

DEBTOR/CREDITOR

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Mortgage Prepayment Thwarts Creditors

The federal appeals court in Richmond upheld the validity of a debtor's pre-bankruptcy asset protection planning.

The debtor received a large inheritance. He used the money to make a substantial prepayment of the mortgage on the home owned jointly with his wife as tenants by the entirety. This converted the cash inheritance owned individually to equity in a residence owned jointly.

The debtor filed a bankruptcy petition and claimed the residence as exempt from his creditors, because of the joint ownership with his wife. The bankruptcy trustee sought to recover the mortgage prepayment as a transfer of property from the debtor to the debtor's spouse without the debtor receiving anything of value in return.

The appellate court rejected the trustee's argument, because the debtor received a valuable reduction in his obligation to the bank. The court expressed concern that a contrary ruling would permit bankruptcy trustees to recover ordinary mortgage payments in virtually every bankruptcy case. The court might not have reached the same result had the debtor instead used the inheritance to repay a loan taken from his 401(k) plan, also an exempt asset.

Shaia v. Meyer (In re Meyer), 244 F.3d 352 (4th Cir. 2001).

Setoff Trumps Lien

A car dealership leased its facility from Chrysler Realty, an affiliate of Chrysler Corp. As security for the rent paid under the lease, the dealership assigned to Chrysler Realty any amounts due from Chrysler Corp. or its subsidiaries. No UCC-1 financing statement was filed by Chrysler Realty to reflect this assignment.

The dealership obtained floor plan financing from a bank. In order to secure the financing, the dealership gave

the bank a security interest in all receivables, including factory receivables owed by Chrysler Corp. The bank filed a UCC-1 financing statement to perfect its security interest.

The federal appeals court in Denver found that Chrysler Realty had the superior right to the receivables from Chrysler Corp. The court treated Chrysler Realty's right as a setoff, rather than an ordinary security interest. The bank's security interest in the borrower's accounts receivable was subject to any setoff rights against those receivables.

Commerce Bank v. Chrysler Realty Corp., 244 F.3d 777 (10th Cir. 2001).

No Discharge for Partner's Fraud

A partnership is liable for the fraudulent act of any general partner acting on behalf of the partnership. Each general partner is liable for the debts of the partnership, if the partnership assets are insufficient. A partner may thus become personally liable for the loss caused by another partner's fraud.

Adding insult to injury, a federal appeals court in New Orleans decided recently that a bankruptcy discharge is not available for debts obtained by fraud, even where the individual seeking the discharge was an innocent partner and did not commit the fraud.

Deodati v. M.M. Winkler Assoc. (In re M.M. Winkler Assoc.), 239 F.3d 746 (5th Cir. 2001).

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This newsletter is intended to inform its readers of developments in the area of debtor/creditor relations. It is not legal advice or a legal opinion regarding any specific matter. You should consult a lawyer regarding any questions relating to your particular situation.

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