



Tuition Payments by Parents as Fraudulent Conveyances

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Michael Traison- 312.860.4230

Jocelyn Lupetin- 516.296.9109

On January 18, 2019, we issued a client alert concerning the recovery of tuition payments as fraudulent conveyances. (<https://www.cullenllp.com/blog/court-to-college-disgorge-tuition-payments-by-insolvent-parents-made-for-adult-children/>). The case discussed in that alert, Geltzer v. Oberlin, Adv. Pro. Case No. 18-01015-MG, was issued by a bankruptcy court in the Southern District of New York.

Over the last few years, various courts have issued decisions addressing this topic.

On November 12, 2019, the Court of Appeals for the First Circuit issued the only Appellate decision on this question, to date. That Court reviewed and reversed a Massachusetts Bankruptcy Court decision.

Interestingly, the Massachusetts Bankruptcy Court had certified an appeal directly to the Court of Appeals without the usual intermediary step of appealing first to the District Court.

At first glance, the facts of In Re Palladino, D. Mass. Case No. 14-111482, are similar to those of other such cases - an 18-year-old child goes to college and her parents pay her tuition. Subsequently, the parents file for protection under Chapter 7 of the Bankruptcy Code and a Chapter 7 Trustee is appointed. The Trustee sues the college as a recipient of a fraudulent conveyance alleging that the transfer was made while the debtors were insolvent and that the debtors did not receive reasonably equivalent consideration in return. (One suspects that it was not unimportant to the Court of Appeals that the debtors were perpetrators of a Ponzi scheme for which they were criminally prosecuted and convicted.)

After a review of the relevant opinions, the determination of whether tuition payments made by insolvent parents on behalf of their adult children constitute fraudulent transfers may hinge upon a Court finding that the applicable state law requires the parent(s) to support the child beyond the age of majority, and/or whether there is another obligation existing in the specific situation which requires the parent(s) to pay the adult child's tuition, which would in turn constitute fair consideration.

Should there be another Court of Appeals ruling inconsistent with that of the First Circuit, the U.S. Supreme Court may be called upon to issue a final decision on this topic.

In the meantime, what can colleges and universities do to insulate themselves from the risk of having to disgorge tuition payments? While the frequency of this scenario may not warrant the taking of any protective measures at this time, one way to avoid allegations of fraudulent transfer would be to require that tuition payments be made by the individual student – the party receiving reasonably equivalent value in exchange for the transfer. While this condition would not prevent a Trustee from pursuing the college as a third-party recipient, the defenses to the trustee’s claim would be much stronger as the college would be in a position to argue that it is as a bona fide recipient of the tuition from the student without knowledge of the insolvency of the parent(s) or any creditor’s claim which may exist at the time of payment.

Please note that this is a general overview of developments in the law and does not constitute legal advice. Nothing herein creates an attorney-client relationship between the sender and recipient. If you have questions regarding these provisions, or any other aspect of bankruptcy law, please contact Michael Traison at [312.860.4230](tel:312.860.4230)

Practices

- Bankruptcy and Creditors' Rights

Attorneys

- Jocelyn E. Lupetin
- Michael H. Traison