

FILED

SEP 30 2004

UNITED STATES
BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ARIZONA

In Re,
GEORGE E. FREEMAN, JR.,

Debtors.

DALE D. ULRICH, Trustee,

Plaintiff,

v.

JEFFREY P. PEARSE; GEORGE E.
FREEMAN, JR.,

Defendants.

Chapter 7

Case No. 04-00721-PHX-SSC

Adv. No. 04-640

MEMORANDUM DECISION
DENYING TRUSTEE'S PARTIAL
MOTION FOR SUMMARY
JUDGMENT AND DENYING
DEBTOR'S CROSS MOTION FOR
SANCTIONS

Preliminary Statement

On May 1, 2004, counsel for Dale D. Ulrich, the Chapter 7 Trustee, filed a Motion for Partial Summary Judgment, requesting that certain pre-petition transfers from the Debtor to Mr. Jeffrey Pearse ("Pearse") be avoided as a fraudulent conveyances pursuant to 11 U.S.C. §548(a)(1)(A) and/or (B) or A.R.S. §44-1004 and/or §1005. The Trustee further requested that said avoided transfers be preserved for the benefit of the bankruptcy estate. 11 U.S.C. §551. The Debtor's counsel responded and cross moved for sanctions. The Trustee's counsel replied only to that part of the Debtor's argument that focused on the alleged fraudulent conveyances. In the final Reply, the Debtor's counsel requested that his Cross Motion for Sanctions be granted, since the Trustee filed no response with respect to the Cross Motion. After oral argument, this Court took the matter under advisement. Given the consent of the parties to this Court's review of whether the Debtor was engaged in a constructive fraudulent

1 conveyance, this is a core proceeding over which this Court has jurisdiction. 28 U.S.C. §§1334
2 and 157. To the extent necessary, this Court has set forth its findings of fact and conclusions of
3 law pursuant to Rule 7052 of the Rules of Bankruptcy Procedure. (West 2004).
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5 Discussion

6 Since the Court will set a further evidentiary hearing in this adversary, believing
7 that genuine issues of material fact have been raised and that this Court may not enter judgment
8 for either party, the Debtor's Cross Motion for Sanctions must necessarily be denied at this time.

9 On January 15, 2004 at 2:38 p.m., the Debtor filed his Chapter 7 bankruptcy
10 petition. Shortly before filing his petition, the Debtor made two transfers by check to Pearse in
11 an attempt to acquire an interest in Pearse's residence located at 11133 E. Gamble Lane,
12 Scottsdale, Arizona. The Debtor made one transfer by check, made payable to Pearse, in the
13 amount of \$9,517.78 on December 22, 2003. The Debtor made the other transfer to Pearse,
14 also by check, in the amount of \$8,482.22 on December 29, 2003. On January 15, 2004, at 4:07
15 p.m., Pearse recorded a quit claim deed transferring a 5 percent interest in his residence to the
16 Debtor. The Quit Claim Deed was executed by Pearse on December 19, 2003.

17 The parties agree that the Pearse residence has a value of \$360,000 and that
18 there is one Deed of Trust as an encumbrance against the property in the approximate amount of
19 \$250,000. Thus, at the time that the Debtor filed his bankruptcy petition, Pearse had
20 approximately \$110,000 in equity in the property.

21 The parties agree that Pearse and the Debtor have been living at Pearse's
22 residence since November 2002. The Debtor does not disagree that after the two transfers, in
23 the aggregate amount of \$18,000, in December 2003, the Debtor had only \$1,173.47 left in his
24 bank account. The Debtor's schedules also reflect that he had \$1,020 in personal property at the
25 time that he filed his bankruptcy petition. Finally, the Debtor does not provide any evidence to
26 the contrary that at the time he filed, he had unsecured debt in the amount of \$139,641. Hence,
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1 there is no genuine issue of material fact as to the Debtor's insolvency at the time that he
2 transferred the \$18,000 to Pearse.

3 The parties principally disagree as to the nature of the agreement between
4 Pearse and the Debtor. Was the Debtor to receive 5 percent of the value of the residence or 5
5 percent of \$360,000, which is equal to \$18,000, or 5 percent of just the equity in the residence
6 or 5 percent of \$110,000, which is equivalent to \$5,500? Each side has presented evidence in
7 support of his or their position. This issue as to the intent of the Debtor and Pearse when they
8 entered into their agreement re the transfer of an interest in Pearse's residence to the Debtor
9 cannot be resolved based upon a review of the agreement itself, and the ultimate disposition of
10 the nature of the agreement will assist in the resolution of the dispute between the parties.
11 Hence, a genuine issue of material fact has been raised as to the nature of the agreement
12 between the Debtor and Pearse, which may only be resolved at a trial in this matter.

13 The Court also questions the value received by the Debtor at the time that he
14 acquired his interest in the residence. Although the Trustee believes that this Court may
15 summarily rule that an unrecorded, but valid, transfer between the Debtor and Pearse is
16 somehow worth less than what the Debtor paid for that interest, without some kind of valuation
17 testimony, this Court is unable to value the Debtor's interest in the residence at the time that he
18 filed his bankruptcy petition. Without a determination as to value, the Court is unable to
19 determine whether the Debtor received reasonably equivalent value for his aggregate payment of
20 \$18,000. This is also a genuine issue of material fact that must be resolved by the Court.

21 Finally, the Trustee alleges that the Debtor had the actual intent to defraud
22 creditors. Given the evidence presented so far, and the Debtor's and Pearse's denial, by way of
23 affidavits, as to the Trustee's allegations, the Court concludes that a genuine issue of material
24 fact has been created as to the Debtor's intent concerning the payment of \$18,000 to Pearse
25 shortly before the Debtor filed his bankruptcy petition.

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1 In turn, the Debtor has failed to convince this Court that he is entitled to
2 judgment, as a matter of fact and law, and that as a result, the Trustee and Trustee's counsel
3 should be sanctioned. The Trustee has certainly presented certain facts to this Court which are
4 troubling, for which this Court must take evidence to draw a conclusion. However, this does
5 not mean that the Trustee and Trustee's counsel somehow acted in bad faith or filed the
6 complaint in this adversary with some kind of improper purpose in mind. There is simply no
7 evidence to support the Debtor's Cross Motion for Sanctions. Again, genuine issues of fact
8 have been raised as a part of the Trustee's Motion for Partial Summary Judgment that may only
9 be resolved by a trial.

10 A motion for summary judgment should be granted if the movant has shown
11 that there are no genuine issues of material fact, and the movant is entitled to judgment as a
12 matter of law. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 106 (1986). The Court has
13 reviewed the Debtor's schedules filed with this Court under penalty of perjury which reflect that
14 the Debtor was insolvent at the time that he filed his petition. The Trustee relied on these
15 Schedules to reflect that the Debtor was insolvent at the time that he transferred \$18,000 to
16 Pearse. Since the Debtor provided no evidence or support to the contrary in his Response, the
17 Court concludes under the Anderson analysis that no genuine issue of material fact exists as to
18 the Debtor's insolvency at the time that the subject transfers occurred.

19 The Debtor cannot dispute, since both documents are time-stamped, that he
20 filed his bankruptcy petition, then the Quit Claim Deed transferring the 5 percent interest in the
21 Pearse residence to the Debtor was recorded. Arizona law is clear that a transfer of an interest
22 in real property does not occur, as to third parties, until the transfer is perfected. A.R.S. §44-
23 1006 provides:

24 1. A transfer is made: (a) With respect to an asset that is real property other
25 than a fixture, but including the interest of a seller or purchaser under a contract
26 for the sale of the asset, when the transfer is so far perfected that a good faith
27 purchaser of the asset from the debtor against whom applicable law permits the
28 transfer to be perfected cannot acquire an interest in the asset that is
superior to the interest of the transferee.

1 A.R.S. §33-411 also states:

2 1. All bargains, sales and other conveyances whatever of lands, tenements
3 and hereditaments, whether made for passing an estate of freehold or
4 inheritance or an estate for a term of years, and deeds of settlement upon
5 marriage, whether of land, money or other personal property, and deeds of trust
6 and mortgages of whatever kind, shall be void as to creditors and subsequent
7 purchasers for valuable consideration without notice, unless they are
8 acknowledged and recorded in the office of the county recorder as required by
9 law.

10 Thus, at the time that the Debtor filed his bankruptcy petition, he had paid
11 \$18,000 for an unrecorded or unperfected 5 percent interest in Pearse's residence. Once the
12 bankruptcy petition was filed, that unrecorded interest became property of the bankruptcy
13 estate. 11 U.S.C. §541.

14 The question then becomes what was the value of that unrecorded 5 percent
15 interest at the time the Debtor filed his petition? The Trustee, with no evidentiary support,
16 concludes that the Debtor received less than reasonably equivalent value. However, without
17 some type of valuation evidence as to that interest, this Court is unable to draw such a
18 conclusion. The Court must determine whether there has been a diminution of the Debtor's pre-
19 petition assets as a result of the transfer of funds for the receipt of the unrecorded interest. The
20 Court must examine the value of all benefits enuring to a debtor by virtue of the transaction in
21 question, directly or indirectly. In re Fox Bean Co., Inc., 287 B.R. 270 (Bankr. D. Idaho 2002).
22 The Court is unable to make such a valuation at this time.

23 There is also an ambiguity created as a result of the Debtor's interest having
24 been removed from the bankruptcy estate as an exempt asset. The Trustee or a party in interest
25 had 30 days after the conclusion of the 341 meeting of creditors or 30 days after any amendment
26 or supplement to the schedules was filed, whichever date was later, to object to a claim of
27 exemption. The Debtor correctly points out that the Trustee took no action in this regard.
28 Based upon the United States Supreme Court Decision of Taylor v. Freeland & Kronz, 112
S.Ct. 1644 (1991), the Debtor's claim of exemption in his 5 percent interest in the residence
became final, and hence, the interest has been removed from the bankruptcy estate. If the

1 interest has been removed from the estate, that may affect an expert's valuation of the Debtor's
2 unrecorded 5 percent interest in the residence as of the time of the bankruptcy petition filing.
3 Moreover, the Debtor argues that the transaction between the Debtor and Pearse must be
4 determined as of the date of the delivery of the Quit Claim Deed to the Debtor. Both Pearse and
5 the Debtor argue that the Deed was delivered on December 19, 2003, prior to the Debtor's
6 filing his bankruptcy petition. Under Arizona law, as to these individuals, the transaction would
7 have become final at the time of the delivery of the Quit Claim Deed, or pre-petition. Roosevelt
8 Savings Bank of the City of NY v. State Farm Fire and Casualty, 556 P.2d 823 (AZ App. 1976).
9 Again, this legal result may affect an expert's valuation of the Debtor's 5 percent interest as of
10 the filing of the Debtor's petition.

11 The Trustee relies on the Decision of Strasser v. Cavan (In re Strasser), 303
12 B.R. 841 (Bankr. D. AZ 2004) in support of his Motion for Partial Summary Judgment. In
13 Strasser, the Court did state that the actions of the parents post-petition to pay certain creditors
14 of the debtor to off-set somehow the pre-petition transfers by the debtor to the parents did not
15 vitiate the nature of the underlying transaction, a fraudulent conveyance. Id. at 847-48.
16 However, in this case, the Debtor did receive an interest in real estate for his pre-petition
17 payments. Thus, the facts in this case are not analogous.

18 The Trustee also misconstrues the Decision of Crater v. Crater (In re Crater),
19 286 B.R. 756 (Bankr. D. AZ 2002). Although pre-petition fraudulent conveyances may impact
20 the ability of a debtor to receive a discharge, the Court recognized in Crater that pre-bankruptcy
21 exemption planning does not result in a denial of a discharge unless deceit or concealment are
22 shown. Although there is an issue of fact as to why this Debtor did not fully disclose his
23 obtainment of a 5 percent interest on all of his schedules, certain key facts, such as his ownership
24 interest on Schedule A, are disclosed. The Court is unable to conclude on this record that the
25 Debtor's conduct was such that by failing to disclose the transfer of the 5 percent interest on all
26 of his schedules, the Debtor somehow engaged in a fraudulent conveyance.

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