Assumed Debt in full in

² The Court does not believe that the Trustee is still asserting that the transfer was made with the actual intent to hinder, delay and defraud creditors under the DCL.

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response to the Court's informal guidance at the pretrials and trial calendar calls, that post-petition, post-Adversary Proceeding fulfillment of the promise was not made, as required by the DCL, in exchange for the transfer.

In a May 13, 2003 letter to the Court, Mattice asserted that his post-petition, post-Adversary Proceeding fulfillment of the promise to be solely responsible for payment of the Assumed Debt and indemnification of the Debtor was proof that full value should be given to his promise for purposes of a DCL analysis of fair consideration.

DISCUSSION

I. Summary of Decision

The Court does not believe that either the fair market value of the Debtor's interest in Stal-Mar Circle when she transferred it to Mattice, or any recovery by the Trustee under Section 550, should be reduced by a hypothetical cost of sale. Therefore, the value of the interest transferred is \$10,408.91, representing one-half of the \$88,000.00 fair market value less \$67,182.18 due on the first mortgage.

Pursuant to the good faith agreement of the parties in the Separation Agreement, Mattice provided \$3,670.00 of fair consideration for the post-Agreement transfer of Stal-Mar Circle in

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the form of: (1) the forgiveness of a \$1,300.00 antecedent debt, or an agreed credit against equitable distribution; (2) a \$1,000.00 cash payment towards the Debtor's attorney's fees; and (3) the transfer of an automobile valued by the parties in good faith at \$1,370.00. This \$3,670.00 in fair consideration resulted in the need for Mattice to demonstrate an additional \$6,738.91 in fair consideration to support the transfer and prevent it from being found to be an avoidable fraudulent conveyance.

For purposes of this Adversary Proceeding, Mattice is entitled to a fair consideration credit of \$6,482.40, representing the Debtor's liability as of the date of the transfer for one-half of the Assumed and Furnace Debts, which Mattice has now paid. At pretrials and trial calendar calls this Court indicated to the attorney for Mattice that it would reduce any recovery by the Trustee under Section 550 by that amount upon proof of the full payment of the Debts, notwithstanding whether they were paid pre-petition or post-petition and after the commencement of the Adversary Proceeding. With that credit, there remains a balance of \$256.51 recoverable from Mattice under Section 550.

For purposes of a DCL fair consideration analysis, this Court believes that an agreement to assume an indebtedness of a transferor can be an element of fair consideration to support the transfer of property. In each case, the agreement must be valued

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based upon all of the facts and circumstances presented, including: (1) whether the agreement is oral or in writing; (2) the financial viability of the transferee; (3) whether security has been provided; (4) the time-frame and other specific requirements for the fulfillment of the agreement; and (5) the value of the asset transferred in the hands of the transferee.

Even within the context of a divorce proceeding, where one spouse agrees to be solely responsible for a joint debt and to indemnify the other spouse in connection with that debt, that agreement, subject to valuation, can be an element of fair consideration for the transfer of property. In such a case, the agreement results in the contractual elimination by the promisor spouse of any right of contribution and reimbursement to the extent that such a right had not previously been waived or contracted away. The agreement, if given full value, can be viewed as an asset of the transferor spouse that directly benefits at least some of the creditors that existed at the time of the transfer, or, alternatively, as the elimination of a contingent liability. In either case, on a balance sheet basis, the result is that there is no diminution in the estate of the transferor spouse.

In view of this Court's representation in this Adversary Proceeding that it would afford Mattice a credit if he paid the

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Assumed and Furnace Debts, it was not necessary for the Court to value his agreement as of the date of the transfer.

II. Deduction from Fair Market Value and Hypothetical Cost of Sale

As a general proposition, in determining the fair market value of property for purposes of the Bankruptcy Code when there is no contemplation that the property to be valued is going to be sold or liquidated and transaction costs actually incurred, this Court believes that it would be inappropriate to reduce the fair market value of the property by the hypothetical costs of a sale or liquidation. The majority of courts have accepted this principle when valuing: (1) a residence in connection with a Section 522(f) judgment lien avoidance motion (See Household Finance Corp., III v. Wilk, 91-CV-6055L, (W.D.N.Y. 2/13/92) (Larimer, J.); (2) the collateral of a secured creditor under Section 506(a) (See Huntington National Bank v. Pees, (In re McClurkin), 31 F.3d 401 (6th Cir. 1994); and (3) property that a debtor has claimed as exempt (See In re Sumerel, 194 B.R. 118 (Bankr. E.D.Tenn 1996)).

Although for settlement purposes it is not uncommon for this Court to see Trustees offer to reduce any potential recovery in a fraudulent conveyance action by the hypothetical costs of a sale or liquidation, those offers have not been made because this Court has previously ruled on the issue. Furthermore, the fact that this Court has approved such settlements when they seemed to be in the

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proper exercise of the Trustee's business judgment after he evaluated the required factors of provability, collectability, and the costs of litigation, did not constitute a ruling regarding hypothetical costs of sale.

In this case the parties never contemplated that Mattice, as the joint owner of Stal-Mar Circle, would liquidate the residence after the Debtor's interest in the property was transferred to him. He always intended to continue his use and enjoyment of the property. Therefore, there is no reason to reduce the determination of the fair market value of the property by the hypothetical costs of a sale or liquidation. If the Court were to do so, it would result in a windfall to Mattice, or a similarly situated transferee, at the unnecessary expense of the Debtor's creditors.

III. An Agreement to Assume the Debt of the Transferor as Fair Consideration

As set forth in the Summary of Decision section above, this Court believes that it is possible for a transferee's agreement to pay the debt of a transferor to be an element of fair consideration. See *In re Tuller's, Inc.*, 480 F.2d 49 (2d Cir. 1973). This is so even in a matrimonial context where there is a transfer of property between spouses pursuant to a separation

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agreement. In each such matrimonial case, however, valuation of the agreement will be critical.

Furthermore, unlike under the Bankruptcy Code, under New York State Law there is no policy of equality of distribution, so that in a fair consideration analysis under the DCL, where fair consideration must be viewed through the eyes of the transferor's creditors, it is not necessary that the rights of all of the creditors of the transferor be unaffected by the transfer.

The decisions of the Appellate Courts in New York State in matrimonial cases often liken a marriage to an economic partnership. Notwithstanding this characterization, in the dissolution of marriages, especially those resolved by a written separation agreement entered into by the spouses, the New York State Courts often do not deal with the assets and liabilities of the matrimonial economic partnership in the same manner as they do when they dissolve an actual business partnership. It is not uncommon for separation agreements to provide for the transfer of property between the spouses and the assignment of matrimonial debt, including joint debt, to one or the other of the spouses. Purported consideration for transfers of property often include waivers of support, promises of future support, and waivers of equitable distribution awards, including enhanced earnings awards. However, some of these purported elements of fair consideration may

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not constitute consideration in money or money's worth as seen through the eyes of the transferor's creditors.

In this case, the Court correctly believed that the Assumed and Furnace Debts were the only unpaid joint debts of the Debtor and Mattice when they became divorced and the transfer of the Debtor's interest in Stal-Mar Circle took place, but it mistakenly believed that these were the Debtor's only unpaid matrimonial debts, and thus the only unpaid debts "in existence" at the time of the transfer that were the predicate for the Trustee to attempt to avoid the transfer of the Debtor's interest in Stal-Mar Circle pursuant to Section 544 and the DCL. As a result, the Court indicated to the attorney for Mattice that it would credit Mattice with any payments on those Debts to the extent that the payments exceeded fifty percent of the balance due at the time of the transfer.

Because of the Court's representation that fair consideration credit would be given if the Assumed and Furnace Debts were paid, it was not necessary for the Court to value Mattice's agreement to be solely responsible for these Debts and to indemnify the Debtor in connection with them. However, it should be noted that at the time of the transfer Mattice was regularly employed, his only debts, other than the mortgage on Stal-Mar Circle, were the Assumed

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and Furnace Debts, and after the transfer he held a fee interest in Stal-Mar Circle.

CONCLUSION

The Motion for Summary Judgment and the Crossmotion for Summary Judgment are each denied and granted in part.

The transfer of the Debtor's interest to Stal-Mar Circle is an avoidable fraudulent conveyance to the extent of \$256.51, which shall be paid by Mattice to the Trustee by August 27, 2003.

IT IS SO ORDERED.

_____/s/_____
HON. JOHN C. NINFO, II
CHIEF U.S. BANKRUPTCY JUDGE

Dated: August 13, 2003