Fraudulent transfers and obligations in Bankruptcy 11 U.S. Code § 548

Under PROMESA, the Oversight Board has sued hundreds of entities that have received monies from the Puerto Rico government (Commonwealth) or its instrumentalities with the intention to avoid and recover all transfers made by the Commonwealth of an interest in the Commonwealth's property and to or for the benefit of the Defendant or any other transferee.

It is alleging in the complaints that the Commonwealth received less than a reasonably equivalent value in exchange for the 2-Year Transfers because the Commonwealth's books and records maintained by its Office of the Controller do not contain any contract evidencing that the Commonwealth received value in exchange for the 2-Year Transfers. The Commonwealth was insolvent on the date that such 2-Year Transfers were made. As such the Transfers were fraudulent transfers that the Oversight Board may avoid pursuant to 11 U.S.C. § 548(a)(1)(B). During the four years prior to the Petition Date (the "Paulian Fraudulent Transfer Period"), the Commonwealth made payments to Defendant ("4-Year Transfer(s)"). Certain of these payments (if any, the "2-Year Transfer(s)" and, together with the 4-Year Transfer(s), the "Transfers") may have occurred during the two years prior to the Petition Date (the "Code Fraudulent Transfer Period").

A fraudulent transfer is when debtor knowingly transfers property ownership in an attempt to reduce the amount a creditor may get in a bankruptcy case or sells the property for less than it is worth. When this happens the bankruptcy trustee (in this case the Oversight Board (O.B.) can void or undo the transfer and bring back into the bankruptcy estate for redistribution to creditors. The intent to keep away from creditors is a requisite for this section to apply. In determining intent to defraud, the courts have looked at circumstances surrounding the sales of the property: for less than fair market value, to whom the transfer/sale is made is it to an insider (such as relative, friend, or business associate, unusual manner of transfer, becoming insolvent after the transfer, failing to disclose transaction.
The transfer will be considered fraudulent and may be voided or undone by trustee when: 1) sale/transfer of property was done for less than the property's reasonable equivalent value even when there is NO INTENT to defraud the creditors; 2) the debtor was insolvent or the property transfer caused his insolvency.
The courts will look at the following factors when determining reasonable equivalent value: fair market value of the property; whether in ordinary course of business; value of other offers for property; whether in exchange for promise of future business.

The two dimensions to fraudulent transfers sometimes are referred to as actual fraud or constructive fraud. The actual fraud, the property owner transferred the property in order to keep the property out of reach of his creditors. The constructive fraud, although there was no intent to defraud the creditors, the sale was for below a reasonably equivalent value and there was signs of financial distress. In other words, even in the situation where there was no fraud but the price of sale was too low, it can be voided or undone by the trustee as a fraudulent transfer.

The period of review for the bankruptcy trustee, referred to commonly as the Look Back Period, is generally two (2) years and can be extended back up to four (4) years, based on state law.