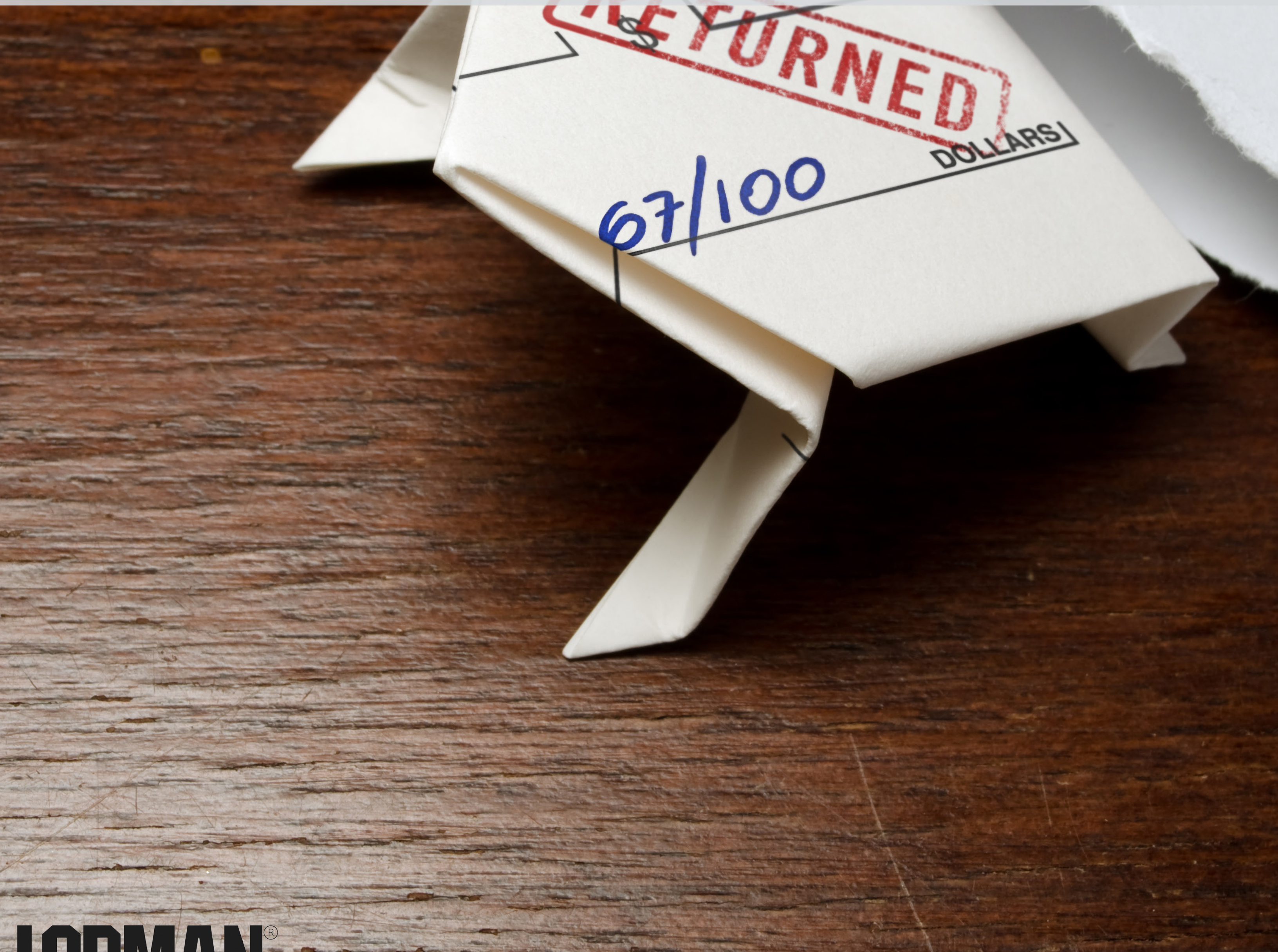
Addressing and Handling Unique Collection Situations: *Fraudulent Conveyances and Bad Check Laws*

Prepared by:
Lynda L. Laing
Strauss Factor Laing & Lyons



LORMAN®

Published on www.lorman.com - March 2022

FRAUDULENT CONVEYANCES

A debtor can commit a fraudulent conveyance by transferring assets to a third party with the intent to prevent creditors from reaching the assets to satisfy their claims. There are two types of fraudulent conveyances- actual and constructive. Actual fraud is committed when a transfer is made with the intent to hinder or defraud creditor. The intent of the transferee is irrelevant. Some examples are transfers when there is actual or threatened litigation against the debtor, the debtor transfers substantially all of his assets, the debtor transfers property but retain possession or control of the property. The courts do look to see if the debtor received reasonably equivalent value of the transferred property

Constructive fraud requires that that the debtor received less than reasonably equivalent value and the debtor is unable to pay debts either at the time the transfer was made or as a result of the transfer. For example, if a husband conveys stock to his wife for no consideration. The wife does not pay for the stock. Husband defaults on a loan a few months after the transfer. Clearly, the creditor has a basis to argument that the transfer is a fraudulent conveyance. The debtor did not receive reasonably equivalent value for the property transferred. The debtor is insolvent as he defaulted on the loan. The debtor is aware of the claims against his assets. However, there is one prong that is missing. The Stock had negative net worth making it worthless. As a result, the transfer was not one made with the intent to delay, hinder, or defraud creditors.

Most states have adopted statutes that set forth what qualifies as a fraudulent transfer. Rhode Island General Laws 6-16-4 sets forth eleven non-exclusive “badges of fraud” which are: (a) A transfer made or obligation incurred by a debtor is voidable 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::

(1) With actual intent to hinder, delay, or defraud any creditor of the debtor; or

(2) Without receiving a reasonably equivalent value in exchange for the transfer or obligor the debtor:

(i) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or

(ii) Intended to incur, or believed or reasonably should have believed that the debtor would incur,

debts beyond the debtor’s ability to pay as they became due.

(b) In determining actual intent under subsection (a)(1), consideration may be given, among other factors, to whether:

(1) The transfer or obligation was to an insider;

(2) The debtor retained possession or control of the property transferred after the transfer;

(3) The transfer or obligation was disclosed or concealed;

(4) Before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;

(5) The transfer was of substantially all the debtor's assets;

(6) The debtor absconded;

(7) The debtor removed or concealed assets;

(8) The value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;

(9) The debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;

(10) The transfer occurred shortly before or shortly after a substantial debt was incurred; and

(11) The debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

(c) A creditor making a claim for relief under subsection (a) has the burden of proving the elements of the claim for relief by a preponderance of the evidence.

In addition, to the above badges, Courts will consider attempts by a debtor to conceal the conversions, the timing of the conversions and the monetary value of the assets converted to determine the existence of fraudulent intent.

Most states have a four-year statute of limitations for such transfers. Courts have also stated that transfers to insiders such as a spouse may also be a fraudulent transfer if the transfer was made with actual intent to hinder, delay, or defraud a creditor. In divorce situations, if the debtor already has financial issues, it may be difficult to transfer the asset without having litigation occur. However, if the liabilities have not yet arisen, the transfer is not a fraudulent conveyance.

The statutes also give remedies to the creditor if such transfer has occurred. In Rhode Island, the creditor can seek recovery of the asset from the transferee. Problems arise when debtors transfer funds into exempt assets such as automobiles. The automobile lender is a transferee who took in good faith and for reasonably equivalent value so in some states, the asset cannot be recovered

BAD CHECK LAW

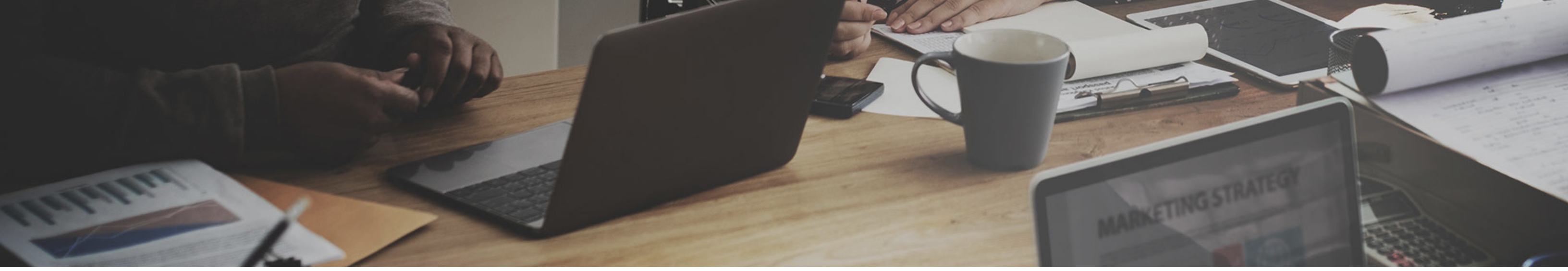
Each state will have different laws concerning bad checks. Rhode Island and other states will have both criminal and civil bad check laws. In Rhode Island section 6-42-1 gives notice of the dishonored check. Under that section if a check is not paid after then days of notice of dishonor the creditor can send a notice pursuant to 6-42-2. That notice allows thirty days to pay and if not paid, the holder may seek damages in District Court. The damages are the amount of the check, collection fee of $25.00 and an amount equal to three times the amount of the check but in no case less the $200.00 and in no case more than $1000.00. This notice must be sent by certified mail.

Under 6-42-4, the law gives a dense to the action if the defendant justifiably stops payment on the check or there was an attachment on the account.

In order for a criminal statute to apply, most states require the party writing the check know they have insufficient funds in the account, or the writer knows he is going to stop payment on the check. Similarly, if the writer writes a fraudulent check because the account does not exist, it is a criminal case. Depending on the amount it could be a misdemeanor or a felony.

Most criminal statutes require the maker at the time of the making the check was worthless. The fact that a check bounces in not enough to show knowledge. Some states presume that people know their bank balances and other states do not have such presumption. If your state requires such knowledge, how do you prove it? Courts will look at whether the debtor wrote multiple worthless checks and had a large overdraft balance. Experience of the maker may also make a difference if the maker is an experience businessperson. Finally, the debtor's own admissions may help establish proof.

Some venders or debt collectors require that consumers give post dated checks. If you give a post-dated check, the vender/debt collector must comply with the Fair Debt Collection Practices Act. Under that Act, the Vender/debt collector must give notice that the check will be deposited three days before and not more then ten days that the check will be deposited.



LORMAN®

2510 Alpine Road Eau Claire, WI 54703
www.lorman.com 866-352-9539 customerservice@lorman.com