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1

### The obligation of the Plaintiff/trustee to bring specificity in a preference case



2

*Angell v. BER Care, Inc. (In re Caremerica, Inc.),*  
409 B.R. 737 (Bankr. E.D.N.C. 2009)



3

#### Facts

- Debtors Caremerica, Inc. and others operated adult care homes in Eastern North Carolina.
- The Trustee brought an adversary proceeding to avoid and recover certain alleged preferential and fraudulent transfers made to Defendant BER Care, Inc. (formerly, PPS, Inc.) and subsequently transferred to other Defendants.
- The Trustee's Complaint contained a list of total amounts of preferential and fraudulent transfers alleged to have been received by each Defendant. The Trustee moved to further amend the Complaint.
- The Amended Complaint included an exhibit listing each alleged transfer and including specific amounts, dates, check numbers, payee reference numbers, names of payees, account numbers and account names corresponding to each transfer and the table that identified the dates and amounts of the transfers received by each defendant. The Exhibit also included relevant bank statements from the account of PPS, Inc.



4

#### Issue :

- Whether a heightened pleading requirement should be applied to the Trustee's preference claims in determining whether to allow a Defendants' motions to dismiss.



5

FRCP Rule 8 (a) (applied by FRBP 7008) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
- (2) a short and plain statement of the claim showing that the pleader is entitled to relief; and
- (3) a demand for the relief sought, which may include relief in the alternative or different types of relief.



6

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7

FRCP 12(b) (applied by FRBP 7012)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
- (2) lack of personal jurisdiction;
- (3) improper venue;
- (4) insufficient process;
- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.



8

Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

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- (2) lack of personal jurisdiction;
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9

Arguments

- The Defendants filed motions to dismiss the Complaint for failure to state a claim upon which relief can be granted and alleged that the complaint should be dismissed pursuant to Rule 12(b)(6).
- The Trustee alleged that the Debtors, for the purpose of protecting their own bank accounts from attachment or garnishment by creditors, transferred funds by and through bank accounts of Ber Care/ PPS as a conduit through which funds were distributed to the Defendants
- The Defendants argued that the Amended Complaint failed to allege facts sufficient to show why the Trustee is entitled to avoid alleged preferential transfers under § 547 of the Bankruptcy Code.
- The Trustee also argued that the new pleading requirements imposed an undue burden on the Trustee to supplement each element of its cause of action with factual support.



10

GENERAL ALLEGATIONS

6. Caremerica, Inc., Caremerica Adult Care, Inc., The Meadows of Hermitage, Inc., The Meadows of Fayetteville Inc., and The Meadows of Wilmington, Inc. were subject to the dominion and control of Ronald E. Burrell and Michael R. Elliott, who used such control to commit fraud or wrong, in violation of their legal duties to the Debtors, resulting in substantial losses to creditors of the Debtors.

7. Piercing the corporate veil of the Debtors, as to one another, is appropriate to protect the rights of creditors of the various Debtors and the Debtors should be considered as a single enterprise (the "Consolidated Debtor").

8. BER Care Inc. is a business corporation organized and existing under the laws of the State of North Carolina, whose principal owners are Ronald E. Burrell, Michael R. Elliott, and John Smith. BER Care, Inc. was formerly named PPS, Inc. until its name was changed on or about April 6, 2005.

9. The assets of BER Care, Inc. were sold in March, 2005 and BER Care, Inc. otherwise ceased operations as a going concern shortly thereafter.

10. Bank accounts of BER Care, Inc. were used by the Debtors as a conduit to transfer funds of the Debtors to third parties, including the Defendants.

11. As to each Defendant who is alleged to be an Insider as set forth on Exhibit A, during the one year period prior to the Petition Date ("Preference Period"), one or more of the Debtors, or, in the alternative, the Consolidated Debtor, by and through Defendant BER Care, Inc. acting as a conduit (jointly, the Debtors and the Consolidated Debtor are hereinafter referred to as the "Transferor") made certain transfers to such Defendant in at least the amount listed beside such Defendant's name under the column heading marked "Preferential Transfers" on Exhibit A, attached hereto.



11

AVOIDANCE AND RECOVERY OF PREFERENTIAL TRANSFER PURSUANT TO 11 U.S.C. §§ 547, 550 AND 551 (Conduit Theory)

14. The Plaintiff incorporates the allegations set forth in paragraphs 1 through 13 above in their entirety.
15. Each Preferential Transfer a constituted transfer of an interest of the Transferor in property.
16. Each Preferential Transfer was made to or for the benefit of the Defendant as a creditor of the Transferor.
17. Each Preferential Transfers was made for, or on account of, an antecedent debt owed by the Transferor to the Defendant before the transfer was made.
18. Each Preferential Transfer was made while the Transferor was insolvent.
19. Each Preferential Transfer was made within the Preference Period.
20. The Preferential Transfers enabled the Defendants to receive more from the Transferor than they would have received in a Chapter 7 case had the Preferential Transfers not been made and the Transferor received payment on its claim to the extent provided by Title 11 of the United States Code (the "Bankruptcy Code").
21. Pursuant to Bankruptcy Code § 547(b), the Preferential Transfers are avoidable.
22. Each Defendant was the initial transferee, or an immediate or mediate transferee of the Preferential Transfers.
23. Each Defendant is accordingly liable to the Trustee on behalf of the bankruptcy estate for the recovery of the Preferential Transfers he, she or it received or benefited from, or the value of the property transferred, pursuant to 11 U.S.C. § 550 and 551.



12

### Standard for Determining the Sufficiency of a Complaint Under Rule 8(a)(2)

Old Standard (Conley Vs. Gibson)	New Standard (Twombly and Iqbal)
A decision by the U.S. Supreme Court in 1957 that provided a basis for a broad reading of the "short plain statement" requirement for pleading under Rule 8 of the Federal Rules of Civil Procedure	<i>Bell Atlantic v. Twombly</i> in 2007 and <i>Ashcroft v. Iqbal</i> in 2009, the Supreme Court announced a new heightened pleading standard for avoidance complaints – a departure from the rule established in the 1957 case <i>Conley v. Gibson</i> . The Court re-interpreted the substance of Federal Rule 8(a)
A complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.	Plaintiff's obligation to provide the grounds of his entitlement to relief requires more than labels and conclusions, and a formulaic recitation of the elements of a cause of action will not do.
Liberal pleading standard when confronting motions to dismiss for failure to state a claim.	Heightened pleading Requirements while confronting motions to dismiss for failure to state a claim.
Trustee's allegations are true, facts are construed as most favorable to the plaintiff, case cannot be dismissed unless proven beyond a doubt that plaintiff can prove no set of facts.	A complaint has facial plausibility only when a plaintiff pleads sufficient factual content to enable a court to draw a reasonable inference that a defendant is liable for the alleged misconduct.

13

### Court's Ruling :

- The Court noted that the Supreme Court recently adopted a heightened pleading standard for claims for relief under Rule 8(a)(2) and the requirements for claims to survive a motion to dismiss under 12(b)(6) and hence, the Court will examine the new pleading standard for claims for relief as set forth in *Twombly* and *Iqbal*.
- The Court added that under new pleading standards, a plaintiff must allege facts regarding the **nature and amount of the antecedent debt**. The conclusory assertion in the amended complaint that each preferential transfer was made "for, or on account of, an antecedent debt owed by the transferor to the Defendant before the transfer was made" did not satisfy this burden.
- Next, the Court found that the **facts in the complaint were insufficient to support the Trustee's contention that the funds flowing through the BER Care/PPS bank accounts originated with the Debtors**. Since avoidance under § 547 is limited to "a transfer of an interest of the debtor in property", a claim for relief under § 547 must assert facts showing that the debtors had an interest in the property exchanging hands. The Court ruled that the Trustee's allegations regarding transfers of interests of the debtors in property **failed to meet the plausibility standard** necessary to overcome a 12(b)(6) motion to dismiss.

14

### Court's Ruling :

- The Court further held that for transfers to insiders, there is no presumption of insolvency, so the Trustee **must allege sufficient facts to show that insolvency is plausible**. The Court determined that the Trustee's **conclusory statement in the case at bar that "each preferential transfer was made while the transferor was insolvent" failed to satisfy this burden**. Moreover, mere labeling of the transferees as insiders was **not enough to establish a reasonable inference of insider status under § 101(31) and 547(b)**.
- Next, the Court found that the Debtors' summary of schedules reflected that the liabilities were far greater than assets and that was sufficient to prove that the unsecured creditors would receive less than 100% on their claims.
- Although the Trustee raised several arguments in opposition to the Court's adoption of the heightened pleading standard for claims for relief, the Court rejected them. The Court admitted that while claims for relief are more difficult to plead sufficiently following *Twombly and Iqbal*, **a trustee is more likely to have access to this information** than the plaintiffs seeking to prove an antitrust conspiracy in *Twombly* or the Pakistani detainee in *Iqbal* who alleged that federal officials purposefully discriminated against him.

15

### Court's Ruling

- The Court stated that if these claimants were held to a heightened pleading standard, so too should be a trustee in bankruptcy. **The Court added that, a trustee had theoretically access to all of the books and records of the Debtors for up to two years prior to bringing these causes of action, with the full discovery powers of the court through 2004 exams and other means available during that time**. So, it was not difficult for a trustee to collate such information and plead with more particularity and specificity.
- The Court granted the Defendants motion to dismiss and granted permission for the Trustee to re-plead his claims against the Defendants under the pleading standards expressed in the Court's order.

16

### Conclusion :

- Heighten Pleadings Standard Apply to Avoidance Complaints
- Plaintiffs in avoidance actions will need to work harder. Merely filing complaints that simply recite the statutory elements of the claim in formulaic fashion will not suffice.
- **Trustees and other plaintiffs must investigate and analyze carefully so that they can develop facts to formulate complaints that meet the new, more stringent pleading requirements.**
- A plaintiff must allege facts addressing all the elements of Sec. 547 such as the **nature and amount of the antecedent debt**, names of transferees, transferor and the dates and amounts of each transfer, a valuation of the debtors' accounts payable and other liabilities, summary of schedules reflecting liabilities far greater than assets etc.

17

### Conclusion :

- The plausibility standard is not akin to a probability requirement, but it asks for **more than a sheer possibility** that a defendant has acted unlawfully.
- A claim has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged.

18

*Feltman v. KeyBank, N.A. (In re Levitt & Sons, LLC),*

Nos. 07-19845-BKC-RBR, 09-2273-BKC-RBR-A, 2010  
Bankr. LEXIS 1284 (U.S. Bankr. S.D. Fla. Apr. 16, 2010)



19

#### Facts

- Prior to the petition date, Debtor Levitt and Sons, LLC, et al operated as a home building company
- Defendant KeyBank was a lender for one or more of the Debtors.
- The Plan Administrator filed a complaint against KeyBank to avoid and recover allegedly preferential and fraudulent transfers on behalf of the Debtors.
- Defendant KeyBank filed a motion to dismiss the complaint under Fed. R. Civ. P. 8(a)



20

#### Issue :

- Whether the Complaint should be dismissed for failure to state an adequate claim for relief under Fed. R. Civ. P. 8(a)



21

#### Arguments

- The Trustee attempted to avoid and recover allegedly preferential and fraudulent transfers on behalf of the Debtors, alleging that by the time of the petition date, a number of the Debtors had become jointly and severally liable, through guaranties and related loan and security documents, for the obligations of the other Debtors.
- KeyBank filed a motion to dismiss the complaint, arguing that the complaint failed to state an adequate claim for relief under Rule 8(a) of the Federal Rules of Civil Procedure.



22

Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
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24

#### Court's Ruling

- The Court agreed with and adopted the legal reasoning of the *Careamerica* court. The Court determined that however inconvenient it may be for a plaintiff, it is apparent that the jurisprudential landscape regarding the adequacy of complaints in civil cases has changed.
- The Court found that the plan administrator's complaint did not specify the extent of the total loan amounts, the nature of the underlying obligations, which entities were obligated, or which entities were the source of the funds allegedly paid to the creditor.
- The Court concluded that the plan administrator's failure to adequately distinguish identity with respect to the various obligors, guarantors, and transferors allegedly involved in the transactions with the creditor was fatal to various counts of the Complaint under the *Twombly* standard.
- The Court granted the Defendant's motion to dismiss and dismissed the complaint without prejudice



25

#### *Gellert v. Lenick Co. (In re Crucible Materials Corp.)*,

Nos. 09-11582 (MFW), 10-55178 (MFW), 2011 Bankr. LEXIS 2513 (U.S. Bankr. D. Del. July 6, 2011)



26

#### Facts

- Debtor Crucible Materials Corporation produced a wide array of steel products for manufacturers, principally in the automotive industry.
- Defendant The Lenick Company is a scrap metals recycling company in Pittsburgh, Pennsylvania.
- The Trustee brought an adversary proceeding against the Defendant company to avoid transfers pursuant to Sections 547 of the Bankruptcy Code.
- The Defendant moved for dismissal of the preference count under Rules 8(a) and 12(b)(6) of the Federal Rules of Civil Procedure



27

#### Issue :

- Whether the Trustee's Complaint was found to be insufficient in detail under Fed. R Civ. P. 8(a)?
- Whether the Trustee's complaint failed to establish a plausible claim for the avoidance of preferential transfers under Fed. R Civ. P. 12(b)(6)



28

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29

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30

Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

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31

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32

Arguments

- The Defendant contended that the Trustee's complaint failed to state a claim upon which relief can be granted, because it sets forth only conclusory allegations parroting the statutory language of section 547 of the Bankruptcy Code.
- The Defendant argued that the Trustee simply relied on legal conclusions rather than factual assertions in its complaint. Further, Exhibit A to the complaint did not contain any proof of transfers such as invoices, bills, canceled checks or other evidence to substantiate the Trustee's claims.
- The Trustee responded that the complaint contained enough factual details to describe adequately the alleged transfers. According to the Trustee, Exhibit A provided the name of the transferee (The Lenick Company), check numbers, check amounts, invoice dates, invoice numbers, and the clear dates of the transfers sought to be avoided. This, the Trustee contended made Count 1 plausible on its face.
- Further, the Trustee asserted that section 547's presumption of insolvency and the complaint's allegation that the Defendant received more than it would have under a chapter 7 bankruptcy was sufficient to make the claim plausible.



33

(Avoidance of Preference Transfers - 11 U.S.C. § 547)

- 7. Plaintiff incorporates all preceding paragraphs as if fully re-alleged herein.
- 8. On or within ninety (90) days before the Petition Date, that is between February 5, 2009 and May 6, 2009 (the "Preference Period"), the Debtors continued to operate their business affairs, including the transfer of property, either by checks, cashier checks, wire transfers, direct deposit or otherwise to certain entities, including Defendant.
- 9. Plaintiff has completed an analysis of all readily available information of the Debtors and is seeking to avoid all the transfers of an interest of the Debtors' property made by one or more of the Debtors to Defendant within the Preference Period.
- 10. Plaintiff has determined that one or more of the Debtors made transfers to Defendant during the Preference Period in an amount not less than \$122,070.69 (the "Transfers"). Attached hereto as "Exhibit A" and incorporated herein by this reference is a list identifying each known Transfer that Plaintiff seeks to avoid and recover in this Complaint.



34

12. Defendant was a creditor of one or more of the Debtors at the time of the Transfers within the meaning of 11 U.S.C. § 101(10)(A). At the time of the Transfers, Defendant had a right to payment on account of an obligation owed to Defendant by one or more of the Debtors. See "Exhibit A" attached hereto and incorporated herein by this reference, which

CMC - The Lenick Company - MFW - -3- COMPLAINT F:\WP\MCMC\SUITS\DC-LEN001.WPD / 05Nov10, 1:52

Case 10-55178-MFW Doc 1 Filed 11/09/10 Page 4 of 7 also identified each known invoice or debt owed to Defendant by one or more of the Debtors and paid by the Transfers sought to be avoided and recovered in this Complaint.

13. The Transfers were to or for the benefit of a creditor within the meaning of 11 U.S.C. § 547(b)(1) because the Transfers either reduced or fully satisfied a debt then owed by one or more of the Debtors to Defendant. Id.

14. The Transfers were for, or on account of, antecedent debts owed by one or more of the Debtors before the Transfers were made. Id.

15. The Debtors were insolvent at all times during the ninety (90) days prior to the Petition Date. Plaintiff is entitled to the presumption of insolvency for the Transfers made during the Preference Period pursuant to 11 U.S.C. § 547(f).



35

Exhibit to Complaint

TRANSFERS DURING PREFERENCE PERIOD					
Defendant:	The Lenick Company				
Bankruptcy Case:	Crucible Materials Corporation, et al.				
Preference Period:	February 5, 2009 - May 6, 2009				
Debtor Entity/ Check No.	Check Amount	Clear Date	Inv No.	Inv Date	Inv Amt (US Dollars)
Crucible Materials Corporation 0225510	\$6,654.40	March 13, 2009	45919-BAL	September 14, 2008	\$19,367.80
Crucible Materials Corporation 0225610	\$6,654.40	March 13, 2009	46768-BAL	November 9, 2008	\$325.65
Crucible Materials Corporation 0225710	\$6,654.40	March 13, 2009	48892-BAL	June 17, 2008	\$3,246.10
Crucible Materials Corporation 0225810	\$6,654.40	March 13, 2009	49527	September 1, 2008	\$29,194.97
Crucible Materials Corporation 0225910	\$6,654.40	March 13, 2009	49528	September 3, 2008	\$30,122.63
Crucible Materials Corporation 0226010	\$28,048.49	March 30, 2009	49794	September 29, 2008	\$28,048.49
Crucible Materials Corporation 0227152	\$10,000.00	April 21, 2009	49795-P1	September 29, 2008	\$10,000.00
Total Invoices: 8				Total Amount:	\$122,070.69



36

#### Court's Ruling

- The Court concluded that the Trustee was not required to provide actual copies of the invoices, bills, canceled checks, or other tangible evidence to substantiate his claims at the motion to dismiss stage.
- The Complaint adequately alleged facts identifying the date of transfer, name of transferee, and transfer amount. However, because there was more than one debtor, the Complaint was deficient because it did not identify the transferor of the alleged preferential transfers. An allegation that "one or more of the debtors" made transfers was not sufficient.
- The Court also found that the Complaint failed to provide sufficient facts detailing the nature of the alleged antecedent debt and failed to provide any details to show that there was in fact an antecedent debt.



37

#### Court's Ruling

- The Court concluded that the Complaint also failed to provide evidence of a pre-existing debtor/creditor relationship from which an antecedent debt could have arisen.
- Beyond stating that the "Defendant was a creditor of one or more of the Debtors at the time of the Transfers," the Trustee completely failed to describe any type of relationship between the Defendant and any of the Debtors. Without such information, the Court determined that the Trustee has failed to describe sufficiently the nature of the antecedent debt.
- The Court granted the motion to dismiss the Complaint but granted the Trustee a leave to amend the Complaint.



38

#### Conclusion

- Where there is more than one debtor in any proceeding, a trustee must identify the transferor by name. Simply alleging that "one or more of the Debtors made transfers" is not sufficient.
- A complaint should provide sufficient facts detailing the nature of the alleged antecedent debt such as detail of any contracts between the parties or any description of the goods or services exchanged etc. Simply providing check numbers, dates and amounts is not enough to survive a motion to dismiss.
- Trustee may not be required to submit the actual copies of the invoices, bills, canceled checks, or other tangible to substantiate its claims at the motion to dismiss stage. Only sufficient facts detailing the transfers, transferor, transferee, nature of antecedent debt etc.



39

*Luria v. United States Dep't of Agric. (In re Taylor, Bean & Whitaker Mortg. Corp.),*

470 B.R. 219 (Bankr. M.D. Fla. 2012)



40

#### Facts

- Debtor Taylor, Bean & Whitaker Mortgage Corporation is a wholesale mortgage lending firm
- Plan Trustee, Neil F. Luria, brought an adversary proceeding against Defendant United States Department of Agriculture, brought pursuant to § 547(b) to avoid the aggregate amount of \$2,729,382.29 made to the Defendant by the Debtor
- Defendant brought Motion to Dismiss the complaint pursuant to FRCP 8(a)



41

#### Issue :

- Whether the Trustee's complaint satisfies the standards under Federal Rule Civ. P. 8(a)(2)



42

Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
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44

#### Arguments

- Defendant asserted that Complaint failed to state a claim upon which relief can be granted under Rule 8(a) of the Federal Rules of Civil Procedure.
- The Trustee alleged that the Debtor made certain transfers to the Defendant during the preference period and those alleged transfers met all the elements of Sec. 547(b) of the Bankruptcy Code.
- The Trustee provided Exhibit along with the Complaint, which listed detailed information with respect to the alleged transfers. The Trustee argued that specifically, Exhibit A delineated the name of the transferee (Defendant); the check numbers related to the transfer(s); the date the check(s) "cleared"; the precise amount of each transfer; and the invoice number associated with each transfer.
- The Defendant maintained that the Complaint failed to state a cause of action under § 547(b) that is plausible on its face because the factual allegations failed to plausibly suggest that the Defendant was a creditor of the Debtor, the nature and amount of an antecedent debt, or that Defendant received more than it would in a hypothetical Chapter 7 liquidation.



45

#### Court's Ruling

- The Court found that Exhibit A attached to the Complaint indicated that the Defendant received particular transfers from the Debtor, in specific amounts, on specific dates. Further, Exhibit A identified the transactions that relate to the purported antecedent debt(s) by invoice number.
- The Court further pointed out that in the Defendant's response to the Complaint, it mentioned that the Trustee's Complaint "makes no allegations that would allow one to infer that the numbers listed in the 'Invoice Number' column actually relate to real invoices". The Court thus stated that this assertion alone created a question of fact that was inappropriate for resolution at the motion to dismiss stage of the proceedings.
- The Court concluded that whether the Defendant received more by way of the subject transfers than it would have under a Chapter 7 liquidation was a factual question inappropriate for resolution on a motion to dismiss.



46

#### Court's Ruling

- The Court further held that the Trustee also incorporated by reference its disclosure statement in the underlying bankruptcy case, which lent factual support to its claim of insolvency.
- Further, the Court ruled that the allegations of the Complaint, taken in conjunction with the factual assertions included in the exhibit, provided sufficient information under Fed. R. Civ. P. 8(a)(2) for the transferee to admit or deny the allegations and assert any affirmative defenses.
- Thus, the Court ruled that accepted as true, the count alleging a preferential transfer adequately stated a claim that was plausible on its face under *Twombly*.
- The Court denied the Defendant's Motion to Dismiss



47

#### Conclusion

- On a motion to dismiss, a court may consider documents attached to the complaint or directly referred to in the complaint.
- Whether a creditor received more by way of the subject transfers than it would have under a Chapter 7 liquidation is a factual question inappropriate for resolution on a motion to dismiss.



48

*Spradlin v. Pryor Cashman LLP (In re Licking River Mining, LLC)*,  
Nos. 14-10201, 16-1031, 2017 Bankr. LEXIS 805 (U.S. Bankr.  
E.D. Ky. Mar. 24, 2017)



49

#### Facts

- Chapter 7 Trustee Phaedra Spradlin for Debtor U.S. Coal Corporation and its nine co-debtor subsidiaries brought a complaint against Defendant Pryor Cashman LLP for avoidance of preference and fraudulent transfers under Sec. 547 and 548 of the Bankruptcy Code.
- The Defendant filed a motion to dismiss under Civil Rule 12(b)(6), alleging that the Trustee's allegations failed to state a claim upon which relief could be granted as a matter of law, the claims were implausible as plead and the claims were not plead with requisite particularity.
- The Trustee filed an amended complaint in response to the Defendant's motion to dismiss.
- The Trustee alleged that the Debtor retained the Defendant as a legal counsel in July 2006 and transferred 375,000 shares of stock to the Defendant in exchange for its willingness to defer payment of the Defendant's attorneys' fees until the Debtor obtained financing for its project.



50

#### Issue :

- Whether the Trustee's complaint failed to state a claim against the Defendant as a mediate or immediate transferee under Sec. 550, as the complaint failed to state a claim for avoidance of any transfers from the Debtor's subsidiaries to Debtor based on either actual or constructive fraud ?
- Whether the Trustee's complaint failed to allege facts sufficient to support an allegation that the Debtor was a mere conduit ?
- Whether the Trustee's complaint failed to allege a sufficient basis to avoid and recover the transfers as actually fraudulent or constructively fraudulent ?
- Whether the Trustee's complaint along with an exhibit were sufficient to allege the transfers as preferential and to enable the Defendant to assert its defenses ?



51

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
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- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.



52

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
- (2) lack of personal jurisdiction;
- (3) improper venue;
- (4) insufficient process;
- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.



53

#### Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
- (2) a short and plain statement of the claim showing that the pleader is entitled to relief; and
- (3) a demand for the relief sought, which may include relief in the alternative or different types of relief.

#### Rule 9 FRAUD OR MISTAKE; CONDITIONS OF MIND.

(b) In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.



54

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55

#### Arguments

- The Trustee alleged that certain transfers made by the Debtor to the Defendant between July 2010 and May 2014 totaling \$1,633,286.18 were fraudulent because the Defendant rendered no legal services to the Debtor's subsidiaries and they received no benefit from the Defendant's services, **yet the Debtor used the subsidiaries' funds to pay the Defendant's legal fees.** In short, the Trustee's argument was that the Debtor generated no income of its own and took payments from the subsidiaries to pay the Debtor's operating expenses.
- The Trustee alleged that the **Debtor was a conduit of subsidiaries** and according to the settlement provisions it was plausible that the Debtor Coal lacked discretion or control over the funds it swept daily from the subsidiaries' accounts
- The Trustee also alleged that payments in the amount of \$135,000.00 made to the Defendant within ninety days of the petition date were avoidable as preferential transfers under § 547.
- The Trustee further sought to recover any avoided transfers on theories that, under § 550, the Defendant either was the initial transferee, the immediate or mediate transferee, or the entity for whose benefit the transfers were made



56

#### Court's Ruling

- The Court found that the Trustee's Complaint failed to describe any specific transfers from the subsidiaries to the Debtor. It did not state which subsidiary made a transfer to the Debtor, the amount each subsidiary transferred, or the date of any transfer. Instead, the complaint simply alleged that all transfers occurred via "sweep accounts", which was not sufficient enough to identify challenged transfers under Civil Rule 8.
- The Court further determined that whether a complaint adequately identifies a particular transfer is determined by asking whether the defendant could respond to the claims with appropriate affirmative defenses. However, in the case at bar, since the amended complaint **did not identify any specific avoidable transfer from the subsidiaries to the Debtor**, the Defendant could not assess its potential defenses with respect to any specific transfer, including defenses available under § 550(b).
- The Court ruled that the blanket allegations, like unspecified subsidiaries generally transferred funds to the Debtor, were insufficient to plead the facts necessary to state a claim for recovery against the Defendant as a subsequent transferee.



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Count I of the Amended Complaint, grounded in actual fraud [¶12] under Kentucky law, states:

*The Subsidiary Debtors...directly or indirectly through U.S. Coal, made payments totaling at least \$1,633,286.18 to the Defendant from July 16, 2010 to the filing of the involuntary bankruptcy...* [Am. Compl. ¶ 86 (emphasis added).]

The language challenging the Cash Transfers in the remaining fraudulent conveyance Counts is identical: "The Subsidiary Debtors ... directly or indirectly through U.S. Coal ..." made transfers. [Id. ¶¶ 93 (Count II), 101 (Count III), 109 (Count IV), 117 (Count V), 125 (Count VI).] 9A With regard to the mechanism of the transfers, the Amended Complaint merely asserts that U.S. Coal generated no funds of its own and instead

took funds from the Subsidiary Debtors to pay 'U.S. Coal's Operating Expenses.' See Motion for an Order Authorizing (i) Debtors to Continue Cash Management System and Maintaining Existing Bank Accounts and Business Forms and (ii) Financial Institutions to Honor and process Related Checks and Transfer (Doc. No. 604). [Id. ¶ 31.]

Even taking into account these general statements, the Amended Complaint fails to describe any specific transfers from the Subsidiaries to U.S. Coal. It does not state which Subsidiary made a transfer to U.S. Coal, the amount each Subsidiary transferred, or the date of any transfer. Instead, the Amended Complaint alleges that all transfers occurred via "sweep accounts." [Am. Compl. ¶ 3.] Thus, the Amended Complaint fails to identify challenged transfers sufficiently under Civil Rule 8:

**HULLY** Applying [Civil Rule 8] to preference and fraudulent transfer claims, the pleader must provide more than a mere recitation of the statutory elements of the cause of action. Instead, the pleader must identify the set of facts upon which he seeks to recover. At the very least, the rules of procedure require the pleader of a preferential or fraudulent transfer claim to reasonably identify the types of transfers sought to be avoided. Some courts have held that such identification must include the amount and date of the transfers together with the name of the transferor [¶15] and transferee.



58

#### Court's Ruling

- The Court ruled that the Trustee failed to state a claim in connection with her constructive fraud and preference claims under which she sought relief against the Defendant as an immediate or mediate transferee within the meaning of § 550(a)(2).
- Rejecting the Trustee's conduit argument as meritless, the Court stated that under the Trustee's argument, virtually every entity that held a contractual payment plan from the Debtor is an initial transferee of an unidentified subsidiary. **The Court explained that the mere existence of a contract with payment terms does not support a plausible inference that a debtor is a mere conduit with no discretion over the funds.**
- The Court held that the complaint did not set forth any facts from which a plausible inference could be drawn that the Debtor lacked discretion in the use of funds swept from the subsidiaries, or that the Debtor was bound to disburse the funds only in accordance with instructions from the subsidiaries. **Thus, the Court ruled that the amended complaint failed to state a factual basis for a plausible inference that the Debtor was a mere conduit of the subsidiaries.**



59

#### Court's Ruling

- Next, the Court ruled that the Trustee's actual fraud claims, to the extent plead against the Defendant as an initial transferee from the Debtor also suffer from fatal deficiencies. The Court determined that the heightened standard set forth in Civil Rule 9(b), applies to intentional fraudulent transfer claims where those claims are premised on a transferor-debtor's actual intent to defraud. The Court added that it is not the fraudulent intent of a debtor that must be pled with particularity; rather it is the **circumstances constituting fraud** and the Trustee did not plead them sufficiently in the present case.
- The Court held that the Trustee's amended complaint did not identify any specific challenged transfer, **did not contain any dates or amounts of the alleged fraudulent transfers and instead lumped all transfers from the Debtor to the Defendant via a total dollar amount.** Since this information was strictly required in the context of claims of actual fraud to give the answering party notice of the misconduct that is being challenged, the Court held that the Trustee's actual fraud claims fail to satisfy Civil Rule 9(b).



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[W]hen [HM21](#) a plaintiff's intentional fraudulent transfer claim is premised on a debtor's actual intent "to defraud," [Rule 9\(b\)](#) does apply, and the [\[427\]](#) plaintiff must plead the "circumstances constituting fraud" with particularity.

In order to meet this requirement in this context, a plaintiff must allege the following, for each transfer:

- the date of the transfer;
- the amount of the transfer (or if the transfer was of property other than money, the property that was transferred and its value);
- the name of the transferor;
- the name of the initial transferee; and
- the consideration paid, if any, for the transfer.

[In re NM Holdings](#), 407 B.R. at 261.

Because the Amended Complaint does not identify the date or amount of any transfer from U.S. Coal to [PC](#), the actual fraud claims fail to satisfy [Civil Rule 9\(b\)](#). To the extent Counts I and III seek recovery from [PC](#) for actual fraud as an initial transferee of the Cash Transfers from U.S. Coal, Counts I and III may be dismissed on this ground.



61

#### Court's Ruling

- With regard to the preference payments, the Court held that Trustee may pursue the claim against the Defendant as the initial transferee of transfers from the Debtor. The Court found that the amended complaint did allege that the total of the transfers to be \$135,000, that it was made within 90 days, made in connection with the promissory note and the Trustee did attach the payment schedule. The Court stated that with these allegations and the exhibit, the Defendant can assert its defenses and can also use discovery methods to discern whether additional facts exist to defend itself against this claim.
- The Court acknowledged that Civil Rule 8 does require more than just pleading the barebones elements of a preferential transfer claim so that the defendant can formulate its answer to the complaint and assert affirmative defenses. However, the Court held that in a case involving avoidance of preferential transfers from multiple debtors, the details of each transfer is not required.



62

As noted above, the Motorwerks court made clear that [HM36](#) Civil Rule 8 requires more than just pleading the barebones elements of a preferential transfer claim so that the defendant can formulate its answer to the complaint and assert affirmative defenses. [In re Motorwerks, Inc.](#), 371 B.R. at 292-93, 294. However, in a case involving avoidance of preferential transfers from multiple debtors, the court in [NM Holdings](#) declined to require the details of each transfer:

The Original Complaint informed Defendants that Plaintiffs sought to avoid and recover preferential transfers under [11 U.S.C. §§ 547\(b\)](#) and [550\(a\)](#). Through the allegations set forth in a table, the Original Complaint identified (1) the name of each debtor/transferor; (2) the name of each defendant/transferee; (3) the form of transfers (checks); and (4) the total amount of the alleged preferential transfers made by a particular debtor/transferor to each defendant/transferee. This provided ample and fair notice to each of the Defendants of "what the plaintiff's claim is and the grounds upon which it rests," as required by [Conley v. Gibson](#). And Defendants were not unduly hindered in their ability to file an answer and to assert any pertinent affirmative defenses. Further, to the extent Defendants were unable [\[447\]](#) to fully defend themselves or fully assert possible defenses because of any details missing from the Original Complaint, the Civil Rules gave them ways to cope with the problem. Defendants could seek full details about the transfers in discovery, and then amend their answers if necessary. The Court concludes that the Original Complaint met the liberal pleading requirements of [Civil Rule 8\(a\)](#).

[In re NM Holdings, Inc.](#), 407 B.R. at 256 (first emphasis added) (citation omitted).

Here, with regard to the Preference Payments, and in light of the Court's rulings as stated above, Trustee may pursue the claim against [PC](#) as the initial transferee of transfers from U.S. Coal. The Amended Complaint alleges the total of the transfers to be \$135,000 within a 90-day



63

*State Bank & Tr. Co. v. Spaeth (In re Motorwerks, Inc.)*

371 B.R. 281 (Bankr. S.D. Ohio 2007)



64

#### Facts

- Debtor Motorwerks, Inc., was engaged in a vehicle leasing business.
- Debtor and State Bank had a business relationship wherein State Bank regularly advanced money to the Debtor purportedly for the purpose of purchasing and leasing vehicles.
- Upon filing of an involuntary bankruptcy petition against the Debtor, Plaintiff State Bank filed a complaint seeking declaratory judgment against Defendant Paul H. Spaeth, the Chapter 7 Trustee for the bankruptcy estate of the Debtor.
- In its complaint, State Bank requested declaratory judgment that it was the owner / assignee of certain pre-petition vehicle lease agreements involving State Bank and the Debtor, that the leases are not property of the Debtor's estate, and that State Bank has the first and best perfected lien on the leased vehicles that secure the obligations of the lessees under the leases.
- The Trustee filed an answer acknowledging the prepetition relationship and lease agreements between State Bank and the Debtor, but denied the validity of many of the leases, assignments and/or security interests State Bank asserted in the vehicles.



65

#### Facts

- State Bank requested dismissal of the Defendant-Trustee's counterclaims pursuant to Fed. R. Civ. P. 12(b)(6)



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#### Issue

- Whether the Trustee's preferential and fraudulent transfer claims adequately identified the transfers to be avoided?



67

Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
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- (3) a demand for the relief sought, which may include relief in the alternative or different types of relief.

Rule 9 FRAUD OR MISTAKE; CONDITIONS OF MIND.

- (b) In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.



68

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- (b) In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.



69

#### Arguments

- The Trustee asserted claims for fraudulent transfers avoidable under the Bankruptcy Code and/or state law, preferential transfers avoidable under § 547, aiding and abetting fraud, aiding and abetting breach of fiduciary duty, equitable subordination, and an objection to proofs of claim filed by, or to be filed by, State Bank.
- State Bank argued that the Trustee's counterclaims failed to state any claim upon which relief can be granted pursuant to Rule 12(b)(6).
- Next, State Bank asserted that the Trustee's fraudulent and preferential transfer avoidance claims pursued under both bankruptcy and state law, should be dismissed pursuant to Federal Civil Rule 8(a) (2) and 9(b) because they lack the required specificity or particularity as they fail to identify the particular transfers that were preferential or fraudulent in nature.



70

#### Court's Ruling

- The Court agreed with State Bank that the Trustee's avoidance claims lacked the required specificity under the federal rules of civil procedure adopted in bankruptcy adversary proceedings.
- The Court found that the Trustee's preferential and fraudulent transfer claims failed to adequately identify the transfers to be avoided.
- The Court found that the Trustee's assertions merely parroted the relevant statutory language. Though the complaint did mention that the Debtor's sole shareholder was engaged in fraudulent schemes, intended to defraud creditors, and the alleged transfers made to State Bank were part of the Debtor's fraudulent scheme. However, the Trustee failed to identify, by date or amount, even one actual transfer from the Debtor to State Bank that was to be avoided. Further, the Trustee asserted that this information was currently unknown and will be the subject of discovery.



71

#### Court's Ruling

- The Court added that the same was the case with respect to the Trustee's allegations to avoid preferential transfers pursuant to § 547. The Court determined that while this claim very generally identified the types of transfers to be avoided, i.e. vehicle lease agreements assigned to or perfected by State Bank during the 90-day period prior to bankruptcy and payments made on leases during that same period, the claim still failed to identify any of the avoidable leases or payments with any specificity. Furthermore, the remainder of the Trustee's allegations, like those in his fraudulent transfer counterclaims, parroted the relevant statutory language of § 547.
- The Court determined that the problem with the Trustee's lack of specificity was that the counterclaims failed to provide State Bank with notice of the underlying transfers to be avoided hindering the bank's ability to prepare an adequate answer and affirmative defenses. The Trustee's omission of the identity of specific transfers to be avoided rendered State Bank unable to respond to the counterclaims with affirmative defenses such as "the bank gave contemporaneous new value for that transfer," "that transfer was made in the ordinary course of business," or "the Debtor received reasonably equivalent value for that transfer"



72

#### Court's Ruling

- The Court concluded that the Trustee's counterclaims failed to provide the minimum information required by Rule 8. However, taking into consideration the fact that pleading rules were liberally applied to the bankruptcy trustees who bring their actions as third party outsiders based on secondhand information, the Court didn't dismiss the Trustee's counterclaims outrightly, but granted a leave to amend his counterclaims.



73

#### Conclusion

- Applying Fed. R. Civ. P. 8 and 9 to preference and fraudulent transfer claims, a pleader **must provide more than a mere recitation of the statutory elements of the cause of action. Instead, the pleader must identify the set of facts upon which he seeks to recover.**
- The rules of procedure require the pleader of a preferential or fraudulent transfer claim to reasonably identify the types of transfers sought to be avoided. Such identification must include the amount and date of the transfers together with the name of the transferor and transferee. **In determining whether a transfer is adequately identified, a good test is to ask whether the defendant could respond to the claim for relief with an appropriate affirmative defense.**



74

*Stanziale v. DMJ Gas-Mktg. Consultants, LLC (In re Tri-Valley Corp.)*

2015 Bankr. LEXIS 29 (Bankr. D. Del. Jan. 7, 2015)

75

#### Facts

- Debtor Tri-Valley Corporation was a crude oil and natural gas exploration, development, and production company that located and developed hydrocarbon resources in California.
- Debtor filed for bankruptcy and the Trustee filed a complaint seeking to avoid and recover alleged preferential transfers totaling \$43,338.59 from Defendant DMJ Gas-Marketing Consultants LLC
- DMJ filed a motion to dismiss the complaint pursuant to Rule 8(a) and 12(b).

76

#### Issue

- Whether the Trustee's complaint must be dismissed because it failed to establish a plausible claim for a preferential transfer under section 547(b)?

77

Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
- (2) a short and plain statement of the claim showing that the pleader is entitled to relief; and
- (3) a demand for the relief sought, which may include relief in the alternative or different types of relief.

78

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79

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
- (2) lack of personal jurisdiction;
- (3) improper venue;
- (4) insufficient process;
- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.

80

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- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.

81

#### Arguments

- Defendant argued that the complaint must be dismissed because it failed to establish a plausible claim for a preferential transfer under section 547(b).
- The Defendant argued that the Trustee simply asserted the elements of section 547(b) and relied on legal conclusions rather than factual assertions. Specifically, the complaint did not contain a specific reference to the nature of the antecedent debt, failed to describe the relationship between it and any of the Debtors, and was devoid of any specificity as to any contracts or any goods or services DMJ may have provided to the Debtors.
- The Defendant next contended that exhibit A to the complaint, which was merely a schedule of payments made during the preference period, was insufficient to describe the nature of the antecedent debt.
- The Defendant also asserted that the complaint failed to allege the identity of the Debtor or Debtors who did business with DMJ for which an antecedent debt could have arisen, or in the alternative, that the complaint inconsistently identified whether one or all of the Debtors made the transfers.

82

#### Arguments

- The Trustee contended that the complaint and exhibit A, when read together, sufficiently detailed the nature of the antecedent debt and its payments. The Trustee argued that the complaint alleged that the parties conducted business together and that the transfers were made for, or on account of, antecedent debt owed to DMJ by the Debtors.
- The Trustee further noted that exhibit A identified TVC as the Debtor-transferor along with the specific account from which the transfers were made. Thus, the complaint was plausible on its face.

83

#### Court's Ruling

- The Court found that the complaint adequately alleged facts identifying the date of transfer, name of transferee, and transfer amount (stating that between "May 9, 2012 to August 6, 2012, the Debtors made transfers to Defendant in the amount of \$43,338.59 (the 'Transfers')." In addition, exhibit A identified the account number from which the transfers were made, as well as the amounts, issue, and clear dates of each payment.
- The Court also found that the complaint sufficiently identified which Debtor made the alleged transfers. Although, the complaint generally alleged that "the Debtors" made transfers to DMJ, Exhibit A specified that all payments to DMJ were issued by the Debtor from its general account at Wells Fargo. This sufficiently identified which Debtor made the alleged transfers.
- However, the Court found that the complaint failed to allege sufficient facts detailing the nature of the alleged antecedent debt. The complaint failed to provide any details to show that there was in fact an antecedent debt, stating only that "the Transfers were made for or on account of antecedent debt owed to the Defendant by the Debtors before the Transfers were made." The Court held that the recitation of the elements of section 547 in place of factual allegations is insufficient to withstand a motion to dismiss.

84

#### Court's Ruling

- The Court ruled that the Trustee's failure to allege sufficient facts to evidence a pre-existing debtor/creditor relationship or the nature of the alleged antecedent debt cannot be cured by the Trustee's allegations subsequently in his opposition brief.
- The Court dismissed the Trustee's claims, but granted a leave to amend his complaint, as the creditor presented no reason why leave should not be granted.

85

#### Conclusion

- Although a Chapter 7 trustee's § 547(b) complaint may adequately allege facts identifying the date of transfer, name of transferee, transfer amount, and which debtor made the alleged transfers, however, if the complaint fails to allege sufficient facts detailing the nature of the alleged antecedent debt or to provide any details to show that there was in fact an antecedent debt, the complaint is insufficient to withstand a motion to dismiss.
- To survive a motion to dismiss, an 11 U.S.C.S. § 547(b) preference complaint must include: (a) an identification of the nature and amount of each antecedent debt and (b) an identification of each alleged preference transfer by (i) date of the transfer, (ii) name of debtor/transferor, (iii) name of transferee and (iv) the amount of the transfer.

86

#### *Giuliano v. Haskett (In re MCG Ltd. P'ship)*

545 B.R. 74, 2016 Bankr. LEXIS 259, 62 Bankr. Ct. Dec. 30 (Bankr. D. Del. 2016)

87

#### Facts

- Debtors Monitor Company Group Limited Partnership were a global consulting firm with approximately 1,200 personnel in offices across 17 countries worldwide.
- During the course of its business, the Debtor made one transfer to the Defendant James Haskett in the aggregate amount of \$14,110.77; the transfer was made via check number 75212 and was sent on September 7, 2012 addressed to James Haskett c/o James B. Haskett & Associates and the check subsequently cleared on September 18, 2012.
- Subsequently, on November 7, 2012, voluntary petitions were filed by the Debtors under Chapter 11 of the Bankruptcy Code and on August 4, 2014, the Trustee initiated an adversary proceeding against the Defendant, for avoidance of transfer in the aggregate amount of \$14,110.77, pursuant to § 547 of the Bankruptcy Code.
- The Defendant filed its motion to dismiss the complaint pursuant to Rule 12(b).

88

#### Issue :

Whether the Trustee's Complaint failed to state a claim upon which relief may be granted and should be dismissed under Rule 12(b)(6)?

89

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
- (2) lack of personal jurisdiction;
- (3) improper venue;
- (4) insufficient process;
- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.

90

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A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.

91

#### Arguments

- The Defendant sought dismissal of the complaint for failure to state a claim upon which relief may be granted pursuant to the *Twombly/Iqbal* pleading standard and its bankruptcy progeny.
- The Defendant alleged that the complaint lacked any detail as to the nature of the antecedent debt or how it arose. The Defendant asserted that the "prior contractual obligations" were not described in the complaint and no contract was attached.

92

#### Arguments

- The Trustee responded that the motion to dismiss should be denied because each cause of action alleged in the complaint met the pleading requirements set forth under Rule 12(b)(6) –

- (1) the transfers were made because of prior contractual obligations or invoices owed by the Debtor to the Defendant before the transfers were made;
- (2) the transfers were made in payment of goods sold or services provided by the Defendant to the Debtor;
- (3) the goods or services paid for by each of the transfers were provided by the Defendant to the Debtor before each transfer was made;
- (4) the transfers constitute a transfer of an interest in property of the Debtor
- (5) the transfers were made on September 18, 2012, while the Debtor was insolvent;
- (6) each of the transfers was to or for the benefit of the Defendant;
- (7) the transfers enabled the Defendant to receive more than he would have received in the case if:
  - (i) the transfer had not been made; and
  - (ii) the Defendant received payment of such debt to the extent provided by the provisions of the Bankruptcy Code.

93

#### Courts Ruling

- The Court held that the complaint merely parroted the language of section 547 and offered no particularized facts giving context to the transfer that took place on September 18, 2012. The Court stated that the complaint falls short of the heightened pleading standards established in *Twombly and Iqbal*, which require the pleading to contain facts that support more than the possibility of relief to survive a motion to dismiss.
- The Court further added that the Complaint also fell short of the Third Circuit's two-part pleading hurdle established in *Fowler*. First, the complaint blended facts and legal conclusions; *Fowler* requires that the factual and legal elements of a claim to be separated. Second, the Court cannot determine whether the facts alleged in the complaint were sufficient to show that Trustee had a plausible claim for relief because it did not allege any facts that gave context or a description of the transfer made from the Debtors to the Defendant beyond whom the check was sent to, the dates the check were sent and received, and the amount of the transfer.
- The Court dismissed the complaint, but gave the Trustee a leave to amend the complaint

94

#### Conclusion

- Under the heightened standard, a complaint must contain either direct or indirect allegations respecting all the material elements necessary to sustain recovery under some viable legal theory
- In order to survive a motion to dismiss, a complaint must satisfy the heightened pleading standards established in *Twombly and Iqbal*, which require the pleading to contain facts that support more than the possibility of relief.

95

The obligation of the Plaintiff/trustee to bring specificity in a fraudulent case



96

*Apton Corp. v. Sonafi Pasteur (In re Apton Corp.),*  
423 B.R. 76 (Bankr. D. Del. 2010)



97

#### Facts

- Debtor Apton Corporation is a biopharmaceutical company that researches, develops, and commercializes pharmaceutical products for the treatment of cancer and gastrointestinal disease.
- Defendants Aventis Pharmaceuticals and SP are in the business of research, development and production of pharmaceuticals.
- The Debtor filed a voluntary petition under Chapter 11 of the Bankruptcy Code in May, 2006.
- The Trustee brought an adversary proceeding to avoid the transfers that Debtor had made prepetition, in connection with its redemption of a debenture sold to Aventis that had joined with Debtor in co-promoting a new drug to fight cancer and through payment to its former noteholders.



98

#### Facts

- Counts I through III of the Complaint set forth constructive fraudulent conveyance claims against Aventis. Counts V through VII set forth constructive fraudulent conveyance claims against the former noteholders.
- Counts I and V of the Complaint filed by the Trustee asserted that the Trustee was a lien creditor pursuant to § 544(b) of the Bankruptcy Code and that the \$3 million transferred to a pharmaceutical company by the Debtors to jointly promote a new drug and the \$3 million transferred to the Debtors former noteholders were each fraudulent transfers under the "Pennsylvania and/or Delaware Uniform Fraudulent Transfer Act.
- The Defendants moved to dismiss the complaint.



99

#### Rule 9. Pleading Special Matters

(a) Capacity or Authority to Sue; Legal Existence.

(1) In General. Except when required to show that the court has jurisdiction, a pleading need not allege:

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(b) Fraud or Mistake; Conditions of Mind. In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.



100

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101

#### Rule 9011

(c) **SANCTIONS.** If, after notice and a reasonable opportunity to respond, the court determines that subdivision (b) has been violated, the court may, subject to the conditions stated below, impose an appropriate sanction upon the attorneys, law firms, or parties that have violated subdivision (b) or are responsible for the violation.

(1) *How Initiated.*

(A) *By Motion.* A motion for sanctions under this rule shall be made separately from other motions or requests and shall describe the specific conduct alleged to violate subdivision (b). It shall be served as provided in Rule 7004. The motion for sanctions may not be filed with or presented to the court unless, within 21 days after service of the motion (or such other period as the court may prescribe), the challenged paper, claim, defense, contention, allegation, or denial is not withdrawn or appropriately corrected, except that this limitation shall not apply if the conduct alleged is the filing of a petition in violation of subdivision (b). If warranted, the court may award to the party prevailing on the motion the reasonable expenses and attorney's fees incurred in presenting or opposing the motion. Absent exceptional circumstances, a law firm shall be held jointly responsible for violations committed by its partners, associates, and employees.

(B) *On Court's Initiative.* On its own initiative, the court may enter an order describing the specific conduct that appears to violate subdivision (b) and directing an attorney, law firm, or party to show cause why it has not violated subdivision (b) with respect thereto.



102

Rule 9011

(C) **SANCTIONS.** If, after notice and a reasonable opportunity to respond, the court determines that subdivision (b) has been violated, the court may, subject to the conditions stated below, impose an appropriate sanction upon the attorneys, law firms, or parties that have violated subdivision (b) or are responsible for the violation.

(1) *How Initiated.*

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(B) *On Court's Initiative.* On its own initiative, the court may enter an order describing the specific conduct that appears to violate subdivision (b) and directing an attorney, law firm, or party to show cause why it has not violated subdivision (b) with respect thereto.



103

Issue :

- Whether the Complaint should be dismissed for failure to state an adequate claim for relief under Fed. R. Civ. P. 9(b)



104

Arguments

- The Former Noteholders and Aventis sought to dismiss the Complaint, alleging that the Complaint failed to state a claim upon which relief can be granted.
- The Former Noteholders also filed a motion for sanctions pursuant to Federal Rule of Bankruptcy Procedure 9011. They argued that legal research would have revealed that the alleged payment was not recoverable under sections 544, 548, or 550 of the Bankruptcy Code, both because it was a payment for antecedent debt and because it was a "settlement payment" under section 546(e). Still, the Trustee's counsel took no action to voluntarily dismiss the Complaint or to remedy its infirmities.
- The Trustee argued that the alleged transfers from the Debtor to the Former Noteholders and Aventis were avoidable pursuant to Sections 544 and 548 of the Bankruptcy Code as they were made within two years of the petition date; (ii) the Debtor received less than reasonably equivalent value for the transfer; and (iii) the transfers occurred at a time when the Debtor was insolvent.



105

Court's Ruling

- The Court found that the facts in the Complaint were not pled with sufficient particularity to satisfy Rule 9(b)
- Counts I and V of the Complaint merely plead that the Trustee was a lien creditor pursuant to § 544 of the Bankruptcy Code and asserted that the \$3 million transfer to Aventis and the Former Noteholders, respectively, violated the Pennsylvania and/or Delaware Uniform Fraudulent Transfer Act. The Court stated that the Trustee did not recite the elements of the Pennsylvania and/or Delaware Uniform Fraudulent Transfer Act, nor did he allege the specific facts that met those elements.
- The Court stated that these counts were just "blanket assertions" and did not state the ground on which these claims rest.



106

Court's Ruling

- The Court further concluded that Counts II and VI were plead with allegations of "date, place or time" and therefore fulfilled the function of Rule 9(b) by placing the defendants on notice of the misconduct with which they were charged.
- The Complaint identified the alleged constructively fraudulent transfers by date and face amount. Since, the Complaint described the circumstances surrounding the transfers and alleged that the Debtor was insolvent at the time of both transfers, the Court found that Counts II and VI of the Complaint complied with Rule 9(b).
- The Court further concluded that while the Trustee properly showed that the Debtor was insolvent at the time the collaboration agreement was terminated, the Trustee failed to allege when the redemption payment was made, how the termination and redemption transactions were related, and which transaction involved less than reasonably equivalent value.



107

Court's Ruling

- Based on the analysis, the Court granted Aventis's motion to dismiss and dismissed Counts I, II, III of the Complaint. The Court also granted in part the Former Noteholders' motion to dismiss as to Count V of the Complaint and denied in part as to Counts VI and VII of the Complaint.
- The Court further determined that the standard for imposing sanctions under Rule 11 is stringent because such sanctions are in "derogation of the general American policy of encouraging resort to the courts for peaceful resolution of disputes," and tend to "spawn satellite litigation counter-productive to efficient disposition of cases."
- The Court ruled that the Complaint sets out facially plausible causes of action against the Former Noteholders and there was no evidence that the Trustee's counsel's claims were "frivolous, legally unreasonable, . . . without factual foundation," or that the firm intended to abuse the bankruptcy system by filing the original Complaint. Therefore, the Court denied the Former Noteholders' motion for sanctions.



108

*Sarachek v. Meltzer (In re Agriprocessors, Inc.),*  
Nos. 08-02751, 10-09194, 2011 Bankr. LEXIS 3669  
(U.S. Bankr. N.D. Iowa Sep. 30, 2011)



109

#### Facts

- Debtor owned and operated one of the nation's largest kosher meatpacking and food-processing facilities in Postville, Iowa
- The Trustee filed a complaint against Defendant, alleged to be a corporate officer of the Debtor, to avoid fraudulent conveyances and preferential transfers under 11 U.S.C.S. § 547 and 548.
- Defendant filed a motion to dismiss.



110

#### Issue :

- Whether the complaint states a claim upon which relief can be granted pursuant to Rule 8 and 9 of the FRCP.
- Whether the Complaint satisfies the pleading standards in the Bankruptcy and Federal Courts — as interpreted in *Twombly* and *Iqbal*



111

#### Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
- (2) a short and plain statement of the claim showing that the pleader is entitled to relief; and
- (3) a demand for the relief sought, which may include relief in the alternative or different types of relief.



112

#### Rule 8 (a) A pleading that states a claim for relief must contain:

- (1) a short and plain statement of the grounds for the court's jurisdiction, unless the court already has jurisdiction and the claim needs no new jurisdictional support;
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113

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(b) Fraud or Mistake; Conditions of Mind. In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.



114

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115

#### Arguments

- Defendant moved to dismiss the Trustee's complaint to avoid fraudulent conveyances, alleging that the Trustee failed to **specify which transfers** are avoidable as § 548 fraudulent conveyances or § 547 preferential transfers.
- He asserted that the Trustee's Complaint did not satisfy the pleading requirements of Fed. R. Civ. P. 8(a)(2) and 9(b). In particular, Defendant argues that Trustee failed to plead the fraudulent transfer claim with specificity under the heightened pleading standards of Fed. R. Civ. P. 9(b).
- Trustee resisted the Defendant's Motion and argued that Rule 9(b) **pleading standards did not apply to his claim for constructive fraud.**



116

#### Court's Ruling

- Relying upon *Sarachek v. The Right Place, Inc.*, the Court held that the heightened pleading requirements of Rule 9(b) **do not** apply to constructive fraudulent transfer claims. The Court stated that Section 548(a)(1)(B) claims must satisfy only the general pleading rules of Rule 8(a) to survive a motion to dismiss.
- The Court thus rejected the Defendant's claim that the Trustee's fraudulent conveyance claim should be dismissed for failing to comply with Rule 9(b).
- The court next ruled that the Trustee's **allegation that he is not aware of equivalent value** is a factual allegation sufficient to support Trustee's claim that Debtor received less than reasonably equivalent value in exchange for the alleged transfers. The allegation satisfies the plausibility standards of *Twombly* and *Iqbal*.



117

#### Court's Ruling

- The Court also ruled that the Trustee has plausibly alleged a series of fraudulent conveyances sufficient to "raise the curtain for discovery" into the Trustee's claims. The parties may utilize the discovery process to develop in more detail the relevant questions of fact.
- The Court denied the Defendant's motion to dismiss.



118

#### Conclusion

- Heightened pleading requirements of Rule 9(b) do not apply to constructive fraudulent transfer claims.
- Section 548(a)(1)(B) claims must satisfy only the general pleading rules of Rule 8(a) to survive a motion to dismiss.



119

*Wahoski v. Classic Packaging Co. (In re Pillowtex Corporation),*

427 B.R. 301 (Bankr. D. Del. 2010)



120

#### Facts

- Debtors Pillowtex Corporation and related entities filed voluntary Chapter 11 bankruptcy petitions.
- The Committee filed a number of adversary proceedings seeking to avoid preferential and fraudulent transfers
- One such adversary proceeding was filed against Defendant Classic Packaging Company
- Defendant produced plastic bags and packaging for the Debtors, printed with Pillowtex brand names on them.
- The Committee's complaint against Classic amongst other things, sought to avoid and recover certain transfers as fraudulent pursuant to Sections 548 and 550 of the Bankruptcy Code.
- The Defendant filed a Motion to dismiss the complaint



121

#### Issue :

- Whether Defendant's motion to dismiss as to the fraudulent transfer count should be granted on the grounds that the Trustee failed to allege any factual support of the fraud, and was just merely reciting the statutory language of § 548 (a).



122

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
- (2) lack of personal jurisdiction;
- (3) improper venue;
- (4) insufficient process;
- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.



123

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124

#### Arguments

- Defendant argued that the Count Two of the Trustee's complaint merely recited the statutory language of the Bankruptcy Code Section 548(a).
- The Defendant further asserted that the Count Two completely lacked any factual allegations to support a fraudulent transfer claim and failed to meet the pleading requirements set forth in *Twombly* and should be dismissed pursuant to Rule 12(b)(6).
- The Plaintiff responded that the fraudulent transfer claim must be preserved as an alternative claim and should not be dismissed.



125

#### Court's Ruling

- The Court agreed with the Defendant and dismissed the Trustee's Complaint without prejudice.
- The Court found that the complaint merely recited the statutory language and failed to provide any factual allegations.
- The Court granted the Defendant's motion to dismiss the fraudulent transfer count.
- The Court noted that the "bare-boned drafting" of the second count did not appear motivated by bad faith or an intent to delay, and although the transaction appeared to be at arm's length, to ensure an adequate opportunity to respond, the Court granted leave to file an amended complaint within fourteen days setting forth adequate facts to support the fraudulent transfer claim



126

#### Conclusion

- Complaint merely recited the statutory language and failed to provide any factual allegations/ It also failed to meet the pleading requirements set forth in *Twombly*, and hence was dismissed pursuant to Rule 12(b)(6).



127

#### *Heath v. Evans (In re Evans),*

Nos. 15-00090 (Chapter 7), 16-00002, 2016 Bankr. LEXIS 3999  
(U.S. Bankr. D. Guam Nov. 10, 2016)



128

#### Facts

- Debtor Myrna Castro Evans allegedly quitclaimed two parcels of real property to her husband, Defendant Roy Kenneth Evans, when she executed a divorce and property settlement agreement.
- Allegedly, the transfer of these two properties was quitclaimed to the Defendant, under duress, for either absent or inadequate consideration within one year of the date she filed for bankruptcy.
- The Trustee brought a complaint against the Defendant Evans for the avoidance of these fraudulent transfers under § 548 of the Bankruptcy Code.
- The Defendant moved to dismiss the Trustee's complaint.
- In response, the Trustee introduced facts not alleged within the Complaint to argue that the elements of his causes of action were satisfied.



129

#### Issue :

- Whether Evans' motion to dismiss should be granted for failure to allege sufficient facts to state claims that were plausible, and for failure to plead fraud claims with particularity under FRCP 9(b) and 12 (b)



130

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134

#### Argument

- The Defendant argued that the Trustee failed to allege specific facts to state a plausible claim and inadequately plead facts sufficient to satisfy the elements of causes of action related to purported fraudulent transfers of real property and hence complaint should be dismissed pursuant to FRCP 9(b) and 12(b).
- The Trustee contended that the complaint met the pleading requirements of the FRCP, but requested leave to amend his complaint if the Defendant's motion to dismiss was granted.



135

#### Court's Ruling

- The Court found that the Defendant was correct that the Trustee failed to plead facts forming the basis for the assertion that the Debtor or Evans knew that the value of the consideration received by the Debtor in exchange for the properties was not of reasonably equivalent value.
- Additionally, the complaint generally referenced that the properties at issue were quitclaimed to her husband under duress, under either absent or inadequate consideration within one year of the date she filed for bankruptcy.
- The Court also found that the facts asserted by the Trustee in opposition to the motion to dismiss was outside the complaint and were improper.
- The Trustee did not allege proper facts in the complaint. Additionally, there were certain facts which were not alleged in complaint at all i.e., the facts such as, the properties were held jointly, that there was misrepresentation by spouse, that the Debtor would be criminally prosecuted unless the spouse dismissed the complaint etc. The Court found that these facts were alleged later in opposition to the Defendant's motion to dismiss and hence, they cant be considered at this stage.



136

#### Court's Ruling

- The Court determined that when the legal sufficiency of a complaint's allegations is tested by a motion under Rule 12(b)(6), review is limited to the complaint and the court typically does not consider material outside the pleading.
- The Court granted Evans motion to dismiss the complaint with leave to amend the complaint, because the circumstances of fraud were insufficiently pleaded, and because the Trustee's opposition relied on factual assertions extrinsic to the complaint to support his claims.



137

#### Conclusion

- When the legal sufficiency of a complaint's allegations is tested by a motion under Rule 12(b)(6), review is limited to the complaint, and allegations made outside of the complaint are not considered proper before the court



138

*Air Cargo, Inc. Litig. Trust v. i2 Techs., Inc. (In re Air Cargo, Inc.),*

401 B.R. 178, 2008 Bankr. LEXIS 2680  
(Bankr. D. Md. 2008)



139

#### Facts

- Debtor, Air Cargo, Inc. was in the business of providing services to various airlines for the movement of cargo, acting as an agent between the airlines and freight forwarders in order to facilitate the transfer of cargo by motor carriers.
- Defendants i2 Technologies, Inc. and Mercer Mgt. Consulting, Inc. provided certain information technology architecture to the Debtor.
- The Debtor filed for bankruptcy and the Trustee filed a complaint against the Defendants for the recovery of certain transfers made to the Defendant by the Debtor as fraudulent under Sec. 548 of the Bankruptcy Code.
- The Defendants filed motion to dismiss the trustee's complaint.



140

#### Issue

- Whether the constructive fraudulent conveyance claims must be pled under the lenient standard of Rule 8, or under the heightened pleading standards of Rule 9(b).



141

#### Arguments

- The Trustee argued that the information technology which the Defendants provided to the Debtor was insufficient to meet the needs of the Debtor and that the Defendants were aware of this fact and still they misrepresented and fraudulently provided the insufficient services to the Debtor.
- The Trustee's complaint contained seven counts including for breach of contract against i2 and Mercer, **intentional misrepresentation and fraud** against i2 (Count III), negligent misrepresentation against i2 and Mercer (Count IV), negligence and malpractice against i2 and Mercer (Count V), avoidance and recovery of fraudulent conveyances from Air Cargo to i2, totaling "no less than \$5.7 million" (Count VI), and the avoidance and recovery of fraudulent conveyances from Air Cargo to Mercer, totaling "no less than \$ 100,000" (Count VII).
- In its motion to dismiss, the Defendants argued that the Trustee's fraudulent conveyance claim failed as a matter of law, on the grounds that it lacked a good faith basis, **failed to identify an actual creditor that could bring such a claim under state law**, failed to establish the absence of fair consideration, and failed to allege the fraudulent conveyance with particularity.



142

#### Court's Ruling

- The Court determined that while a complaint attacked by a Rule 12(b)(6) motion to dismiss does not need detailed factual allegations, a plaintiff's obligation to provide the 'grounds' of his 'entitlement to relief' requires more than labels and conclusions and a formulaic recitation of a cause of action's elements will not do.
- The Court further added that - while Federal Rule of Civil Procedure 8 requires only a "short and plain statement of the claim showing the pleader is entitled to relief," Federal Rule of Civil Procedure 9(b) requires the circumstances of a claim to be "pleaded with particularity."
- The Court pointed out Rule 9(b) does not apply where constructive fraud is alleged.
- The Court stated that in a complaint to avoid a **constructively fraudulent conveyance**, there is **no requirement to prove any misrepresentation or intent** to defraud on the part of the transferor. Rather, the complaint must simply allege that the transferee did not receive fair consideration.



143

#### Court's Ruling

- The Court further held that although the Trustee did not have to meet the heightened pleading standards of Fed. R. Civ. P. 9(b), however even if the pleading standards of Rule 9(b) had to be applied, the Trustee would have met them because the Trustee described events surrounding the conveyance and the reasons it was **not made for reasonably equivalent value**.
- The Court denied the Defendants' motion to dismiss the complaint.



144

#### Conclusion

- Fed. R. Civ. P. 9(b) does **not** apply where constructive fraud is alleged. In a complaint to avoid a constructively fraudulent conveyance, there is no requirement to prove any misrepresentation or intent to defraud on the part of the transferor. Rather, the complaint must simply allege that the transferee did not receive fair consideration and insolvency.



145

*Mukamal v. BMO Harris Bank N.A. (In re Palm Beach Fin. Partners, L.P.)*

488 B.R. 758, 2013 Bankr. LEXIS 1078, 57 Bankr. Ct. Dec. 209, 2013 WL 1114356 (Bankr. S.D. Fla. 2013)



146

#### Facts

- Debtors Palm Beach Finance Partners, L.P. and Palm Beach Finance II, L.P. were investors in a purchase financing operation run by Thomas Petters.
- Petters, however, was not operating a legitimate purchase financing operation and was running a Ponzi scheme.
- Defendant M&I Marshall & Ilsley Bank was the Debtor's primary depository bank.
- The Debtors filed for bankruptcy and the Trustee brought a complaint against the Defendant bank alleging that M&I received fraudulent transfers and knew of Petters' fraud, and engaged in wrongdoing which allowed Petters' fraud to continue undetected.
- The Defendant bank filed a motion to dismiss the complaint pursuant to Federal Civil Rules 12(b)(6) and 9(b).



147

#### Facts

- The Court granted the Defendant's motion to dismiss with leave to file an amended complaint.
- The Trustee filed an amended complaint and the Defendant filed Motion to dismiss the amended complaint.



148

#### Issue

- Whether the Trustee's complaint should be dismissed pursuant to Fed. R. Civ. P. 12(b)(6) because the Trustee filed a "shotgun complaint" that did not meet the requirements of Fed. R. Civ. P. 8(a) ?
- Whether the Trustee's complaint was subject to the pleading requirements found in Fed. R. Civ. P. 8 (a) and 9(b).



149

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

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152

#### Arguments

- The Trustee alleged that the Defendant bank received fraudulent transfers from the Debtor and the losses incurred by the Debtors should be recovered from the Defendant as the Debtors' primary depository bank.
- Specifically, the Trustee alleged that the bank was a transferee of funds which were received on deposit by the bank.
- The Bank alleged that the Trustee's complaint did not meet the requirements of Fed. R. Civ. P. 8(a) and Fed. R. Civ. P. 12(b)(6).
- The Defendant bank contended that it was not a transferee of these funds, but was instead a "mere conduit".



153

#### Court's Ruling on Trustee's Initial Complaint

- The Court dismissed the Trustee's complaint without prejudice pursuant to Fed. R. Civ. P. 12(b)(6) because the Trustee filed a "shotgun complaint" that did not meet the requirements of Fed. R. Civ. P. 8(a)
- The Court found that the Trustee's complaint was a textbook example of a "shotgun pleading." The complaint spanned 68 pages, excluding 76 pages of exhibits, and contained 322 numbered paragraphs. **Furthermore, each claim, of which there are twelve, reasserted the allegations set forth in paragraphs 1 through 239.** The Court added that by reasserting the allegations in paragraphs 1 through 239 in each claim, the Trustee made it difficult, if not impossible, for the Defendants and the Court to discern which allegations was meant to support which claims.
- The Court ruled that since the Trustee's complaint did not comply with Rule 8(a)'s notice pleading requirements, the complaint should be dismissed and granted the Trustee a leave to file an amended complaint which complied with Rule 8(a).



154

#### Court's Ruling on Trustee's Amended Complaint

- The Court rejected the Defendants' argument that the amended complaint still exhibited all the objectionable characteristics of a shotgun pleading.
- The Court held that the amended complaint incorporated several important changes aimed at avoiding the issues inherent in shotgun pleadings.
- The Court found that the Trustee condensed the amended complaint by removing certain allegations and exhibits. The amended complaint was 48 pages long, contained 236 numbered paragraphs; in contrast to the Trustee's initial complaint, which was 66 pages long and contained 322 numbered paragraphs. **Second, the Court found that not every claim simply reasserted and realleged every preceding paragraph.**
- The Court ruled that the Trustee sufficiently corrected his pleading deficiency and the amended complaint no longer constituted a shotgun pleading.



155

#### Court's Ruling on Amended Complaint

- Next, with regard to the Defendant's conduit defense, the Court held that it **could not determine at the motion to dismiss stage** whether the bank was entitled to the protection of the mere conduit rule because there was no basis to conclude that as a matter of law the bank acted in good faith.
- The Court, however, dismissed the aiding and abetting fraud claims because the Trustee **failed to adequately allege that the bank had actual knowledge of the Ponzi scheme.**
- The Court dismissed the **fraudulent inducement and fraudulent misrepresentation claims** because the Trustee failed to allege the precise statements or misrepresentations made, the time and place of and persons responsible for the statements, to whom the statements were made, and how each defendant participated in the alleged fraud.



156

#### Court's Ruling on Amended Complaint

- The Court denied the Defendants' motion to dismiss to the extent that it sought dismissal of all the claims of fraudulent transfer.
- The Court granted the Defendants' motion to dismiss as to the remaining claims for failure to state claims for relief plausible on the face of the amended complaint.



157

#### Conclusion

- Shotgun pleadings fail to comply with Rule 8(a)'s notice pleading requirements because such pleadings make "it is virtually impossible to know which allegations of fact are intended to support which claim(s) for relief.
- A "shotgun pleading" invariably begins with a long list of general allegations, most of which are immaterial to most of the claims for relief. The pleading then incorporates every antecedent allegation by reference into each subsequent claim for relief.
- An affirmative defense - especially one which turns on a fact-intensive analysis of a party's good faith - is generally not an appropriate basis for dismissal at this stage.



158

*Angell v. Augusta Seed Corp. (In re Tanglewood Farms, Inc.),*

2013 Bankr. LEXIS 499, 2013 WL 474704 (Bankr. E.D.N.C. Feb. 7, 2013)

159

#### Facts

- Prior to its bankruptcy, Debtor Tanglewood Farms, was in the business of purchasing, selling, and storing grain. James H. Winslow is the president and 100% stockholder of the Debtor.
- Two years prior to the petition date, the Debtor made three payments to Defendant Augusta Seed in the total sum of \$100,000.00. Two of the payments were made from the Debtor's bank accounts in the name of the Debtor. The third payment was made by the Debtor's president Winslow but funded by the Debtor pursuant to a loan from the Debtor to Winslow.
- All three payments took place within the two years prior to the petition date. The Debtor's records did not indicate that the Debtor received any property in exchange for the transfers.
- The Trustee brought an adversary proceeding to avoid the payments pursuant to Sec. 548 and to recover the proceeds from the Defendant pursuant to Sec. 550 and 551.
- The Defendant filed a motion to dismiss the complaint with prejudice for failure to state a claim upon which relief can be granted pursuant to Rule 7012 of the Federal Rules of Bankruptcy Procedure, incorporating Rule 12(b)(6) of the Federal Rules of Civil Procedure

160

#### Issue –

- Whether the Trustee's complaint contains facts sufficient to show a plausible claim for the avoidance of the fraudulent transfers, satisfying the burden of Rule 12(b)(6).

161

#### Rule 12(b)

Every defense to a claim for relief in any pleading must be asserted in the responsive pleading if one is required. But a party may assert the following defenses by motion:

- (1) lack of subject-matter jurisdiction;
- (2) lack of personal jurisdiction;
- (3) improper venue;
- (4) insufficient process;
- (5) insufficient service of process;
- (6) failure to state a claim upon which relief can be granted; and
- (7) failure to join a party under Rule 19.

A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed. If a pleading sets out a claim for relief that does not require a responsive pleading, an opposing party may assert at trial any defense to that claim. No defense or objection is waived by joining it with one or more other defenses or objections in a responsive pleading or in a motion.

162

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163

#### Rule 9. Pleading Special Matters

(a) Capacity or Authority to Sue; Legal Existence.

(1) In General. Except when required to show that the court has jurisdiction, a pleading need not allege:

- (A) a party's capacity to sue or be sued;
- (B) a party's authority to sue or be sued in a representative capacity; or
- (C) the legal existence of an organized association of persons that is made a party.

(2) Raising Those Issues. To raise any of those issues, a party must do so by a specific denial, which must state any supporting facts that are peculiarly within the party's knowledge.

(b) Fraud or Mistake; Conditions of Mind. In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake. Malice, intent, knowledge, and other conditions of a person's mind may be alleged generally.

164

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165

#### Arguments

- The Trustee argued that the Debtor received less than reasonably equivalent value in exchange for the transfers and was insolvent on the date of the transfers. At the time of the transfers, according to the Trustee, the Debtor 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.
- The Defendant asserted that the Trustee failed to state with particularity the circumstances which constitute fraud pursuant to Rule 7009 of the Federal Rules of Bankruptcy Procedure, incorporating Rule 9(b) of the Federal Rules of Civil Procedure.
- In response, the Trustee stated that the complaint, as filed, contained sufficient factual allegations to show a plausible claim for relief under the relevant Bankruptcy Code provisions, and that Rule 9(b) was not applicable to the complaint because the Trustee made no allegations of actual intent to defraud.

166

#### Court's Ruling

- The Court found that the Trustee's complaint contained facts sufficient to show a plausible claim for the avoidance of the fraudulent transfers, satisfying the burden of Rule 12(b)(6). The Court added that because the transfers undisputedly occurred within the two years of the petition date, it was immaterial whether the cause of action was brought under the constructive fraud provisions of North Carolina's Uniform Fraudulent Transfer Act or § 548.
- Further, the Court held that Rule 9(b), requiring the circumstances of fraud to be stated with particularity, was not applicable here because this was a constructive fraud case.
- The Court also held that the complaint alleged facts sufficient to show that the transfers were made while the Debtor was insolvent or that Debtor was left with unreasonably small capital as a result of the transfer.
- Specifically, the egregious nature of the Debtor's insolvency as of the petition date, as indicated in the Debtor's schedules, raised an inference that the Debtor's insolvency predated the petition to the time of the alleged fraudulent transfers.

167

#### Court's Ruling

- The Court next determined that the argument that the transfers left the Debtor with unreasonably small capital was bolstered by the fact that the Debtor set up a fictitious bank account to pay its obligations because it was unable to do so out of its operating account.
- In view of all of the above, the Court ruled that the Trustee made a plausible claim that the conveyances were fraudulent pursuant to § 548 of the Bankruptcy Code.
- The Court denied the Defendant's motion to dismiss the complaint.

168

Conclusion

- Fed. R. Civ. P. 9(b), requiring the circumstances of fraud to be stated with particularity, is not applicable to constructive fraud cases.

169

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170