



THE ENFORCER

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Estes v. Titus: An Arrow in The Creditor's Quiver

You have secured a money judgment for your client. Upon your attempts at collection you, learn that the debtor has recently obtained a divorce. The Judgment of Divorce reveals that the terms of the property settlement are heavily, and suspiciously, slanted in the non-debtor spouse's favor. With the debtor seemingly insolvent, you fear that he has rendered himself uncollectible. Based on the recent decision in *Estes v. Titus*¹, if a creditor can allege a prima facie case of a fraud under the Uniform Fraudulent Transfer Act² (UFTA) all may not be lost.

Prior to the Michigan Supreme Court's decision in *Estes*, it was unclear whether a third party creditor could challenge a fraudulent distribution of property under a judgment of divorce. *Estes* was different in that the claim was that the fraud was perpetrated against a third party rather than the spouse. Ordinarily, divorce judgments are protected from collateral attack by third parties. The rationale being that a divorce court is statutorily restricted to make determinations as to the husband and wife alone. Now, in the wake of *Estes*, a third party creditor may seek to set aside fraudulent transfers in a divorce judgment.

Factual Background

In *Estes*, Jan Estes, the personal representative and widow of Douglas Estes, sought to challenge what she perceived to be a fraudulent transfer. In 2002, Estes had filed a wrongful death complaint against Jeff Titus, the man convicted of murdering her husband. Once Jeff Titus was incarcerated, Julie Titus filed for divorce. In March of 2003, a judgment was entered in the Titus divorce giving Julie Titus almost all of the marital assets pursuant to a property settlement agreement.

Fearful that such a division of assets would preclude her from collecting in her wrongful death action, Estes sought, unsuccessfully, to intervene in the divorce. When Estes

obtained her wrongful death judgment for \$550,000, she sought to join Julie Titus as a defendant. This was premised on her claim that the property settlement was fraudulent pursuant to the UFTA. The divorce trial court denied her motion to intervene. The court believed it lacked the authority to invalidate or challenge the divorce judgment.

Distinguishing an UFTA action from a Collateral Attack on the Divorce Decree

The courts have traditionally refused to allow third parties to invalidate a divorce judgment, where neither spouse had challenged its validity or where third parties alleged irregularities. *Estes* provides that an UFTA action is not a collateral attack on a divorce judgment. First, a judgment rendered in a UFTA case does not invalidate a divorce judgment, but instead merely awards the property interests of the debtor to the creditor. In addition, an UFTA action does not seek to challenge a divorce decree based upon an irregularity. Rather, it is an attack based on a claim of fraud as a result of the transfer itself.

Alleging Fraud under the Uniform Fraudulent Transfer Act

While *Estes* now opens the door to setting aside transfers pursuant to a divorce judgment, the creditor must still allege a prima facie case of fraud. The UFTA seeks to prevent a debtor from transferring assets to a third party with the intent of obstructing creditors from proceeding against those same assets. The UFTA requires that a creditor establish that there has been a "transfer" of an "asset" with actual intent to defraud the creditor.

Further, to establish fraud the UFTA requires that there be a "transfer" of an "asset". The UFTA defines a "transfer" as, "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, and creation of a lien or other encumbrance."³ In the realm of divorce, creditors can take



comfort in the fact that a divorce decree is considered to be the equivalent of a bill of sale or quitclaim deed and thus a transfer.⁴

Finally, the UFTA requires that a party seeking to establish fraud on the part of a creditor establish that a "transfer" was made, "with actual intent to hinder, delay, or defraud any creditor of the debtor."⁵ Actual intent to delay, hinder or defraud may be found where at least one "badge of fraud" prescribed by MCL 566.34(2) is present.

In a concurring opinion, Justice Marilyn Kelly addressed the concern that there would be many UFTA claims after entry of divorce decrees. The fear would be that the claim would be based on the "insider" status of the spouse.⁶ She stated:

By contrast, regarding most divorce cases, the only badge of actual fraud that might plausibly be alleged is that the transfer took place while the parties were "insiders" under the act. In my opinion, this allegation will not survive a motion for summary disposition. For the UFTA to apply, the transferee must be an insider when the transfer occurs. Although a husband and wife are insiders while married, they normally cease to have that status when the divorce judgment is entered. And it is only when the judgment is entered that the transfer of property takes place, assuming, of course, that the individuals do not exchange the property beforehand. *Estes* at 594.

Entireties Property

Generally, an "asset" is all of the debtor's property. However, in the case of divorce there is an important exception. MCL 566.31(b)(iii), provides that property held by spouses as tenants by the entirety do not constitute "assets" where the creditor's judgment is against only one spouse. Because such property is not an "asset" under the UFTA, distribution through a divorce judgment is not considered a "transfer".

Divorce counsel should note that division of entireties property is not subject to an UFTA claim as it was not available to satisfy the creditor's claim before the transfer. Nevertheless, attempts by spouses to "cherry pick" their other assets could be met with an UFTA claim by an aggrieved creditor (or bankruptcy trustee).

Endnotes

1. 481 Mich. 573 (2008)
2. MCL 566.31 et seq.
3. MCL 566.31(l)
4. MCL 552.401
5. MCL 566.34 (1)(a)
6. UFTA provides for a finding of actual fraud when the transferee is an insider and the claim is brought within one year of the transfer.

