11 U.S.C. § 548(a)(2)
BFP v Resolution Trust Corp
Reasonably Equivalent Value
Land Sale Contract Forfeiture

Trevette R. Vermillion v. Stewart and Nancy Scarbrough
(In re Vermillion)

Case No. 693-62730-psh11
Adv. No. 93-6173-psh
Civil No. 95-6106-HO

11/8/95 District Court (J. Hogan) aff'g Higdon Unpublished

District Court affirmed the memorandum opinion of Judge Higdon published at 176 B.R. 563.

Held: Applying the policy considerations and holding of the Supreme Court's BFP v. Resolution Trust Corp. opinion, the court held that an Oregon land sale contract forfeiture procedure conducted pursuant to state law established reasonably equivalent value as a matter of law with respect to the fraudulent transfer provisions found at 11 U.S.C. § 548(a)(2).

E95-18(9)

U.S. BANKRUPTCY COURT
DISTRICT OF OREGON
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DISTRICT OF OREGON
EUGENE, OREGON

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF OREGON

TREVETTE R. VERMILLION,	)	
Plaintiff-Appellant,	)	Case No. 95-6106-HO
v.	)	ORDER
STEWART SCARBROUGH and NANCY SCARBROUGH	)	
Defendants-Appellees.	)	

This is an appeal from the bankruptcy court's order granting defendant's motion for summary judgment (#35). This court has jurisdiction under 28 U.S.C. § 158(a).

FACTS

In 1978, defendant Ms. Scarbrough purchased an interest in a land sale contract (the Hilderbrand/Bridges contract). She conveyed that interest to herself and co-defendant Stewart Scarbrough (the defendants) in 1980. In 1982, defendants assigned their interest and delegated their obligations under the Hildebrand/Bridges contract to Michael Grassmueck. Incident to this transaction, Grassmueck contracted to pay

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defendants $47,074.05 in installments with a balloon payment July 5, 1992 (the Scarbrough/Grassmueck contract). The Scarbrough/Grassmueck contract provided for forfeiture in the event of default.

In 1986, Grassmueck assigned his interest and delegated his obligations under both the Hildebrand/Bridges and Scarbrough/Grassmueck contracts to plaintiff. Plaintiff satisfied the Hildebrand/Bridges contract in 1988. However, plaintiff defaulted on the Scarbrough/Grassmueck contract, owing $40,873.57. On November 13, 1992, defendants recorded a declaration of forfeiture pursuant to ORS 93.905 *et seq.* The right to possess the forfeited property vested in defendants ten days later. Plaintiff stipulates that defendants complied with Oregon's statutory forfeiture procedure.

Plaintiff filed a chapter 11 bankruptcy petition on June 28, 1993. Shortly thereafter, plaintiff commenced this proceeding under 11 U.S.C. § 548 to recover the forfeited property. Plaintiff argued the forfeiture was an avoidable transfer because (1) the forfeiture occurred within one year of the filing of the bankruptcy petition, (2) plaintiff was insolvent at the time of the transfer or became insolvent as a result thereof, and (3) plaintiff received less than a reasonably equivalent value in exchange for the transfer. See 11 U.S.C. § 548(a)(2)(A). The bankruptcy court granted defendants' motion for summary judgment on the premise that

consideration received from a forfeiture conducted in conformance with state forfeiture law satisfies the bankruptcy code's requirement that transfers of property by insolvent debtors within one year of the filing of a bankruptcy petition be in exchange for a reasonably equivalent value.

DISCUSSION

This appeal presents an issue of law subject to de novo review. In re Daniels - Head & Associates, 819 F.2d 914 (9th Cir. 1987). That issue is whether the consideration received from a real estate forfeiture conducted in conformance with state law conclusively satisfies the bankruptcy code's requirement that transfers of property by insolvent debtors within one year prior to the filing of a bankruptcy petition be in exchange for a reasonably equivalent value. See 11 U.S.C. § 548(a)(2).

Section 548 of Title 11 of the bankruptcy code sets forth a debtor in possession's powers to avoid fraudulent transfers.[1] Under section 548, a debtor in possession may set

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[1] 11 U.S.C. section 548 provides in relevant part:

> "(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 voluntarily or involuntarily--
>
> "(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 was made or such obligation was incurred, indebted; or

aside not only transfers infected with actual fraud but also transfers infected with constructive fraud, including sales by insolvent debtors at unreasonably low prices. The issue here is whether a bankruptcy court must conduct a factual inquiry whether the satisfaction of a debt through a statutory forfeiture procedure constitutes reasonable consideration for the forfeited property.

The United States Supreme Court recently addressed this issue with regard to foreclosure sales. In re BFP, BFP v. Resolution Trust Corp., __ U.S. __, 114 S.Ct. 1757 (1994)(5-4 decision). In BFP, a five Justice majority held that the consideration received by a debtor pursuant to a foreclosure sale effected in compliance with state law is "reasonably equivalent" as a matter of law for purposes of section 548 of the bankruptcy code. Id., 114 S.Ct. at 1765. The Court stated that it was unwilling, absent clear statutory language, to infer that Congress intended to intrude into state foreclosure law by subjecting foreclosure sales to a case-by-

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

The trustee's powers are applicable to a debtor in possession through 11 U.S.C. section 1107.

The parties do not dispute that a forfeiture is a "transfer" for purposes of 11 U.S.C. section 548.

case reasonableness inquiry. Id., 114 S.Ct. at 1764-65. The court noted both the traditional co-existence of federal fraudulent transfer law and state foreclosure law as well as Congress's use of the words "reasonably equivalent value" instead of "fair market value." Id. 114 S.Ct. at 1761. Thus, the Court interpreted the language of section 548 as suggesting that Congress recognized the lower prices that may obtain in the context of restricted-market foreclosure sales. Id.

Plaintiff argues BFP is not applicable to forfeitures. Plaintiff contends that in a forfeiture proceeding, unlike a foreclosure sale, there is no "sale" involving a third party and, therefore, no compelling state interest in maintaining the security of title in forfeited property. Appellant's Brief (#44) at 6. Plaintiff also argues that state forfeiture law, which Oregon codified in 1985, lacks the time-honored, "peaceful co-existence" that foreclosure law has with fraudulent transfer law and that, therefore, Oregon has a lesser interest in the forfeiture process than in the foreclosure sale process. Appellant's Brief (#44) at 6. Accordingly, plaintiff argues bankruptcy courts must pursue a case-by-case factual inquiry into whether consideration received by a debtor as a result of a statutory forfeiture is reasonably equivalent to the value of the forfeited property.

Under plaintiff's interpretation, if the bankruptcy court found that the consideration received (which would generally

be the satisfaction of a mortgage or debt under a land sale contract) was too low, the forfeiture proceeding would be voided even though it complied with state law. The debtor would regain title to the previously forfeited property and incorporate the corresponding liability into his chapter 11 reorganization plan. The statutory forfeiture procedure would be for nought, as would any post-forfeiture transactions (beside good faith purchasers for value) affecting the foreclosed property's title.

Despite plaintiff's arguments to the contrary, the same considerations underlying the BFP majority opinion are present here. First, inquiry by federal courts as to the reasonableness of consideration in a foreclosure sale would undermine a state statutory scheme which carefully balances the rights of borrowers and creditors. See, BFP, 114 S.Ct. at 1763. The constructive fraud provisions of the bankruptcy code identify factual situations suggestive of fraud, for example a transfer to a close relative or an insider or a sale at an unreasonably low price. Out of respect for state legislation, however, the appearance of fraud should be tempered when a transfer is carried out according to state statutory guidelines. As discussed in BFP, federal inquiry into the fraudulent nature of conduct that conforms to state law would offend principles of comity. See id. 114 S.Ct. at 1763.

Second, the language of section 548 does not clearly

endorse judicial inquiry into the existing state forfeiture scheme. The court noted in BFP that "absent clearer textual guidance than the phrase `reasonably equivalent value' -- a phrase entirely compatible with pre-existing practice -- we will not presume such radical departure" from the co-existence of federal fraudulent transfer law and state foreclosure law. Id., 114 S.Ct. at 1764. Given the existence of the state forfeiture scheme, BFP's statutory interpretation of section 548 of Title 11 is directly relevant here.

Third, a state has an interest in maintaining "the general welfare of society [through] the security of the titles to real estate." BFP, 114 S.Ct. at 1764 (internal citations omitted). Although a third party may not be directly involved in a forfeiture proceeding, the foreclosing creditor certainly has an interest in obtaining secure title. Moreover, third parties such as lenders and title companies may have an indirect interest in the forfeiture procedure's capacity to facilitate secure title transfers.[2] Presumably, the Oregon legislature would not have enacted forfeiture laws if they were not needed.

State forfeiture law and federal fraudulent transfer law

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[2] The legislative history indicates that Oregon's forfeiture statute was supported by the "Oregon Land Title Association, The Oregon Association of Realtors, the Oregon Bar, and Legal Aid." Don Carter of McEwen, Gisvold, Rankin, and Stuart testified before the Senate Judiciary Committee that the bill "serves a beneficial purpose for sellers, buyers, and lenders on contract interests. . . ." Hearings on H.B. 2361 Before the Senate Judiciary Committee, June 7, 1985 (testimony of Don Carter).

together form a regulatory scheme which adequately balances the interests of both debtor and creditor. Obviously, state forfeiture laws benefits the creditor by facilitating collection of an obligation in default.

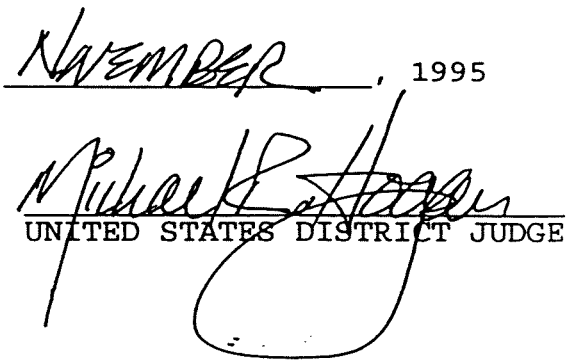
At the same time, a debtor who feels that the value of real property exceeds the liability remaining on the underlying land sale contract has several ways of protecting equity under Oregon forfeiture laws. During the ten days between the declaration of forfeiture and the vesting of title in the creditor, the debtor can cure a default by tendering past due payments and costs. ORS 93.915. The debtor might also realize any equity by refinancing or selling the property before title vests in the foreclosing creditor, then using the equity to cure the default.

Federal bankruptcy provides remedies for a trustee or debtor in possession. If the property is forfeited and title vests in the foreclosing creditor, an insolvent debtor in possession can void a forfeiture upon establishing that the debtor has an "actual intent to hinder, delay, or defraud." 11 U.S.C. § 548(a)(1). Moreover, in the event the debtor in possession can show that the forfeiture process was not in compliance with state law, the forfeiture will be voidable if the consideration received by the debtor was not "reasonably equivalent" to the value of the forfeited property. 11 U.S.C. § 548(a)(2).

The remedies provided under state forfeiture law and

federal bankruptcy law strike a careful balance not only for debtor and creditor relations, but also for state and federal relations. Under BFP and Title 11 to the United States Bankruptcy Code, there is no basis for federal courts to inquire whether consideration received as a result of statutory forfeiture of real property is reasonably equivalent to the value of the forfeited property. The order of the bankruptcy court (#35) granting defendants' motion for summary judgment is affirmed.

DATED this 8th day of NOVEMBER, 1995



UNITED STATES DISTRICT JUDGE

U.S. BANKRUPTCY COURT
DISTRICT OF OREGON
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UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

TREVETTE R VERMILLION

Plaintiff-Appellant,

v.

Civil No. 95-6106-HO
USBC No. 93-6173fra

STEWART SCARBROUGH AND
NANCY SCARBROUGH

Defendants-Appellees.

JUDGMENT

The order of the bankruptcy court (#35) granting defendants' motion for summary judgment is affirmed.

Dated: November 9, 1995.

Donald M. Cinnamond, Clerk

by Lea Force
Lea Force, Deputy

JUDGMENT **DOCUMENT NO:** _____

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