

RESOURCES

North Carolina Fraudulent Transfer Act Hopefully Soon to be Amended and Called Voidable Transactions Act

In the current legislative session of the North Carolina General Assembly, it is anticipated that amendments to the North Carolina Fraudulent Transfer Act will be enacted to make long needed changes to that statute.

North Carolina's Fraudulent Transfer Act, codified in Article 3A of Chapter 39 of the General Statutes, is based upon the Uniform Fraudulent Transfer Act that was promulgated by the Uniform Law Commission in 1984 and enacted in 43 states, including North Carolina, the District of Columbia and the U.S. Virgin Islands. That act replaced the very similar Uniform Fraudulent Conveyance Act, which was promulgated in 1918 and remains in force in two states (New York and Maryland) as of 2014, and was drafted to make it more consistent with the Bankruptcy Code which was enacted in 1978.

Last year, the Uniform Law Commission promulgated 2014 amendments to the Uniform Fraudulent Transfer Act which are the first made to the act since its original promulgation. The amendments address narrowly-defined issues and are not a substantive revision. The principal amendments are as follows:

- **Name Change.** The amendments change the title of the act to the "Uniform Voidable Transactions Act". That change is not a change of substance, but one to recognize that the original title of the act, though sanctioned by historical usage, has always been misleading in two respects. One, fraud is not, and never has been, a necessary element of a claim under the act. And, second, the act has always applied to the incurrence of obligations (whether by loan, guaranty or the like) as well as to transfers of property.
- **Choice of Law.** The amendments add, for the first time, a choice of law for claims made under the act. That choice of law is the debtor's location at the time the transfer is made or the obligation is incurred. An individual debtor is located at the individual's principal residence. A debtor that is a corporation, limited liability company or partnership is located at its place of business if there is only one place of business, and at its chief executive office if there is more than one place of business.
- **Evidentiary Matters.** New provisions add uniform rules allocating the burden of proof and defining the standard of proof with respect to claims and defenses under the act. Generally, the burden of proof on asserting a claim is on the creditor and the standard of proof is the preponderance of the evidence, and not the higher standard of clear and convincing evidence.
- **Deletion of Special Definition of "Insolvency" for Partnerships.** Under the act, a debtor is "insolvent" if, at a fair valuation, the sum of the debtor's debts is greater than the sum of its assets. The act as originally written had a special definition of "insolvency" applicable to partnerships that added to the sum of the partnership's assets the net worth of each of its general partners. The amendments delete that special definition with the result that a partnership will be subject to the general definition. This change is to recognize there are some partnerships, like limited liability partnerships, for whose debts general partners are not generally liable, and to eliminate the disparate treatment of including the net worth of general partners within the definition of "insolvency", but not giving similar treatment to a third party guarantor of the partnership's debts.
- **Defenses.** The amendments make several refinements to the defenses available to a transferee or obligee:
 - As originally enacted, the act created a complete defense to an intentional fraudulent transfer claim if the transferee or obligee took in good faith and for a reasonably equivalent value. There is no equivalent defense in the Bankruptcy Code. The amendments add the additional requirement that the equivalent

value must be given to the debtor.

- As originally enacted, the defense for a subsequent transferee that took in good faith and for value, and for a subsequent transferee from that transferee, literally applied only to an action for a money judgment and not to recover the property transferred. The amendments provide, consistent with comparable provisions of the Bankruptcy Code, that the defense also applied to recovery of or from the transferred property or its proceeds, by levy or otherwise.
- As originally enacted, the act created a defense to a fraudulent transfer, other than an intentional fraudulent transfer, if the transfer resulted from an enforcement of a security interest in compliance with Article 9 of the Uniform Commercial Code. The amendments exclude from that defense acceptance of collateral in full or partial satisfaction of the secured debt (a remedy sometimes referred to as “strict foreclosure”).
- **Series Organization.** The amendments add a new section which provides that each “protected series” of a “series organization” is to be treated as a separate person for purposes of the act, even if the series is not treated as a legal entity for other purposes. This change responds to the emergence of the “series organization” as a common form of business organization.
- **Medium Neutrality.** In order to accommodate modern technology, the amendments replace references in the act to a “writing” with “record” and make related changes.
- **Official Comments.** Comments have been inserted explaining the provisions added by the amendments and the original comments and prefatory note have been supplemented and otherwise refreshed. It is anticipated that the amendments, once enacted, will contain a provision authorizing the Revisor of Statutes to print, as annotations to the act, all relevant portions of the official comments and all explanatory comments as the Revisor deems appropriate.
- **Effective Date.** The amendments will apply to transfers made or obligations incurred after their effective date. They will not apply to transfers made or obligations incurred before the effective date.

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