Forbes http://onforb.es/1DB3pGT

Jay AdkissonContributor

I cover Wealth Preservation in its legal permutations

Opinions expressed by Forbes Contributors are their own

PERSONAL FINANCE 4/27/2015 @12:38AM 1,646 views

The Fraudulent Transfer Laws Do Indeed Apply To Future Creditors

Comment Now

Quite possibly no area of fraudulent transfer law is as terribly misunderstood as the issue of transfers to "future creditors".

The misinformation is all over the board. Some say that the fraudulent transfer laws do not apply at all to future creditors. Others say that future creditors have to be expected creditors, as in the case of an obstetrician who can expect to have X number of lawsuits ever few years. Still others would say that future creditors arelimited to those creditors who already have a claim against the debtor, but the debtor doesn't know it yet (i.e., the surgeon who leaves a sponge in her patient's abdomen only to be discovered many years later).

They are all wrong. The concept of "future creditors" in fraudulent transfer laws do not embrace any of these concepts.

Yet, these are precisely the sort of statements that one hears at asset protection seminars, including some pretty high-level conferences, and in various asset protection professional literature. They are all wrong too.

To fully understand this concept, you must clear your mind of all preconceptions of what "future creditor" means or doesn't mean. If you must, hypnotize yourself to believe that I have zapped you with a Neurolyzer to cleanse your memory of the subject. Open your mind, and recall that the realization of truth is the beginning of wisdom.

We start with Section 4 of the Uniform Fraudulent Transfer Act ("UFTA"). I'm going to stick with the 1984 version, as opposed to the 2014 revisions (which do not change this analysis at all), since the 1984 version is still the law in the vast majority of states. Section 4 provides in part:

> *4. TRANSFERS FRAUDULENT AS TO PRESENT AND FUTURE CREDITORS.*
>
> *(a) 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:*
>
> *(1) with actual intent to hinder, delay, or defraud any creditor of the debtor . . ..*

The first thing we want to look at is the title of Section 4, which clearly applies to "future creditors".

The second thing we want to look at is the clause in paragraph (a) which makes a transfer fraudulent "whether the creditor's claim arose before or after the transfer was made or the obligation was incurred" — this is the phrase that works to apply Section 4 to future creditors.

The third thing we want to look at is subsection (1), which is the "intent test" of fraudulent transfer law.

Here, let me digress and point out that subsection (1) is the so-called test for the ill-named "actual fraudulent transfer" test of fraudulent transfer law, the other primary test being the "constructive fraudulent transfer" which is found in Section 5. The Section 5 "constructive fraudulent transfer" test only applies to existing creditors, so we're not concerned about it here. From 4(a), I've also omitted the discussion of two other minor tests for fraudulent transfers found in subsections (a)(2) and (a)(3) as not being pertinent to this discussion, though they also apply to "future creditors".

Section 4(a) by its plain text makes crystal clear that it applies to "future creditors" — there is utterly no grounds for confusion on this point. Yet, some litigants have tried to argue the contrary, only to be repeatedly rejected:

> *Section [four] subdivision (a) does not require that, from the debtor's perspective, a creditor who challenges a transfer as fraudulent under the UFTA to have been reasonably foreseeable as the debtor's creditor before pursuing remedies under the UFTA. Furthermore, the statute does not require that the debtor intended to hinder, delay, or defraud the specific creditor who challenges a transfer of an asset as violative of the UFTA. On the contrary, section [four], subdivision (a) provides that a current creditor can challenge a transfer as fraudulent, regardless whether that creditor had a claim at the time of the transfer, if that creditor can prove, inter alia, the transfer was made to hinder, delay, or defraud* any *creditor.*

Kilker v. Stillman, 2012 WL 5902348 at *4 (Cal.App., Unpublished, 2012) (emphasis in original).

So, it is crystal clear that Section 4 applies to future creditors — there simply is no sensible contrary argument.

Thus, if a person makes a transfer with the intent of defeating a future creditor, even if that creditor is totally unknown the debtor and doesn't even have a claim at the time of transfer, then under Section 4 that transfer is a fraudulent transfer.

Ah, but now we have injected the element of "intent", and so must consider that issue as it is very important to our analysis, not so much from a technical legal perspective as from a practical litigation perspective.

It is important to consider that the burden of proving that the debtor acted with an intent to "hinder, delay, or defraud" her creditors is a burden that is born by creditors. In other words, a creditor does not establish an "actual fraudulent transfer" by merely reciting those magic words, but instead must come up with persuasive admissible evidence that the debtor had that intent.

Whether there are existing creditors or future creditors, the analysis does not change and the burden of proof remains on the creditor. It is undoubtedly easier in most cases to establish the debtor's ill intent where there is an existing creditor, but that is a practical issue of the creditor proving up its case and not a change in the legal requirements.

Where there were no existing creditors at the time that the debtor made the transfer, it will be difficult for the creditor-come-lately to prove the debtor's ill intent — difficult, but not impossible. If the creditor can find evidence that the debtor made the transaction with the specific intent to defeat future creditors, then the creditor can win.

This proof can be found in evidence that the debtor has engaged in planning with precisely that intention, or what is now commonly termed "asset protection planning" and which is aimed at unknown future creditors, but (properly, at least) not existing ones.

This is why it is so important that planning done be for reasons other than asset protection planning or any other regard to creditors, existing or future, and that the file be sterile as to any creditor or asset protection references. Readers will recall, for instance, that it was something as innocuous as a reference to "asset protection planning" in an attorney's time slips that blew up the debtor's planning in the infamous *Frankel* case.

Yet, I continue to see attorneys send engagement letters, planning memos, e-mails, and all sorts of other junk to clients that references their "asset protection planning" or "here's how we protect these assets from creditors" or somesuch. That's just creating evidence for a future creditor challenge under Section 4, and frankly it's all unnecessary — there is never a compelling reason to use that terminology when dealing with clients.

Instead, debtors need to be able to explain their planning as done for some reason other than creditors, for succession planning, for estate planning, for business planning, for charitable planning, for whatever so long as it doesn't involve creditors.

It would be quite easy for me to rant on and on along those lines, but I don't want to get away from the point: The fraudulent transfer laws do indeed apply to future unknown creditors, and if you hear somebody say anything different, they're just flat wrong.

And hopefully you won't need another zap of the Neurolyzer to remember that.

This article at http://onforb.es/1DB3pGT and http://goo.gl/FeM9FA

This article is available online at: http://onforb.es/1DB3pGT 2015 Forbes.com LLC™ All Rights Reserved