UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	:	Case No. 08-60881
	:	
Deborah A. Gavin,	:	Chapter 7
	:	
Debtor.	:	Judge Caldwell
	:	

	:	
Susan L. Rhiel, Trustee,	:	
Plaintiff,	:	
v.	:	**Adv. Pro. No. 09-2059**
Mortgage Electronic Registration	:	
Systems, Inc., *et al.*,	:	
Defendants.	:	

MEMORANDUM OPINION AND ORDER ENTERING FINAL JUDGMENT IN FAVOR OF DEFENDANTS

I. Jurisdiction

This Court has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. §§ 157(a) and 1334, and the standing General Order of Reference for this district. This is a core proceeding.

II. Background

On November 5, 2008, Deborah Ann Gavin ("Mrs. Gavin") filed a petition for relief under Chapter 7 of Title 11 of the United States Code (the "Bankruptcy Code"). On February 3, 2009, Susan Rhiel ("Plaintiff"), Trustee of Mrs. Gavin's Chapter 7 estate, initiated this adversary proceeding against Mortgage Electronic Registration Systems, Inc. ("MERS"); Quicken Loans Inc. ("Quicken"); and Mrs. Gavin's non-debtor husband, Bryan Gavin ("Mr. Gavin") (collectively "Defendants"). In the Complaint, Plaintiff alleges that Mrs. Gavin granted a mortgage on her interest in Mr. and Mrs. Gavin's marital residence to MERS and Quicken, but did not sign the note which that mortgage secured. Plaintiff argues that, because Mrs. Gavin had no liability on the note, the granting of the mortgage constitutes a fraudulent conveyance which would entitle Plaintiff to relief under the Bankruptcy Code.

On August 13, 2010, the Court held a trial on the merits. After the trial, the Court entered an Order Directing the Submission of Post-Trial Memoranda and Setting the Date for Presentation of Closing Arguments (Doc. No. 51, as amended by Doc. No. 70) (the "Scheduling Order"). The Scheduling Order instructed the parties to more thoroughly brief several issues, including the issues of whether the release of the prior mortgages or the future savings resulting from the refinancing can constitute reasonably equivalent value; whether Mrs. Gavin was insolvent at the time that this transfer occurred; and whether recovery of property or preservation of lien is a more appropriate remedy.

In its Scheduling Order, the Court also expressed concerns as to whether or not all necessary parties had been joined based upon testimony that Quicken had sold the mortgage at issue to a third party. In response to this, Plaintiff filed an Amended Complaint (Doc. No. 55) on September 15, 2010, without seeking leave of court. The Amended Complaint added Bank of

America, formerly known as Countrywide Home Loans, Inc. ("Bank of America"), as a defendant. This in turn led to a slew of post-trial filings, including an Answer to the Amended Complaint (Doc. No. 57) filed by MERS and Quicken, a Motion to Strike the Amended Complaint (Doc. No. 58) filed by Bank of America, and Plaintiff's Response to the Motion to Strike (Doc. No. 71). Each party also filed briefs and responses as instructed by the Scheduling Order. On March 24, 2011, the Court heard closing arguments regarding the matters tried, and oral arguments regarding the issues discussed in the Scheduling Order and the post-trial filings of the parties.

After careful consideration of the arguments of the parties made at hearing and by brief, and of the evidence adduced at trial, the Court finds that the satisfaction of the original two notes, and resultant release of the liens on Mrs. Gavin's undivided one-half interest in the subject property, constitute the receipt of reasonably equivalent value for purposes of this fraudulent transfer action. Because this finding prohibits recovery by Plaintiff, the Court need not reach the remaining issues identified above. Accordingly, judgment is entered in favor of the Defendants.

III. Findings of Fact

The Court makes the following findings of fact based upon (a) the stipulations of the parties; (b) the evidence adduced at trial, including exhibits admitted into evidence and the testimony of witnesses; and (c) the items of which it has taken judicial notice.

In the summer of 2007, Bryan and Deborah Gavin acquired the real property commonly known as 5704 Morlich Square, Dublin, Ohio (the "Property"). At all times relevant to this case, Mr. and Mrs. Gavin have been married to each other. The Property was acquired at a purchase price of $360,000.00.

The closing on the Property took place August 7, 2007. Mr. and Mrs. Gavin obtained title to the Property by deed. In order to acquire the Property, Mr. Gavin executed two promissory notes in favor of Quicken (the "Original Notes"). Mrs. Gavin did not sign the notes. Mr. and Mrs. Gavin executed two mortgages in favor of MERS, as nominee for Quicken, securing the Original Notes (the "Original Mortgages"). The first mortgage secured one note with a principal amount of $288,000.00. The second mortgage secured the other note with a principal amount of $54,000.00. The loan proceeds from the two notes together totaled $342,000.00. The deed and both mortgages were recorded in the Office of the Delaware County, Ohio Recorder on September 4, 2007.

After the closing, Quicken was unable to market the Original Notes. In order to obtain a marketable loan, Quicken offered Mr. and Mrs. Gavin the opportunity to refinance. On October 5, 2007, Mr. Gavin executed a third promissory note in favor of Quicken (the "Refinancing Note") with a principal amount of $342,000.00. Mrs. Gavin again did not sign the Refinancing Note. The proceeds of this note were used to satisfy the balance of the Original Notes. As a result of this satisfaction, the Original Mortgages were released. That same day, Mr. and Mrs. Gavin executed a new mortgage in favor of MERS, as nominee for Quicken, securing the Refinancing Note (the "Refinancing Mortgage"). This mortgage was recorded October 27, 2007.

IV. Conclusions of Law

Plaintiff asserts that she may avoid the Refinancing Mortgage as a constructive fraudulent transfer under section 548(a)(1)(B) of the Bankruptcy Code, and under the Ohio Uniform Fraudulent Transfer Act (the "Ohio UFTA"), found in section 1336.04(A)(2) of the Ohio Revised Code, as made applicable by section 544(b) of the Bankruptcy Code.

Section 548(a)(1)(B) of the Bankruptcy Code provides that a trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within 2 years before the date of the filing of the petition, if the debtor voluntarily or involuntarily--

> (i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and
>
> (ii)(I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;
>
> (II) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital;
>
> (III) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured; or
>
> (IV) made such transfer to or for the benefit of an insider, or incurred such obligation to or for the benefit of an insider, under an employment contract and not in the ordinary course of business.

11 U.S.C. § 548(a)(1)(B). Similarly, the Ohio UFTA provides that a transfer made or an obligation incurred by a debtor is fraudulent as to a creditor, whether the claim of the creditor arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

> (2) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and if either of the following applies:
>
> (a) The Debtor was engaged or was about to engage in a business or transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction;
>
> (b) The debtor intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they became due.

Ohio Rev. Code § 1336.04(A)(2). The constructive fraudulent transfer provisions of section 548 and the Ohio UFTA are nearly identical in that each requires a finding that (1) the debtor did not receive reasonably equivalent value in exchange for the transfer, and (2) the debtor meets some form of insolvency test. *See Slone v. Lassiter (In re Grove-Merritt)*, 406 B.R. 778, 805 (Bankr. S.D. Ohio 2009) (noting that the only practical differences between the statutes are the look-back periods). Under either statute, Plaintiff bears the burden of demonstrating a fraudulent transfer has occurred. *Id*.

As a preliminary matter, the Court finds and the parties do not appear to contest that Mrs. Gavin's granting of a mortgage interest in the Property by virtue of the Refinancing Mortgage constitutes a "transfer" for the purposes of each statute. Thus, the key issues before the Court are (1) whether the Debtor received reasonably equivalent value in exchange for that transfer, and (2) whether or not the statutory insolvency tests have been met.

A. The Satisfaction of the Original Mortgages Constitutes Reasonably Equivalent Value under Both 11 U.S.C. § 548(a)(1)(B) and Ohio Rev. Code § 1336.04

In order to establish a constructive fraudulent transfer under section 548 or the Ohio UFTA, Plaintiff must show that Mrs. Gavin did not receive reasonably equivalent value in exchange for her granting of the Refinancing Mortgage. To determine this, the Court must analyze (1) whether Mrs. Gavin received value, (2) whether it was received in exchange for the transfer, and (3) whether what was transferred was reasonably equivalent to what was received. *In re Grove-Merritt,* 406 B.R. at 806. The corporate Defendants assert, and the Court agrees, that Mrs. Gavin received reasonably equivalent value when the satisfaction of the Original Notes resulted in the release of the Original Mortgages.

1. Mrs. Gavin received value.

Mrs. Gavin received value when the liens against her interest in the Property were released as a result of the satisfaction of the Original Notes. Under both the Bankruptcy Code and the Ohio UFTA, the definition of "value" includes the satisfaction of an antecedent debt. *See Grove-Merritt*, 406 B.R. at 807; 11 U.S.C. § 548(d)(2)(A); Ohio Rev. Code § 1336.03(A). Under the Bankruptcy Code, a consensual mortgage lien is a "debt" for purposes of this definition. *Glance v. Carroll (In re Glance)*, 487 F.3d 317, 320–21 (6th Cir. 2007). The Original Mortgages constituted liens on Mrs. Gavin's interest in the Property. These liens on the Property were debts, the satisfaction of which constituted value received by Mrs. Gavin for the purposes of section 548.

Though *Glance* did not involve a fraudulent transfer claim under the Ohio UFTA, the result is the same under Ohio law. The Ohio UFTA does not explicitly state whether a lien on property can be considered a debt, the satisfaction of which would constitute value. As noted by both parties in their briefs, Ohio law permits one to mortgage their property to secure another's debt. *See Rhiel v. Chase Home Finance, LLC (In re Colbert)*, 434 B.R. 844 (Bankr. S.D. Ohio 2010) (citing *Peoples Ins. Co. v. McDonnell*, 41 Ohio St. 650 (1885)). This has been interpreted by many Ohio courts to create a surety relationship between the mortgagor and mortgagee. *Colbert*, 434 B.R. at 847-48 (collecting cases). Mrs. Gavin, though not personally obligated on the Original Notes, guaranteed them with her interest in the Property.

Further guidance can be found in the uniform act itself. Section 3(a) of the Uniform Fraudulent Transfer Act, after which Ohio Rev. Code § 1336.03 was modeled, is expressly adapted from 11 U.S.C. 548(d)(2)(A). *See* Uniform Fraudulent Transfer Act § 3 cmt. 2 (1984). Case law such as *Glance*, though not expressly addressing Ohio law, is still persuasive in interpreting the statute. Recognizing that a release of lien provides "value" to a debtor comports with the concept of value as envisioned by the act. *Id*. ("Value" is to be determined in light of the purpose of the Act to protect a debtor's estate from being depleted to the prejudice of the debtor's unsecured creditors.).

Here, by virtue of the lien created by the Original Mortgages, Mrs. Gavin was liable *in rem* for payment of the Original Notes to the extent of her interest in the Property. The satisfaction of the Original Notes, and the resultant release of the liens on her interest in the Property, created a net increase in the total equity in her estate that would be available to her unsecured creditors. As will be explained below, this value was given to her in an even exchange for the granting of the Refinancing Mortgage. The exchange resulted in zero net loss to Mrs. Gavin's estate, and thus no depletion which would prejudice creditors. This definition of value comports both with the Sixth Circuit's reasoning in *Glance* and with the Uniform Fraudulent Transfer Act.

Plaintiff advances several theories as to why the satisfaction of the Original Notes and resultant release of the liens on Mrs. Gavin's interest in the Property would not constitute "value" for the purposes of a fraudulent transfer action. First, Plaintiff argues that a debtor does not receive value when a transfer is solely for the benefit of a third party. *See, e.g., In re W.E. Tucker Oil Company, Inc.*, 55 B.R. 78 (Bankr. W.D. Ark. 1985); *In re Bell & Beckwith*, 64 B.R. 620 (Bankr. N.D. Ohio 1986) (constructive fraudulent transfer found where debtor granted mortgages while having received no economic benefit). Such an argument might be persuasive had Mrs. Gavin not received an economic benefit.

Here, the proceeds of the Refinancing Note did not solely benefit Mr. Gavin. Mrs. Gavin received a benefit by virtue of the extinguishment of the liens on her interest in the Property. Arguably, this is a direct benefit to Mrs. Gavin (the proceeds of the Refinancing Note reduced the balance owed on the Original Notes, which reduced her *in rem* liability). However, even an indirect benefit can be considered value for purposes of a fraudulent transfer action. "It is well settled that 'reasonably equivalent value can come from one other than the recipient of the payments, a rule which has become known as the indirect benefit rule.'" *Lisle v. John Wiley & Sons, Inc. (In re Wilkinson)*, 196 Fed. Appx. 337, 341 (6th Cir. 2006) (quoting *Frontier Bank v. Brown (In re Northern Merch., Inc.*), 371 F.3d 1056, 1058 (9th Cir. 2004)). The indirect benefit rule was first explained in *Rubin v. Manufacturers Hanover Trust Co.*:

> [A] debtor may sometimes receive "fair" consideration even though the consideration given for his property or obligation goes initially to a third person…. [T]he transaction's benefit to the debtor need not be direct; it may come indirectly through benefit to a third person…. If the consideration given to the third person has ultimately landed in the debtor's hands, or if the giving of the consideration to the third person otherwise confers an economic benefit upon the debtor, then the debtor's net worth has been preserved, and [the statute] has been satisfied -- provided, of course, that the value of the benefit received by the debtor approximates the value of the property or obligation he has given up.

Rubin v. Manufacturers Hanover Trust Co, 661 F.2d 979, 991–92 (2nd Cir. 1981). Though the proceeds of the Refinancing Notes were used to satisfy a debt upon which only Mr. Gavin was personally liable, this satisfaction directly and necessarily resulted in the release of the liens on Mrs. Gavin's interest in the Property.

Plaintiff also argues that she is entitled to relief because the transaction was for the benefit of Quicken and not Mrs. Gavin. It is true that Quicken could not market the Original Notes, and certainly benefited from obtaining a marketable note. However, the proper issue before the Court is not whether a third party benefited or to whom a benefit was intended, but whether the debtor received value. Plaintiff appears to argue that Mrs. Gavin received no net benefit from the refinancing, whereas Quicken received a positive net benefit by virtue of its gaining a marketable loan. This argument conflates the value received by Mrs. Gavin with the result of the entire transaction. The Court's current focus is to determine whether or not Mrs.

Gavin received value, which she did. Who ultimately gained the most from the transaction is irrelevant to that question.

2. The value Mrs. Gavin received was given in exchange for the granting of the liens on her interest in the Property.

As discussed above, the satisfaction of the Original Notes and resultant release of liens constituted value received by Mrs. Gavin. The Court now turns to the issue of whether such value was received in exchange for the granting of the Refinancing Mortgage. Mrs. Gavin signed the Refinancing Mortgage as part of her and Mr. Gavin's transaction with Quicken to refinance the Original Notes. The original liens on Mrs. Gavin's interest in the property were extinguished as part of this same transaction. Neither event would have occurred in the absence of the other. Accordingly, the Court finds that the value received by Mrs. Gavin was received in exchange for the granting of the Refinancing Mortgage.

In its Scheduling Order, the Court expressed concerns regarding how the timing provision contained in 11 U.S.C. § 548(d)(1) might affect whether the receipt of value by Mrs. Gavin was truly in exchange for the granting of the Refinancing Mortgage. Section 548(d)(1) states that, for the purposes of section 548, "a transfer is made when such transfer is so perfected that a bona fide purchaser from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest in the property transferred that is superior to the interest in such property of the transferee[.]" 11 U.S.C. § 548(d)(1). The Court then directed the parties' attention to *Chase Manhattan Mortg. Corp. v. Shapiro (In re Lee)*, 530 F.3d 458 (6th Cir. 2008), which involved interpretation of a similar timing provision found in 11 U.S.C. § 547(e)(2).

In *Lee*, the debtor refinanced his residential mortgage loan by executing a new note, using the proceeds of that note to pay off the balance of the original note, and executing a new mortgage to secure the new note. The debtor executed the loan documents on October 6, 2003.

However, the new mortgage was not recorded until December 17, 2003. The debtor filed for bankruptcy relief on March 4, 2004.

The Chapter 7 trustee argued that the mortgage was avoidable because the recording of the transfer occurred within the 90 days prior to the date of filing. Pursuant to section 547(e)(2), if a transfer is perfected more than 30 days from the date it occurred, it is deemed to have taken place on the date of perfection. Because the mortgage was not perfected until recorded, the transfer was deemed to have taken place on December 17, 2003, within the preference period.

The lienholder attempted to assert the earmarking doctrine, a judicially-created defense to preference actions which protects creditors by “earmarking” property transferred on account of an antecedent debt such that the “transfer” element is negated. In determining that the earmarking doctrine did not protect the late perfection of the refinanced mortgage, the Sixth Circuit agreed with a majority of courts who have found that the distribution of funds and the granting of a mortgage are multiple distinct transactions for the purposes of section 547.

The Sixth Circuit’s reasoning in *Lee* does not prevent this Court from finding that the value Mrs. Gavin received was in exchange for the granting of the liens on her interest in the Property. The timing provisions in section 547, like those in section 548, are used for determining whether the transfer in question occurred within the applicable look-back period. The *Lee* court characterized refinancing as “multiple transfers” as opposed to a “single unitary transaction” solely to determine the applicability of the earmarking doctrine in the context of a preference action. The *Lee* court was not attempting to determine if one transfer was performed in exchange for another transfer, and this Court does not believe that the Sixth Circuit intended for its analysis to prevent a finding of reasonably equivalent value.

As discussed in the Scheduling Order, courts have regularly "collapsed" transactions to validate or avoid alleged constructive fraudulent transfers. *See, e.g., Orr v. Kinderhill Corp.*, 991 F.2d 31, 35 (2d Cir. 1993); *United States v. Tabor Court Realty*, 803 F.2d 1288, 1302 (3d Cir. 1986); *Yoder v. T.E.L. Leasing, Inc. (In re Suburban Motor Freight, Inc.)*, 124 B.R. 984, 998 (Bankr. S.D. Ohio 1990); *Creditors' Comm v. Jumer (In re Jumer's Castle Lodge, Inc.)*, 338 B.R. 344, 356 (C.D. Ill. 2006). Unlike preference actions such as *Lee* which concern when a transfer occurred, an analysis of reasonably equivalent value in the context of a fraudulent transfer action seeks to determine whether one transfer was made in exchange for the other. *See Jumer's Castle Lodge, Inc.*, 338 B.R. at 356 ("The defendants argue that there were two transfers that occurred …, the transfer of the . . . proceeds from the loan and then the transfer … to secure the loan…. While this argument might be true in the most technical sense, it is not rational or reasonable. The defendants are attempting to separate the two events as if either would happen independently, which they would not…. These two events are co-dependent and, theoretically, happened simultaneously."). Here, the granting of the lien by Mrs. Gavin and the satisfaction of the Original Notes were two co-dependent events, neither of which would have occurred without the other. They were done in exchange for one another, thus satisfying the Court's inquiry.

Because the Refinancing Mortgage was perfected after the Original Notes were satisfied, Plaintiff argues that *Lee* requires this Court to find that Mrs. Gavin necessarily transferred property to the corporate Defendants at a time when she had no debt. As a result, Plaintiff argues there could be no exchange of reasonably equivalent value. The Court disagrees. Unlike section 547(e)(2)(A), section 548 does not provide a "grace period" during which a secured creditor would have an opportunity to protect its interest. Under Plaintiff's line of reasoning, in order for a secured creditor to protect itself from potential constructive fraudulent transfer liability, it would need to perfect its security interest on or before the date on which value is conveyed to the debtor. The consequence of this would be the possible invalidation of many routine transactions which fail the exchange requirement. Plaintiff has failed to cite any case law in support of her position as requested in the Scheduling Order. The Court does not believe the Sixth Circuit intended such a result in *Lee*, and declines to apply the timing provisions of section 548 in such a manner.

3. The value Mrs. Gavin received was reasonably equivalent to the mortgage interest in the Property she conveyed to the corporate Defendants.

Having established that Mrs. Gavin received value in exchange for her granting the liens on her interest in the Property, the Court must now determine if the value received was reasonably equivalent to that which was transferred. Courts generally compare the value transferred to the value received. *Silagy v. Gagon (In re Gabor)*, 280 B.R. 149, 158 (Bankr. N.D. Ohio 2002) (citing *John Ownbey Co. v. Commissioner*, 645 F.2d 540, 545 (6th Cir. 1981)). Valuation is determined from the standpoint of the debtor. *Gabor*, 280 B.R. at 158. In determining the existence of fair consideration or equivalent value, courts review "all the surrounding circumstances to determine whether the transaction is fair." *Id.* Courts have found reasonably equivalent value where the value transferred and received has zero net effect on the debtor's estate. *See Wilkinson*, 196 Fed. Appx. at 343.

Pragmatically, it may seem obvious that the release of an undersecured lien on an interest in property is equivalent to the encumbering of that same interest in property with the same amount of debt. However, the determination of reasonably equivalent value is a question of fact. *Gabor*, 280 B.R. at 162. Therefore, a brief discussion is appropriate.

Here, Mrs. Gavin holds an undivided one-half interest in the Property. Since the property was purchased for $360,000.00, her interest is worth approximately $180,000.00. At the time of the refinancing transaction, the Property was entirely encumbered by the Original Mortgages, which secured the Original Notes. When the Original Notes were satisfied, the liens created by the Original Mortgages were extinguished. This resulted in an increase in Mrs. Gavin's equity (and decrease in her *in rem* liability) equal to $180,000.00, the value of her interest in the Property. At that same time, Mrs. Gavin granted a lien in the Property to the corporate Defendants, resulting in a decrease in equity (and increase in her *in rem* liability) equal again to $180,000.00. The transaction resulted in no net increase or decrease to Mrs. Gavin's equity in the Property (or *in rem* liability). Put differently, the value received was effectively equal to that transferred, because the transaction had no net effect on Mrs. Gavin's estate.

The Court finds that Mrs. Gavin received reasonably equivalent value in exchange for her granting of the Refinancing Mortgage to the corporate Defendants. Consequently, Plaintiff cannot establish a constructive fraudulent transfer under 11 U.S.C. § 548 or the Ohio UFTA. The Court notes that this result comports with the purposes of section 548 and the Uniform Fraudulent Transfer Act as described above. Mrs. Gavin's participation in the refinancing transaction ultimately did not affect the value of her estate, and thus did not harm her creditors.

V. Conclusion

Having found that Mrs. Gavin received reasonably equivalent value, judgment will be entered in favor of Defendants. Because this decision today does not prejudice Defendants, the Court need not address the issue of solvency or the other remaining issues identified by the Scheduling Order.

The Court is cognizant of the fact that several adversary proceedings with similar but distinct issues have been held in abeyance pending the outcome of this case. As noted in the Scheduling Order, the Original Mortgages in this case have been released and are not subject to avoidance. Consequently, this case does not involve, nor does this Court decide, the issue of whether a purchase-money mortgage may be challenged as a constructive fraudulent transfer on the grounds that the debtor did not sign the promissory note. However, the Court notes that the rationale employed in the case at bar is likely applicable in such a context.

Accordingly, judgment is entered in favor of Defendants.

IT IS SO ORDERED.

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