

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)	
)	
LINDA SUSAN HORNE,	)	CASE NO. BK97-80261
)	
DEBTOR	)	A97-8070
_____)	
THOMAS D. STALNAKER,)	
	)	CH. 7
Plaintiff)	
vs.)	
)	
JANET L. MCGINNIS,)	
)	
Defendant)	

MEMORANDUM

Hearing was held on January 20, 1998, on the adversary complaint. Appearances: Robert Becker for Thomas Stalnaker, Trustee; and Jay Ferguson for Janet L. McGinnis. This memorandum contains findings of fact and conclusions of law required by Fed. Bankr. R. 7052 and Fed. R. Civ. P. 52. This is a core proceeding as defined by 28 U.S.C. § 157(b)(2)(E) and (H).

Background

Linda Susan Horne (hereafter "Horne"), the debtor in the underlying bankruptcy case, filed her Chapter 7 bankruptcy petition on February 6, 1997. In this Chapter 7 case, the Trustee has filed an adversary complaint seeking to compel turnover of a parcel of real property in which the Trustee asserts the debtor had an interest. The Trustee claims that Horne's interest is property of the estate. The defendant, the holder of the title of record, denies that Horne has any interest in the real estate and affirmatively asserts she is the sole owner of said real estate.

Prior to her bankruptcy, Horne was divorced from Ronald Horne, Sr., by a decree of dissolution entered by the District Court of Douglas County, Nebraska, on November 16, 1994. According to paragraph 8(H) of the divorce decree, Horne

received all right, title and interest in the marital home located at 2744 South 12th Street, Omaha, Nebraska, subject to the encumbrances thereon.

Thirteen months after the divorce decree, on December 2, 1995, Horne and Ronald Horne, Sr., executed a warranty deed conveying the property to the defendant, Janet L. McGinnis, (the mother of Ronald Horne, Sr., and the ex-mother-in-law of Horne), (hereafter "McGinnis"), for the recited consideration of "One dollar and Other Valuable Consideration".

Fourteen months after the transfer of real estate to McGinnis, Horne filed the Chapter 7 bankruptcy petition.

Horne, in an affidavit (Ex. 14) used in a prior proceeding in this bankruptcy case and in her Amended Schedule A, C and D (filing no. 8), asserted that she transferred the property to McGinnis for no consideration and that McGinnis agreed to transfer the property back to her six months after her bankruptcy case. However, at trial, she testified that the purpose of the transfer was to assure that she and her children, McGinnis' grandchildren, had a place to live. Horne further testified that the property was transferred to McGinnis in return for release of an unsecured debt obligation to McGinnis. McGinnis took the property subject to the encumbrances on the property of at least \$12,000.00.

McGinnis testified that the property was transferred in return for cancellation of Horne's individual indebtedness as well as joint indebtedness of Horne and her ex-husband. McGinnis testified the total amount of indebtedness was approximately \$30,000.00. McGinnis stated the condition of the property was "only fair" because the property had been neglected by Horne. She testified that the value of the home in December, 1995, was not more than \$30,000.00 and maybe not more than \$25,000.00. McGinnis testified that Horne and Ronald Horne, by the time of their divorce, owed her at least \$20,000.00. After the divorce, Horne continued to borrow money from McGinnis. McGinnis testified that, in the period following the divorce and prior to the transfer, Horne incurred additional indebtedness of at least \$10,000.00. McGinnis denied any agreement to transfer the property back to the debtor after her bankruptcy.

Ronald Horne, Sr., also testified that the transfer of the real estate was in return for debt forgiveness. He

testified that the amount of joint indebtedness to his mother, prior to his divorce from Horne, was closer to \$30,000.00.

Analysis

Procedural Issues

This adversary proceeding was filed as a turnover action pursuant to section 542 of the Bankruptcy Code. While it is true that the Trustee seeks turnover, in order to accomplish this, the Trustee must successfully avoid the real estate transfer under the Uniform Fraudulent Transfer Act as enacted in Nebraska at Neb. Rev. Stat. § 36-701, *et seq* (Reissue 1989) via section 544(b) of the Bankruptcy Code.

The pleadings and pretrial statement do not specifically reference the Uniform Fraudulent Transfer Act nor did the Trustee specify under which provisions of the Act the transfer is voidable. However, at trial, the parties litigated the issues as if the Trustee is pursuing a recovery under the Uniform Fraudulent Transfer Act. Federal Rule of Bankruptcy Procedure 7015 make Federal Rule of Civil Procedure 15 applicable to adversary proceedings. Federal Rule of Civil Procedure 15(b) allows amendment of the pleadings to conform to issues not initially raised by the pleadings but tried by the express or implied consent of the parties. Therefore, the pleadings, as actually tried, will be considered to include a claim based on 11 U.S.C. § 544(b) and the Uniform Fraudulent Transfer Act.

Fraudulent Transfer

The Uniform Fraudulent Transfer Act provides two separate grounds for recovery by a future creditor such as the Chapter 7 Trustee. The relevant section in part states:

(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; **or**

(2) without receiving a reasonably equivalent value in exchange for the transfer or obligation, **and** 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 he or she would incur, debts beyond his or her ability to pay as they became due.

Neb. Rev. Stat. § 36-705(a) (Reissue 1989) (emphasis supplied).

To recover the real property in question, as a fraudulent transfer, the Trustee must successfully prove the elements under subsections (a)(1) or (a)(2) of Nebraska Statutes section 36-705.

Nebraska Statutes Section 36-705(a)(2)

While the Trustee argued that the debtor did not receive the reasonably equivalent value for the transfer of the real estate to McGinnis, the Trustee did not present any evidence on the elements of sub-section (a)(2). The Trustee did not allege, argue or prove that Horne was engaged in a business for which the remaining assets were unreasonably small (section (a)(2)(i)) nor that Horne intended to incur debts beyond her ability to pay as they became due (section (a)(2)(ii)). The Trustee failed to meet his burden of proof on the claim contained in Neb. Rev. Stat. § 36-705(a)(2) and, therefore, avoidance of the transfer on that basis is denied.

Nebraska Statutes Section 36-705(a)(1)

Any recovery under 36-705(a)(1) must be based upon the actual intent to hinder, delay, or defraud a creditor. The only direct evidence of actual intent presented by the Trustee was the affidavit of Horne (Ex. 14) and her Amended Schedule A, C and D (filing no. 8). However, at trial, Horne took a position opposite that which she had stated in the affidavit

and amended schedules. Horne's testimony generally supported the position of McGinnis that the transfer of the real estate was in return for loan forgiveness. Horne's affidavit and Amended Schedules are in direct conflict with her testimony at trial. No independent evidence of the accuracy of her affidavit and amended schedules was presented. No independent evidence of the inaccuracy of her trial testimony was presented. Her credibility is an issue in this case and, because of the conflicting versions of the facts presented by her, the court, as trier of fact, gives very little credence to any of her evidence.

The inquiry concerning "actual intent" is not limited to direct evidence. The Uniform Fraudulent Transfer Act provides eleven factors to be considered by the trier of fact in making the determination of actual fraud. Nebraska Statutes Section 36-705(b) states:

(b) In determining actual intent under subsection (a)(1) of this section, 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 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 of 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.

Neb. Rev. Stat. § 36-705(b) (Reissue 1989).

Of the eleven factors, the Trustee offered no evidence on subsections 3, 4, 5, 6, 7, 9, 10 and 11. Subsection 1, the insider provision; subsection 2, retention of possession; and subsection 8, adequate value, are the only factors on which evidence was presented to the Court.

Subsection 1 pertains to a transfer to an insider. The Uniform Fraudulent Transfer Act defines an insider, in relevant part, as "a relative of the debtor". Neb. Rev. Stat. § 36-702(7)(i)(A) (Reissue 1989). The term "relative" means a person who is connected to another person by blood or marriage. See BLACKS LAW DICTIONARY 1158 (5th ed. 1979). McGinnis is the ex-mother-in-law of Horne.

Horne and Ronald Horne had been divorced for over a year prior to the transfer of the real estate. Under the term's ordinary meaning, McGinnis is not a relative of Horne. However, because of the prior marital relationship, Horne and McGinnis shall be considered "related" for the purpose of this case. Therefore, the transfer was to an "insider."

Subsection 2 pertains to retention of possession of the transferred property by the debtor. The debtor testified that she remained in the house until she was forced to leave through legal action taken by McGinnis over a year after the transfer. It is undisputed that Horne retained possession of the real estate after the transfer. However, both Horne and McGinnis testified that Horne was supposed to pay rent for the right to possession. Her rent payments were not made regularly because of her financial situation.

The factor to examine in subsection 8 of 36-705(b) is the value of the consideration exchanged for the property. McGinnis testified that the house, at the time of the transfer, was not in the best of condition and worth not more than \$30,000.00, perhaps not more than \$25,000.00. Horne, McGinnis and Ronald Horne all testified that the transfer was in exchange for loan forgiveness. McGinnis took the house subject to the encumbrances on the property of at least \$12,000.00. Assuming that the house was worth \$30,000.00 at the time of the transfer, and the secured debt upon the house was only \$12,000.00, McGinnis received a net value from the exchange, on a secured basis, of \$18,000.00. McGinnis, in addition, forgave, at a minimum, \$20,000 dollars of indebtedness. The assumption of \$12,000.00 in secured debt and forgiveness of \$20,000.00 in unsecured debt is adequate consideration.

Of the Eleven factors, the Trustee only offered evidence on three and only proved that the transfer was to an insider and that Horne retained possession as a tenant after the transfer. These two factors are insufficient to support a circumstantial inference of actual fraud.

Trustee's Duty

This case presented a difficult dilemma for the Trustee. He was presented with sworn testimony of the debtor, in affidavit form, and amended schedules signed under penalty of perjury, that the debtor had conveyed real estate for a fraudulent purpose. He had no choice but to pursue this action. However, his only witness, the debtor, was not his client and he had no control over what she might say in the serious atmosphere of a federal courtroom. The Trustee and his counsel performed their duty in a professional manner, but had to deal with a debtor that seems to have difficulty focusing on the truth.

Conclusion

The Trustee failed to meet his burden of proof on either theory to avoid the title of McGinnis under the Uniform Fraudulent Transfer Act as enacted in Nebraska. Since the debtor has no right or interest in the real property in question, the Trustee's request for turnover must be denied.

Separate journal entry to be entered.

DATED: February 26, 1998

BY THE COURT:

/s/ Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

Copies faxed by the Court to:

BECKER, ROBERT 393-2374

Copies mailed by the Court to:

Jay Ferguson, 1823 Harney #1013, Omaha, NE 68102
United States Trustee

Movant (*) is responsible for giving notice of this journal entry to all other parties (that are not listed above) if required by rule or statute.

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEBRASKA

IN THE MATTER OF:)	
)	
LINDA SUSAN HORNE,	)	CASE NO. BK97-80261
	)	A97-8070
<u>DEBTOR(S)</u>)	
	)	CH. 7
THOMAS D. STALNAKER,	)	Filing No.
Plaintiff(s))	
vs.	)	<u>JOURNAL ENTRY</u>
)	
JANET L. MCGINNIS,	)	DATE: February 26, 1998
	)	HEARING DATE: January
<u>Defendant(s)</u>	)	20, 18

Before a United States Bankruptcy Judge for the District of Nebraska regarding the adversary complaint.

APPEARANCES

Robert Becker, Attorney for Trustee
Jay Ferguson, Attorney for Janet L. McGinnis

IT IS ORDERED:

The Trustee's request for turnover is denied. See Memorandum entered this date.

BY THE COURT:

/s/ Timothy J. Mahoney
Timothy J. Mahoney
Chief Judge

Copies faxed by the Court to:
BECKER, ROBERT 393-2374

Copies mailed by the Court to:
Jay Ferguson, 1823 Harney #1013, Omaha, NE 68102
United States Trustee

Movant (*) is responsible for giving notice of this journal entry to all other parties (that are not listed above) if required by rule or statute.