United States Bankruptcy Court
Northern District of Illinois
Eastern Division

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Bankruptcy Caption: In re Geo Contractors, Inc.,

Bankruptcy No. 98 B 39931

Adversary Caption: Sheldon Solow, Trustee v. George Kachavos

Adversary No. 00 A 00556

Date of Issuance: 12/06/01

Judge: John H. Squires

Appearance of Counsel:

Attorney for Plaintiff: David Audley, Esq.

Attorney for Defendant: Richard J. Grossman, Esq.

Trustee: Sheldon Solow

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

IN RE:	)	
GEO CONTRACTORS, INC.,	)	
	)	Chapter 7
Debtor.	)	Bankruptcy No. 98 B 39931
______________________________	)	Judge John H. Squires
	)	
SHELDON SOLOW, TRUSTEE,	)	
	)	
Plaintiff,	)	
	)	
v.	)	Adversary No. 00 A 00556
	)	
GEORGE KACHAVOS,	)	
	)	
Defendant.	)	

MEMORANDUM OPINION

This matter comes before the Court on the amended complaint of the Chapter 7 case trustee, Sheldon Solow (the "Trustee") against George Kachavos ("George") to avoid an alleged fraudulent conveyance under 11 U.S.C. § 544. For the reasons set forth herein, the Court denies the relief requested by the Trustee and holds that the transfer from Geo Contractors, Inc. (the "Debtor") for the benefit of George was not fraudulent under the Illinois Uniform Fraudulent Transfer Act and thus is not avoidable and recoverable by the Trustee under 11 U.S.C. § 544(b). Accordingly, the Court enters judgment in favor of George.

I. JURISDICTION AND PROCEDURE

The Court has jurisdiction to entertain this matter pursuant to 28 U.S.C. § 1334 and Internal Operating Procedure 15(a) of the United States District Court for the Northern District of Illinois. It is a core proceeding under 28 U.S.C. § 157(b)(2)(H).

II. FACTS AND BACKGROUND

The Debtor was in existence from 1994 to 1997. George is the father of Nicholas and William Kachavos ("Nick" and "William," respectively), the sole owners and officers of the Debtor. George was in a consultant position with the Debtor, was paid a salary, was there on a daily basis, and had an office at the Debtor's location.

The focus of this matter concerns the following transfer. On December 5, 1997, more than one year before the filing of the Debtor's bankruptcy petition, the Debtor issued a check in the amount of $94,788.97 payable to George. See Trustee's Exhibit No. 8 at p. 7 and George's Exhibit No. 8 at p. 1. The check was delivered to the Bank of Matteson and directly deposited into George's account number 36-3985658, without the endorsement of George. George, in turn, benefitted because those proceeds were utilized to pay off the balance of a home equity line secured by a mortgage on his principal residence. See Trustee's Exhibit Nos. 5, 6 and 7.

On July 23, 1993, George and his wife established a home equity line with the Bank of Matteson to fund a bridge loan for the purchase of another residence. See Trustee's Exhibit Nos. 5 and 6 and George's Exhibit Nos. 1 and 2. This equity line had a credit limit

of $100,000 and was scheduled to mature on July 23, 2000. Id. Starting in 1996, loans were made to the Debtor by George on the equity line in order to enable the Debtor to obtain working capital. See George's Exhibit Nos. 3 and 9. Those advances for the year 1997 totaled $94,788.97. Accordingly, the Debtor paid that sum to the Bank of Matteson for the benefit of George on December 5, 1997. These loans that George made to the Debtor were not evidenced by any promissory notes. George prepared a written summary record of the advances made by him and the repayments made by the Debtor. See George's Exhibit No. 9.

On November 26, 1997, before the subject $94,788.97 was transferred by the Debtor for the benefit of George, a payment was credited to one of the Debtor's bank accounts located at the Bank of Matteson in the total sum of $155,732.00. See Trustee's Exhibit No. 2. The sum was paid to the Debtor by Peak Construction, a general contractor, solely in relation to a construction project located in Cook County, Illinois, commonly referred to as the "Southgate Commercial Center Project," at which the Debtor served as a subcontractor for Peak Construction, providing sewer, water and site work. Prior to receiving the payment from Peak Construction, the Debtor did not have funds sufficient to pay the $94,788.97 it owed to George. Thus, it used some of the proceeds from that payment relating to the Southgate Commercial Center Project, on which it was owed an account receivable, to fund the subject transfer for George's benefit. It is undisputed that George never worked on or otherwise had an claim to any funds paid to the Debtor from Peak Construction relating to the Southgate Commercial Center Project.

At the time of the transfer from the Debtor for George's benefit, Continental Concrete Pipe Corp ("Continental") was a general unsecured creditor of the Debtor's estate, holding a potentially allowable claim under 11 U.S.C. § 502. Continental had supplied concrete materials to the Debtor for the Southgate Commercial Center Project. Tom Locke ("Tom"), a representative of Continental, testified that on December 5, 1997, he exchanged two partial mechanic's lien waivers dated December 4 and 5, 1997 in the amounts of $39,193.00 and $30,204.75, respectively, for two post-dated checks from the Debtor, via Nick, in those same amounts dated December 12, 1997. See Trustee's Exhibit Nos. 3 and 4 and George's Exhibit Nos. 12 and 13. Tom further testified that this procedure was normal and in accord with the course of dealing between the parties and had been done in other projects between the Debtor and Continental.

The Debtor utilized the lien waivers from Continental to obtain payments from Peak Construction for the Southgate Commercial Center Project. On February 27, 1998, the Debtor stopped payment on the $39,193.00 check written to Continental. See George's Exhibit No. 8 at p. 2 and Trustee's Exhibit Nos. 13 and 14. It is undisputed that Continental was never informed on December 5, 1997 that the Debtor had been paid by Peak Construction on the Southgate Commercial Center Project or that the Debtor had paid $94,788.97 for George's benefit.

The Debtor filed a Chapter 7 bankruptcy petition on December 11, 1998. The Trustee was thereafter appointed on December 29, 1998. On June 20, 2000, the Trustee filed a two-count complaint against the Defendant. Count I of the complaint alleged that the

transfer from the Debtor for the benefit of George was for the payment of an antecedent debt owed to him. The Trustee contended that the payment constituted a preferential transfer to an insider that may be avoided under 11 U.S.C. § 547(b). In Count II of the complaint, the Trustee contended that the transfer constituted a fraudulent conveyance avoidable under 11 U.S.C. § 544(b) and under the Illinois version of the Uniform Fraudulent Transfer Act, 740 ILCS 160/1 et seq. (the "UFTA").

On October 20, 2000, George filed a motion for summary judgment as to Count I of the complaint and filed a motion to dismiss Count II of the complaint. On December 5, 2000, the Court entered a Memorandum Opinion and Order which granted George's motion for summary judgment on Count I of the complaint. See Solow v. Kachavos (In re Geo Contractors, Inc.), Bankr. No. 98 B 39931, Adv. No. 00 A 00556, 2000 WL 1800593 (Bankr. N.D. Ill. Dec. 5, 2000). The Court held that the subject transfer was outside of the one-year preference period. Id. at *3. In addition, the Court granted George's motion to dismiss Count II of the complaint without prejudice. Id. at *6. The Court held that the complaint was devoid of the necessary allegations to sustain a cause of action under the UFTA and § 544(b). Id.

On December 21, 2000, the Trustee filed the instant amended complaint which seeks a finding that the transfer from the Debtor for the benefit of George was fraudulent under the UFTA and that such transfer should be avoided pursuant to § 544(b). The Court held an evidentiary hearing on the amended complaint and thereafter took the matter under advisement.

III. APPLICABLE STANDARDS

The Trustee seeks to avoid the subject transfer of property from the Debtor for George's benefit pursuant to 11 U.S.C. § 544(b)(1) which provides in pertinent part:

> [*T*]*he 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.

11 U.S.C. § 544(b)(1) (emphasis supplied). Furthermore, if transfers are avoidable under § 544(b)(1), they can be recovered under 11 U.S.C. § 550 from, among others, "the entity for whose benefit such transfer was made." See 11 U.S.C. § 550(a)(1)

In a case under § 544(b)(1), the Trustee has the rights of an unsecured creditor to avoid transactions that can be avoided by such creditor under state law. 11 U.S.C. § 544(b)(1); In re Image Worldwide, Ltd., 139 F.3d 576-77 (7th Cir. 1998). The Trustee need not identify the creditor, so long as an unsecured creditor exists. Id. at 577; In re Leonard, 125 F.3d 543, 544 (7th Cir. 1997). The transaction can be avoided completely even if the Trustee cannot produce creditors whose liens total more that the value of the property, Id. at 544-45, but the Trustee has done so in this case by providing the Court with evidence that Continental is a creditor of the Debtor with a potentially allowable claim under § 502. See Trustee's Exhibit No. 21 (Debtor's Schedule F-Creditors Holding Unsecured Nonpriority Claims).

The applicable state law asserted by the Trustee under § 544(b)(1) is the UFTA. The relevant portions of the UFTA provide:

> § 5. (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:
> >
> > > (A) 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
> > >
> > > (B) intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they became due.
>
> § 6. (a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at that time or the debtor became insolvent as a result of the transfer or obligation.
>
> (b) A transfer made by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made if the transfer was made to an insider for an antecedent debt, the debtor was insolvent at that time, and the insider had reasonable cause to believe that the debtor was insolvent.

740 ILCS 160/5(a), 160/6(a) and (b).

Sections 5 and 6 of the UFTA are analogous to 11 U.S.C. § 548(a)(1) and (2).[1] See Scholes v. Lehmann, 56 F.3d 750, 756 (7th Cir.), cert. denied sub nom. African Enter., Inc. v. Scholes, 516 U.S. 1028 (1995). "Because the provisions of the UFTA parallel § 548 of the Bankruptcy Code, findings made under the Bankruptcy Code are applicable to actions under the UFTA." Levit v. Spatz (In re Spatz), 222 B.R. 157, 164 (N.D. Ill. 1998) (citation omitted); see also Image Worldwide, 139 F.3d at 577 (because the Illinois UFTA is a uniform act which derived phrases from § 548 the court may look to cases under § 548 and other cases interpreting other states' versions of the UFTA for assistance).

Pursuant to § 5 of the UFTA, the Trustee may recover the transfer made by the Debtor under two theories: (1) if the Debtor made the transfer with actual intent to defraud a creditor; or (2) if the Debtor did not receive reasonably equivalent value in exchange for the transfer and was insolvent at the time of the transfer or became insolvent as a result of the transfer. The UFTA speaks to two types of fraud -- "fraud in fact" and "fraud in law." Scholes, 56 F.3d at 756-57.

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[1] An important difference between § 548 and the UFTA is that § 548 authorizes avoidance of transfers made within one year before the bankruptcy filing. 11 U.S.C. § 548(a). Causes of action for fraudulent conveyances can be brought under the UFTA, however, within four years after the transfer was made. 740 ILCS 160/10(a). Because the transfer at issue was made more than one year before the bankruptcy filing, relief under § 548 is not available to the Trustee, and he must, and does, rely on the UFTA.

"Fraud in fact" or actual fraud pursuant to § 5(a)(1) of the UFTA occurs when a debtor transfers property with the intent to hinder, delay or defraud his creditors. Bay State Milling Co. v. Martin (In re Martin), 145 B.R. 933, 946 (Bankr. N.D. Ill. 1992), appeal dismissed, 151 B.R. 154 (N.D. Ill. 1993). The moving party must prove a specific intent to hinder, delay or defraud. Lindholm v. Holtz, 221 Ill. App.3d 330, 334, 581 N.E.2d 860, 863 (2d Dist. 1991) (citing Gendron v. Chicago & NorthWestern Transp. Co., 139 Ill.2d 422, 437, 564 N.E.2d 1207, 1214-15 (1990)). The Trustee has the burden of proving all elements of actual fraud under Illinois law by clear and convincing evidence. Martin, 145 B.R. at 946 (citation omitted); Ray v. Winter, 67 Ill.2d 296, 304, 367 N.E.2d 678, 682 (1977).

In determining whether a transfer is made with actual intent to defraud, the UFTA sets forth several factors--also known as the "badges of fraud"-- from which an inference of fraudulent intent may be drawn. Section 5(b) of the UFTA sets forth the following indicia:

> (1) the transfer or obligation was to an insider;
> (2) the debtor retained possession or control of the property transferred after the transfer;
> (3) the transfer or obligation was disclosed or concealed;
> (4) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;
> (5) the transfer was of substantially all the debtor's assets;
> (6) the debtor absconded;
> (7) the debtor removed or concealed assets;
> (8) the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;
> (9) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;

> (10) the transfer occurred shortly before or shortly after a substantial debt was incurred; and
> (11) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

740 ILCS 160/5(b).

When these "badges of fraud" are present in sufficient number, it may give rise to an inference or presumption of fraud. Steel Co. v. Morgan Marshall Indus., Inc., 278 Ill. App.3d 241, 251, 662 N.E.2d 595, 602 (1st Dist. 1996) (citation omitted). Under the Federal Rules of Evidence, "a presumption imposes on the party against whom it is directed the burden of going forward with evidence to rebut or meet the presumption, but does not shift to such party the burden of proof in the sense of the risk of nonpersuasion, which remains throughout the trial upon the party on whom it was originally cast." Fed. R. Evid. 301.

Full consideration for the transfer is not, as a matter of law, an absolute defense to fraud in fact. In re Spatz, 222 B.R. at 169. As such, if the moving party proves fraudulent intent, then explicitly the transfer is deemed fraudulent, even if it is in exchange for valuable or full consideration. Id.

The UFTA expressly provides a defense to fraud in fact under § 9(a) which provides:

> (a) A transfer or obligation is not voidable under paragraph (1) of subsection (a) of Section 5 against a person who took in *good faith and for a reasonably equivalent value* or against an subsequent transferee or obligee.

740 ILCS § 160/9(a) (emphasis supplied). Courts have recognized that a defense under § 9 of the UFTA consists of two elements: good faith and reasonably equivalent value. See

Spatz, 222 B.R. 168 (citations omitted); Kennedy v. Four Boys Labor Serv., Inc., 279 Ill. App.3d 361, 370, 664 N.E.2d 1088, 1093 (2d Dist. 1996).

Under § 5(a)(2) of the UFTA, "fraud in law," on the other hand, does not require any showing of fraudulent intent. Scholes, 56 F.3d at 757; General Elec. Capital Corp. v. Lease Resolution Corp., 128 F.3d 1074, 1079 (7th Cir. 1997). Because of its nature, the conveyance is deemed constructively fraudulent. Daley v. Chang (In re Joy Recovery Tech. Corp.), 257 B.R. 253, 268 (Bankr. N.D. Ill. 2001). The Trustee has the burden of proving fraud in law by a preponderance of the evidence. See Martin, 145 B.R. at 946 (citations omitted). A different standard of proof applies to this theory because intent to defraud is presumed when the elements of constructive fraud are established. Id. (citations omitted).

In order to establish that a conveyance is fraudulent in law, four elements must be present: (1) the debtor made a voluntary transfer; (2) at the time of the transfer, the debtor had incurred obligations elsewhere; (3) the debtor made the transfer without receiving a reasonably equivalent value in exchange for the transfer; and (4) after the transfer, the debtor failed to retain sufficient property to pay the indebtedness. Lease Resolution, 128 F.3d at 1079 (citations omitted).

The distinction between "fraud in fact" and "fraud in law" cases is derived from whether or not there was any consideration for the conveyance under attack. Second Nat'l Bank of Robinson v. Jones, 309 Ill. App. 358, 365, 33 N.E.2d 732, 736 (4th Dist. 1941). Lack of consideration or inadequate consideration for a debtor's conveyance, coupled with the existence or prospect of other unpaid creditors, triggers the "fraud in law" theory in

which intent to hinder, delay or defraud is presumed from the circumstances. See Capitol Indem. Corp. v. Keller, 717 F.2d 324, 327 (7th Cir. 1983); Wilkey v. Wax, 82 Ill. App.2d 67, 70, 225 N.E.2d 813, 814 (4th Dist. 1967). When the natural consequences of the transfer is to harm creditors, the law constructively and conclusively presumes fraudulent intent irrespective of the debtor's actual intent. Gendron, 139 Ill.2d at 438, 564 N.E.2d at 1215.

What constitutes "reasonably equivalent value" for purposes of the UFTA has not been defined by Illinois case law.[2] The Illinois Supreme Court, in discussing a prior statute, has stated that one of the necessary elements to establish a fraudulent conveyance is that "there must be a transfer made for no or inadequate consideration." Gendron, 139 Ill.2d at 438, 546 N.E.2d at 1215 (citations omitted). The Illinois Appellate Court has since implied that there is no "reasonably equivalent value" when there is "no or inadequate consideration." Regan v. Ivanelli, 246 Ill. App.3d 798, 805, 617 N.E.2d 808, 814 (2d Dist. 1993); see also Image Worldwide, 139 F.3d at 577 (discussing Illinois interpretation of "reasonably equivalent value").

In determining whether reasonably equivalent value was received under the UFTA, courts should consider how that phrase has been construed under the Bankruptcy Code. Image Worldwide, 139 F.3d at 577. The Bankruptcy Code does not define the term "reasonably equivalent value." Whether "reasonably equivalent value" has been given is a question of fact. Joy Recovery, 257 B.R. at 268; In re Crystal Med. Prods., Inc., 240 B.R.

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[2] 740 ILCS 160/4(b) sets forth a definition for "reasonably equivalent value" that does not apply to this matter.

290, 300 (Bankr. N.D. Ill. 1999). The factors utilized to determine reasonably equivalent value are: (1) whether the value of what was transferred is equal to the value of what was received; (2) the market value of what was transferred and received; (3) whether the transaction took place at an arm's length; and (4) the good faith of the transferee. Barber v. Golden Seed Co., Inc., 129 F.3d 382, 387 (7th Cir. 1997); Grigsby v. Carmell (In re Apex Auto. Warehouse, L.P.), 238 B.R. 758, 773 (Bankr. N.D. Ill. 1999). There is no fixed formula for determining reasonable equivalence, but will depend on all the facts of each case, an important element being fair market value. Barber, 129 F.3d at 387.

Under § 6(a) of the UFTA, the elements of the cause of action are: (1) the creditor's claim arose before the transfer; (2) the debtor made the transfer without receiving a reasonably equivalent value in exchange for the transferred property; and (3) the debtor either was insolvent at the time of the transfer or became insolvent as a result of the transfer. See Joy Recovery, 257 B.R. at 271; In re Liquidation of Medcare HMO, Inc., 294 Ill. App.3d 42, 50, 689 N.E.2d 374, 380 (1st Dist. 1997); Falcon v. Thomas, 258 Ill. App.3d 900, 909, 629 N.E.2d 789, 795 (4th Dist. 1994). Actual insolvency is not required. 258 Ill. App.3d at 911, 629 N.E.2d at 796. The test is whether the conveyance directly tended to or did impair rights of existing creditors. Id. (citation omitted).

One difference between § 160/6 of the UFTA and § 160/5 is that § 160/6 includes the requirement that a creditor who has the right to assert some claim must have a claim that arose before the alleged fraudulent transaction. See 740 ILCS 160/6(a). The Trustee has demonstrated, and the Debtor does not dispute, that at least one such creditor

exists–Continental.

Finally, under § 6(b) of the UFTA, the elements of the cause of action are: (1) the creditor's claim arose before the transfer; (2) the debtor made the transfer to an insider for an antecedent debt; (3) the debtor was insolvent at the time of the transfer; and (4) the insider had reasonable cause to believe that the debtor was insolvent. An "insider" is defined by the UFTA to include a relative of an officer, director, or person in control of a corporate debtor. See 740 ILCS 160/2(g)(2)(F).

IV. DISCUSSION

Initially, George argues that because he did not actually receive the $94,788.97 check from the Debtor, or endorse it, there was no "transfer" to him under § 544(b) that the Trustee can avoid. The Court summarily rejects this argument inasmuch as a "transfer" for purposes of the Bankruptcy Code is broadly defined as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property. . . ." See 11 U.S.C. § 101(54). The Court finds that there was a transfer to George, albeit an indirect one, when the Debtor made a deposit of the funds into George's bank account. Those funds were subsequently utilized to pay off the home equity line of credit, and clearly benefitted George. Accordingly, the Court finds that there was a "transfer" to George which may potentially be avoided pursuant to § 544(b).

A. Section 5(a)(1) of the UFTA

The Court finds that the Trustee failed to establish by clear and convincing evidence

that the transfer from the Debtor for the benefit of George was made with actual intent to defraud, hinder or delay other creditors pursuant to § 5(a)(1) of the UFTA. The evidence adduced at trial failed to demonstrate that the transfer constituted actual fraud or fraud in fact. Both George and Nick testified that the payment from the Debtor for the benefit of George was made pursuant to the usual and ordinary course of practice followed by the parties in previous years. Further, George testified that he did not intend to defraud the creditors of the Debtor when he accepted the payment and paid off his home equity line. Rather, he testified that his receipt of the money in December 1997 was a result of the ordinary and customary practice between the parties in which the Debtor in previous years–1995 and 1996–paid George in full at the end of the calendar year.

In addition, Nick testified that the transfer was not intended to hinder, delay or defraud the Debtor's creditors. Rather, he stated that the transfer was made pursuant to the ordinary course between the parties, namely to repay George the funds advanced to the Debtor as working capital. The Debtor's stop payment order on the post-dated check given to Continental was not placed until February 27, 1998, and is some evidence of the Debtor's likely intent at that time to at least hinder or delay Continental's efforts to collect its debt. Similarly, the Debtor's subsequent deposit of checks for accounts receivable into another account in another bank, rather than the account on which the checks to Continental were drawn, is evidence of a subsequent intent on the part of the Debtor to at least hinder or delay Continental's claim. However, these actions taken by the Debtor, which were over two months after the December 5, 1997 transfer, do not prove the proscribed intent at the time

of the subject transfer.

At this point it is helpful to analyze the evidence in terms of the above cited eleven "badges of fraud." The Trustee correctly argues that the evidence establishes the presence of some of the badges of fraud. Notwithstanding same, the Court concludes that it is unable to infer the requisite actual fraudulent intent or intent to hinder or delay other creditors on December 5, 1997, when the Debtor made the transfer for George's benefit.

First, the transfer was to an insider for purposes of § 160/2(g)(2)(F) of the UFTA. George was employed by the Debtor and was the father of its two officers and directors. While a transfer between family members is not proof, per se, of fraudulent intent, a familial relationship is weighty proof of such intent. Berland v. Mussa (In re Mussa), 215 B.R. 158, 168 (Bankr. N.D. Ill. 1997) (citation omitted). Second, the Debtor did not retain possession or control of the property transferred after the transfer. Rather, the monies were deposited into George's account at the Bank of Matteson and then utilized to pay off George's home equity line of credit. The Debtor was not a signatory on George's account.

The third badge of fraud is present because the transfer was not disclosed to any other creditors of the Debtor, nor was it disclosed on the Debtor's Schedules. It is undisputed that Continental was not informed of the transfer. The Trustee argues that this nondisclosure by Nick constituted a "lie" to Tom (actually a misrepresentation by omission). The Court will not draw this inference inasmuch as Tom apparently did not ask Nick whether he intended to pay George (or anyone else), and Tom agreed to accept the post-dated checks, in any event. Moreover, Tom knew that without the partial lien waivers from Continental, Nick

would not receive the necessary payment from Peak Construction, which was the source from which Tom and Continental expected the Debtor would pay Continental's claim. Even if Nick's nondisclosure to Tom could be viewed as fraudulent as to Continental, this begs the question of whether the subject transfer for George's benefit was fraudulent. The Court is not prepared to effectively step together the Debtor's delay in paying Continental's claim (to which it knowingly agreed) with the undisclosed transfer for George's benefit, and conclude that the latter must be an avoidable fraudulent transfer. After all, one of the two post-dated checks to Continental was ultimately paid. It was not until early February 1998 that the Debtor placed a stop payment order on the second check to Continental.

Fourth, there was no evidence adduced at trial which demonstrated that before the transfer was made, the Debtor had been sued or threatened with suit. Tom testified that he visited the Debtor's offices on several occasions to inquire about receiving the money owed to Continental, but he did not threaten the Debtor with a lawsuit. Additionally, no other evidence was presented which indicated that the Debtor had been sued or threatened with suit by any other creditor.

The Trustee failed to prove the fifth badge of fraud that the transfer was of substantially all of the Debtor's assets. The Debtor's bank records indicated that the transfer of the sum of $94,788.97 left it with almost nothing in its bank account. However, there was evidence adduced at the trial which showed that the Debtor had other assets worth, at book value, approximately $360,740.00 as of December 31, 1997. See Trustee's Exhibit No. 11. Those assets included vehicles, furniture, fixtures and equipment. Id. Moreover, the

evidence showed that on January 28, 1998, a deposit of over $53,000.00 was made into the Debtor's account at the Bank of Matteson from additional accounts receivable. See Trustee's Exhibit No. 9. Thus, the Trustee failed to demonstrate that the transfer was of substantially all of the Debtor's assets.

Sixth, no evidence was adduced that demonstrated that the Debtor absconded with property. The Court rejects the Trustee's argument that the Debtor effectively "absconded" by going out of business, but waiting for over one year after the subject transfer before filing its bankruptcy petition. Abscond is defined as "[t]o depart secretly or suddenly, esp. to avoid service of process; to conceal oneself." See Black's Law Dictionary 6 (7th ed. 1999). No evidence to that effect was adduced at trial. To merely wait to file a bankruptcy petition does not equal absconding. Furthermore an "absconding debtor" has been defined as one "who flees from creditors to avoid having to pay a debt." Id. at 411. No such evidence was produced.

Seventh, there was no evidence presented which showed that the Debtor removed or concealed any of its assets. The transfer for George's benefit was not disclosed by Nick to Tom, but that is not the functional equivalent of removal or concealment. Rather, the transfer was the literal preferring in the payment of one legitimate creditor's claim over another's claim.

Eighth, the evidence demonstrated that the value of the consideration received by the Debtor, namely the working capital previously furnished it by George, via draws on his home equity line of credit, was reasonably equivalent to the value of the asset transferred.

George testified that the amount of the subject transfer equaled the total amount of money he had advanced to the Debtor in 1997 as working capital. See George's Exhibit No. 9, pp. 2-3. Moreover, George received the sum in good faith in accord with the course of dealing between the parties for the prior year. There was no evidence presented by the Trustee to rebut George's testimony.

The ninth badge of fraud appears to be present because the Debtor was insolvent or became insolvent shortly after the transfer was made. The UFTA provides that a debtor is insolvent if the sum of the debtor's debts is greater than all of the debtor's assets at a fair valuation. See 740 ILCS 160/3(a). Moreover, a debtor who generally is not paying its debts on time is presumed to be insolvent. 740 ILCS 160/3(b).

The Debtor's balance sheet as of December 31, 1997 shows that the Debtor was insolvent or became insolvent shortly after the transfer was made. The Debtor's balance sheet as of this time period shows that its liabilities exceeded its assets. See Trustee's Exhibit No. 11. Another exhibit for the same period was admitted into evidence on behalf of George and shows the Debtor's assets exceeding its liabilities. See George's Exhibit No. 11. The Court affords less weight to this exhibit because it appears that this version of the Debtor's balance sheet has been altered. On the top of the exhibit was a facsimile transmission which indicated it had been sent in December 2000, after the filing of the Trustee's complaint in June 2000, and possibly in anticipation of this trial. There was no evidence adduced at the trial to show that the Debtor was not paying its debts on time.

Tenth, the transfer occurred shortly after a substantial debt was incurred. The debt

to Continental was incurred in October 1997, just two months before the subject transfer. Finally, the eleventh badge of fraud is not present because the Debtor did not transfer the essential assets of the business to a lienor who transferred the assets to an insider of the Debtor.

The Court finds that only five of the eleven "badges of fraud" are proven by the evidence adduced at trial. Accordingly, the Court concludes that the record is insufficient to compel a finding that the subject transfer was actually fraudulent as proscribed by the statute.

Even if the Court were to find that the "badges of fraud" are present in a sufficient number, George has demonstrated that he paid full consideration for the money transferred and that he received the transfer from the Debtor, notwithstanding his general knowledge of the Debtor's financial cash flow problems, in good faith. George and Nick both testified that the subject transfer was made for full consideration as repayment of the loans made by George to the Debtor. The fact that these advances to the Debtor were not evidenced by written promissory notes does not prove that they were not loans by George to the Debtor, as opposed to gifts or capital contributions. George testified, without rebuttal, that the subject transfer was made in the ordinary course of business between the Debtor and him and mirrored payments received in the prior years of 1995 and 1996. In addition, George testified that he was not actively involved in the Southgate Commercial Center Project because he did not negotiate or bid it, nor was he aware of the financial details of same. Rather, he only observed the work, and knew Continental was an unpaid supplier on the

project. Moreover, he testified that he had no part of the decision making process regarding which accounts payable were to be paid. He testified that those decisions were left to Nick and William.

The Court concludes that the evidence shows that George was the beneficial recipient of a preferential transfer, but not an active participant and recipient of an actual fraudulent transfer. In short, the Court concludes that the Trustee has failed to prove that the transfer from the Debtor to George was done with actual intent to hinder, delay or defraud the Debtor's creditors.

B. Section 5(a)(2) of the UFTA

Moreover, the Trustee failed to demonstrate that the Debtor's transfer to George constituted fraud in law under § 5(a)(2) of the UFTA. The evidence and testimony demonstrated that the transfer on December 5, 1997 for the benefit of George from the Debtor was made for full consideration as repayment of a loan made to the Debtor from George earlier that year. See George's Exhibit Nos. 4, 7 and 9. The key element under § 5(b) is whether there was full or adequate consideration given to the Debtor for the transfer. The Court finds that there was adequate consideration, or reasonably equivalent value, as previously discussed.

The Court finds that the fact that George may have been preferred over other creditors is immaterial to determine whether the transfer to him was fraudulent. Illinois law clearly reflects that the fact that a creditor may have been preferred over other creditors does not constitute a fraudulent transfer. See Crawford County State Bank v. Doss, 174 Ill.

App.3d 574, 528 N.E.2d 436 (1st Dist. 1988). The Crawford court specifically posited:

> The transfer is not subject to attack by reason of knowledge on the part of the transferee that he is preferred to other creditors, nor does the transferee lack good faith because he knew his debtor's purpose to prefer or because he actively sought the preference. Neither can the transfer be attacked on the ground that the creditor knew that the transferor was insolvent, that the collection of the claims of other creditors would be hindered or defeated, or that the debtor intended to defeat the collection of their claims. Knowledge on the part of the creditor receiving the preference that the debtor has acted with fraudulent intention is immaterial if the creditor has done nothing except to receive payment of his claim.

174 Ill. App.3d at 581, 528 N.E.2d at 440-41 (quotation omitted).

In the final analysis, the totality of the evidence lends the Court to conclude that the subject transfer was probably preferential, but not an avoidable fraudulent transfer. Hence, the Court declines to infer constructive fraudulent intent.

C. Section 6(a) of the UFTA

Next, the Court must examine whether the transfer from the Debtor to George violated § 6(a) of the UFTA. First, it is undisputed that Continental's claim arose prior to the transfer. The second element of a claim under this section, reasonably equivalent value, is the same element required in § 5(a)(2) and need not be discussed again. The Court held that the Trustee has not met his burden to show that the Debtor did not receive reasonably equivalent value in exchange for the transfer of the sum of $94,788.97 for George's benefit. The final element under this section, that the Debtor was rendered insolvent by the transfer, has been established under § 5(a)(2). However, because the Trustee failed to establish all of the requisite elements, the Court holds that the transfer from the Debtor to George did not

violate § 6(a) of the UFTA.

D. Section 6(b) of the UFTA

Lastly, the Court must decide whether the Trustee has demonstrated all of the requisite elements under § 6(b) of the UFTA. First, Continental's claim arose before the transfer. Next, the Debtor made the transfer for the benefit of George, an insider, for an antecedent debt, namely advances of working capital for the Debtor. Further, the Trustee demonstrated, as previously discussed, that the Debtor was insolvent at the time of the transfer. However, the Trustee failed to prove that George had reasonable cause to believe that the Debtor was insolvent.

There was no credible and persuasive evidence to show that on December 5, 1997, George had reasonable cause to believe that the Debtor was insolvent. The only evidence of the Debtor's balance sheet insolvency was its financial statements for calendar year 1997. At the time of the subject transfer, however, the Debtor's year end financial statements had not been prepared. The 1997 calendar and fiscal year financial statements (Trustee's Exhibit No. 11) were prepared after December 31, 1997, when the Debtor's books were closed for that year. George's admitted knowledge of the Debtor's cash flow problems does not constitute the functional equivalent of knowledge that the Debtor was insolvent or was rendered so by the transfer for his benefit. No compelling evidence exists to show that George knew, or had reasonable cause to believe, that the Debtor was insolvent on December 5, 1997 or was rendered insolvent by the transfer in question. Therefore, the Court concludes that the Trustee has failed to establish all of the requisite elements to render

the transfer fraudulent under § 6(b).

V. CONCLUSION

For the foregoing reasons, the Court holds that the transfer of the sum of $94,788.97 from the Debtor for the benefit of George was not a fraudulent transfer under the UFTA and therefore cannot be avoided and recovered by the Trustee pursuant to § 544(b). Consequently, the Court enters judgment in favor of George.

This Opinion constitutes the Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. A separate order shall be entered pursuant to Federal Rule of Bankruptcy Procedure 9021.

ENTERED:

DATE: ________________

____
John H. Squires
United States Bankruptcy Judge

cc: See attached Service List