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BILL



ANALYSIS

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Senate Bill 982 (Substitute S-1 as reported)
Senate Bills 983, 984, and 985 (as reported without amendment)
Sponsor: Senator Tonya Schuitmaker
Committee: Judiciary

Date Completed: 10-11-16

RATIONALE

The Uniform Fraudulent Transfer Act provides a creditor with the means to reach assets of a debtor who has transferred the assets to another person or incurred an obligation under circumstances that are considered "fraudulent". The Act specifies circumstances under which a transfer or obligation is fraudulent; describes when a transfer is considered made; specifies the relief that a creditor may obtain; describes when a transfer is or is not voidable; and prescribes the period of limitations for an action brought under the Act. The Act is based upon a model act proposed and edited by the Uniform Law Commission, which generally promotes the uniformity of law among states on subjects in which consistency is practical. In 2014, the Commission amended the model Uniform Fraudulent Transfer Act and renamed it the Uniform Voidable Transactions Act. Reportedly, the changes were made to address ambiguities in the previous version in the law and to bring the Act up to date with current practices and technology. In order to keep the versions of the Act consistent, it has been suggested that corresponding modifications in the Michigan statute be made.

CONTENT

Senate Bill 982 (S-1) would amend Uniform Fraudulent Transfer Act to do the following:

- Refer to transactions that can be avoided as "voidable" transactions, instead of "fraudulent" transactions.
- Specify that a creditor making a claim for relief to avoid a transaction would have the burden of proving the elements of the claim by a preponderance of the evidence.
- Provide that a claim for relief would be governed by the law of the jurisdiction where the debtor was located when the transfer was made, and prescribe rules for determining a debtor's location.
- Identify the party that would have the burden of proving certain matters, and establish a preponderance of the evidence standard.
- Make an exception to a provision under which a transfer is not voidable if it results from the enforcement of a security interest under the Uniform Commercial Code.
- Preclude the entry of a judgment against an immediate or mediate good-faith transferee of a good-faith transferee who took for value.
- Specify that a debtor that was not paying debts as they became due other than as a result of a bona fide dispute would be presumed to be insolvent.
- Delete a provision that specifies when a partnership is insolvent.
- Specify that a series organization and each of its protected series would be considered a separate person for purposes of the Act.

The bill also would rename the Act as the "Uniform Voidable Transactions Act".

Senate Bill 983, Senate Bill 984, and Senate Bill 985 would amend the Business Corporation Act, the Nonprofit Corporation Act, and the Support and Parenting Time Enforcement Act, respectively, to refer to Uniform Voidable Transactions Act instead of the Uniform Fraudulent Transfer Act.

Senate Bill 982 (S-1) is tie-barred to Senate Bills 983, 984, and 985, which are tie-barred to Senate Bill 982. Each bill would take effect 90 days after its enactment.

A more detailed description of Senate Bill 982 (S-1) follows.

Voidable Transactions

Under the Act, a transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation in either of the following circumstances: a) with the actual intent to hinder, delay, or defraud any creditor of the debtor, or b) without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor was engaged or about to engage in a business or transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction, or the debtor intended to incur debts beyond the debtor's ability to pay as they became due.

Also, a transfer made or obligation incurred by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made or obligation was incurred if the debtor made the transaction or incurred the obligation without receiving a reasonably equivalent value in exchange and the debtor was insolvent at that time, or became insolvent as a result of the transaction or obligation. In addition, a transfer made by the debtor is fraudulent as to a creditor whose claim arose before the transaction was made if the transfer was made to an insider for an antecedent debt, the debtor was insolvent at that time, and the insider had reasonable cause to believe that the debtor was insolvent.

In these provisions, where the Act refers to a transaction as "fraudulent", the bill would refer to the transaction as "voidable".

Under the bill, a creditor making a claim for relief to avoid any of the transactions described above would have the burden of proving the elements of the claim for relief by a preponderance of the evidence.

Under the Act, a transfer is not voidable if it results from either termination of a lease upon default by the debtor when the termination is pursuant to the lease and applicable law, or from enforcement of a security interest in compliance with Article 9 (Secured Transactions) of the Uniform Commercial Code. Under the bill, a transfer would not be voidable if it resulted from termination of a lease, as currently provided, or from enforcement of a security interest under Article 9, other than an acceptance of collateral in full or partial satisfaction of the obligation it secured.

In addition, a transfer by an insolvent debtor to an insider for an antecedent debt is not voidable under a variety of circumstances, including to the extent the insider gave new value to or for the benefit of the debtor after the transfer was made unless the new value was secured by a valid lien. Under the bill, instead, a transfer to an insider for an antecedent debt would not be voidable to the extent the insider gave new value to or for the benefit of the debtor after the transfer was made, except to the extent the new value was secured by a valid lien.

The Act provides that an obligation is incurred if one of the following occurs: a) if oral, when it becomes effective between the parties, or b) if evidenced by a writing, when the writing executed by the obligor is delivered to or for the benefit of the obligee. The bill would refer to a "record" instead of a "writing". "Record" would mean information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form. "Electronic"

would mean relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

Action for Relief

In an action for relief against a transfer or obligation under the Act, a creditor may obtain one or more of the following:

- Avoidance of the transfer or obligation to the extent necessary to satisfy the creditor's claims.
- An attachment against the asset transferred or the transferee's other property to the extent authorized under Section 4001 of the Revised Judicature Act and applicable court rules.
- An injunction against further disposition of the asset transferred or other property, appointment of a receiver to take charge of the asset or other property of the transferee, or any other relief the court determines appropriate, subject to principles of equity and in accordance with court rules and statutes.

Regarding an attachment, the bill instead would permit a creditor to obtain an attachment or other provisional remedy against the asset transferred or other property of the transferee if available under applicable law.

(Under Section 4001 of the Revised Judicature Act, upon an ex parte application showing that the person against whom a claim is asserted is not subject to the judicial jurisdiction of the State, or cannot be served with process that would subject the person to the State's jurisdiction, the court has the power of attachment to apply to the satisfaction of the claim an interest in the person's things that are subject to the State's jurisdiction. Michigan Court Rules prescribe the circumstances and procedures under which a person may obtain a writ of attachment after commencing an action. Except in an action brought on a foreign judgment, the rules provide that attachment may not be used unless the defendant is subject to the jurisdiction of the court.)

Burden of Proof

The bill would prescribe rules for determining the burden of proving matters referred to in Section 8 (which specifies circumstances under which a transfer or obligation is not voidable, provides for the entitlement of a good faith transferee or obligee, and prescribes rules that apply when a transfer is voidable in an action brought by a creditor).

The standard of proof required to establish those matters would be preponderance of the evidence.

A party that sought to invoke the provisions of the Act relating to the following matters would have the burden of proving the applicability of those provisions:

- A transfer or obligation not voidable against a person that took in good faith and for reasonably equivalent value.
- The entitlement of a good-faith transferee or obligee to a lien or right to retain an interest in a transferred asset, enforcement of an obligation, or a reduction in the amount of liability on a judgment.
- That a transfer is not voidable if it results from termination of a lease upon a debtor's default, or enforcement of a security interest under Article 9 of the Uniform Commercial Code.

Except as provided below, a creditor would have the burden of proving each applicable element of an action to avoid a transfer or, if a judgment were based on the value of the asset transferred, proving the value of the asset when transferred, subject to an adjustment.

A party seeking an adjustment would have the burden of proving the adjustment.

The transferee would have the burden of proving the applicability to the transferee of provisions precluding the entry of a judgment against a good-faith transferee who took for value, or an immediate or mediate good-faith transferee of the first good-faith transferee.

Debtor's Location

The bill specifies that a claim for relief in the nature of a claim for relief under the Act would be governed by the local law of the jurisdiction in which the debtor was located when the transfer was made or the obligation was incurred.

For this purpose, a debtor would be located as follows:

- An individual: his or her principal residence.
- An organization with only one place of business: its place of business.
- An organization with more than one place of business: its chief executive office.

"Organization" would mean a person other than an individual. The Act defines "person" as an individual, partnership, corporation, association, organization, government or governmental subdivision or agency, business trust, estate, trust, or any other legal or commercial entity. The bill would define "person" as an individual, estate, partnership, association, trust, business or nonprofit entity, public corporation, government or governmental subdivision, agency, or instrumentality, or other legal or commercial entity.

Solvency

Under the Act, a debtor is insolvent if, at a fair valuation, the sum of the debtor's debts is greater than the sum of the debtor's assets. A debtor that is generally not paying debts as they become due is presumed to be insolvent. Under the bill, a debtor that was not paying debts as they became due other than as a result of a bona fide dispute would be presumed to be insolvent. The party against whom the presumption was directed would have the burden of proving that the nonexistence of insolvency was more probable than its existence.

The Act also states that a partnership is insolvent if the sum of its debts is greater than the aggregate, at a fair valuation, of all of the partnership's assets and the sum of the excess of the value of each general partner's nonpartnership assets over the partner's nonpartnership debts. The bill would delete this provision.

Good-Faith Transferee

Except as otherwise provided, to the extent a transfer is avoidable in an action by a creditor, the creditor may recover a judgment for the value of the asset transferred, as adjusted as required by equity, or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered either against the first transferee of the asset or the person for whose benefit the transfer was made, or against a subsequent transferee, other than a good-faith transferee who took for value or from any subsequent transferee.

The bill specifies that the judgment could be entered against the first transferee of the asset or the person for whose benefit the transfer was made, or an immediate or mediate transferee of the first transferee, other than a good faith transferee who took for value, or an immediate or mediate good-faith transferee of a good-faith transferee who took for value. Recovery by avoidance of the transfer or by execution of or from the asset transferred or its proceeds, by levy or otherwise, would be available only against the first transferee of the asset or the person for whose benefit the transfer was made, or a subsequent transferee. (Execution is the enforcement of a money judgment by seizure and sale of property owned by the judgment debtor by a sheriff, bailiff, or other officer of a county, district, court district, or municipality.)

Protected Series

Under the bill, a series organization and each of its protected series would be a separate person for the purposes of the Act, even if for other purposes a protected series was not a person separate from the organization or its other series.

"Series organization" would mean an organization that, pursuant to the law under which it is organized, has the following characteristics: a) the organic record of the organization provides for creation by the organization of one or more protected series, however denominated, with respect to specified property of the organization, and for records to be maintained for each protected series that identify the property of or associated with the protected series; b) debt incurred or existing with respect to the activities of, or property of or associated with, a particular protected series is enforceable against the property of or associated with the protected series only, and not against the property of or associated with the organization or other protected series of the organization; and c) debt incurred or existing with respect to the activities or property of the organization is enforceable against the property of the organization only, and not against the property of or associated with a protected series of the organization.

"Protected series" would mean an arrangement, however denominated, created by a series organization that, pursuant to the law under which the series organization is organized, has the characteristics set forth above.

Other Provisions

The sections that the bill would amend or add would apply to a transfer made or obligation incurred on or after the bill's effective date. Those sections would not apply retroactively, nor would they apply to a right of action that accrued before the bill's effective date. For these purposes, a transfer would be made and an obligation would be incurred at the time currently provided in the Act.

The bill specifies that the Act would modify, limit, or supersede the Federal Electronic Signatures in the Global and National Commerce Act, but would not modify, limit, or supersede 15 USC 7001(c) or authorize electronic delivery of any notices described in 15 USC 7003(b).

(Under 15 USC 7001(a), with respect to any transaction in or affecting interstate or foreign commerce, a signature, contract, or other record may not be denied legal effect, validity, or enforceability solely because it is in electronic form; and a contract may not be denied legal effect, validity, or enforceability solely because an electronic signature or electronic record was used in its formation. Under 15 USC 7001(c), if a statute, regulation, or other rule of law requires that information relating to a transaction in interstate or foreign commerce be provided to a consumer in writing, the use of an electronic record satisfies the requirement if the consumer consents to the use of an electronic record, and the consumer is provided with certain information before and after consenting to the use of the record. Under 15 USC 7003(b), the requirements of Section 7001 do not apply to certain documents, including official court documents, documents required to accompany any transportation of hazardous or dangerous materials, and any notice of: a) termination of utility services; b) default, eviction, or foreclosure under an agreement secured by, or a rental agreement for an individual's primary residence; c) cancellation of health or life insurance; or d) recall or material failure of a product that endangers health or safety.)

MCL 566.31 et al. (S.B. 982)
450.1122 (S.B. 983)
450.2122 (S.B. 984)
552.624a (S.B. 985)

BACKGROUND

The source of following information is the website of the National Conference of Commissioners on Uniform State Laws (the Uniform Law Commission).

The Uniform Law Commission proposed the Uniform Fraudulent Conveyance Act (UFCA) in 1918 to address the recourse of unsecured creditors in situations in which debtors manipulate property to defeat the creditors' interest. For example, a debtor might foresee insolvency and try to conceal property that a creditor could use to satisfy the debt. Alternatively, a debtor that never intended to satisfy the debt might manipulate property in order to become judgment-proof.

The UFCA was created to supersede the Statute of 13 Elizabeth (a centuries-old English law), which had been enacted in some form by many states and introduced the concept of fraudulent conveyance into the law of every American jurisdiction. The UFCA was adopted in 26 states and its provisions were incorporated into the Federal Bankruptcy Act.

In 1984, the Uniform Fraudulent Conveyance Act was revised and renamed the Uniform Fraudulent Transfer Act. The new law was drafted for several reasons. The terminology of the original 1918 law had become archaic, and creditor-debtor relationships had changed and become more complicated. Also, the Bankruptcy Reform Act of 1978 had changed the Federal law on fraudulent transfers in significant ways, and revising state law had become imperative.

In 2014, the Uniform Law Commission adopted amendments "addressing a small number of narrowly defined issues", and changed the name of the law to the Uniform Voidable Transactions Act.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bill's proposed changes to the Michigan statute are based on modifications made in 2014 to the model Uniform Fraudulent Transfer Act drafted by the Uniform Law Commission. The proposed changes would reflect current technology and practices with respect to voidable transactions. The bill would rename the Act because its current title is misleading; fraud is not a necessary element in order to set aside a transaction. The bill also would include choice of laws and standard of proof provisions, which would make it easier for Michigan courts to apply the Act to cases.

Legislative Analyst: Jeff Mann

FISCAL IMPACT

The bills would have no fiscal impact on State or local government.

Fiscal Analyst: Ryan Bergan

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.