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## It's Worth Whatever Someone Paid for It: How Courts Have Misinterpreted BFP's Reasoning

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# It's Worth Whatever Someone Paid for It: How Courts Have Misinterpreted *BFP*'s Reasoning

Jacob Ryder\*

## ABSTRACT

Historically, bankruptcy courts have used the Bankruptcy Code's avoidance powers—fraudulent conveyances in § 548 and preferential transfers in § 547—to avoid pre-bankruptcy-petition transfers. These avoidance powers were used even when the transfer in question was a mortgage or tax foreclosure sale. This has changed in response to the U.S. Supreme Court's opinion in *BFP v. Resolution Trust Corp.* The *BFP* Court concluded that § 548 could not be used to avoid a mortgage foreclosure sale that complied with state foreclosure law. To do so, the Court had to interpret the operative language in § 548: “reasonably equivalent value.” The Court reasoned that an asset's fair market value had no application in the context of a forced sale and ultimately concluded that the price received in the forced sale was a reasonably equivalent value of the asset.

Following *BFP*, courts have uniformly applied *BFP*'s reasoning to other forced sales, such as tax foreclosure sales in the context of § 548. However, courts are split as to whether *BFP* should prevent the avoidance of forced sales in the context of § 547. Some courts have not extended *BFP* to § 547, while other courts have done so. This Comment will provide background information about and examine both sides of the circuit split and the arguments in favor of each approach. This Comment will then endorse the view that *BFP*'s reasoning applies to prevent the avoidance of forced sales that comply with state law under § 547 preferential transfers.

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## I. INTRODUCTION

Suppose an individual has two creditors, each holding an unsecured debt. If one of the creditors were to purchase the individual's house in a pre-bankruptcy-petition sale, should the sale be subject to avoidance? In a new situation, suppose an individual has two creditors, one of which is secured on the individual's house, and the other is unsecured. In a pre-bankruptcy-petition sale, the secured creditor bids the amount it is owed, but that amount is far less than the house's fair market value. Should this sale be subject to avoidance?

Bankruptcy courts are split on whether *BFP v. Resolution Trust Corp.*<sup>1</sup> applies to the Bankruptcy Code § 547,<sup>2</sup> and a solution to this split will answer the above hypothetical questions.<sup>3</sup> Whether

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1. *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994).

2. 11 U.S.C. § 547.

3. Compare *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 336 (S.D. Tex. 1999) (extending *BFP's* reasoning to § 547), with

the solution is to expand *BFP* to § 547 or not, creditors will be impacted.<sup>4</sup> Expanding *BFP* will, at least in certain situations, limit a trustee's ability to recover assets.<sup>5</sup> A trustee could no longer recover an asset that had left the estate through certain forced sales despite the sales satisfying the requirements of § 547.<sup>6</sup> If *BFP* does not apply to § 547, a creditor could require the trustee to recover an asset that left the estate through certain forced sales.<sup>7</sup> This issue is certainly limited to a small portion of bankruptcy cases, but the solution to the circuit split could mean the difference between a creditor recovering something or nothing.

This Comment will begin by providing background on the relevant topics: the bankruptcy code,<sup>8</sup> forced sales,<sup>9</sup> and pre-*BFP* cases.<sup>10</sup> This Comment will then analyze the *BFP* case<sup>11</sup> and the circuit split that has ensued regarding *BFP*'s application to § 547.<sup>12</sup> Finally, this Comment will endorse the position that *BFP*'s reasoning applies to § 547 just as it does to § 548.<sup>13</sup>

## II. BACKGROUND

### A. *The Bankruptcy Code*

#### 1. *General*

Article One, § Eight of the United States Constitution grants Congress the power to create nationwide bankruptcy laws.<sup>14</sup> Congress first exercised this power in 1800 with the creation of the

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Andrews Northwest Bank Minn., N.A. v. Andrews (*In re Andrews*), 262 B.R. 299, 306 (M.D. Pa. 2001) (declining to extend *BFP*'s reasoning to § 547).

4. See *infra* Section II.G (examining the significance of the circuit split).

5. See, e.g., Chase Manhattan Bank v. Pulcini (*In re Pulcini*), 261 B.R. 836, 845 (W.D. Pa. 2001) (holding that the trustee had no power to avoid the forced sale, therefore the estate had fewer assets to satisfy debts).

6. See, e.g., *id.* (holding that the trustee had no power to avoid the forced sale).

7. See, e.g., Andrews Northwest Bank Minn., N.A. v. Andrews (*In re Andrews*), 262 B.R. 299, 306 (M.D. Pa. 2001) (declining to extend *BFP*'s reasoning to § 547 and avoiding the pre-petition sheriff sale under § 547).

8. See *infra* Section II.A (providing information on the Bankruptcy Code).

9. See *infra* Section II.B (providing information on forced sales).

10. See *infra* Section II.C (examining how cases handled similar situations prior to the *BFP* decision).

11. See *infra* Section II.D (examining the Supreme Court's reasoning and conclusion in *BFP*).

12. See *infra* Section II.F (examining the Supreme Court's reasoning and conclusion in *BFP*).

13. See *infra* Part III (explaining why *BFP* should apply to § 547).

14. U.S. CONST. art. I, § 8; FEDERAL JUDICIAL CENTER, THE EVOLUTION OF U.S. BANKRUPTCY LAW: A TIMELINE (2019).

Bankruptcy Act of 1800.<sup>15</sup> Years of development led to the Bankruptcy Act of 1978,<sup>16</sup> commonly known as the Bankruptcy Code (“the Code”). Congress has amended the Code several times, but its foundation remains the Bankruptcy Act of 1978.<sup>17</sup> Congress organized the Code into nine chapters, each chapter addressing a different aspect of bankruptcy law.<sup>18</sup> The first three chapters—one, three, and five—are general provisions.<sup>19</sup> There are six forms of bankruptcy proceedings named after the chapter in which they are found in the Code.<sup>20</sup> This Comment addresses only Chapters 7 and 13.<sup>21</sup> Chapter 7 governs the liquidation of a debtor’s bankruptcy estate,<sup>22</sup> and Chapter 13 governs the adjustment of a debtor’s personal debts.<sup>23</sup>

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15. Bankruptcy Act of 1800, 2 Stat. 25 (repealed 1803).

16. 11 U.S.C. §§ 101–1532.

17. ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS, BANKRUPTCY BASICS 5 (2011); *see also* 11 U.S.C. §§ 101–1532. The Code is governing law but is not a comprehensive set of rules. *See* ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS, BANKRUPTCY BASICS 5 (2011). The Federal Rules for Bankruptcy Procedure and Local Rules both provide additional requirements for bankruptcy proceedings. *See id.*; FED. R. BANK. P. 1001–9037. Additionally, the Federal Rules of Bankruptcy Procedure incorporate by reference the Federal Rules of Civil Procedure where they are to apply in the bankruptcy context. FED. R. BANK. P. 7002.

18. 2 COLLIER ON BANKRUPTCY ¶ 103.01 (Richard Levin & Henry J. Sommer eds., 16th ed. 2019).

19. Chapter One contains general provisions including definitions, applicability, and rules of construction. 11 U.S.C. §§ 101–12. Chapter Three contains provisions on bankruptcy case administration. *Id.* §§ 301–66. Chapter Five includes information on creditors and claims, debtor’s duties and benefits, and the bankruptcy estate. *Id.* §§ 501–62.

20. Those chapters are 7, 9, 11, 12, 13, and 15. Chapter Seven governs the liquidation of a debtor’s estate. *See id.* §§ 701–84. Chapter Nine governs the adjustment of a municipality’s debts. *See id.* §§ 901–46. Chapter 11 governs the reorganization of business debts. *See id.* §§ 1101–74. Chapter 12 governs a relatively specific scenario of the adjustment of debts for a family farmer or fisherman. *See id.* §§ 1201–32. Chapter 13 governs the adjustment of debts for an individual with regular income. *See id.* §§ 1301–30. Finally, Chapter 15 governs ancillary bankruptcy cases and cross-border bankruptcy cases. *See id.* §§ 1501–32.

21. *See id.* §§ 701–84, 1301–30. Although this Comment focuses on only consumer bankruptcies, *BFP*’s reasoning also applies to bankruptcies under other chapters of the Code. COLLIER, *supra* note 18, ¶ 103.02.

22. COLLIER *supra* note 18, ¶ 700.01; *Overview of Bankruptcy Chapters*, THE U.S. DEP’T OF JUST., <https://bit.ly/3u703gH> [<https://perma.cc/6AH3-G5E8>] (updated May 14, 2015).

23. *See* 11 U.S.C. § 13. The Code has two countervailing goals: (1) to give an unfortunate debtor a “financial fresh start”; and (2) to protect creditors’ claims against a debtor. *See* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (explaining the financial fresh start that the Code envisions); KEVIN M. LEWIS, CONG. RSCH. SERV., R45137, BANKRUPTCY BASICS: A PRIMER, 11 (2018) (explaining that the Code protects creditors’ claims).

## 2. *Creditors*

A creditor is any party that has a claim against the debtor.<sup>24</sup> The Code defines a claim as a:

(A) right to payment, whether or not such right is reduced to judgment . . . disputed, undisputed, legal, equitable, secured, or unsecured; or

(B) right to an equitable remedy for breach of performance if such breach gives rise to a right to payment, whether or not such right to an equitable remedy is reduced to judgment . . . disputed, undisputed, secured, or unsecured.<sup>25</sup>

The rights of a creditor vary depending on the creditor's classification. The Code creates ten levels of priority for unsecured claims but does not mention secured claims in its delineation of priority.<sup>26</sup> Secured claims are left out of § 507 because secured creditors hold special rights in the property subject to their lien.<sup>27</sup>

### a. Secured Interests

A creditor with a lien secured on property must be paid out of the proceeds of the sale of the property before any other creditor can receive money from such a sale.<sup>28</sup> While this is beneficial to the creditor, a secured claim is secured only to the extent of the collateral's value and unsecured for any excess over the collateral's value.<sup>29</sup> At the conclusion of the bankruptcy proceeding, a judicial discharge<sup>30</sup> extinguishes only the personal liability of the debtor.<sup>31</sup> It does not, however, remove the creditor's lien on the property.<sup>32</sup>

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24. 11 U.S.C. § 101(10). The Code defines "creditor" to include numerous bodies:

(A) entity that has a claim against the debtor that arose at the time of or before the order for relief concerning the debtor;

(B) entity that has a claim against the estate of a kind specified in section 348(d), 502(f), 502(g), 502(h) or 502(i) of this title or

(C) entity that has a community claim.

*Id.*

25. *Id.* § 101(5).

26. *See id.* § 507(a).

27. *See id.* § 522(c)(2) (explaining that property exempted from the case may not be used to satisfy any debt except a debt secured by a lien); *see also* BRUCE A. MARKELL & LAWRENCE PONOROFF, *A SHORT AND HAPPY GUIDE TO BANKRUPTCY* 40–41 (2016) (explaining that the benefit of having a secured claim is the special rights in the property).

28. MARKELL & PONOROFF, *supra* note 27, at 40–41.

29. FED. R. BANK. P. 3012 advisory committee's note.

30. *See infra* Section II.A.3 (discussing judicial discharge).

31. MARKELL & PONOROFF, *supra* note 27, at 41.

32. *Id.*

Because liens survive discharge, it is said that “liens and other secured interests survive bankruptcy.”<sup>33</sup>

#### b. Unsecured Interests

Intuitively, many bankruptcy estates lack sufficient funds to satisfy debts owed to every creditor.<sup>34</sup> To allocate the remaining funds in a consistent manner, the Code created a ten-level hierarchy that assigns a level of priority to certain categories of claims.<sup>35</sup> Only general priority claims are included in this ten-level hierarchy.<sup>36</sup> General unsecured creditors that do not fall within one of the priority categories are compensated, *pro rata*, with any amount of money that is left after distributing to priority claims pursuant to the hierarchy.<sup>37</sup>

### 3. Chapter 7 Bankruptcy Process

In a Chapter 7 bankruptcy, the Chapter 7 trustee<sup>38</sup> liquidates the debtor’s non-exempt assets<sup>39</sup> and distributes the proceeds from the sale to satisfy the debtor’s obligations.<sup>40</sup> The debtor receives a

33. *Ferry v. Sanderfoot*, 500 U.S. 291, 297 (1991).

34. COLLIER, *supra* note 18, ¶ 507.02.

35. 11 U.S.C. § 507. The first class of claims is domestic support obligations. *Id.* § 507(1). The second class is administrative expenses. *Id.* § 507(2). The third class is unsecured claims under Section 11 U.S.C. § 502(f). *Id.* § 507(3). The fourth and fifth class related to claims surrounding employees. *Id.* § 507(4)–(5). The sixth class relate to claims of farmers and fisherman. *Id.* § 507(6). The seventh class relates to claims for deposits in connection with purchases or rentals of property or services that were not provided. *Id.* § 507(7). The eighth class is claims of governmental units. *Id.* § 507(8). The ninth class relates to the debtor’s deposit of money in an insured depository institution. *Id.* § 507(9). The final class is for claims relating to injury resulting from driving while intoxicated. *Id.* § 507(10).

36. COLLIER, *supra* note 18, ¶ 507.02.

37. 11 U.S.C. § 726(b). *Pro rata* distribution requires that each creditor get compensated “[p]roportionately; according to an exact rate, measure, or interest.” *Pro Rata*, BLACK’S LAW DICTIONARY (11th ed. 2019). The Code also requires that creditors of the same class receive equal treatment. *See* 11 U.S.C. §§ 726(b), 1322(a)(3). Therefore, each unsecured creditor must be compensated in the same amount until a creditor with a smaller claim has been compensated in full. *See* 11 U.S.C. §§ 726(b), 1322(a)(3).

38. COLLIER, *supra* note 18, ¶ 700.02; *see infra* Section II.A.5 (discussing trustees’ duties).

39. The debtor may exempt assets in accordance with § 522. 11 U.S.C. § 522(d).

40. COLLIER, *supra* note 18, ¶ 700.04. This is done in accordance with the Code’s priority distribution scheme found in § 507 for unsecured creditors. *See supra* notes 21–24 and accompanying text (explaining the Code’s priority scheme). Secured creditors are not included in this list because they are ensured payment to the extent of their secured collateral. *See* ADMINISTRATIVE OFFICE OF THE

judicial discharge of the remaining unpaid debts after the debtor's non-exempt assets have been used to pay unsecured creditors.<sup>41</sup>

Two types of parties may initiate a Chapter 7 bankruptcy proceeding.<sup>42</sup> The first type is a debtor, an individual with an unmanageable amount of debt; the second type is a creditor, an entity or individual seeking repayment of a debt.<sup>43</sup> Once a party files a bankruptcy petition with the court, the Code imposes an automatic stay, which prevents further collection actions by creditors.<sup>44</sup>

The debtor must file numerous documents with the court as part of a bankruptcy petition.<sup>45</sup> The court then appoints a trustee to oversee the proceeding.<sup>46</sup> The court sends notice of the bankruptcy to all creditors identified by the debtor in the case<sup>47</sup> and gives the creditors a deadline for filing proofs of claim.<sup>48</sup> In accor-

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UNITED STATES COURTS, BANKRUPTCY BASICS 9–22 (2011); *see supra* notes 28–33 (discussing secured interests).

41. COLLIER, *supra* note 18, ¶ 700.05.

42. *Id.* ¶ 700.02.

43. *Id.*

44. 11 U.S.C. § 362(c). A U.S. House of Representatives report explains the significance of the automatic stay:

The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.

H.R. REP. NO. 95-595, at 340–44 (1977).

45. Among these documents are form schedules A–J. *Bankruptcy Forms*, U. S. COURTS, <https://bit.ly/3c9zznG> [<https://perma.cc/XDY2-DSBX>] (last visited Mar. 21, 2021). The schedules satisfy most of the debtor's reporting duties outlined in § 521. *See* 11 U.S.C. § 521(a)–(c), (f), (h). Schedules A and B define the bankruptcy estate by providing all real property and personal property the debtor owns. *Bankruptcy Forms*, U. S. COURTS, <https://bit.ly/3c9zznG> [<https://perma.cc/XDY2-DSBX>] (last visited Mar. 21, 2021). Schedule C allows the debtor to exempt certain property from the bankruptcy proceedings. *Id.* Section 522 outlines the property that may be exempted. *See* 11 U.S.C. § 522(d). Schedule D requires the debtor to list the creditors who hold claims secured by property. *Bankruptcy Forms*, U. S. COURTS, <https://bit.ly/3c9zznG> [<https://perma.cc/XDY2-DSBX>] (last visited Mar. 21, 2021). Schedule E requires the debtor to list priority creditors. *Id.* Schedule F requires the debtor to list all general, unsecured creditors. *Id.* Schedule G requires the debtor to list all executory contracts and leases. *Id.* Schedule H requires the debtor to list any co-debtors if applicable. *Id.* Schedule I requires the debtor to list his full, gross income. *Id.* Finally, Schedule J requires the debtor to list his monthly expenses. *Id.* The debtor must use the provided forms in his petition. FED. R. BANK. P. 9009.

46. COLLIER, *supra* note 18, ¶ 700.02; *see infra* Section II.A.5 (discussing trustees' duties).

47. COLLIER, *supra* note 18, ¶ 700.03.

48. *Id.* A proof of claim is what a creditor files to document its assertion that the debtor owes it money. 1 COLLIER CONSUMER BANKRUPTCY PRACTICE GUIDE ¶ 19.04 (2019).



dance with § 341, the trustee conducts a creditors' meeting, usually within 40 to 60 days after the petition is filed, at which time "creditors and the trustee have an opportunity to examine the debtor."<sup>49</sup> Following the creditors' meeting, the trustee liquidates the estate's non-exempt assets and distributes the proceeds to the creditors in accordance with the distribution scheme in § 507.<sup>50</sup> The court will then give all creditors a deadline by which any creditor may object to a judicial discharge of the estate's remaining debt.<sup>51</sup> If no creditor objects, the court will discharge the estate's remaining unpaid debts.<sup>52</sup> After a debtor receives a judicial discharge, the debtor is no longer personally liable for any unpaid debts that were at issue in the bankruptcy proceeding, and creditors may no longer pursue those debts.<sup>53</sup>

#### 4. Chapter 13 Bankruptcy Process

Whereas Chapter 7 involves liquidating assets to satisfy debts, Chapter 13 requires reorganizing and paying debt through a long-term payment plan.<sup>54</sup> Unlike a Chapter 7 proceeding that can be initiated by a creditor, the debtor<sup>55</sup> must initiate a Chapter 13 proceeding.<sup>56</sup> The debtor must also create and propose a repayment plan.<sup>57</sup> The court will conduct a hearing<sup>58</sup> and confirm the debtor's repayment plan if it satisfies the requirements of § 1325.<sup>59</sup> The plan

49. COLLIER, *supra* note 18, ¶ 700.03; 11 U.S.C. § 341.

50. 11 U.S.C. § 507(a); *see supra* notes 22–24 and accompanying text (discussing the Code's priority distribution scheme). Alternatively, the trustee might find there are no assets that can be liquidated. Gary E. Sullivan, *A Fresh Start to Bankruptcy Exemptions*, *BYU L. REV.* 335, 396 (2018). In this case, the debts are discharged without compensating creditors. *Id.*

51. COLLIER, *supra* note 18, ¶ 700.04. Grounds to prevent a judicial discharge are found in § 727(a), and a creditor must prove that one of the listed reasons exists to successfully prevent a discharge. *See* 11 U.S.C. § 727(a); COLLIER, *supra* note 18, ¶ 727.01.

52. COLLIER, *supra* note 18, ¶ 700.05.

53. *Id.* This is true of unsecured creditors; however, claims of secured creditors survive a judicial discharge. *See supra* Section II.A.2.a (explaining secured creditors rights).

54. *See* 11 U.S.C. §§ 1301–30.

55. Section 109 limits who may be a debtor in a Chapter 13 proceeding. *See id.* §109(e). Only an individual or an individual and a spouse with regular income who owes unsecured debt less than \$419,275 and secured debts less than \$1,184,200 may be a debtor under Chapter 13. *Id.* Section 109 also imposes an obligation for a debtor to undergo debt counseling prior to filing the bankruptcy petition. *Id.* § 109(h).

56. COLLIER, *supra* note 18, ¶ 1300.15.

57. 11 U.S.C. § 1321.

58. *Id.* § 1324(a).

59. 11 U.S.C. § 1325(a). Section 1325 explains the requirements a plan must satisfy for a court to confirm it and incorporates by reference the requirements of

must provide the trustee with all or a portion of the debtor's disposable income, as necessary to complete the plan;<sup>60</sup> provide for full payment of all claims entitled to priority in § 507;<sup>61</sup> treat similarly classified claims in the same manner if the plan classifies claims;<sup>62</sup> and provide continuous payments for three or five years.<sup>63</sup>

Similar to a Chapter 7 proceeding, the automatic stay in a Chapter 13 proceeding becomes effective upon the debtor's filing for bankruptcy.<sup>64</sup> The court will also appoint a trustee who supervises the proceeding to make sure that the plan accords with § 507 and that the debtor makes timely payments.<sup>65</sup> The debtor will receive a judicial discharge after successfully completing the court-approved repayment plan.<sup>66</sup>

### 5. *The Trustee's Duties and Powers*

Both Chapter 7 and 13 require a trustee to ensure compliance with the bankruptcy rules and provisions.<sup>67</sup> A trustee's duties differ slightly from a Chapter 7 to a Chapter 13 proceeding.<sup>68</sup>

Congress listed a Chapter 7 trustee's duties under § 704.<sup>69</sup> The trustee must, among other things, collect and liquidate the debtor's non-exempt property,<sup>70</sup> ensure that the debtor fulfills his obligations under the Code,<sup>71</sup> investigate the financial affairs of the debtor,<sup>72</sup> apprise parties of the status of the estate,<sup>73</sup> and make a final report and file a final account of the administration of the es-

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forming a plan under § 1322. 11 U.S.C. § 1325(a)(1). When a plan is confirmed, its provisions "bind the debtor and each creditor, whether or not the claim of such creditor is provided for by the plan, and whether or not such creditor has objected to, has accepted or has rejected the plan." *Id.* § 1327(a). In other words, "the effect of confirmation is sweeping" and binds every party to the terms therein. MARKELL & PONOROFF, *supra* note 27, at 223.

60. 11 U.S.C. § 1322(a)(1).

61. *Id.* §§ 1322(a)(2), 507(a); *see supra* notes 22–24 and accompanying text (discussing the Code's priority distribution scheme).

62. 11 U.S.C. § 1322(3).

63. *Id.* § 1322(d). Payment plans are usually over a period of three years, but the court may extend the plan to five years for cause. *Id.* § 1322(d)(2)(C).

64. *Id.* § 362(c).

65. *Id.* §§ 1302(b)(2)(B)–(C), 1302(b)(5).

66. COLLIER, *supra* note 18, ¶ 1328.01.

67. MARKELL & PONOROFF, *supra* note 27, at 203.

68. The Chapter 13 trustee plays a more active role than the Chapter 7 trustee. *Id.* at 203–04.

69. *See* 11 U.S.C. § 704(a).

70. *Id.* § 704(a)(1).

71. *Id.* § 704(a)(3).

72. *Id.* § 704(a)(4).

73. *Id.* § 704(a)(7).

tate.<sup>74</sup> The trustee must also examine creditors' proofs of claim<sup>75</sup> if there is a reason to do so<sup>76</sup> and object to a judicial discharge if it would be improper.<sup>77</sup>

Section 1302 lists a Chapter 13 trustee's duties and incorporates many Chapter 7 trustee duties by reference.<sup>78</sup> Additionally, a Chapter 13 trustee must dispose of money received in accordance with regulations,<sup>79</sup> attend any hearing that concerns the value of property or confirmation or modification of the plan,<sup>80</sup> and advise and assist the debtor in performing under the plan.<sup>81</sup>

Under Chapter 7 and 13, the trustee has the power to increase the size of the estate by recovering assets that have improperly left the estate by avoiding pre-bankruptcy-petition transfers.<sup>82</sup>

## 6. Avoidance Provisions

Two Code provisions govern a trustee's ability to avoid pre-petition transfers: (1) § 548, which governs the avoidance of fraudulent transfers,<sup>83</sup> and (2) § 547, which governs the avoidance of preferential transfers.<sup>84</sup>

Section 548 serves to capture property that the debtor improperly put out of the reach of creditors prior to filing bankruptcy.<sup>85</sup> Fraudulent transfer law has long been applied to debtor-creditor relationships,<sup>86</sup> and "[S]ection 548 incorporated the law of fraudulent transfers into the Bankruptcy Code."<sup>87</sup> Section 548, in relevant part, provides:

74. *Id.* § 704(a)(9).

75. "A proof of claim is a written statement setting forth a creditor's claim." FED. R. BANK. P. 3001(a). While § 501(a) permits a creditor to file a proof of claim, Bankruptcy Rule 3002 requires a creditor to file a proof of claim if it is seeking a distribution from the estate. *See* 11 U.S.C. § 501(a); FED. R. BANK. P. 3002(c)(a).

76. 11 U.S.C. § 704(a)(5).

77. *Id.* § 704(a)(6).

78. *See id.* § 1302(b)(1). This provision incorporates § 704(a)(2)–(7) and (9) by reference. *See id.*

79. *Id.* § 1302(b)(3).

80. *Id.* § 1302(b)(2).

81. *Id.* § 1302(b)(4).

82. The conditions for avoidance are set out in several sections, each of which govern a different mechanism of avoidance. *See id.* §§ 544–53, 724(a). Relevant to this Comment are the trustee's powers to avoid preferential transfers and fraudulent transfers. *See id.* §§ 547, 548.

83. *See id.* § 548.

84. *See id.* § 547.

85. *In re Brasby*, 109 B.R. 113, 121 (Bankr. E.D. Pa. 1990).

86. COLLIER, *supra* note 18, ¶ 548.01.

87. *Id.* The Code imposes restrictions to narrow the application of fraudulent transfer law in Bankruptcy proceedings. *Id.*

(a)(1) The trustee may avoid any transfer<sup>88</sup> . . . of an interest of the debtor in property . . . that was made . . . on or within 2 years before the date of the filing of the petition, if the debtor voluntarily or involuntarily—

a)(1)(B)(i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and

(a)(1)(B)(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.<sup>89</sup>

Under § 548, a trustee may avoid transfers that a debtor makes through “actual fraud” or “constructive fraud.”<sup>90</sup> Constructive fraud exists when the asset is not exchanged for a “reasonably equivalent value” and is transferred within two years prior to the debtor’s filing the bankruptcy petition.<sup>91</sup> The Code, however, does not define “reasonably equivalent value.”<sup>92</sup>

Section 547, the preference provision, is similar to § 548 in that it gives a trustee the power to avoid pre-petition transfers, but there are some important differences between the sections.<sup>93</sup> First, the goal of § 547 is to prevent a transfer that benefits one creditor at the expense of other creditors.<sup>94</sup> Section 547, in relevant part, provides:

(b) the trustee may . . . avoid any transfer of an interest of the debtor in property—

(1) to or for the benefit of a creditor;

(2) for or on account of an antecedent debt owed by the debtor before such transfer was made;

(3) made while the debtor was insolvent;

(4)(A) made on or within 90 days before the date of the filing of the petition . . . ; and

(5) that enables such creditor to receive more than such creditor would receive if—

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88. “Transfer” is defined as “the creation of a lien; the retention of title as a security interest; the foreclosure of a debtor’s equity of redemption; or each mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property; or an interest in property.” 11 U.S.C. § 101(54).

89. 11 U.S.C. §§ 548(a)(1)(B)(i), 548(a)(1)(B)(ii)(I).

90. *Id.* § 548(a)(1)(A)–(B). Actual fraud is when a transfer is made with actual intent to hinder, delay, or defraud a past or future creditor. S. Rep. No. 95-989, at 89 (1978).

91. 11 U.S.C. § 548(a)(1)(B).

92. *See BFP v. Resolution Trust Corp.*, 511 U.S. 531, 546–47 (1994) (responding to Justice Souter’s dissent, the majority explained that the statute was ambiguous).

93. COLLIER, *supra* note 18, ¶ 548.01.

94. *Microage Inc. v. Mitsubishi Elec. & Elecs. USA, Inc. (In re MICROAGE Corp.)*, 288 B.R. 855, 860 (Bankr. D. Ariz. 2003).

- (A) the case were a case under chapter 7 of this title;
- (B) the transfer had not been made; and
- (C) such creditor received payment of such debt to the extent provided by the provisions of this title.<sup>95</sup>

Next, § 547 looks retroactively at the 90 days prior to filing a bankruptcy petition, instead of at the 2-year period used in § 548.<sup>96</sup> Third, and most importantly, the standard for when a trustee may avoid a pre-petition transfer is different.<sup>97</sup> Section 548 asks whether the transfer was in exchange for a “reasonably equivalent value” of the asset.<sup>98</sup> Section 547, however, asks whether the creditor received more than the creditor would have received, if no advance payment were made and the case had been filed under Chapter 7.<sup>99</sup>

### B. Forced Sales

A trustee may attempt to avoid two types of forced sales: a mortgage foreclosure sale and a tax foreclosure sale.<sup>100</sup>

A mortgage foreclosure sale occurs when a person fails to make timely payments on his or her mortgage, and the mortgagee forces the sale of the property to recover the money it loaned to the debtor.<sup>101</sup> Generally, state foreclosure procedure provides safeguards to protect a debtor.<sup>102</sup>

A tax foreclosure sale occurs when a person fails to pay some form of taxes for a long enough period of time to require such action by the taxing entity.<sup>103</sup> For example, a municipality may force

95. 11 U.S.C. § 547(b).

96. Compare 11 U.S.C. § 547(b)(4)(A), with 11 U.S.C. § 548(a)(1). If, however, the creditor is an insider, § 547 extends the look-back window to one year prior to the bankruptcy petition. 11 U.S.C. § 547(b)(4)(B).

97. COLLIER, *supra* note 18, ¶ 548.01.

98. 11 U.S.C. § 548(a)(1)(B)(i).

99. 11 U.S.C. § 547(b)(5). The transfer will be subject to avoidance if the creditor received more in the advance payment than it would have under a Chapter 7 proceeding. *Id.*

100. See *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 336 (S.D. Tex. 1999) (involving a mortgage foreclosure sale); see also *RL Mgmt. Group, LLC v. Coffman (In re RL Mgmt. Grp., LLC)*, 2014 Bankr. LEXIS 206, at \*1 (E.D. Mich. Jan. 10, 2014) (involving a tax foreclosure sale).

101. Bill Fay, *Foreclosures*, DEBT.ORG, <https://bit.ly/32vRCOK> [<https://perma.cc/CA44-5BXB>] (May 18, 2020).

102. *Talbot v. Fed. Home Loan Mortg. Corp. (In re Talbot)*, 254 B.R. 63, 68 (Bankr. D. Conn. 2000). These protections sometimes include competitive bidding. *Id.*

103. Oddette Williamson & Jillian McLaughlin, *Tax Lien Sales Put Low-Income Seniors and the Disabled at Risk of Foreclosure*, 34 AMERICAN BAR ASS'N 7 (2012).

the sale of a home to recover unpaid property taxes.<sup>104</sup> Tax sales sometimes require competitive bidding, which is similar to the procedural safeguards found within mortgage foreclosure sale procedures.<sup>105</sup>

State property law governs both mortgage foreclosures and tax sales, and each state has different policies and procedures for forced sales.<sup>106</sup> This Comment will later discuss the interplay between federal bankruptcy law and state foreclosure law.<sup>107</sup>

### C. *Pre-BFP Cases*

Prior to the Supreme Court's ruling in *BFP v. Resolution Trust Corp.*,<sup>108</sup> federal bankruptcy courts routinely applied § 547 to avoid state mortgage and tax foreclosures if the sale satisfied the elements of § 547.<sup>109</sup> The court's holding in *In Re Wheeler*<sup>110</sup> typifies the pre-*BFP* cases that applied § 547 to avoid mortgage foreclosure sales:

FNMA is receiving property with a market value several thousand dollars in excess of their claim. Thus, it becomes evident that the foreclosure sale did enable FNMA to receive more than they would receive in a Chapter 7 liquidation. The court determines that this foreclosure sale was a preferential transfer under §547(b).<sup>111</sup>

### D. *BFP v. Resolution Trust Corp.*

In *BFP v. Resolution Trust Corp.*, the U.S. Supreme Court addressed the issue of whether the Code—specifically, § 548 fraudu-

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104. *Id.*

105. *Smith v. SIPI, LLC (In re Smith)*, 811 F.3d 228, 234 (7th Cir. 2016) (explaining that there are interest rate bidding practices that are not similar to the competitive price bidding practices seen in mortgage foreclosure sales).

106. *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 540 (1994).

107. *See infra* notes 140–43, 158 and accompanying text (discussing federalism concerns).

108. *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994).

109. *See In re Smith*, 21 B.R. 345, 352 (Bankr. M.D. Fla. 1982) (finding the mortgage foreclosure sale constituted a preference under § 547); *In re Park North Partners, Ltd.*, 80 B.R. 551, 555 (N.D. Ga. 1987) (remanding the case for a determination of whether the creditor received more than he would have under a Chapter 7 bankruptcy and concluding that the mortgage foreclosure sale would be subject to avoidance if the elements of § 547 were satisfied); *In re Winters*, 119 B.R. 283, 285 (M.D. Fla. 1990) (finding the foreclosure sale satisfied the elements of § 547 when comparing the sale price to the fair market value of the asset); *Villarreal v. Showalter (In re Villarreal)*, 413 B.R. 633, 642 (S.D. Tex 2009) (finding the transfer of the property in the foreclosure sale satisfied each element of § 547 and accordingly avoided the foreclosure sale).

110. *In re Wheeler*, 34 B.R. 818 (N.D. Ala. 1983).

111. *Id.* at 821.

lent transfers—could be used to avoid a mortgage foreclosure sale that complied with state foreclosure law.<sup>112</sup> The Court ultimately held that the Code could not avoid such a transfer because a “‘reasonably equivalent value,’ for foreclosed property, is the sale price in fact received at the foreclosure sale, so long as the requirements of the State’s foreclosure law have been complied with.”<sup>113</sup>

In *BFP*, a partnership purchased a home in California, subject to a deed of trust,<sup>114</sup> with Imperial Savings Association (“Imperial”).<sup>115</sup> The partnership then granted a second deed of trust to the owners of the home as security for a promissory note.<sup>116</sup> The partnership failed to make payments under the first deed of trust, and Imperial entered a notice of default.<sup>117</sup> After some delays,<sup>118</sup> foreclosure proceedings concluded with a sale on July 12, 1989, when Paul Osborne, a third party, purchased the home for \$433,000.<sup>119</sup> In October 1989, the partnership filed Chapter 11 bankruptcy and petitioned the bankruptcy court to set aside the conveyance to Osborne as a fraudulent transfer under § 548.<sup>120</sup>

The court analyzed whether the amount received at the foreclosure sale constituted a “reasonably equivalent value” of the home.<sup>121</sup> This inquiry turned on Congress’s intent by using the phrase “reasonably equivalent value” and whether that intent was ambiguous.<sup>122</sup> Initially, the Supreme Court looked at the three existing approaches used to determine reasonably equivalent value.<sup>123</sup>

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112. See *BFP*, 511 U.S. at 533.

113. *Id.* at 545.

114. A deed of trust is “[a] deed conveying title to real property to a trustee as security until the grantor repays a loan.” *Deed of Trust*, BLACK’S LAW DICTIONARY (11th ed. 2019).

115. *BFP*, 511 U.S. at 533.

116. *Id.*

117. *Id.* Under many states’ laws, prior to foreclosing on a property, a loaning entity is required to file a notice of default which informs the borrower of their failure to pay. Lydia Nussbaum, *ADR’s Place in Foreclosure: Remediating the Flaws of a Securitized Housing Market*, 34 CARDOZO L. REV. 1899, 1920–21 (2013).

118. The foreclosure proceedings were temporarily delayed when the partnership filed for voluntary bankruptcy. *BFP*, 511 U.S. at 533. Thereafter, the partnership’s bankruptcy petition was dismissed, and the foreclosure sale commenced. *Id.* at 534.

119. *Id.* at 533–34.

120. *Id.* at 534. Sections 547 and 548 are applicable to bankruptcies filed under every section of the Code. COLLIER, *supra* note 18, ¶ 103.02.

121. *BFP*, 511 U.S. at 534 (explaining that the house sold, at auction, for \$433,000, but “Petitioner alleged that the home was actually worth over \$725,000 at the time of the sale to Osborne”).

122. *Id.* at 535. Specifically, the Court interpreted what Congress intended as the benchmark against which a court could judge the value of a forced sale asset and, thus, whether the sale achieved a reasonably equivalent value. See *id.*

123. See *id.*

The first approach, the Fifth Circuit's *Durrett*<sup>124</sup> view, used an asset's fair market value as the benchmark against which a court could judge whether a transfer was for a reasonably equivalent value.<sup>125</sup> The *Durrett* view effectively created a federal minimum sale price that state foreclosure sales would have to meet.<sup>126</sup> If not met, the sale would be subject to avoidance.<sup>127</sup>

The second approach, the Seventh Circuit's *all facts and circumstances* approach, sought a middle ground between the fair market value and the sale price of the foreclosure sale itself as the benchmark for reasonably equivalent value.<sup>128</sup> Under normal circumstances, this method would incorporate a rebuttable presumption of reasonably equivalent value when the sale in question was a state foreclosure sale.<sup>129</sup> This standard implicitly set a reasonable forced sale price as the standard against which to judge reasonably equivalent value.<sup>130</sup>

The final approach, the Ninth Circuit's, equated the price received at a non-collusive, regularly conducted real estate foreclosure sale with a reasonably equivalent value.<sup>131</sup> The benchmark for reasonably equivalent value was the sale price itself.<sup>132</sup>

The Supreme Court reasoned that the concept of fair market value is inapplicable to a forced sale scenario, stating that "fair market value" presumes market conditions that, by definition, simply do not obtain in the context of a forced sale."<sup>133</sup> The Court noted that because the limitations inherent in a forced sale, property sold in such a manner was "worth less" than its fair market counterpart.<sup>134</sup> Further, the Court explained that Congress could have used the phrase "'received less than fair market value in exchange for such transfer or obligation'" if it believed that fair market value were the appropriate benchmark.<sup>135</sup> However, Congress

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124. *Durrett v. Washington Nat. Ins. Co.*, 621 F.2d 201 (5th Cir. 1980).

125. *See Durrett*, 621 F.2d at 203–04.

126. *Id.*

127. *See e.g., BFP*, 511 U.S. at 535 (explaining that the *Durrett* court postulated a minimum sale price of 70 percent of the home's fair market value to escape the trustee's avoidance powers under § 548).

128. *See In re Bundles*, 856 F.2d 815, 824 (7th Cir. 1988).

129. *See id.*

130. *See id.* (explaining that a court may begin its analysis with the fair market value but acknowledged that forced sales create unique market environments and concluding that bankruptcy courts are to consider "the fair market value as affected by the fact of foreclosure").

131. *See BFP*, 511 U.S. at 535.

132. *Id.*

133. *Id.* at 538.

134. *Id.* at 539.

135. *Id.* at 537.



intentionally used the phrase “reasonably equivalent value,” which suggested Congress did not intend to use fair market value as a benchmark.<sup>136</sup> Accordingly, the Court dismissed the *Durrett* approach, which used fair market value.<sup>137</sup>

The Court was then left with two benchmarks against which it could judge “reasonably equivalent value”: first, the Ninth Circuit’s *foreclosure-sale price itself* approach and second, the Seventh Circuit’s *reasonable foreclosure sale price* approach.<sup>138</sup> The Court rejected the *reasonable foreclosure sale price* approach after discussing the federalism concerns posed by the Code’s interaction with state foreclosure law.<sup>139</sup>

In rejecting this approach, the Court cited the co-existence of fraudulent transfer law and state foreclosure law dating back 400 years to old English law.<sup>140</sup> The Court explained that the mere inadequacy of a sale price had never been a basis for setting aside a forced sale in the context of federal fraudulent transfer law.<sup>141</sup> The Court conceded that federal law trumps state law when a conflict exists.<sup>142</sup> However, absent clear congressional intent to disrupt the balance that had been forged over hundreds of years, the Court would not allow the Federal Bankruptcy Code to impede state foreclosure law.<sup>143</sup>

The Court concluded that the Ninth Circuit’s *forced sale price itself* is the correct benchmark against which to evaluate whether a foreclosure sale commanded a “reasonably equivalent value.”<sup>144</sup> A bankruptcy trustee cannot avoid a state mortgage foreclosure sale

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136. *Id.* (explaining that § 548 is the only instance in the Code that Congress used this phrase).

137. *Id.*

138. *See id.* at 538, 540.

139. *See id.* at 540–45.

140. *See id.* at 540–41.

141. *BFP*, 511 U.S. at 542 (noting that inadequate price may, however, be a basis for avoidance under some states’ foreclosure laws).

142. *Id.* at 546 (agreeing with the dissent “that where the ‘meaning of the Bankruptcy Code’s text is itself clear,’ its operation is unimpeded by contrary state law or prior practice”) (internal citations omitted).

143. *Id.* at 540, 543. The dissent explained that the majority was requiring something more than clear intent, but the majority reasoned that because the language is ambiguous, Congress’s intent could not be clear. *Id.* at 551 (Souter, J., dissenting); *id.* at 540, 543 (majority opinion). The decision to view the phrase as ambiguous was influenced by the important state interest of ensuring stability of titles to real property after foreclosure sales. *Id.* at 542.

144. *Id.* at 545. Implicit in the Supreme Court’s position is circular reasoning that the price received in a foreclosure sale is a reasonably equivalent value of the asset, merely because it was the price received. *See id.* at 545, 549. This ensured federal law would not encroach on state law by preventing the Bankruptcy Code from avoiding any validly conducted state foreclosure sale. *See id.* at 540–43.

that complies with state law—regardless of the sale price.<sup>145</sup> The Court expressly limited its holding to mortgage foreclosures and noted that the result may be different in a case involving other types of forced sales, such as tax foreclosure sales.<sup>146</sup>

The dissent believed that the benchmark for reasonably equivalent value advocated by the majority was implausible.<sup>147</sup> However, the dissent did not offer an alternative approach.<sup>148</sup>

Regarding the federalism issue, the dissent explained that the Code should trump state law.<sup>149</sup> The dissent explained that “[a]lthough this formulation [of § 548] makes no pretense to mathematical precision, an ordinary speaker of English would have no difficulty grasping its basic thrust.”<sup>150</sup> On this basis, the dissent concluded that the plain meaning of the statute was clear.<sup>151</sup> When the plain meaning of a statute is clear, the state regulation must yield to the extent it actually conflicts with federal law.<sup>152</sup> The dissent concluded that the language of § 548 granted to the bankruptcy trustee the power to avoid foreclosure sales that, despite complying with state law, failed to exchange the asset for a “reasonably equivalent value.”<sup>153</sup>

#### E. Expansion of BFP Within § 548

Despite the Court’s disclaimer that its *BFP* decision was limited to § 548 mortgage foreclosure sales, bankruptcy courts have had a uniform approach in applying *BFP*’s reasoning to § 548 tax sales.<sup>154</sup> Courts have determined that *BFP*’s reasoning should ap-

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145. *Id.*

146. *Id.* at n.3.

147. *Id.* at 551 (Souter, J., dissenting).

148. See *BFP*, 511 U.S. at 551 (Souter, J., dissenting); *id.* at 547 (majority opinion) (“[O]ne searches Justice Souter’s opinion in vain for any alternative responses to the question of the transferred property’s worth.”).

149. *Id.* at 566–67 (Souter, J., dissenting).

150. *Id.* at 552.

151. See *id.* The dissent also expressed dissatisfaction with the majority’s position that, due to the importance of the state interest in maintaining good titles to real property, Congress must either expressly override the state interest or not override at all. *Id.*

152. *Id.* at 567 (explaining that this is not changed even when the federal law does not use language that pre-empts state law).

153. *Id.* at 569–70.

154. See *Tracht Gut, LLC v. Cnty. of L.A. (In re Tracht Gut, LLC)*, 503 B.R. 804, 815–17 (B.A.P. 9th Cir. 2014) (explaining how courts have approached *BFP*’s application to pre-petition tax foreclosure sales in the context of § 548 avoidance).

ply where a state's foreclosure sale requires competitive bidding and should not apply where there is no competitive bidding.<sup>155</sup>

### F. *The Circuit Split*

As previously noted, prior to the Supreme Court's ruling in *BFP*, federal bankruptcy courts uniformly applied § 547 to avoid state foreclosure sales.<sup>156</sup> Following *BFP*, bankruptcy courts have split on the question of whether *BFP*'s reasoning should extend to § 547 preferences.<sup>157</sup> The courts that have extended *BFP* to § 547 have done so mainly for one of two reasons. First, some courts have reasoned that *BFP*'s federalism policy considerations are as applicable to § 547 as § 548.<sup>158</sup> These courts believe that the same federalism concerns that shaped the Supreme Court's reasoning in *BFP* are present in and guide a § 547 preference analysis.<sup>159</sup>

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155. Compare *Kojima v. Grandote Int'l Ltd. Liab. Co. (In re Grandote Country Club Co.)*, 252 F.3d 1146, 1150 (10th Cir. 2001) (applying the Colorado Uniform Fraudulent Transfer Act, the court extended *BFP* to a tax sale that required competitive bidding), with *Sherman v. Rose (In re Sherman)*, 223 B.R. 555, 558–59 (B.A.P. 10th Cir. 1998) (applying Wyoming tax sale law, the court declined to extend *BFP* to tax sale that did not require competitive bidding); see also *Smith v. SIPI, LLC (In re Smith)*, 811 F.3d 228, 234 (7th Cir. 2016) (explaining that *BFP* did not apply because Illinois tax sales did not require competitive bidding).

156. See *infra* Section II.B (explaining how courts handled cases which involved using § 547 to avoid mortgage or tax foreclosure sales prior to *BFP*).

157. Compare *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 336 (S.D. Tex. 1999) (extending *BFP*'s reasoning to § 547), with *Andrews Nw. Bank Minn., N.A. v. Andrews (In re Andrews)*, 262 B.R. 299, 306 (M.D. Pa. 2001) (declining to extend *BFP*'s reasoning to § 547). See also Andrew Butler, *Vexatious Valuations: The Impropriety of Importing BFP to Preference Actions*, 27 J. BANKR. L. & PRAC. 1, 4–6 (2018) (explaining the arguments of each side of the circuit split regarding § 547).

158. See *RL Mgmt. Group, LLC v. Coffman (In re RL Mgmt. Grp., LLC)*, No. 13-51849, 2014 Bankr. LEXIS 206, at \*16–18 (E.D. Mich. Jan. 10, 2014) (explaining the applicability of state interests articulated in *BFP* to a § 547 analysis); *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 341 (S.D. Tex. 1999) (explaining that “[t]o hold this foreclosure to be a preferential transfer would create the same problems with state real property title records that would have been created by classifying the transaction as a fraudulent transfer”).

159. See *RL Mgmt. Group, LLC v. Coffman (In re RL Mgmt. Grp., LLC)*, No. 13-51849, 2014 Bankr. LEXIS 206, at \*16–18 (E.D. Mich. Jan. 10, 2014) (explaining the applicability of state interests articulated in *BFP* to a § 547 analysis); *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 341 (S.D. Tex. 1999) (explaining that “[t]o hold this foreclosure to be a preferential transfer would create the same problems with state real property title records that would have been created by classifying the transaction as a fraudulent transfer”).

Second, other courts that have extended *BFP* have done so by extending *BFP*'s presumption that the price received at a forced sale reflects the value of the property.<sup>160</sup> One court reasoned:

It compels the conclusion that a pre-petition transfer of a debtor's interest in real property to a lien creditor who purchases the property at a regularly-conducted, non-collusive sheriff's sale and who then sells the property to a third party for an amount greater than the amount of its lien is not avoidable in accordance with § 547(b) as a preference. In particular, the lien creditor does *not* "receive more" for purposes of § 547(b)(5) than it would receive in a chapter 7 liquidation.<sup>161</sup>

Some bankruptcy courts, however, have not extended *BFP*'s reasoning to § 547.<sup>162</sup> These courts have not done so for one of two main reasons. First, *BFP* interpreted the phrase "reasonably equivalent value," which does not appear in § 547.<sup>163</sup> Because § 547 uses different language, courts have concluded that § 548's reasoning has no place in a § 547 analysis.<sup>164</sup> Second, though judicial intervention was necessary to interpret the ambiguous § 548

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160. See *Veltre v. Fifth Third Bank (In re Veltre)*, 562 B.R. 890, 893–94 (W.D. Pa. 2017) (adopting the reasoning of *Pulcini* and *Rocco*, which applied *BFP*'s rationale of the value of an asset to § 547); *JP Morgan Chase Bank v. Rocco (In re Rocco)*, 319 B.R. 411, 416 (W.D. Pa. 2005) (affirming the reasoning used in *Pulcini* and explaining that even under an *Andrews*'s fair market value analysis the result in the case would not differ); see also *Rambo v. Chase Manhattan Mortg. Corp. (In re Rambo)*, 297 B.R. 418, 429–31 (E.D. Pa. 2003) (discussing the conclusions of cases based on the benchmark against which the court valued the asset).

161. *Chase Manhattan Bank v. Pulcini (In re Pulcini)*, 261 B.R. 836, 844 (W.D. Pa. 2001); see *JP Morgan*, 319 B.R. at 416 (affirming the reasoning used in *Pulcini*).

162. See *Hackler v. Arianna Holdings Co., LLC (In re Hackler)*, 571 B.R. 662, 668 (D.N.J. 2017) (holding that the trustee could avoid a pre-petition tax foreclosure sale); *Berley Assocs. v. Eckert (In re Berley Assocs.)*, 492 B.R. 433, 443 (D.N.J. 2013) (holding the trustee could avoid a pre-petition tax foreclosure sale and citing *Andrews* with approval); *Nw. Bank Minn., N.A. v. Andrews (In re Andrews)*, 262 B.R. 299, 306 (M.D. Pa. 2001) (declining to extend *BFP*'s reasoning to § 547).

163. See *Whittle Dev., Inc. v. Branch Banking Trust Co. (In re Whittle Dev., Inc.)*, 463 B.R. 796, 802 (N.D. Tex. 2011) (explaining that *BFP*'s section 548(a)(2)(A) analysis "concerned what, as a matter of law, 'reasonably equivalent value' meant. No such legal issue presents itself in avoidance actions under section 547(b)(5)(A) since the operative question is simply whether the creditor did in fact receive more than it would have had the transfer not occurred") (internal citations omitted); see also Andrew Butler, *Vexatious Valuations: The Impropriety of Importing BFP to Preference Actions*, 27 J. BANKR. L. & PRAC. 1, 4–6 (2018) (explaining that some courts view *BFP* as having nothing to offer in the context of § 547).

164. See *supra* note 163 and accompanying text (explaining why *BFP* is inapplicable in light of different statutory language).

phrase “reasonably equivalent value,” there is no need for such interpretation in § 547.<sup>165</sup> Unlike § 548’s “reasonably equivalent value,” § 547’s phrase “received more than under a Chapter 7 liquidation” is mathematically certain.<sup>166</sup> Accordingly, judicial interpretation is unwarranted, and § 547 may be used to avoid all transfers that satisfy its elements—even foreclosures that comply with state law.<sup>167</sup>

### G. Significance

The resolution of this circuit split is important to the creditor-debtor relationship. Creditors will be impacted directly. Applying *BFP*’s reasoning to § 547 would negatively impact creditors. A debtor could transfer assets out of its estate, even in violation of § 547, and the trustee would not be able to avoid the sale if it complied with state foreclosure laws.<sup>168</sup> If the transfer were a foreclosure sale conducted in accordance with state law, the debtor’s estate would have a smaller pool of assets to satisfy all of its creditors’ debts.<sup>169</sup> Accordingly, each creditor would receive less from the estate because of the transfer that violated § 547.<sup>170</sup>

If *BFP* is not applied to § 547 sales, unsecured creditors may require that the trustee avoid validly conducted state foreclosure

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165. See *Villarreal v. Showalter (In re Villarreal)*, 413 B.R. 633, 642 (S.D. Tex. 2009) (explaining that the *BFP* Court used policy to reason through § 548, but “[s]ection 547 does not lend itself to such an interpretation and th[is] Court may not ignore Congressional language in favor of judicial policy”); *Andrews*, 262 B.R. 306 (asking “[w]hy not apply simple mathematics to this issue?”). The court explained that “[Congress] chose to use the term ‘more.’ This simple mathematical approach does not ignore the windfall to creditors . . . .” *Id.* The court ultimately held that avoidance is proper under § 547 when the foreclosure sale price is substantially less than the fair market value of the property. *Id.*

166. See *supra* note 165 and accompanying text (explaining that the statutory language is “mathematically certain”); *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 552 (1994) (Souter, J., dissenting) (explaining that “an ordinary speaker of English would have no difficulty grasping its basic thrust: the bankruptcy court must compare the price received by the insolvent debtor and the worth of the item when sold and set aside the transfer if the former was substantially ‘less than’ the latter”) (internal citations omitted).

167. See *Rambo v. Chase Manhattan Mortg. Corp. (In re Rambo)*, 297 B.R. 418, 427 (E.D. Pa. 2003) (explaining that the proper analysis of *BFP*’s application to § 547 begins with the language of the statute and not the policies that would support it).

168. *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 340–41 (S.D. Tex. 1999) (holding that the court had no power to avoid a foreclosure sale that complied with state law).

169. *Id.*

170. *Id.*

sales that satisfy the requirements of § 547.<sup>171</sup> The estate would have more assets, so each creditor would receive a greater payout as a result.<sup>172</sup>

### III. ANALYSIS

#### A. *BFP's Reasoning Should Apply to § 547*

The courts that have declined to extend *BFP* have done so primarily based on an analysis of the statutory language—not policy.<sup>173</sup> Some courts have reasoned that, because the statutory language is different, *BFP* is necessarily inapplicable to a § 547 analysis.<sup>174</sup> Other courts have acknowledged the legitimacy of *BFP's* rationales but have declined to extend *BFP* because the phrase “received more” is sufficiently clear and does not require judicial interpretation.<sup>175</sup>

Some courts have extended *BFP*.<sup>176</sup> Of these courts, some have done so on faulty reasoning. These courts have extended *BFP* primarily because the federalism policy considerations that drove the § 548 analysis are just as applicable to § 547.<sup>177</sup> A smaller number of courts, however, have extended *BFP*, more correctly, because they have determined that *BFP's* discussion of how to value property is equally applicable to § 547.<sup>178</sup>

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171. See *Chase Manhattan Bank v. Pulcini (In re Pulcini)*, 261 B.R. 836, 844 (W.D. Pa. 2001) (holding that the trustee could not avoid the sheriff's sale in question).

172. *Id.*

173. *Rambo v. Chase Manhattan Mortg. Corp. (In re Rambo)*, 297 B.R. 418, 427–28 (E.D. Pa. 2003) (explaining that other courts have reached a determination without a discussion of the statutory predicate).

174. See *supra* note 163 and accompanying text (explaining why *BFP* is inapplicable in light of different statutory language).

175. See *supra* notes 166–67 and accompanying text (explaining that judicial interpretation is not necessary where Congressional intent is clear).

176. See *supra* notes 158–60 and accompanying text (explaining that certain courts have extended *BFP*).

177. See *RL Mgmt. Group, LLC v. Coffman (In re RL Mgmt. Grp., LLC)*, No. 13-51849, 2014 Bankr. LEXIS 206, at \*16–18 (E.D. Mich. Jan. 10, 2014) (explaining the applicability of state interests articulated in *BFP* to a § 547 analysis); *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 340–41 (S.D. Tex. 1999) (explaining that *BFP's* principal rationale is applicable to § 547).

178. See *Veltre v. Fifth Third Bank (In re Veltre)*, 562 B.R. 890, 893–94 (W.D. Pa. 2017) (adopting the reasoning of *Pulcini* and *Rocco*, which applied *BFP's* rationale of the value of an asset to § 547); *Chase Manhattan Bank v. Pulcini (In re Pulcini)*, 261 B.R. 836, 844 (W.D. Pa. 2001) (explaining that fair market value is not the correct measuring stick in the context of a forced sale, and that “the lien creditor does not ‘receive more’ for purposes of § 547(b)(5) than it would receive in a chapter 7 liquidation”).

### 1. *Declined to Extend*

The courts that have declined to extend *BFP* to § 547 have narrowly approached the issue and have erred in doing so. *BFP*'s reasoning was couched in a case that determined the application of § 548, but it should not be limited to that scenario.<sup>179</sup> Section 548 asks whether the asset was transferred in exchange for a “reasonably equivalent value.”<sup>180</sup> To answer that question, a court must determine the value of the asset.<sup>181</sup> The Supreme Court grappled with this very question when it considered against what benchmark “reasonably equivalent value” would be judged.<sup>182</sup> The answer to this question is just as applicable to § 547 as it is to § 548.<sup>183</sup> Without understanding how to value an asset, how can a court determine whether a creditor had received more?<sup>184</sup>

The *BFP* Court clearly reasoned that fair market value was not the proper measuring stick for an asset's value.<sup>185</sup> Instead, the Court determined that the mortgage foreclosure sale price itself was the only proper measure for the asset's value.<sup>186</sup>

The courts that have not extended *BFP* have ignored *BFP*'s central reasoning and have returned to using the asset's fair market value as the benchmark.<sup>187</sup> These courts missed the pivotal rea-

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179. See *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 535, 547 (1994) (addressing § 548); *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 336 (S.D. Tex. 1999) (extending *BFP*'s reasoning to § 547).

180. 11 U.S.C. § 548(a)(1)(B)(i).

181. See *BFP*, 511 U.S. at 547 (examining the deficiency in the dissent's position relating to the question of valuation). The majority explained this deficiency: [T]he dissent simply reiterates the “single meaning” of “reasonably equivalent value” (with which we entirely agree): “A court should discern the ‘value’ of the property transferred and determine whether the price paid was, under the circumstances, ‘less than reasonable.’” Well and good. But what is the “value”? The dissent has no response. (internal citations omitted). *Id.*

182. *Id.* (explaining that the majority “considered three . . . possible answers to the question—fair market value, reasonable forced-sale price, and the foreclosure-sale price itself—and have settled on the last”) (internal citations omitted).

183. See e.g., *Veltre*, 562 B.R. at 893–94 (adopting the reasoning of *Pulcini and Rocco*, which applied *BFP*'s rationale of how to determine the value of an asset to § 547).

184. See *BFP*, 511 U.S. at 547 (explaining that the dissent's position does not answer the crucial question—“what is the ‘value?’”).

185. *Id.* at 537–38.

186. *Id.* at 549 (explaining that, in the context of forced sales, the fair market value is not useful and that “the only legitimate evidence of the property's value at the time it is sold is the foreclosure-sale price itself”).

187. See *Hackler v. Arianna Holdings Co., LLC (In re Hackler)*, 571 B.R. 662, 668 (D.N.J. 2017) (using an expert's valuation of the property to determine that the creditor “received more” than it would have under a Chapter 7 proceeding); *Berley Assocs. v. Eckert (In re Berley Assocs.)*, 492 B.R. 433, 443 (D.N.J. 2013)

soning *BFP* supplied to answer the inherent comparative value question within § 548 and § 547.<sup>188</sup>

## 2. *What Is an Asset Worth?*

*BFP*'s reasoning should extend to § 547 preference actions. However, some courts have arrived at this conclusion on faulty reasoning. It is not simply that the same federalism considerations arise in each context that justifies expanding *BFP*.<sup>189</sup> The Supreme Court's explanation of how to value property is what drives this conclusion.<sup>190</sup> Under the dictates of *BFP*, when a court is analyzing whether a creditor received "more" than it would have in a Chapter 7 liquidation, the court cannot consider the fair market value of the asset.<sup>191</sup> Instead, the court must look to the sale price actually received in the forced sale when assessing the "value" of the asset.<sup>192</sup>

The effect of incorporating *BFP*'s reasoning to § 547 depends on the type of creditor. In the instance of a secured creditor, the creditor can avoid any preference action under § 547 if it bids only the amount of the lien it holds against the property.<sup>193</sup> If it does not bid more than its lien, a creditor can never "receive more" than it would have in a Chapter 7 liquidation.<sup>194</sup> The property's value is the price received in a forced sale.<sup>195</sup> The creditor would always

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(explaining the "windfall" the creditor received and citing *Andrews* with approval); *Northwest Bank Minn., N.A. v. Andrews (In re Andrews)*, 262 B.R. 299, 306 (M.D. Pa. 2001) (explaining that a pre-petition forced sale can be avoided under § 547 if the "claim of the foreclosing party is substantially less than the fair market value of the property").

188. See *BFP*, 511 U.S. at 547–48.

189. See, e.g., *RL Mgmt. Group, LLC v. Coffman (In re RL Mgmt. Grp., LLC)*, No. 13-51849, 2014 Bankr. LEXIS 206, 16–18 (E.D. Mich. Jan. 10, 2014) (concluding that *BFP* is applicable to § 547 based on the applicability of the need to protect state interests articulated in *BFP*).

190. *BFP*, 511 U.S. at 547–48.

191. *Id.* at 535–39. "[P]roperty that *must* be sold within those strictures is simply worth *less*." *Id.* at 539. See *Newman v. FIBSA Forwarding, Inc. (In re FIBSA Forwarding, Inc.)*, 230 B.R. 334, 340–41 (S.D. Tex. 1999) (explaining that an asset's fair market value could not be used to determine whether a transfer was made in exchange for a reasonably equivalent value).

192. See *supra* notes 182–88 and accompanying text (explaining that price received—not the fair market value—drives the analysis).

193. *Veltre v. Fifth Third Bank (In re Veltre)* 562 B.R. 890, 894 (W.D. Pa. 2017) (adopting the reasoning of *Pulcini and Rocco*, which applied *BFP*'s rationale of valuing an asset to § 547, and determining that the creditor could not receive more than in a Chapter 7 proceeding).

194. *Id.*

195. See *BFP*, 511 U.S. at 548 (explaining that "the only legitimate evidence of the property's value at the time it is sold is the foreclosure-sale price itself").



receive exactly the amount it would have received under a Chapter 7, which is the amount of its lien.<sup>196</sup>

If, however, the secured creditor bids above the amount of the lien it holds against the property, the transfer would be subject to avoidance as a preferential transfer.<sup>197</sup> Again, in a Chapter 7 liquidation, the creditor would receive only the amount of its lien.<sup>198</sup> If the creditor pays an amount greater than its lien, then the value of the asset is greater than the creditor's lien.<sup>199</sup> Because the creditor received an asset that is "worth more" than its lien, the transfer would be subject to avoidance.<sup>200</sup>

In the unlikely case of an unsecured creditor purchasing a debtor's asset in a forced sale, the opposite result would yield. The transfer would likely always be subject to avoidance as a preference, even if the creditor were to bid the amount of debt it is owed. In accordance with the Bankruptcy Code, unsecured creditors are paid on a *pro rata*<sup>201</sup> basis.<sup>202</sup> A creditor that receives its full debt amount would almost always receive more than it would have under a Chapter 7 if there are no other assets in the estate.<sup>203</sup>

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196. See *Veltre*, 562 B.R. at 894 (explaining a creditor could only receive property that is "worth" the amount of its lien). This reasoning ignores the reality of certain situations in which the creditor may receive a windfall. See *Whittle Dev., Inc. v. Branch Banking Trust Co. (In re Whittle Dev., Inc.)*, 463 B.R. 796, 802 (N.D. Tex. 2011) (explaining that the policy goals of the Code would be "furthered if a secured creditor can be prevented from reclaiming property and earning a windfall at the expense of the estate"). However, under the dictates of *BFP*, the value of the property is determined by the price it can achieve in a forced sale, not a price for which it may later be sold. See *Chase Manhattan Bank v. Pulcini (In re Pulcini)*, 261 B.R. 836, 844 (W.D. Pa. 2001) (explaining that "a lien creditor who purchases the property . . . and who then sells the property to a third party for an amount greater than the amount of its lien is not avoidable in accordance with § 547(b) as a preference"). The court further explained, "In particular, the lien creditor does not 'receive more' for purposes of § 547(b)(5) than it would receive in a Chapter 7 liquidation." *Id.*

197. 11 U.S.C. § 547.

198. See *Veltre v. Fifth Third Bank (In re Veltre)* 562 B.R. 890, 894 (W.D. Pa. 2017) (explaining that because a creditor will receive the amount of its lien, the creditor could never receive more than it would in a Chapter 7 liquidation).

199. See *BFP*, 511 U.S. at 548 (explaining that "the only legitimate evidence of the property's value at the time it is sold is the foreclosure-sale price itself").

200. See, e.g., *Hackler v. Arianna Holdings Co., LLC (In re Hackler)*, 571 B.R. 662, 668 (D.N.J. 2017) (holding that the trustee could avoid a pre-petition tax foreclosure sale where the creditor received a property with an estimated value of \$335,000 in a forced sale in which the creditor paid \$40,000).

201. See *supra* note 37 and accompanying text (defining "*pro rata* distribution").

202. 11 U.S.C. §§ 726(b), 1322(a)(3).

203. See *supra* Section II.A.2.b (explaining the distribution scheme and rules for unsecured creditors). Due to the *pro rata* compensation scheme and rule providing equal treatment for creditors of the same class, an unsecured creditor who

### 3. *Hypothetical Examples*

Assume a debtor owns a house with a fair market value of \$50,000 and owes two debts: one debt secured on his house owed to National Bank for \$30,000 and another general unsecured debt to a mechanic for \$15,000.<sup>204</sup> If National Bank were to purchase the house at a forced sale for its lien amount, there would be no way to avoid the transfer as preferential transfer.<sup>205</sup> In this example, National Bank received a house with a value of \$30,000 at the forced sale.<sup>206</sup> In a hypothetical Chapter 7 liquidation, National Bank would have received its secured interest—\$30,000.<sup>207</sup> Because it received exactly the value of the lien amount, the transfer could not be subject to avoidance as a preference.<sup>208</sup> If, however, National Bank bid more than its lien amount, the transfer may be subject to avoidance as a preference.<sup>209</sup>

In a new scenario, assume a debtor owns a house with a fair market value of \$50,000 and owes two unsecured debts: one debt of \$30,000 to a car mechanic and one debt of \$15,000 to a friend. In an unlikely event, assume the friend purchases the debtor's home in a forced sale, and the debtor then filed for bankruptcy. No matter what the purchase price is, the sale would likely be subject to avoid-

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received full payment would receive more than he would under a Chapter 7 unless all other unsecured creditors were paid an equal amount, which is unlikely given that the debtors generally file bankruptcy because a lack of assets to satisfy all debts. *See* Section II.A.2.b.

204. These scenarios ignore the provision that allows a debtor to exempt a certain amount of home equity from his bankruptcy estate. *See* 11 U.S.C. § 522(d).

205. *See supra* notes 193–96 and accompanying text (explaining that a secured creditor could not have forced-sale purchase avoided if it pays its lien amount).

206. Again, this ignores the idea of the property's fair market value. *See supra* notes 134, 148, 191, and 196 and accompanying text (explaining that an asset's fair market value is irrelevant in a forced-sale value analysis). This situation would result in avoidance under § 547 only if the court strayed from *BFP*'s prohibition on using the fair market value. *See supra* note 187 and accompanying text (discussing courts that have reinstated a fair market analysis). Under such a fair market analysis, the creditor would have received \$50,000, which is more than \$30,000—what it would have received under a hypothetical Chapter 7. *See supra* note 200 and accompanying text (explaining a case that looked back to the property's fair market value instead of the price paid at foreclosure).

207. *See Veltre v. Fifth Third Bank (In re Veltre)* 562 B.R. 890, 894 (W.D. Pa. 2017) (explaining that because a creditor will receive the amount of its lien, the creditor could never receive more than it would in a Chapter 7 liquidation).

208. *Id.*

209. For example, if National Bank purchased the home for \$50,000, it would have received more than what it would have received under a Chapter 7 liquidation—its lien amount. *See supra* note 200 and accompanying text (explaining a scenario where a trustee could avoid a transfer because the creditor received “more” than it would have under a Chapter 7 distribution).

ance as a preference. If the sale were for the amount of debt owed to the friend, \$15,000, the friend would receive more than he would have under Chapter 7.<sup>210</sup> This is due to the Code's *pro rata* distribution scheme for unsecured creditors.<sup>211</sup> The \$15,000 he received at the sale would had to have been split proportionally, or *pro rata*, with each unsecured creditor to comply with distribution rules in a Chapter 7 liquidation.<sup>212</sup> In this case, because there are two creditors, each creditor would receive one half of \$15,000 or \$7,500.<sup>213</sup> Because the friend's purchase of the home enabled him to receive \$15,000, more than the \$7,500 he would have received under a Chapter 7, this transfer would be subject to avoidance as a preferential transfer.<sup>214</sup>

#### IV. CONCLUSION

This Comment has examined pre-*BFP* cases,<sup>215</sup> *BFP v. Resolution Trust Corp.*,<sup>216</sup> and the resulting circuit split.<sup>217</sup> Courts had little difficulty applying § 547 to forced sales before the Supreme Court's ruling in *BFP*.<sup>218</sup> However, since the *BFP* decision, courts have struggled with determining the scope of cases over which the precedent controls.<sup>219</sup>

This Comment has examined the cases in which courts have not extended *BFP*.<sup>220</sup> Courts on this side of the circuit split base their conclusion on one of two reasons: § 547 uses different language than § 548, and the language in § 547 is clearer than the language in § 548.<sup>221</sup> These courts have misinterpreted what the *BFP*

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210. See *supra* note 203 and accompanying text (explaining that, due to *pro rata* distribution scheme, a transfer that allows an unsecured creditor to receive full payment is likely subject to avoidance). See also *supra* Section II.A.2.b (discussing treatment of unsecured creditors).

211. See *supra* note 37 and accompanying text (discussing the *pro rata* distribution scheme).

212. See *supra* note 37 and accompanying text (discussing the *pro rata* distribution scheme).

213. See *supra* Section II.A.2.b (discussing treatment of unsecured creditors and explaining that two creditors of the same class must be treated equally to the extent the creditor with the smaller claim is not paid in full).

214. See *Hackler v. Arianna Holdings Co., LLC (In re Hackler)*, 571 B.R. 662, 668 (D.N.J. 2017) (holding that the trustee could avoid a pre-petition tax foreclosure sale where the creditor received a property with an estimated value of \$335,000 in a forced sale in which the creditor paid \$40,000).

215. See *supra* Section II.C.

216. See *supra* Section II.D.

217. See *supra* Section II.F.

218. See *supra* Section II.C.

219. See *supra* Section II.F.

220. See *supra* Section II.F.

221. See *supra* Section II.F.

Court contemplated.<sup>222</sup> While the *BFP* Court's analysis was in the context of § 548's phrase "reasonably equivalent value," it was truly an analysis of what the correct standard to judge a "reasonably equivalent value" is—the "true" value of an asset.<sup>223</sup>

This Comment then examined courts that have extended *BFP* to § 547.<sup>224</sup> Even some of these courts have struggled to understand *BFP*'s reasoning.<sup>225</sup> Some courts have extended *BFP* because the policy considerations that drove *BFP*'s conclusion are equally present in § 547 cases.<sup>226</sup> Other courts have extended based on *BFP*'s conclusion of how to value property.<sup>227</sup> The federalism issue *BFP* addressed likely drove the Court's conclusion. However, it is the conclusion that binds lower courts, and *BFP* stands for the proposition that only the forced sale price can evidence an asset's value.<sup>228</sup>

Finally, this Comment endorsed the view that *BFP* applies to § 547 and provided hypothetical examples to illustrate its operation.<sup>229</sup> The Supreme Court's dictate as to how to value property is as applicable to § 547 as it is to § 548. After all, an asset is worth only what someone has paid for it.

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222. See *supra* Section II.F.

223. See *supra* Section III.A.

224. See *supra* Section II.F.

225. See *supra* Section II.F.

226. See *supra* Section II.F.

227. See *supra* Section II.F.

228. See *supra* Section III.A.1.

229. See *supra* Section III.A.

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