The New Bankruptcy Act: A Revision of Section 67d-The Death of a Dilemma

Steph McEvily
THE NEW BANKRUPTCY ACT:
A REVISION OF SECTION 67d—
THE DEATH OF A DILEMMA*

A primary goal of bankruptcy law is to secure fair distribution of a bankrupt's assets among its creditors.1 This goal may be frustrated if a debtor satisfies one debt prior to another, or conceals or disposes of property to deprive creditors of their rights.2 A debtor may prefer, for example, to pay one creditor—a relative or someone with whom the debtor wants to continue to do business—over other, less favored creditors. Or a debtor may wish to avoid all debts and attempt to convey his or her property to prevent the trustee from acquiring title.

To prevent these inequities, the Bankruptcy Act3 (the Act) provides two methods for a trustee to recapture assets which are unfairly transferred: section 60, which applies to voidable preferences;4 and section 67d, which applies to fraudulent conveyances.5

* The author wishes to thank Professor Alan Resnick of the Hofstra University School of Law for his advice and support throughout the preparation of this Note.

1. Wilson v. City Bank, 84 U.S. (17 Wall.) 473, 480 (1873) ("The primary object [of a bankruptcy law] is to secure a just distribution of the bankrupt's property among his creditors... ").

2. See text accompanying notes 24 & 48 infra.


   (a)(1) A preference is a transfer, as defined in this title, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or suffered by such debtor while insolvent and within four months before the filing by or against him of the petition initiating a proceeding under this title, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class.

   (b) Any such preference may be avoided by the trustee if the creditor receiving it or to be benefited thereby or his agent acting with reference thereto has, at the time when the transfer is made, reasonable cause to believe that the debtor is insolvent.

   (2) Every transfer made and every obligation incurred by a debtor within one year prior to the filing of a petition initiating a proceeding under this title by or against him is fraudulent (a) as to creditors existing at the time of such transfer or obligation, if made or incurred without fair consideration by a debtor who is or will be thereby rendered insolvent, without re-
The trustee must prove eight elements to recapture the debtor's assets as a "preferential transfer." Most significant are the requirements that the transfer satisfy an antecedent debt and take place within four months of the filing of the bankruptcy petition. The debtor's property may be recovered as a "fraudulent conveyance" if the debt was satisfied within one year of the declaration of bankruptcy, and either (1) the debtor actually intended to defraud other creditors by making the transfer, or (2) if no such intent existed, there was no fair consideration because the creditor who was paid lacked good faith. In the latter case fraud will be presumed.

The different elements required by each provision underscore a distinction between the two sections long recognized as important. Unfortunately, the fair-consideration requirement included within the definition of fraudulent conveyances has blurred this distinction. The requirement was designed to prevent depletion of the bankrupt's estate, either through improvidence or with the intention of depriving creditors or favoring friends, shortly be-

---

6. For the text of the statutory provision concerning preferential transfers, see note 4 supra.
8. For the text of the statutory provision concerning fraudulent conveyances, see note 5 supra.
11. Bankruptcy Act § 67d(1)(e), 11 U.S.C. § 107(d)(1)(e) (1976), provides: [Consideration given for the property or obligation of a debtor is "fair" (1) when, in good faith, in exchange and as a fair equivalent therefor, property is transferred or an antecedent debt is satisfied, or (2) when such property or obligation is received in good faith to secure a present advance or antecedent debt in an amount not disproportionately small as compared with the value of the property or obligation obtained.
12. See Bullard v. Aluminum Co. of America, 468 F.2d 11 (7th Cir. 1972); Gilmer v. Woodson, 332 F.2d 541 (4th Cir. 1964); Nicklaus v. Peoples Bank & Trust Co., 258 F. Supp. 482 (E.D. Ark. 1965), aff'd, 369 F.2d 683 (8th Cir. 1966).
fore filing the bankruptcy petition. To be "fair," consideration given in exchange for the transfer made or obligation incurred by the debtor must be an equivalent value given in good faith. The subjectivity and vagueness inherent in the concept of good faith has produced inconsistent decisions and confusion—and enabled one court to label a transfer a fraudulent conveyance to nullify a preference not voidable under the statute.

Section 548 of the Bankruptcy Reform Act of 1978 (the New Act) attempts to clarify this distinction by omitting the subjective requirement of fair consideration. It contains essentially the same elements as section 67d(2) of the present Act, but includes meaningful changes. Initially, it reverses the order of the elements of a fraudulent conveyance, placing first, rather than last, the requirement of actual intent of the debtor-transferor to defraud creditors. The more significant alteration is the substitution of "reasonably equivalent value" for "fair consideration." "Value" is defined as

15. See Bullard v. Aluminum Co. of America, 468 F.2d 11 (7th Cir. 1972).

Fraudulent transfers and obligations .

(a) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor—

(1) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer occurred or such obligation was incurred, indebted; or

(2) (A) received less than a reasonably equivalent value in exchange for such transfer or obligation; and

(B) (i) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;

(ii) was engaged in business, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital; or

(iii) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.
“property or satisfaction or securing of a present or antecedent debt of the debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor.”

Thus, nowhere in the New Act do fair consideration or good faith appear. Fraud can still be presumed, but only on the basis of the value exchanged, regardless of the existence of good faith. This modification should eliminate judicial confusion by providing a more objective standard—limiting the latitude formerly accorded the trier of fact, and restoring the distinction between preferential transfers and fraudulent conveyances.

**Fraudulent Conveyances**

Although the roots of bankruptcy law reach back to the fourteenth century, when Italian city-states had well-developed procedures for dealing with defaulting debtors, our notions of fraudulent conveyances are traced back to the Statute of Elizabeth, enacted in England in 1570. It declared that conveyances “to the end, purpose and intent, to delay, hinder or defraud creditors . . . of their just and lawful . . . debts” were “clearly and utterly void, frustrate, and of none effect.” Thus the law of fraudulent conveyances was not developed primarily to further the goal of equitable distribution, rather it was to foil debtors intending to defraud creditors. Early American enactments, as well as present day codifications, repeated both the words and sentiment.

The Uniform Fraudulent Conveyance Act clarified and broadened the scope of the statutes that descended from the Statute of Elizabeth. The draftsmen of the Chandler Act incorporated the

---

23. An Act Against Fraudulent Deeds, Alienations, &c., 1570, 13 Eliz., c. 5, §§ 1, 2.
24. J. Maclachlan, supra note 21, at 275.
essential portions of the Uniform Fraudulent Conveyance Act into the Bankruptcy Act. In addition, they added three new clauses, now found in section 67d(2), which permit a presumption of fraud in three situations when the transfer is made “without fair consideration.” Section 67d(1)(e) defines consideration as fair:

(1) when, in good faith, in exchange and as a fair equivalent therefor, property is transferred or an antecedent debt is satisfied, or (2) when such property or obligation is received in good faith to secure a present advance or antecedent debt in an amount not disproportionately small as compared with the value of the property or obligation obtained.

Both good faith and a fair equivalent value are elements of this definition. Good faith is a question of fact, its existence determined by the circumstances of each case. As a result, the term has never been adequately defined, because it lacks a predictable base from which to determine its presence or absence.

28. 4 W.M. COLLIER, supra note 14, ¶ 67.23, at 475 n.6. See also In re Vanity Fair Shoe Corp., 84 F. Supp. 533, 534 (S.D.N.Y. 1949), aff’d, 179 F.2d 766 (2d Cir. 1950).
29. Former section 67e, Bankruptcy Act of July 1, 1898, ch. 541, § 67e, 30 Stat. 544 (current version at 11 U.S.C. § 107(d)(2) (1976)), provided:

That all conveyances, transfers, assignments, or incumbrances of his property, or any part thereof, made or given by a person adjudged a bankrupt under the provisions of this Act subsequent to the passage of this Act and within four months prior to the filing of the petition, with the intent and purpose on his part to hinder, delay, or defraud his creditors, or any of them, shall be null and void as against the creditors of such debtor, except as to purchasers in good faith and for a present fair consideration; and all property of the debtor conveyed, transferred, assigned, or encumbered as aforesaid shall, if he be adjudged a bankrupt, and the same is not exempt from execution and liability for debts by the law of his domicile, be and remain a part of the assets and estate of the bankrupt and shall pass to his said trustee, whose duty it shall be to recover and reclaim the same by legal proceedings or otherwise for the benefit of the creditors.

32. Cohen v. Sutherland, 257 F.2d 737, 742 (2d Cir. 1958); see 4 W.M. COLLIER, supra note 14, ¶ 67.33, at 506.
34. See Bullard v. Aluminum Co. of America, 468 F.2d 11, 13 (7th Cir. 1972); Holahan v. Henderson, 277 F. Supp. 890, 899 (W.D. La. 1967), aff’d, 394 F.2d 177 (5th Cir. 1968).
35. 4 W.M. COLLIER, supra note 14, ¶ 67.41, at 589.
As to whose "good faith" should be examined, one court has asserted: "The act includes in the definition of fair consideration the element of good faith on the part of the transferee of the property in question,"\textsuperscript{36} since the transferee can best assess the fairness of the situation.\textsuperscript{37} The language of the Act's definition of fair consideration supports this interpretation: "[C]onsideration given for the property or obligation of a debtor is 'fair' (1) when, in good faith in exchange and as a fair equivalent therefor, property is transferred or an antecedent debt is satisfied, or (2) when such property is received in good faith to secure a present advance or antecedent debt . . . ."\textsuperscript{38} The definition refers to that which is given for property of the debtor, and requires good faith by the creditor-transferee when conveying property in exchange for property of the debtor-transferor, or when receiving property of the debtor to secure an advance or antecedent debt.

The fair-equivalent requirement of fair consideration varies according to the nature of the property involved in the transaction.\textsuperscript{39} Substantial disparity between the values of the property exchanged may indicate bad faith.\textsuperscript{40}

Thus, in determining the presence of good faith, and of fair consideration, considerable latitude is given to the trier of fact.\textsuperscript{41} This latitude, which results from the lack of definition of good faith, has produced inconsistent outcomes and, consequently, a blurring of the distinction between preferential and fraudulent transfers.\textsuperscript{42}

**Preferences**

A preference occurs when a debtor transfers property to a creditor in satisfaction of an existing debt, thereby favoring that creditor by precluding other creditors from obtaining the property. There is nothing inherently wrong with such a transfer; thus, it may be avoided only if all the elements contained in section 60 are present.\textsuperscript{43} The law of preferences has been described as the

\textsuperscript{36} In re Messenger, 32 F. Supp. 490, 494 (E.D. Pa. 1940).
\textsuperscript{37} G. Glenn, The Law of Fraudulent Conveyances 395 (1931).
\textsuperscript{39} J. MacLachlan, supra note 21, at 271.
\textsuperscript{40} See id.
\textsuperscript{41} See Mayo v. Pioneer Bank & Trust Co., 270 F.2d 823, 829-30 (5th Cir. 1959).
\textsuperscript{42} See cases cited note 12 supra.
\textsuperscript{43} For the text of the provisions concerning preferential transfers, see note 4 supra.
single greatest contribution of the Bankruptcy Act to the field of commercial law, because it weakens inducements to negotiate preferential transfers with insolvent debtors. Daniel Webster recognized its importance in the earliest bankruptcy laws: "[T]he right of preference is the foundation upon which the structure [of unsound credit] rests!" In addition to providing a barrier to the business disruptions caused by aggressive collection, the preference law attempts to afford an adequate remedy to less favored creditors who have no recourse under state law: "The object of prohibiting preferences is to prevent favoritism, whether for secret benefit to himself or other reason, among a debtor's creditors, who ought, in fairness, to stand on the same footing." To achieve this goal, Congress enacted section 60, empowering the trustee to challenge transfers made up to four months prior to bankruptcy.

Section 60a defines a preference as a transfer of the debtor's property within four months of filing a petition for bankruptcy, to or for the benefit of a creditor, for or on account of an antecedent debt, that enables the creditor to get a greater percentage of his or her debt satisfied than other creditors in the same class. To avoid the preference, the trustee must prove that the preferred creditor had reasonable cause to believe that the debtor was insolvent at the time of transfer.

A transfer may be both a fraudulent conveyance and a voidable preference. This usually occurs when the debtor actually intends to defraud creditors; thus, fraud is not merely presumed because of a lack of good faith on the part of the creditor. In such cases, a trustee may proceed under section 60 or section 67d or

---

44. J. Maclachlan, supra note 21, at 284.
46. J. Maclachlan, supra note 21, at 3. The preference law is commonly referred to as the "grab" law.
47. Id. at 284.
50. Bankruptcy Act § 60a(1), 11 U.S.C. § 96(a)(1) (1976). Although the New Act will change the applicable time period, discussion of these changes is not relevant here.
51. Id.
52. Id.
both. Under section 60a, the elements of a preference must be established, including that the transfer occurred within four months of bankruptcy. The preference is not voidable unless the creditor or his or her agent had reasonable cause to believe that the debtor was insolvent at the time of transfer. Under section 67d(2)(d), a trustee must prove that the transfer occurred within one year of bankruptcy, and that the debtor intended to defraud creditors.

Although both provisions focus on the insolvency of the debtor and the creditor's belief or intent, they contain distinct requirements as well. A notable difference between the two sections is the applicable time limitation: four months for preferential transfers; one year for fraudulent conveyances. Thus, if the preferential transfer of an asset from a debtor to a creditor occurs outside the four month limitation, the transaction will not be considered a voidable preference. In addition, a preference involves satisfaction of an antecedent debt, while a fraudulent conveyance may concern a simultaneous exchange between the debtor and the creditor—the question being the consideration given.

Although transfers may be fraudulent as well as preferential, the two concepts are not necessarily connected. In fact, examination of the provisions of sections 60 and 67d demonstrates a wide difference between them: "[A]n intent to prefer is not to be confounded with an intent to defraud, nor a preferential transfer with a fraudulent one." An intent to prefer is not wrong in itself, but a preferential transfer may be avoided once the required elements are proved.

**IMPORTANCE OF THE DISTINCTION**

Courts have recognized the distinction between the requisite intent of the transferee for preferences and fraudulent conveyances since the formulation of bankruptcy laws. In the early case of *Coder v. Arts*, the mortgage in question effected a preference; however, it was not voidable, because neither the mortgagee nor his agent had reasonable cause to believe the debtor insolv-
vent. The trustee, upon failing to recapture the property as a voidable preference, proceeded as if it were a fraudulent conveyance. He argued that since a preference necessarily results in delaying, hindering, or defrauding creditors, the debtor must be presumed to intend such consequences; thus he maintained that the preference was voidable as a fraudulent conveyance. The Supreme Court rejected this reasoning, because a finding of actual intent to defraud was necessary to avoid a transfer under the applicable statute. The Court asserted that although preferences and conveyances are often "spoken of in such a way as to confuse one with the other," there is a definite distinction between them: Preferences are "not necessarily fraudulent," but "are set aside when made within four months, with a view to obtaining an equal distribution of the bankrupt's estate." In Van Iderstine v. National Discount Co., another early case, the trustee tried to avoid a conveyance because the transferee knew that the debtor intended a preference. Rejecting this argument, the Court explained that it is "not in itself unlawful to prefer." It articulated the differences between a preference and a fraudulent conveyance: "One is inherently and always vicious; the other is innocent and valid, except when made in violation of the express provisions of a statute. One is malum per se and the other is malum prohibitum,—and then only to the extent that it is forbidden.

Twenty years later in Irving Trust Co. v. Chase National Bank, the Second Circuit reemphasized the need for establishing actual intent of the debtor to defraud prior to finding a conveyance fraudulent. Again, the trustee did not succeed in persuading the court to convert a nonvoidable preference into a fraudulent conveyance:

The facts alleged show only a nonvoidable preference, and the additional allegation that the debtor intended to defraud his

63. Id. at 240.
65. 213 U.S. at 241.
66. Id. at 244.
67. Id. at 241.
68. Id.
69. 227 U.S. 575 (1913).
70. Id. at 582.
71. Id.
72. 65 F.2d 409 (2d Cir. 1933).
creditors, without showing how they were to be hindered or de-
frauded except as incidental to the preference, would not, in our
opinion, be sufficient to convert the transaction into a fraudulent
conveyance.\textsuperscript{73}

Thus the preference's necessary consequence of hindering and de-
laying creditors did not establish proof of the debtor's intent to de-
raud. The creditor bank that received the transfer in repayment of
a loan was not compelled to surrender the money.

\textit{Nicklaus v. Peoples Bank and Trust Co.}\textsuperscript{74} is a more recent
case decided under present section 67d. The defendant bank
learned that the value of the security it held for a loan to the bank-
rupt was less than the amount of the loan. It also discovered that
some bills of lading with drafts attached by the bankrupt corpora-
tion had been returned unpaid. The bank demanded payment on
the bankrupt's note and received a credit at his broker and a cash-
ier's check. The bankrupt had procured the check through credit
he had obtained from another bank by depositing spurious bills of
lading. The defendant bank had no notice that the bankrupt had
obtained this credit.\textsuperscript{75}

The funds could not be recovered as a preference, because four
months had lapsed since the transfer. However, the payment re-
ceived by the bank would have constituted a preference if it had
been made within four months of bankruptcy. Since the bank had
inquiry notice of the bankrupt's insolvency, the trustee argued that
it was charged with knowledge that the bankrupt could not
have obtained the payment without committing fraud.\textsuperscript{76} Under
these circumstances, according to the trustee, the bank could not
have been acting in good faith, and the satisfaction of the anteced-
ent debt lacked fair consideration.\textsuperscript{77}

The court refused to accept this reasoning, stating that "a pref-
erential payment to a creditor does not in itself constitute a fraudu-
 lent conveyance."\textsuperscript{78} The bank did not possess actual knowledge
that the bankrupt had committed fraud and the court would not in-
fer knowledge from the bank's notice of the debtor's insolvency.\textsuperscript{79}

\textsuperscript{73} \textit{Id.} at 412.
\textsuperscript{74} 258 F. Supp. 482 (E.D. Ark. 1965), \textit{aff'd}, 369 F.2d 683 (8th Cir. 1966).
\textsuperscript{75} \textit{Id.} at 484-85.
\textsuperscript{76} \textit{Id.} at 485.
\textsuperscript{77} \textit{Id.}
\textsuperscript{78} \textit{Id.} at 486.
\textsuperscript{79} \textit{Id.}

http://scholarlycommons.law.hofstra.edu/hlr/vol7/iss2/11
Since section 60 was not applicable, knowledge of the bankrupt's insolvency was irrelevant. Furthermore, the court did not construe fair consideration under section 67d(1)(e) to mean "a creditor does not act 'in good faith' in receiving a cashier's check and applying it to the satisfaction of antecedent debt merely because he suspects that the debtor making the payment is insolvent." While the court might have found bad faith if the bank had knowledge, or reasonable cause to believe, that the debtor had committed fraud, it refused to equate the knowledge of insolvency required to avoid a preference with the lack of good faith required to avoid a fraudulent conveyance.

Thus, although both sections of the Act promote equitable distribution, they do so in different ways. The law of preferences seeks to prevent favoritism among creditors by empowering a trustee to avoid a transfer which is not unlawful in itself. As defined in section 60a, a preference is not prohibited; it is only unlawful if made within the time period and under the conditions specified in section 60b. A fraudulent conveyance, however, contains no escape hatch, since it involves no effort to pay a valid debt. The debtor-transferor who conveys assets to defraud creditors is generally attempting to benefit only him- or herself. Due to the importance attached to preventing fraudulent conveyances, even if a transferee gives a fair equivalent value, and has no reason to suspect fraud, property transferred may be recaptured if the debtor intends to defraud creditors. On the other hand, a preferential transfer is not voidable if the transferee has no reason to suspect that the debtor is insolvent: It would be unfair to require an innocent transferee to forfeit property which was thought to be legally obtained.

**Bullard v. Aluminum Co. of America**

The blurring of the distinction between preferential and fraudulent transfers is illustrated in a Seventh Circuit case, *Bullard v. Aluminum Co. of America*. The subjective element of good faith required for fair consideration enabled the court to avoid, as a fraudulent conveyance, a transfer that was in reality a nonvoidable preference.

---

80. *See* note 11 *supra*.
81. 258 F. Supp. at 486.
82. *See* note 4 *supra*.
84. 468 F.2d 11 (7th Cir. 1972).
Alcoa, the defendant corporation, appealed a summary judgment which held that the transfer in question was fraudulent under section 67d(2)(a) of the Bankruptcy Act. Kritzer Radiant, the bankrupt corporation, was insolvent at the time of the transfer and owed Alcoa more than $46,000 on a note personally guaranteed by the president of Kritzer Radiant. Alcoa had received a judgment in state court against the president for the amount of the note. The transfer consisted of payment by Kritzer Radiant to Alcoa of fifty cents on the dollar in full satisfaction of the debt owed on the note. In addition to releasing the corporation from its obligation to pay the debt, Alcoa released the president of the corporation from the judgment against him.

After asserting that section 67d(2)(a), which deals with presumed fraud, is the applicable provision, the court formulated the issue: “[T]he question becomes, under the undisputed facts as set forth above, whether the transfer from Kritzer Radiant to Alcoa was for ‘fair consideration.’” Thus the court did not address whether the debtor actually intended the transfer to defraud creditors.

The court maintained that fair consideration requires both fair equivalent value and good faith; the existence of good faith depends on whether the transaction is made at arm’s length. Even if fair equivalent value were present, a transfer lacking good faith would be fraudulent. Considering the undisputed facts, and noting the relationship between the parties to the settlement, the court concluded that the transfer lacked fair consideration and thus was fraudulent. Citing United Towing Co. v. Phillips, the court found that transfers to benefit third parties are not made in exchange for fair consideration. Since the president of Kritzer Radiant “was released entirely and without any consideration on his part from a legally enforceable state court judgment against him,” the benefit ran to him, not to the corporation. Therefore, there

86. 468 F.2d at 12.
87. Id. at 12-13.
88. Id. at 13.
89. Bankruptcy Act § 67d(2)(d), 11 U.S.C. § 107(d)(2)(d) (1976), requires actual intent to defraud on the part of the debtor to avoid a conveyance as fraudulent.
90. Id. at 13-14.
91. 242 F.2d 627 (5th Cir.), cert. denied, 355 U.S. 861 (1957).
92. 468 F.2d at 14.
was no fair consideration for the transfer, rendering it fraudulent under section 67d(2)(a) of the Act.  

An examination of the Seventh Circuit's analysis reveals that there was, in fact, fair consideration for the transfer. The requirement of good faith to establish fair consideration enabled the court to void a nonvoidable preference by describing it as a fraudulent conveyance after manipulating the facts to find a lack of good faith.

Fair consideration requires both fair equivalent value and good faith. The definition itself, as well as precedent, indicates that it is the good faith of the transferee that is at issue. The court in Bullard failed to indicate whether its decision was premised on Alcoa's lack of good faith, or its failure to give fair equivalent value. Although the court implied that its holding was based, in part, on the presence of bad faith, it refused to focus specifically on Alcoa's intent, asserting that the section of the Act involved rendered the transfer fraudulent "irrespective of the intent of the parties to the transaction." If Alcoa's intent had been examined, the court would have found good faith. The existence of good faith is determined at the time of transfer of the debtor's assets to the creditor; the transaction occurred almost a year before the petition of bankruptcy was filed. There is no evidence that Alcoa knew or could have known at that time that Kritzer Radiant would go bankrupt. Although correspondence between Alcoa and its attorneys indicates that Alcoa was aware of possible financial difficulties, mere suspicion of insolvency does not constitute bad faith. Suspicion or knowledge of insolvency is not suspicion or

93. Id.
94. See text accompanying note 14 supra.
95. See text accompanying note 38 supra.
97. The court merely stated that on the facts it agreed with the district court that "the transfer here was a fraudulent one within the meaning of § 67(d)(2)(a) of the Bankruptcy Act." 468 F.2d at 14.
98. Id.
99. Id. at 14.
100. Id.
102. 468 F.2d at 13.
103. In Nicklaus v. Peoples Bank & Trust Co., 258 F. Supp. 482 (E.D. Ark. 1965), aff'd, 369 F.2d 683 (8th Cir. 1966), the court stated: "I do not believe that un-
knowledge of fraud.\textsuperscript{104} Since bankruptcy was not a certainty when the agreement was made, Alcoa's release of both the corporation and its president for only half the debt owed left Kritzer Radiant with more funds with which to alleviate its financial difficulties. From this perspective, at least, Alcoa was not acting in a bad faith.

Other common law interpretations support the conclusion that Alcoa acted in good faith. In \textit{Gilmer v. Woodson},\textsuperscript{105} under circumstances similar to those in \textit{Bullard}, the Fourth Circuit stated: 

"[G]ood faith cannot be said to be lacking unless the transferee knowingly participated in the debtor-transferor's purpose to defeat other creditors or lacked good faith in valuing the property exchanged."\textsuperscript{106} In \textit{Bullard} whether Kritzer Radiant intended to defeat creditors through the transfer was not an issue in the case. Since this purpose was never established, Alcoa cannot be said to have participated in such a scheme. The transferee's valuation of the property he exchanged seemed to be in good faith: An agreement in accord and satisfaction is a recognized method of settlement among creditors and debtors.\textsuperscript{107} The transfer was not indicative of lack of good faith by the transferee in valuing the property exchanged, since settling for fifty cents on the dollar represents a customary settlement between a creditor and an insolvent debtor; thus, there was no substantial disparity between the values of the property exchanged.\textsuperscript{108}

In \textit{Holahan v. Henderson},\textsuperscript{109} the Fifth Circuit ruled that consideration is fair "if it was received [by the creditor] in good faith for an antecedent debt."\textsuperscript{110} It is ironic that the court in \textit{Bullard} ignored this definition of fair consideration, refusing to consider the transferee's good faith, yet cited \textit{Holahan} for the assertion that

\begin{footnotes}
\item[104] Id. Although a creditor's suspicion or knowledge of insolvency is insufficient to avoid a fraudulent conveyance, "reasonable cause to believe that the debtor is insolvent" is necessary to avoid a preference. Bankruptcy Act § 60b, 11 U.S.C. § 96(b) (1976).
\item[105] 332 F.2d 541 (4th Cir. 1964).
\item[106] Id. at 547 (citation omitted).
\item[107] See, e.g., Geeslin v. Knight Bros., Inc., 554 F.2d 865 (8th Cir. 1977); Engbretson v. Seiberling, 122 Iowa 522, 98 N.W. 319 (1904); Sigler v. Sigler, 98 Kan. 524, 158 P. 864 (1916).
\item[108] See J. MACLACHLAN, supra note 21, at 271.
\item[109] 277 F. Supp. 890 (W.D. La. 1967), aff'd, 394 F.2d 177 (5th Cir. 1968).
\item[110] Id. at 897 (emphasis added) (footnote omitted).
\end{footnotes}
good faith depends on whether the "transaction carries the earmarks of an arms-length bargain."\textsuperscript{111}

In addition, the intent referred to in section 67d(2)(a)—irrelevant to operation of the section—is the actual intent of the debtor, not, as the court concluded, the intent of the creditor. Regardless of the debtor's intent, lack of fair consideration by the creditor will render the transfer fraudulent. But the intent of the creditor is very much an issue under this section. A transfer in which the creditor gives fair equivalent value can be fraudulent only if the creditor lacks good faith. The relationship between actual intent and fair consideration, as found in sections 67d(2)(a),(b), and (c), was appropriately described by the district court in \textit{In re Southern Land Title Corp.}:\textsuperscript{112} "The first three situations, from which fraud is conclusively presumed, regardless of actual intent, have one common prerequisite of an absence of 'fair consideration' to the debtor in return for his conveyance. Lack of proof that there was an absence of 'fair consideration' is fatal to the presumption . . . ."\textsuperscript{113}

The \textit{Bullard} court, on one hand asserted the necessity of good faith, and, on the other, refused to examine whether Alcoa had met this requirement. The court may have relied on the absence of fair equivalent value to conclude that no fair consideration was given; if it did, this reliance was misplaced. The value of the property exchanged was not an issue before the court. Furthermore, fair consideration is judged quantitatively with regard to the type of property in question, as well as to other circumstances.\textsuperscript{114} Under the circumstances as described by the court, an agreement in accord and satisfaction, settling for fifty cents on the dollar, is not the kind of price that should excite suspicion of bad faith. It has long been a practice for creditors, who fear that a debtor's financial difficulties will interfere with the collection of a debt, to settle for less than the contract price.\textsuperscript{115} Rather than indicating bad faith, forgiveness of half what actually is owed can be viewed favor-

\textsuperscript{111} 465 F.2d at 13 (quoting Holahan v. Henderson, 277 F. Supp. 890, 899 (W.D. La. 1967), aff'd, 394 F.2d 177 (5th Cir. 1968)).
\textsuperscript{113} Id. at 1062 (emphasis added) (citations omitted) (footnotes omitted).
\textsuperscript{114} Id. at 1063-64. See also Cohen v. Sutherland, 257 F.2d 737, 742 (2d Cir. 1958); J. MACLACHLAN, supra note 21, at 271.
ably. The creditor elects not to sue the debtor for the full contract price, relieving the debtor of an obligation at a loss to him- or herself. Furthermore, since it is not unlawful in itself to prefer, it should not be unlawful to be preferred by altering the terms of the contract to receive part payment of the debt in return for discharging the debtor, especially if satisfaction occurs more than four months prior to bankruptcy. Although this may enable some creditors to receive more than others, thereby resulting in an inequitable distribution of the debtor's assets, the statute's four-month preference period is a recognition that there is a point beyond which it becomes impracticable and undesirable to void transactions.

The Bullard court's conclusion that fair consideration was not given ultimately rests on the consideration having run to a third party. This argument seems to combine both the quantitative and good faith elements of fair consideration. Although one court has held to the contrary, transfers made for the benefit of third parties generally are not made for "fair" consideration. However, the consideration at issue in Bullard did not solely benefit the president of the bankrupt corporation. Indiana state law provided that a surety may recover from the principal any amount of the principal's debt it is forced to pay. If the president had not been released, he would have had a claim against Kritzer Radiant Corporation for the amount of the judgment against him. Thus, the only effective way to release the corporation was to release its president as well.

The court may have considered it bad faith for the president to use his position to have the corporation pay a debt for which he was guarantor. However, close corporations such as Kritzer Radiant generally are not granted loans unless an agent of the corporation accepts personal liability. And it is unfair to compel the president to pay off a note he guarantees for the benefit of the corporation when the holder of the note agrees to a settlement.

In addition, the existence of good faith generally depends on

117. 468 F.2d at 14.
118. See Williams v. Twin City Co., 251 F.2d 678, 681 (9th Cir. 1958).
120. See IND. CODE ANN. § 34-1-55-8 (Burns 1973).
whether there was "abuse of the provisions, purpose, or spirit of the chapter."121 An important purpose of the Act is to give debtors a fresh start.122 Certainly, Alcoa's action did not give Kritzer Radiant a "fresh start," but the settlement did offer Kritzer a reprieve by relieving the corporation and its president from half the payment due. Inclusion of the president in the settlement was central to the agreement's effectiveness: If the president had not been released from the judgment, he would have had a valid claim against Kritzer Radiant.

The above arguments illustrate that there was fair consideration for the agreement between the bankrupt corporation and Alcoa. An examination of the facts of the case reveals that the situation involved not a conveyance which was fraudulent for lack of fair consideration, but a preferential transfer which could not be avoided.

Essentially, the eight elements of a preference123 were present in Bullard, except for the four-month limitation.124 Payment of half the debt owed to Alcoa undoubtedly was made from Kritzer Radiant's funds125 and resulted in depleting the corporation's estate. The payment benefited the creditor, Alcoa, who received half, rather than none, of the debt due, and it satisfied an antecedent debt that was owed at the time of transfer.126 The court of appeals agreed with the district court that the corporation was definitely insolvent,127 asserting that "Alcoa acquired an advantage over the other creditors at a time when Alcoa was certainly aware of the precarious financial position of Kritzer Radiant."128 Thus, in addition to believing that Alcoa had received more than its ratable share, the court found that Alcoa had knowledge of Kritzer Radiant's insolvency. The court stated that Alcoa possessed Kritzer Ra-

122. The Supreme Court described this purpose of the Act in Local Loan Co. v. Hunt, 292 U.S. 234 (1934): "One of the primary purposes of the Bankruptcy Act is to 'relieve the honest debtor from the weight of oppressive indebtedness and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.'" Id. at 244 (quoting Williams v. United States Fidelity & Guar. Co., 236 U.S. 549, 554-55 (1915)).
123. For a discussion of these elements, see Johnson, A Primer to Voidable Preferences, 70 COM. L.J. 128 (1965).
124. For the text of the statutory provision concerning preferential transfers, see note 4 supra; text accompanying notes 51 & 52 supra.
125. 468 F.2d at 12.
126. Id.
127. Id. at 13.
128. Id. at 14.
diant’s financial statement, which reflected its negative net worth. Furthermore, it quoted from correspondence between Alcoa and its attorneys that indicated Alcoa’s awareness of the possibility that Kritzer Radiant would go bankrupt. It appears the court deemed Alcoa’s knowledge of Kritzer Radiant’s insolvency and its receipt of more than its ratable share—both elements required for a preference but not for a fraudulent conveyance—to be evidence of Alcoa’s lack of good faith.

Using the Nicklaus court’s interpretation of fair consideration, the court in Bullard would have decided against the trustee. Alcoa’s knowledge of Kritzer Radiant’s insolvency, presumed from Alcoa’s possession of the financial statement and Alcoa’s letter to its attorneys, would have been irrelevant. If the Bullard court had conceded that awareness of the debtor’s insolvency is not indicative of the creditor’s bad faith, it could have maintained the distinction between sections 60 and 67d—as the Nicklaus court did.

Seven of the eight elements of a preference were present in the transfer, but because the transaction occurred more than four months before bankruptcy, the court was unable to treat it as a voidable preference. However, the vagueness inherent in the term “good faith,” and the lack of definition supplied by the statute, enabled the court to conclude that Alcoa’s presumed knowledge of Kritzer Radiant’s insolvency was indicative of a lack of good faith. The court did not base its holding on Alcoa’s knowledge of insolvency, since such knowledge is insufficient to avoid a conveyance as fraudulent. Instead, the court asserted that consideration given to the third-party president, rather than to the transferor-corporation, constitutes evidence of a lack of fair consideration, thereby rendering the transaction fraudulent.

The requirement of good faith in the definition of fair consideration, and the absence of either a statutory or uniform case law definition of good faith, permitted the Bullard court to reach its conclusion. Because the court believed that Alcoa in fact lacked good faith, it utilized its discretion to interpret the facts and arrive at what it considered a just result.

129. Id. at 13.
130. See text accompanying notes 74-81 supra.
131. 468 F.2d at 14.
133. The Bullard court reasoned: “Since transfers made to benefit third parties are not considered as made for ‘fair’ consideration, we agree that on these facts,
The definition of fair consideration evidently so confused the court that it was unable to articulate whether the benefit to the third party rendered the transfer fraudulent for lack of good faith or fair equivalent value. The court discussed the necessity for good faith, and then asserted that section 67d(2)(a) renders a transfer fraudulent "irrespective of the intent of the parties to the transaction." 

By omitting fair consideration from the definition of a fraudulent conveyance, section 548 of the New Act should prevent this kind of reasoning and confusion. The substitution of "reasonably equivalent value"--with no mention of good faith--should provide a more objective standard. Although a question of fact will remain in each case, precedents defining reasonably equivalent value should develop more easily, since, unlike good faith, the term is generally quantifiable.

If the court in Bullard had analyzed only the quantitative element of the settlement between Alcoa and Kritzer Radiant, it would not have become embroiled in whether Alcoa's knowledge of the debtor's insolvency represented lack of good faith. Consequently, it could have relied on the accepted practice of settlements in accord and satisfaction of debts, decided that the debtor had received a "reasonably equivalent value in exchange for [the] transfer," and maintained the distinction between voidable preferences and fraudulent conveyances.

THE NEW PROVISION

Section 548(a) of the New Act contains elements similar to those of section 67d(2) for establishing a fraudulent conveyance. However, there are significant changes that relate to the problem discussed above.

which are not disputed by the defendant, the transfer here was a fraudulent one within the meaning of § 67d(2)(a) of the Bankruptcy Act." 468 F.2d at 14 (citation omitted).

134. Id. at 13.
135. Id. at 14.
138. Id.
Most notably, it is no longer necessary to address fair consideration in determining whether fraud should be presumed; the term has been replaced by the requirement of reasonably equivalent value. The substitution of reasonably equivalent value for section 67d(1)(e)'s fair consideration should allow the trier of fact less latitude, because it demands that this more objective standard combine with one of the other necessary conditions before fraud can be presumed.

Section 548(a) retains the one year statute of limitations. In addition, it requires either actual, as opposed to constructive, fraud, or receipt of less than reasonably equivalent value and one of three other conditions: Insolvency, a business left with unreasonably small capital, or the intent or belief of the debtor that he or she will incur debts beyond his or her ability to pay.141

Section 548(a)(2) sets out essentially the same provisions as section 67d(2).142 An important change is the reversal of the order of the elements. The standards contained in section 67d(2) appear to have been arranged in decreasing order of objectivity.143 The last clause adheres most closely to the Statute of Elizabeth—which refers to the transferor's subjective intent to hinder, delay, or defraud creditors—while the other clauses simply codify the case law that arose under the Statute.144 The order in which the standards are set forth in section 548(a) indicates an intention to return to the roots and purpose of the original doctrine.

The law of fraudulent conveyances in bankruptcy was not developed primarily to promote general equitable distribution.145 It is based on the view that a "wicked thing" has been done.146 A debtor either has meant to defraud a creditor, or has acted so recklessly in transferring his or her property without consideration (now reasonably equivalent value) that fraudulent intent should be inferred.147 This purpose is more apparent in the language of section 548(a) than that of section 67d(2). Defining a fraudulent trans-

---

140. See note 16 supra and accompanying text.
141. See note 16 supra.
143. J. MACLACHLAN, supra note 21, at 270.
144. Id. at 275. See text accompanying notes 22-25 supra.
145. J. MACLACHLAN, supra note 21, at 275. See text accompanying notes 22-25.
146. Hartman, supra note 22, at 72.
147. Id.
fer primarily as one in which the debtor actually intends to defraud, and secondarily as one in which certain conditions, including receipt of less than equivalent value, are present, puts a different emphasis on the elements. This emphasis conforms with the goals of the original statute.

CONCLUSION

The replacement of section 67d(2) with section 548(a) of the New Act will alleviate judicial confusion and promote uniformity. The purpose behind requiring fair consideration—preventing depletion of the bankrupt’s estate by improvidence or favoritism immediately preceding bankruptcy—will not be frustrated. Moreover, section 548(a) adheres to the intent of Congress to maintain the distinction between preferences and fraudulent conveyances—between transfers which are malum prohibitum and those which are malum per se.

Steph McEvily

148. See text accompanying note 13 supra.
149. See Coder v. Arts, 213 U.S. 223, 243 (1909) ("... Congress must be presumed to have intended by the introduction of § 67e to require a surrender only of such transfers as would have been fraudulent at common law... ").