

CONSUMER CASE AVOIDANCE ISSUES

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i. Understand how preferences and fraudulent transfers can impact a consumer Chapter 7

Fraudulent Transfers and Preferences (consumer debt)

- Fraudulent Transfer – any transfer of property for which inadequate consideration is received at a time when the transferor is insolvent or rendered insolvent by the transfer.
- Preference Payment – a payment made within 90 days of bankruptcy on account of an old debt, and in the case of insiders: within one year of bankruptcy.
- Change of Interest -- in an Estate debtors must disclose any change interest in an estate within four years of filing bankruptcy.

Preferences and Fraudulent Transfers (non-consumer debt)

- Fraudulent Transfer – any transfer of property [generally within two years of filing bankruptcy] for which inadequate consideration is received at a time when the transferor is insolvent or rendered insolvent by the transfer.
- Preference Payment – a payment made within 90 days of bankruptcy on account of an old debt -- in the case of insiders: within one year of bankruptcy.
 - Pay recent invoices to avoid preference claims
 - Preference payments that total less than \$6,425 are exempt
- Change of Interest in an Estate -- debtors must disclose any renounced interest in an estate within four years of filing bankruptcy.

Preferences and Fraudulent Transfers (Consumer v. Non-Consumer Debt)

- The Consumer Lawyer must understand the differences and advise clients accordingly.
- Proving the majority of the debt is non-consumer will reduce potential claims.
- Debtor may not have to delay filing because of preference statutory period if the case is non-consumer.

ii. When timing of the filing can be beneficial

Timing of Filing

- When facing a large priority and/or non-dischargeable tax claim, your client has incentive to maximize the estate to pay such claims.
- Filing the case within the statutory preference period to allow the trustee to recover those payments for the benefit of the priority creditors.
- Reversing asset seizure if the case is filed within 90 days of the seizure.
- Debtor may have made voluntary payment and realized after the fact that those payments should be directed to a non-dischargeable creditor.

iii. Pre-bankruptcy planning

Pre-bankruptcy planning

- Converting non-exempt assets into exempt assets.
- Not without risk.
- No single test has been universally accepted by the courts.
 - What is the amount of conversion to exempt property?
 - What is the proximity to the bankruptcy filing?
 - Did the conversion involved newly acquired funds or previously secured property?
 - Did the conversion benefit insiders of the debtor?
 - Did the debtor mislead creditors during the conversion?

Pre-Bankruptcy planning

- Crucial factors to successful pre-bankruptcy planning.
 - Was the debtor forthright in all disclosures?
 - Did the debtor show proper grounds for the transfers?
 - Did the debtor show that bankruptcy was unavoidable?
 - Consider the amount of planning relative to the debt.
 - The derivation of the debt can be important.
 - Consider what the debtor is really trying to accomplish.

iv. What happens when a bankruptcy trustee is unwilling to pursue a fraudulent transfer claim?

Bankruptcy Trustee unwilling to pursue a fraudulent transfer claim

- A creditor may ask for appointment of an alternate trustee at the first meeting of creditors. The petitioning creditor must possess at least 20% of the claims.
- A creditor may request abandonment of the claim if the trustee is unwilling to pursue it.
- A majority of Federal Circuit Courts of Appeal have allowed creditors to pursue fraudulent transfer claims when:
 - 1) the Bankruptcy Court approves the creditor's standing;
 - 2) the trustee is unwilling or unable to assert the claim or causes of action on behalf of the estate; and
 - 3) allowing the creditor to pursue claims is likely to benefit the estate.

v. When can a creditor pursue a fraudulent transfer claim even if the trustee has done so?

Pursuing a fraudulent transfer claim even if trustee has done so

- Creditors pursuing claims pre-bankruptcy usually have to defer to the trustee and are no longer permitted to pursue such claims.
- Case law suggests that a creditor is limited from bringing those claims to circumstances in which the claims against third parties are not based upon fraudulent transfer or similar theory.
- Judge Haines in *Hoyt v. Aerus Holdings, L.L.C.*, 447 B. R. 283 (Bkrcty. D. Ariz. 2011) prevented creditors from pursuing third parties and concluded that claims owned by the bankruptcy trustee could not be pursued by those creditors unless abandoned by the bankruptcy trustee.



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Randy is a Certified Bankruptcy Specialist (Arizona Board of Legal Specialization) and a Certified Business Bankruptcy Specialist (American Board of Certification). His areas of practice include complex bankruptcy law and litigation, construction, real estate, and contract law.

He is a popular lecturer and author on topics regarding bankruptcy, construction, and real estate for the State Bar of Arizona, Maricopa County Bar Association, American Bankruptcy Institute, and other professional organizations.



Randy has been named to Super Lawyers' "Top 50 Arizona" list of attorneys multiple times and has been selected by *The Best Lawyers in America*® every year since 2010. *Best Lawyers*® also has twice selected Randy as its "Lawyer of the Year" (Scottsdale), in Bankruptcy and Creditor Debtor Rights (2019) and in Bankruptcy Litigation (2021).

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