

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

In Re:

CHAPTER 7

Gerald Butler

Bky. 3-93-4300

Debtor.

Molly T. Shields, Trustee Of The Estate Of
Gerald N. Butler,
Plaintiff,

Adv. 95-3-194

vs.

Norman Goldetsky and Percy Greenberg,
Defendants.

ORDER

This matter was heard on October 16, 1995, on motion by Defendants for dismissal pursuant to Rule 7012 Fed.R.Bankr.P. David S. Johnson appeared on behalf of Defendants Norman Goldetsky and Percy Greenberg; and, Marc J. Manderscheid appeared on behalf of Plaintiff Molly T. Shields, Trustee. The Court, having heard arguments, reviewed the pleadings and briefs of the parties, and otherwise being fully advised regarding the matter; now makes this ORDER pursuant to the Federal and Local Rules of Bankruptcy procedure.

I.

Defendants are the owners of certain real property commonly known as the Crown Iron Works Building, 1225-1333 Tyler Avenue N.E., Minneapolis, Minnesota ("Property"). On August 30, 1985,

Crown

Partners III ("Partners III") entered into a contract for deed with Defendants and their spouses for the purchase of the Property. The Debtor, Gerald N. Butler, was the general partner of Partners III, a Minnesota general partnership that was formed to purchase and own the Property.

The terms of the contract for deed required Partners III to make monthly payments to the Defendants, pay real estate taxes when due, insure the Property, and keep it in good condition and repair. Defendants, in turn, were obligated to make all payments on an underlying mortgage. Between August 30, 1985, and May 23, 1989, Partners III defaulted on the contract for deed numerous times by failing to make timely payments to Defendants, failing to maintain insurance, and failing to pay real estate taxes. As a result of these defaults, Defendants commenced proceedings to cancel the contract for deed on at least seven occasions. Prior to the last cancellation proceeding, the parties worked out agreements to

reinstate the contract.

Finally, on May 13, 1991, Defendants canceled the contract for deed with Partners III for the Property through a nonjudicial statutory cancellation procedure, pursuant to Minnesota Statute Section 559.21. The cancellation was, in all aspects, in accordance with applicable Minnesota law. Notice was provided to all interested parties, and the allowed time in which to cure the default lapsed without cure. Thereafter, the Defendants retook possession of the Property.

At the time of the cancellation, the Debtor, Gerald Butler, was the sole partner of Partners III. The balance due on the contract was approximately \$1,123,000. The value of the property was as high as \$2,200,000. Approximately two years later, on September 3, 1993, Gerald Butler filed for bankruptcy relief under 11 U.S.C. Chapter 7. Molly T. Shields was appointed trustee in the case.

On August 25, 1995, the Trustee filed this adversary proceeding, pursuant to 11 U.S.C. Section 544(b) and the Minnesota Fraudulent Transfer Act, M.S.A. Section 513.41 et. seq., to avoid the cancellation and recover the property. Shields alleges that the cancellation constituted a transfer of the Debtor's interest in the Property for less than reasonably equivalent value, and that the transaction is avoidable by her pursuant to M.S.A. Sections 513.44(a)(2) and 513.47(a)(1).

The Defendants seek dismissal of the adversary proceeding for failure to assert a justiciable claim, under F.R.Civ.P 12(b)(6)(1), alleging that: 1) the Trustee lacks standing to bring the action because the cancellation was against Partners III, and not against the Debtor; 2) the Trustee has not alleged sufficient specific facts regarding valuation of the Property and financial condition of the Debtor at the time of the cancellation; and, 3) that regularly conducted, noncollusive statutory cancellations of contracts for deed cannot, as a matter of law, constitute a fraudulent transfer under the Minnesota Fraudulent Transfer Act.

II.

11 U.S.C. Section 544(b) empowers a trustee to avoid prepetition transfers of a debtor that would otherwise be avoidable by unsecured creditors under applicable state law, absent the bankruptcy filing. The statute provides:
Section 544. Trustee as lien creditor and as successor to certain creditors and purchasers

(b) The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

M.S.A. Section 513.44, provides, in pertinent part:

513.44. Transfers fraudulent as to present and future creditors

(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

(1) with actual intent to hinder, delay, or defraud any creditor of the debtor; or

(2) without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:

(i) was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or

(ii) intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due.

The Fraudulent Transfer Act defines the term "transfer," in M.S.A. Section 513.41(12), as:

(12) "Transfer" means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, lease, and creation of a lien or other encumbrance.

Finally, the term "value" is treated in M.S.A. Section 513.43, which provides:

513.43. Value

(a) Value is given for a transfer or an obligation if, in exchange for the transfer or obligation, property is transferred or an antecedent debt is secured or satisfied, but value does not include an unperformed promise made otherwise than in the ordinary course of the promisor's business to furnish support to the debtor or another person.

(b) For the purposes of sections 513.44(a)(2) and 513.45, a person gives a reasonably equivalent value if the person acquires an interest of the debtor in an asset pursuant to a regularly conducted, noncollusive foreclosure sale or execution of a power of sale for the acquisition or disposition of the interest of the debtor upon default under a mortgage, deed of trust, or security agreement.

(c) A transfer is made for present value if the exchange between the debtor and the transferee is intended by them to be contemporaneous and is in fact substantially contemporaneous.

Fraudulent transfers are avoidable under M.S.A. Section 513.47(a)(1).

Standing

The Defendants argue that the Trustee lacks standing to bring the action because the contract vendee was Partners III, not the debtor. However, under Minnesota partnership law, when only one partner remains in a partnership, creditors of the old partnership

become creditors of the individual continuing the business. See M.S.A. Section 323.40(2). Furthermore, a partnership is defined as an association of two or more persons. See M.S.A. Section 323.02(8). Upon becoming the sole partner of Partners III, Gerald Butler became the owner of the vendee's interest in the contract for deed to the Property, and the contract was canceled against his interest. The Trustee has standing to bring this action.

Sufficiency Of The Allegations As To Value And Financial Condition

The Defendants argue that, because the action involves a fraud claim, Rule 7009 Fed.R.Bankr.P. applies. The rule requires that circumstances of alleged fraud be stated with particularity.(2) The Defendants contend that the Plaintiff did not allege any independent significant facts in the complaint that would, if true, tend to show either value of the Property, or Mr. Butler's general financial condition, at the time of the cancellation. However, the pleading is sufficient to survive a Rule 12(b)(6) motion for dismissal.

The action is not for intentional fraud under M.S.A.. Section 513.44(a)(1), which would involve both a voluntary transfer and actual intent to hinder, delay or defraud creditors. The action is for constructive fraud under Section 513.44(a)(2), which, in this case, involves an alleged involuntary transfer of an interest in property for less than reasonably equivalent value. The alleged transfer is identified, and the other necessary elements of the action are adequately pleaded in the complaint.

Value is pleaded on information and belief, based on valuation furnished by Mr. Butler in an earlier adversary proceeding in this Court between the Defendants, as plaintiffs, and the Debtor as defendant.(3) In that proceeding, the Debtor had valued the Property at approximately \$2,200,000 at the time of cancellation. The Defendants did not challenge the valuation, and the Court used the figure in its analysis of the issues presented in the litigation. It has not been alleged, and the Court does not find here, that the recitation of value in the previous adversary is res judicata in this proceeding. But, the Trustee's allegation of value is sufficiently grounded to adequately plead that element of the cause of action in this adversary proceeding.

The same is true regarding the allegation of Mr. Butler's financial condition at the time of cancellation of the contract for deed. Facts found in the earlier adversary proceeding regarding Mr. Butler's general business dealings at the time; and, his subsequent filing of bankruptcy within two years after the cancellation; provide sufficient basis for the inference that he was incurring debts beyond his ability to pay as they became due, both before and after the cancellation.

For the Defendants to prevail on a motion to dismiss under Rule 12(b)(6), it must appear, from the pleadings, that no set of facts can be proven which would warrant relief on the stated claim. Reasonable inferences from pleaded facts must be viewed in light most favorable to the Plaintiff. See: In Re Aluminum Mills Corp., 132 B.R. 869, 882 (Bankr.N.D.Ill. 1991). Reasonable inferences from the pleadings, viewed in light most favorable to the Plaintiff, are that: at cancellation of the contract for deed, the value of the Property was \$2,200,000; and, Mr. Butler thereafter incurred debts that he was unable to pay as they became due. Application of M.S.A. Section 513.44(a)(2) to Regularly Conducted, Noncollusive Statutory Cancellations of Contracts For Deed.

The Defendants argue that, as a matter of law, M.S.A. Section 513.44(a)(2) does not apply to regularly conducted, noncollusive

statutory cancellations of contracts for deed under M.S.A. Section 559.21. The issue presented is purely a state law question. The parties have not cited, and the Court has been unable to find, any Minnesota Supreme Court cases addressing the issue. Apparently, there exists no Minnesota state court precedent on the question(4). Resolution of the issue will depend upon the consideration and integration of Minnesota statutes and case law involving and affecting the state's most fundamental laws governing the ownership and transfer of real property. Existing Minnesota law presents no clear answer.

A decision regarding application of Minnesota's Fraudulent Transfer Act to regularly conducted, noncollusive statutory contract for deed cancellations, could have a substantial impact on Minnesota's real estate record ownership and title system. Application of the Act could result in widespread uncertainty of ownership regarding numerous properties, based on long past transactions; and, it could result in diminished public confidence in the reliability of official records pertaining to the ownership and transfer of real estate. Consideration and decision of this important state law question is properly placed in the Minnesota Supreme Court.

M.S.A. Section 480.061 empowers the Minnesota Supreme Court to answer questions of law certified to it by federal courts, including the bankruptcy court, if there are involved in proceedings before the certifying court questions of state law that may be determinative of the action; and, where it appears to the certifying court that there exists no controlling precedent in the decisions of the Minnesota Supreme Court. In the opinion of this Court, the question whether Minnesota's Fraudulent Transfer Act applies to regularly conducted, noncollusive statutory cancellation of contracts for deed, should be certified to the Minnesota Supreme Court under the statute. Accordingly, certification will be made by separate order, pursuant to the statute.

III.

Based on the foregoing, it is hereby ordered:

- 1) Plaintiff, Molly T. Shields, as Trustee, has standing to bring this adversary proceeding;
- 2) The complaint pleads the elements of a cause of action under M.S.A. Section 513.41 et. seq. with sufficient particularity;
- 3) The question of application of the Minnesota Fraudulent Transfer Act to regularly conducted, noncollusive statutory cancellations of contracts for deed will be certified to the Minnesota Supreme Court, pursuant to M.S.A. Section 480.061;
- 4) Final ruling on the Defendants' motion to dismiss this adversary proceeding is deferred pending certification to, and decision by, the Minnesota Supreme Court, on application of the Minnesota Fraudulent Transfer Act to regularly conducted, noncollusive statutory cancellations of contracts for deed.

Dated: January 16, 1996

By The Court:

Dennis D. O'Brien
Chief U.S. Bankruptcy Judge

(1) F.R.Bankr.P. 7012(b), provides that Rule 12(b)-(h) F.R.Civ.P. applies in adversary proceedings. Rule 12(b)(6) allows the defense of failure to state a claim upon which relief can be granted, to be asserted by motion.

(2) Rule 7009 F.R.Bankr.P. provides that Rule 9 F.R.Civ.P. applies

in adversary proceedings. Rule 9(b) reads: Fraud, Mistake, Condition of the Mind. In all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity. Malice, intent, knowledge, and other condition of mind of a person may be averred generally.

(3) That action, Goldetsky & Greenberg v. Butler, Adv. 3-93-286, resulted in denial of the Debtor's discharge.

(4) No Minnesota lower court decisions have been found that address the issue, either.