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Uniform Voidable Transactions Act Signed into Law on December 6, 2019

December 9, 2019

Governor Cuomo signed legislation modernizing New York's 95-year-old fraudulent conveyance law and making it consistent with the Federal Bankruptcy Code and the laws of at least 44 other States. The Uniform Voidable Transactions Act ("UVTA") primarily clarifies the rights and remedies available to parties who have engaged in transactions with financially distressed entities.

The UVTA replaces New York's current fraudulent conveyance law (the "UFCA"), which was enacted in New York in 1925. The UFCA was terribly outdated and created conflicting and confusing case law that led to an inordinate amount of expensive litigation, often inuring to the benefit of those who transferred assets in order to put them beyond the reach of creditors.

The new UVTA clarifies the remedies available to creditors injured by a transfer of property or incurrence of an obligation (collectively, a "Transaction") that is (i) intentionally fraudulent because it was incurred with actual intent to hinder, delay or defraud creditors ("Intentionally Fraudulent") or (ii) constructively fraudulent because it was for less than a "reasonable equivalent" by a financially distressed debtor ("Constructively Fraudulent").

The UVTA takes effect 120 days after its approval by the Governor, or on or about April 4, 2020, and will apply only to Transactions made on or after that date.

Summary of Significant Changes

Choice of Law

The UVTA applies the law of the place where the debtor/transferor is located when the Transaction occurs to assess the voidability of the Transaction. An organization is located at its place of business, or if it has more than one place of business, at its chief executive office. Previously, the choice of law rules applied a multi-factor test that often resulted in expensive litigation and produced unpredictable results.

Burden of Proof

The UVTA makes the burden of proof of all claims and defenses a preponderance of the evidence. This changes the current application of a clear and convincing burden of proof required under the UFCA to establish Intentionally Fraudulent Transaction claims. The UVTA makes clear that these claims are ordinary civil actions –

not actions akin to common law fraud which has a heightened standard of proof. The UVTA expressly allocates the burden of proof on each element of the affirmative claim to the plaintiff and allocates the burden of proof on most elements of affirmative defenses to the defendant.

Statute of Limitations

The UVTA shortens the time to challenge a Transaction from 6 years to 4 years. The UVTA also includes a discovery rule for Intentionally Fraudulent Transactions that allows a Transaction to be challenged for one year after the Transaction was or could have been discovered, shortening the similar two-year discovery rule under the UCFA.

Partnership Insolvency

The UVTA removes a provision of the UFCA applicable only to partnerships that made every Transaction with a partner while the partnership is insolvent voidable as to creditors of the partnership. Partnerships are now subject to the same provisions of the UVTA as other entities.

Clarification of Insider Preferences

The UVTA adds a provision that renders voidable a Transaction with an insider on account of an antecedent debt (which generally constitutes a reasonable equivalent) while the debtor was insolvent if the insider had reasonable cause to believe that the debtor was insolvent. The existence of the reasonable equivalent value would not shield the insider from liability if the insider had such reasonable cause to believe the debtor was insolvent. Under the UFCA, on the other hand, a Transaction with an insider while the debtor was insolvent could similarly be avoided even if the insider had given a reasonably equivalent value—such as is generally the case when the insider's legitimate debt from the debtor is repaid by the Transaction. Case law under the UFCA deemed such Transactions to lack "good faith," one of the two requirements that had to be met to show fair consideration. This case law was dubbed the state insider preference law. Under the new UVTA, the same result can be achieved, but rather than through deeming the insider's transactions to lack good faith and thus lack fair consideration, the statute simply provides that insiders are liable so long as they had reasonable cause to believe that the debtor was insolvent when the debt was repaid.

Badges of Fraud

The UVTA eliminates a provision of the UFCA that made Transactions without fair consideration by a defendant during pending litigation voidable as to the plaintiff in that litigation (but not other creditors) if the plaintiff later obtained a judgment that was not satisfied. Under the UVTA the existence of such litigation is a "badge of fraud" that may be relied on, along with other factors, by all injured creditors (not just the plaintiff) to prove intent in an Intentionally Fraudulent Transaction claim.

Good Faith as Element of Fair Consideration

The UVTA eliminates a provision of the prior UFCA that allowed a Transaction to be avoided as Constructively Fraudulent if it was received in bad faith, even if the transferee provided equivalent value in exchange. Under the UVTA, a transferee's intent is now irrelevant as to the claim that a Transaction is voidable. The transferee's good faith is relevant only to the transferee's affirmative defense to a Transaction that has been found voidable based on the debtor's improper intent. The UVTA clarifies that the transferee must prove its good faith only when asserting this defense. The language of the UVTA mirrors that of the Bankruptcy Code.

Measure of Fair Consideration in Transfers of Secured Interests

The UVTA abandons as outdated the "disproportionality" test of fair value for potential avoidance of a grant of a security interest. The debtor's interest in the residual value of the encumbered property is adequately protected by existing laws governing secured interests.

Regularly Conducted Foreclosure of Real and Personal Property

Under the UVTA regularly conducted real property foreclosures and the exercise of remedies under Article 9 of the UCC with respect to personal property are protected from avoidance. Strict foreclosures, or situations where a secured creditor accepts property in satisfaction of a debt without a sale are still susceptible to avoidance.

Attorneys' Fees for a Creditor Who Obtains a Judgment Avoiding a Transaction

Finally, the UVTA allows courts to award attorneys' fees to a party who obtains a judgment setting aside a Transaction, whether it be Constructively Fraudulent or Intentionally Fraudulent. The UFCA permitted such fee awards only if a party established that a Transaction was Intentionally Fraudulent.

Conclusion

New York's adoption of the UVTA significantly changes and clarifies prior law governing debtor and creditor rights, giving parties more certainty when conducting business with financially distressed persons and entities.

If you have any questions about the new law, do not hesitate to contact any of us by phone or email:

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