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# PROPERTY TRANSFERS UNDER SECTION 727 OF THE BANKRUPTCY CODE: DEFINING THE MOMENT OF TRANSFER

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## INTRODUCTION

Section 727(a)(2)(A) of the Bankruptcy Code provides that, “[t]he court shall grant the debtor a discharge, unless . . . the debtor, with intent to hinder, delay, or defraud a creditor . . . has transferred, removed, destroyed, mutilated, or concealed . . . property of the debtor, within one year before the date of filing of the petition.”<sup>1</sup> The statute at first glance appears to be quite clear in its purpose and effect. If a debtor fraudulently transfers property at least one year prior to filing for bankruptcy, he<sup>2</sup> is granted a discharge. Whereas, if such a transfer occurs *within* a year of the bankruptcy filing, a discharge will be denied. As is often the case, however, what appears simple on its face does not always end up so after legal minds begin their dissection. What if a debtor fraudulently transfers real property in an effective transaction between the parties prior to a year before his bankruptcy petition, but the transfer is *recorded* within the year time frame? Did the transfer for the purpose of the statute occur when it

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\* Class of 1999, University of Southern California Law School; B.A. 1995, University of California, Los Angeles. I would like to express my gratitude to Shannon Rust for her most helpful comments. Also, I would like to thank my father T. Steven Roosevelt, the protagonist in *In re Roosevelt*. I would like to dedicate this Note to my mother, sister, Kelly, and friends whose support has kept me going throughout the years.

1. Bankruptcy Code, 11 U.S.C. § 727(a) (1994). From this point forward all references to particular sections refer to sections of the Bankruptcy Code.

2. The *Southern California Law Review* strongly endorses a policy of gender parity, however, for simplicity, I have chosen to retain the consistent use of “he” to refer to hypothetical persons.

was effective between the parties, or when it was recorded? This issue was presented before the Ninth Circuit in *In re Roosevelt*.<sup>3</sup>

On June 10, 1989, T. Steven Roosevelt (Steven) and his then wife, Judy Ann Roosevelt (Judy), executed a postnuptial "marriage settlement agreement" which set forth the separate and community property of each. Among the transmutations, Judy received Steven's joint interest in the family residence. The marital agreement was recorded on April 12, 1990. At the time of its execution, Steven was a defendant in a California state court lawsuit initiated by Finalco, Inc. Steven filed for bankruptcy on November 9, 1990. Alleging an intentional fraudulent transfer of the residence, Finalco instituted an adversary proceeding objecting to Steven's discharge pursuant to section 727(a) of the Code.<sup>4</sup>

The trial court found that Steven made the transfers effected by the marital settlement agreement with the intention to hinder, delay, or defraud his creditors, and that Judy took thereunder as a good faith transferee.<sup>5</sup> The court concluded, however, that the marital agreement was sufficient to transfer all of Steven's interest in the residence to Judy, and further held that the transfer effectuated by the marital settlement agreement took place more than one year prior to the filing of the bankruptcy petition. Having so concluded, the trial court granted Steven his discharge.<sup>6</sup>

Congress has enacted other provisions of the Bankruptcy Code dealing with transfers. For instance, in its 1978 enactment of section 548(d) regarding the avoidance power of the bankruptcy trustee, Congress decreed that:

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3. *Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 87 F.3d 311, 313 (9th Cir. 1996), *cert. denied*, 117 S. Ct. 1691 (1997).

4. *See id. In re Roosevelt* has subsequently been overruled, but it was done so on a basis that in no way affects the court's analysis of the timing issue of section 727. Instead, the case was overruled for applying the incorrect standard of review. *See Murray v. Bammer (In re Bammer)*, 131 F.3d 788, (9th Cir. 1997). The court stated:

In some cases we have held that discharge decisions are reviewed for abuse of discretion. *See, e.g., In re Roosevelt*, 87 F.3d 311, 314, *as amended*, 98 F.3d 1169 (9th Cir. 1996); *Friedkin v. Sternberg (In re Sternberg)*, 85 F.3d 1400, 1404-05 (9th Cir. 1996). Insofar as these dictate de novo review of legal conclusions and clear error review of factual findings, they do not conflict with our decision today. Insofar as they presume a standard of review other than de novo for mixed questions, however, they conflict both with our decision today and with *McConney* and its progeny, *and to that extent* we overrule them.

*Id.* at 792 (emphasis added).

5. *See Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 176 B.R. 534, 535 (B.A.P. 9th Cir. 1995). The finding that Judy had taken her share of property under the marriage settlement agreement as a good faith transferee has no effect on the analysis in this article and I take no position on this finding.

6. *See id.* A denial of discharge is an extremely harsh remedy. Not only is the transfer in question brought back into the bankruptcy estate, but the debtor remains liable for all of his debts. *See infra* note 128 and accompanying text.

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*For the purposes of this section,*<sup>7</sup> a transfer is made when such transfer is so perfected that a bona fide purchaser from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest in the property transferred that is superior to the interest in such property of the transferee . . . .<sup>8</sup>

In essence, this provision states that under section 548, a transfer is deemed made when it is recorded, as opposed to when the transfer is effective between the parties. The issue presented in *In re Roosevelt* was whether this so-called “bona fide purchaser rule” (the BFP rule) should also be applied in the context of section 727(a)(2), making a transfer completed upon recordation under that section.<sup>9</sup>

Both the Bankruptcy Appellate Panel and the Ninth Circuit Court of Appeals rejected the engraftation of the BFP rule into section 727 and stated that there is no such notice requirement in this section.<sup>10</sup> Thus, the Ninth Circuit held that a transfer is effective for the purpose of section 727(a)(2)(A) when it is effective between the parties to the transfer—the so-called “party rule.”<sup>11</sup>

However, the Third Circuit Court of Appeals had previously taken a contrary position. In *In re MacQuown*,<sup>12</sup> the debtor’s wife executed a will that left all of her property to her children in August, 1977. In December, 1977, the debtor and his wife executed a deed that transferred the family residence to the wife alone. The debtor filed his petition for bankruptcy in September of 1979. The transferee never gave consideration for the transfer, nor did she record the deed until June 13, 1979. The bankruptcy court ruled here, as in *In re Roosevelt*, that the debtor had made the conveyance with the intent to defraud his creditors. The Third Circuit Court of Appeals, however, applied a bona fide purchaser analysis to section 14(c), the predecessor to section 727, as opposed to the party rule as announced in *In re Roosevelt*, and in so doing held that the debtor had transferred the prop-

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7. It is interesting to note that this phrase did not play a greater part in the deliberations of any court that heard this matter. Finalco’s main argument centered around analogizing section 548 to section 727 of the Bankruptcy Code.

8. Bankruptcy Code, 11 U.S.C. § 548(d) (1994) (emphasis added).

9. See *In re Roosevelt*, 87 F.3d at 315-16 (“Finalco contends that, even if the Marital Agreement was valid between Steven and Judy, that discharge was still improperly granted because § 727(a)(2) does not deem a transfer ‘made’ until it is recorded.”).

10. See *id.* at 318; *In re Roosevelt*, 176 B.R. at 538. See also Bankruptcy Code, 11 U.S.C. § 727(a) (1994) (The section provides in pertinent part that “[t]he court shall grant the debtor a discharge, unless . . . the debtor, with intent to hinder, delay or defraud a creditor . . . has transferred . . . property of the debtor, within one year before the date of filing of the petition.”).

11. See *In re Roosevelt*, 87 F.3d at 318.

12. Dean Witter Reynolds, Inc. v. MacQuown (*In re MacQuown*), 717 F.2d 859 (3d Cir. 1983).

erty within the one-year reach back provision of section 14(c). As a result, MacQuown was denied his discharge.<sup>13</sup>

Few cases deal with the question of when a transfer is complete for the purposes of section 727.<sup>14</sup> Notwithstanding this paucity of authority, the issue is worthy of discussion for several reasons. Most importantly, the Ninth Circuit's decision created a split in authority as to the question of timing. Courts in jurisdictions undecided on this issue are thus left with conflicting guidance from which to determine the proper rule to be applied. Debtors and possible future litigants have no definitive answer as to the question of the timing of a transfer made under section 727(a)(2)—a fundamentally unfair position in light of the Code's policy of providing uniform laws in the context of bankruptcies. Finally, the concern has been raised that the Ninth Circuit's adoption of the party rule "could reek [*sic*] havoc in not only the bankruptcy arena, but also the title laws of virtually every state in the union which have all improved upon the uncertainties of common law concepts of title by replacing them with the reliability and certainty of public record as proof of ownership."<sup>15</sup> This argument rests on the premise that although the party rule would apply only to discharges under section 727(a)(2), the analysis which gives rise to the conclusion that it is the proper rule could affect the analysis of other sections of the Code. Thus, the certainty which the recording statutes are designed to preserve may be undermined if transfers are analyzed from the date they are effective between the parties to the transfer, as opposed to the date of recording.

Part II of this Note addresses the role of the federal courts in deciding the proper transfer rule, and concludes that the federal courts are indeed the proper authority to make such a decision. Part III discusses the language of section 727 (a)(2)(A), and establishes that it does not provide a clear answer as to which rule is proper. Additionally, this Part examines the ways in which parties to actions involving section 727(a)(2) have used its legislative history to bolster arguments in their favor. Part III contends that these arguments alone are also not conclusive, due to the conflicting authority granted by courts to statutory construction.

Arguments proposed in favor of the bona fide purchaser rule are examined in Part IV. The syllogism for the adoption of the BFP rule is based

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13. See *id.* at 861-63.

14. See 6 WILLIAM MILLER COLLIER, COLLIER ON BANKRUPTCY 727, ¶ 727.02[2][c] (Lawrence P. King ed. 1998) (Collier cites to only a limited number of cases other than *In re Roosevelt* and *In re MacQuown*).

15. Petition for Writ of Certiorari at 9, *In re Roosevelt*, 117 S. Ct. 1691 (1997) (No. 96-1183).

on the premise that since both sections 727(a)(2) and 548 involve situations where the debtor has transferred property with the intent to defraud his creditors, and because section 548 codifies the BFP rule, then perforce, section 727(a)(2) should imply the same. Proponents of the BFP rule also argue that by focusing on the date of recording, the courts will have conclusive evidence of the timing of a transfer, thereby enabling parties to avoid evidentiary disputes or potential frauds. Finally, this Part posits that the adoption of the BFP rule would encourage debtors to disclose their transfers, and accordingly, would prevent them from concealing a fraudulent transfer for more than a year in order to avoid the reach back provision of section 727(a)(2).

In Part V, I refute those arguments in favor of the BFP rule and propose two additional reasons to adopt the party rule. The first reason looks to the rule of construction which states that courts are to construe provisions denying discharges, including section 727(a)(2), in a way that favors the debtor and disfavors the creditor.<sup>16</sup> The party rule accomplishes this by allowing the greater number of debtors to be discharged. Secondly, the BFP rule would make a debtor, who was otherwise eligible for discharge, ineligible if the transferee, over whom he had no control, decided to record during the one-year period. This feature would thus unfairly extend the reach back provision of the statute. In contrast, the party rule prevents this result since the transfer is deemed made when it is effective between the parties, the timing of which the debtor does have control. This Part concludes that the party rule is better tailored to serve the deterrent purpose of section 727(a)(2) than is the BFP rule.

Part VI confronts the concern that the party rule will set a dangerous precedent—wreaking havoc in bankruptcy and other areas of the law by displacing the reliability and certainty of public record as proof of ownership.<sup>17</sup> It reasons first that other sections of the Bankruptcy Code, including sections 544 and 548, will continue to protect creditors from fraudulent transfers.<sup>18</sup> In addition, it is a fundamental aspect of our adjudicatory system that trial courts are both charged with and deemed capable of deter-

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16. See *Rosen v. Bezner*, 996 F.2d 1527, 1531 (3d Cir. 1993) (“[11 U.S.C. § 727(a)] is to be construed liberally in favor of the debtor.”); *Commerce Bank & Trust Co. v. Burgess* (*In re Burgess*), 955 F.2d 134, 136 (1st Cir. 1992) (same); *First Beverly Bank v. Adeeb* (*In re Adeeb*), 787 F.2d 1339, 1342 (9th Cir. 1986) (same); *Devers v. Bank of Sheridan* (*In re Devers*), 759 F.2d 751 (9th Cir. 1985) (same). See also, *Irving Fed. Sav. and Loan v. Billings*, 146 B.R. 431, 433 (Bankr. N.D. Ill. 1992) (“The court . . . is obligated to apply [§ 727] liberally to protect the debtor.”).

17. See *Petition for Writ of Certiorari* at 9, *In re Roosevelt* (No. 96-1183).

18. Bankruptcy Code, 11 U.S.C. §§ 544, 548 (1994).

mining facts by their observation of the demeanor of witnesses.<sup>19</sup> Therefore, courts need not rely on the certainty created by the date of recording as proponents of the BFP rule claim, especially when such a rule is at odds with the purpose behind section 727(a)(2). Finally, if the reliability and certainty of public records were infallible, there would be no need for title insurance or other protections against the current flaws in the recording systems.

## II. THE ROLE OF FEDERAL LAW IN THE DETERMINATION OF WHEN A TRANSFER IS MADE

The United States Constitution provides Congress with plenary power to enact uniform laws on the subject of bankruptcy.<sup>20</sup> In 1978, Congress exercised this plenary power in enacting the new Bankruptcy Code—intended as a complete revision of existing bankruptcy law.<sup>21</sup> *Pari passu*, among the issues necessarily considered by Congress was the issue of when a transfer was deemed to have occurred under section 727(a)(2). Congress failed to define the timing of a transfer under that section. Because the power of Congress is plenary in the area of bankruptcy, and federal statutes are intended to have uniform application throughout the United States, the determination of when a complained of transfer occurs under the Bankruptcy Code is perforce a question of federal law to be determined by federal courts.<sup>22</sup>

Nevertheless, there has been some conflict in authority as to whether the federal courts or state law should determine the date of the validity of the transfer under section 727(a)(2). Some courts have mistakenly looked to state law to determine when the timing of a transfer is valid against third parties without first deciding the appropriate rule—either the party or the

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19. See, e.g., *United States v. Scheffer*, 118 S. Ct. 1261, 1266 (1998) (holding that a fundamental premise of the trial system is that the jury is the lie detector, and that the determination as to the weight and credibility of witnesses belongs to them).

20. U.S. CONST. art. I, § 8, cl. 4.

21. “The bill is a complete rewriting of all of the bankruptcy law. It starts from scratch, because to attempt to make amendments to an 80-year-old law that has continually been amended during its long life would be to create an unintelligible and unworkable statute.” Respondent’s Brief in Opposition at 10 n.2, *In re Roosevelt* (No. 96-1183) (citing CONG. REC. (Jan 4, 1977), p. E20 (statement of the Hon. Don Edwards, D-Cal., before the United States House of Representatives at the introduction of House Resolution 8200, which ultimately became the Bankruptcy Reform Act, Pub. L. No. 95-598, 93 Stat. 2549 (codified at 11 U.S.C. §§ 101, *et seq.*))).

22. See *McKenzie v. Irving Trust Co.*, 323 U.S. 365, 369-70 (1945) (“What constitutes a transfer and when it is complete . . . is necessarily a federal question, since it arises under a federal statute intended to have uniform application throughout the United States.”); *Finalco, Inc. v. Roosevelt* (*In re Roosevelt*), 87 F.3d 311, 315 (9th Cir. 1996) (“The question of when a transfer is ‘made’ is a question of federal law . . .”).

BFP rule—that is required by application of federal law.<sup>23</sup> For instance, in *In re Ingersoll*, the court looked only to state law to determine that, under section 727(a)(2), a transfer is effective against third parties when it is recorded.<sup>24</sup> The court never discussed the federal law question in deciding that a transfer may be made by virtue of an exchange between a transferor and a transferee.

This type of analysis violates *McKenzie v. Irving Trust Co.* In *McKenzie*, the Supreme Court held that the Bankruptcy Code is a federal statute intended to have uniform application throughout the United States, and the timing issue of transfers is necessarily a federal question.<sup>25</sup> Courts are therefore required to analyze the timing of transfers under federal law.<sup>26</sup> The Framers were clear in their intent that the plenary power enabled Congress to enact bankruptcy laws to be uniformly applied in all states.<sup>27</sup>

### III. THE COURTS MUST DECIDE BETWEEN THE PARTY RULE AND THE BONA FIDE PURCHASER RULE

#### A. ANALYSIS OF THE STATUTORY LANGUAGE

The first step in examining a statute is to analyze the plain language of the statute.<sup>28</sup> Section 727(a)(2)(A) provides that a court shall grant a

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23. See *In re Roosevelt*, 87 F.3d at 315. See, e.g., *Ingersoll v. Kriseman (In re Ingersoll)*, 124 B.R. 116, 121 (M.D. Fla. 1991) (citing state law that a transfer is effective against third parties once it is recorded, but never consulting federal law to determine if a transfer is made when it is effective against third parties or if it is made when it is effective to the parties to the transfer); *Lister v. Gonzalez (In re Gonzalez)*, 92 B.R. 960, 961-62 (S.D. Fla. 1988) (same); *Ford v. Poston*, 773 F.2d 52 (4th Cir. 1985) (same).

24. *In re Ingersoll*, 124 B.R. at 121 (citing state law that a transfer becomes effective as to bona fide purchasers or third parties once it is recorded in the clerk's office).

25. *McKenzie*, 323 U.S. at 369-70; *In re Roosevelt*, 87 F.3d at 315. See also *Dean Witter Reynolds, Inc. v. MacQuown (In re MacQuown)*, 717 F.2d 859, 862-63 (3d Cir. 1983) (deciding between the bona fide purchaser rule and the party rule as applied to section 14(c)(4), the predecessor to section 727(a)(2), before turning to state law to determine when a transfer is valid under state law).

26. See *McKenzie*, 323 U.S. at 369-70.

27. See THE FEDERALIST NO. 42 (James Madison) ("The power of establishing uniform laws of bankruptcy . . . will prevent so many frauds where the parties or their property may lie or be removed into different States . . .").

28. See *United States v. Ron Pair Enters.*, 489 U.S. 235, 242 (1989) ("The plain meaning of legislation should be conclusive, except in the 'rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intentions of its drafters.'"). But see *Dewsnup v. Timm*, 502 U.S. 410, 420 (1992) (Scalia, J., dissenting) ("Read naturally and in accordance with other provisions of the statute, [section 506(d) of the Bankruptcy Code] automatically voids a lien to the extent the claim it secures is not an 'allowed claim' and a 'secured claim' under the Code. In holding otherwise, the Court replaces what Congress said with what it thinks Congress ought to have said—and

debtor a discharge unless the debtor, with an intent to defraud his creditors, has transferred his property within one year before the date of the filing of a petition for bankruptcy.<sup>29</sup> The statute lacks a definition of when a transfer is deemed made for the purposes of the section.<sup>30</sup>

The Code contains a broad definition of the word transfer. In section 101(54), transfer is defined as, “every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property.”<sup>31</sup> This definition allows courts and Congress great latitude to construe conflicting definitions as to what constitutes a transfer in several different sections of the Code.<sup>32</sup> Congress’ failure to provide certainty as to timing of a transfer within section 727(a)(2), coupled with such a broad definition of transfer, precludes an answer to the choice between the party rule or the BFP rule in section 727(a)(2) by simply examining the language of the statute.

#### B. THE LEGISLATIVE HISTORY

The following section briefly discusses the role that current Supreme Court jurisprudence has given to legislative history. It then echoes legislative history arguments made by the parties in *In re Roosevelt* to bolster their positions. This section concludes that reference to such arguments does not solve the main issue—whether the BFP or the party rule is the best interpretation of section 727(a)(2).

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in the process disregards, and hence impairs for future use, well-established principals of statutory construction.”).

29. Bankruptcy Code, 11 U.S.C. § 727(a)(2)(A) (1994).

30. Compare *In re Kock*, 20 B.R. 453, 454 (Bankr. D. Neb. 1982) (“No definition of when a transfer is deemed to have occurred is contained in § 727.”), with Bankruptcy Code, 11 U.S.C. § 548(d)(1) (1993) (stating that a transfer is accomplished when it is valid against a bona fide purchaser for the purposes of the fraudulent transfer provision).

31. 11 U.S.C. § 101(54) (1994).

32. See Melissa M. Cowan, *Determining Insider Status Under Bankruptcy Code Section 547(b)(4)(B): When “I Resign” May Not Be Enough to Terminate Insider Status*, 41 UCLA L. REV. 1541 (1994). Cowan states:

This broad definition results in conflicting interpretations of Section 547(b)(4)(B) . . . .

Replacing the word “transfer” with one of Section 101(54)’s definitions would limit the word to mean a “conditional . . . parting . . . with an interest in property,” which projects a meaning of a contingent interest . . . .

A contradictory interpretation results if the phrase “mode of absolute . . . disposing . . . of property” replaces the word “transfer.” The statute then adopts a sense of finality in the disposition of the debtor’s property, indicating that a transfer is the time when an agreement is fulfilled.

*Id.* at 1560-61.

Courts have long struggled with the use of legislative history in statutory construction.<sup>33</sup> Canons of statutory construction include resorting to legislative history if the statute's language is not determinative.<sup>34</sup> The current majority of Supreme Court Justices, however, rely on the notion that, "when Congress has studied, debated and enacted specific bankruptcy legislation concerning a particular issue, strict statutory construction leads to the implementation of bankruptcy policy."<sup>35</sup> According to this view, the language of a carefully drafted statute will reflect the policy and goals it attempts to regulate. The use of "strict statutory construction" has thus precluded the Court from relying on so-called legislative intent to obtain a result its members think is the proper solution to an issue.<sup>36</sup>

Justice Scalia has taken a nearly absolutist position of not using legislative intent in statutory construction. As he has stated, "[t]he *practical* threat is that, under the guise or even the self-delusion of pursuing unexpressed legislative intents, common-law judges will in fact pursue their own objectives and desires, extending their lawmaking proclivities from the common law to the statutory field."<sup>37</sup> In this regard, there would be no need to refer to specific references in the legislative history to obtain a definitive solution.

Others argue, however, that the entire objective of statutory construction is to ascertain the legislative intent, and, accordingly, there can be no justification for ignoring the legislative history.<sup>38</sup> Justice Breyer contends

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33. It is not my goal to present a comprehensive analysis of the courts' principals of statutory construction. On the other hand, since this Note is centered upon the interpretation of a statute, I believe some discussion of the basic process by which courts attempt to interpret statutes is both useful and necessary.

34. See, e.g., John Paul Stevens, *The Shakespeare Canon of Statutory Construction*, 140 U. PA. L. REV. 1373 (1992).

35. Carlos J. Cuevas, *The Rehnquist Court, Strict Statutory Construction and the Bankruptcy Code*, 42 CLEV. ST. L. REV. 435, 455 (1994).

36. See *id.* at 439. But see *Dewsnup v. Timm*, 502 U.S. 410, 419 (1992) ("[T]his Court has been reluctant to accept arguments that would interpret the [Bankruptcy] Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history.').

37. ANTONIN SCALIA, *A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW* 17-18 (1997) (*italics in original*).

38. Jack L. Landau, in an article on statutory construction writes:

In my view, once it is accepted that the objective of statutory construction is ascertainment of the legislature's intent, there can be no justification for turning a blind eye to legislative history. As Justice Frankfurter said many years ago: 'If the purpose of construction is the ascertainment of meaning, nothing that is logically relevant should be excluded.' Legislative history, in one case or another, may not be reliable, probative, or persuasive; but it always must be available for examination by the court, to be evaluated and assigned the weight it warrants.

Jack L. Landau, *Some Observations About Statutory Construction in Oregon*, 32 WILLAMETTE L. REV. 1, 46 (1996), (quoting Felix Frankfurter, *Some Reflections on the Reading of Statutes*, 47 COLUM. L.

that language alone does not “explain legislation well enough to warrant abandoning the use of legislative history.”<sup>39</sup> In many cases, the Supreme Court has used legislative history where the statutory language is ambiguous.<sup>40</sup> Some commentators have even gone so far as to say that the use of legislative history has supplanted the role that plain meaning analysis once held in statutory construction.<sup>41</sup>

Nevertheless, the Supreme Court has recently returned to a strict constructionist jurisprudence, and accordingly, is much less deferential to legislative history when interpreting a statute. In cases of ambiguity, however, the Court will still use legislative history in its analysis. Because the problem at hand cannot be resolved through an observation of unambiguous language, it is necessary to examine legislative history. Unfortunately, the legislative history of section 727 (a)(2)(A) does not clarify whether the party rule or the BFP rule should apply.

Proponents of the party rule cite section 101(54) of the Code, which defines transfer as “every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property . . . .”<sup>42</sup> From this definition, they presume that Congress intended to give the word “transfers” the widest latitude. For example, the Senate Report for the Bankruptcy Code indicated that, “[a] transfer is a disposition of an interest in property. . . . Under this definition any transfer of an interest in property is a transfer . . . .”<sup>43</sup> This does not necessarily mean, however, that a transfer of property should be considered “made” when it becomes effective between the parties of the transfer for the purposes of section 727. At least one court has proclaimed that, “[t]he time of transfer generally is equated with the perfection of the transaction.”<sup>44</sup> Thus, the term “transfer” still leaves open the issue of whether a

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REV. 527, 544 (1947) (footnote omitted)).

39. Stephen Breyer, *On the Uses of Legislative History in Interpreting Statutes*, 65 S. CAL. L. REV. 845, 867 (1992).

40. See *United States v. Vogel Fertilizer Co.*, 455 U.S. 16, 26 (1982) (“The legislative history of section 1563(a)(2) resolves any ambiguity in the statutory language and makes it plain that Treas. Reg. Section 1.1563-1(a)(3) is not a reasonable statutory interpretation.”); *Midlantic Nat’l Bank v. New Jersey Dep’t of Env’tl. Protection*, 474 U.S. 494 (1986); *Offshore Logistics, Inc. v. Tallentire*, 477 U.S. 207 (1986); William N. Eskridge, Jr., *The New Textualism*, 37 UCLA L. REV., 621, 628 (1990) (citing *Kelly v. Robinson*, 479 U.S. 36 (1986)). See also *Dewsnup*, 502 U.S. at 419-20 (using legislative history to construe the Bankruptcy Code when the language was not very ambiguous).

41. See Robert J. Araujo, *The Use of Legislative History in Statutory Interpretation: A Look at Regents v. Bakke*, 16 SETON HALL LEGIS. J. 57, 127 (1992).

42. Bankruptcy Code, 11 U.S.C. § 101(54) (1994).

43. S. REP. NO. 95-989, at 27 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5813; H.R. REP. NO. 95-595, at 314 (1978), reprinted in 1978 U.S.C.C.A.N. 5963, 6271.

44. *First Eastern Bank v. Jacobs (In re Jacobs)*, 60 B.R. 811, 815 (Bankr. M.D. Pa. 1985) (cita-

transaction is perfected when it is effective between the parties, or when no bona fide purchaser from the debtor-transferor and no creditor could thereafter have acquired a right superior to that of the transferee.<sup>45</sup>

Proponents of the party rule further argue that the elimination of the Bankruptcy Act and its replacement by the Bankruptcy Reform Act in 1978 was intended by Congress to be a comprehensive re-examination and re-enactment of the statutes relating to bankruptcy. At the time of its enactment, Congress presumptively knew about the absence of a recording provision of former section 14(c)(4)<sup>46</sup> (the predecessor to section 727(a)(2)) and its retention in former 67(d)(5)<sup>47</sup> (the predecessor to section 548(d)) of the Bankruptcy Act, as well as the district court opinions of *In re Plank* and *In re McKane* suggesting a split of authority in the interpretation of section 14(c)(4).<sup>48</sup> Moreover, section 548 clearly states, “[f]or the purposes of this section” prior to its pronouncement of its recording provision.<sup>49</sup> Significantly, courts have on many occasions noted that the difference of specificity in one section implies a different meaning if the degree of specificity is not used in another section.<sup>50</sup> They thus look to the well-known Sherlock Holmes story of the dog in the night who did not bark while a murder was being committed,<sup>51</sup> analogizing the story to the rule of

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tions omitted).

45. Cf. 4 COLLIER, *supra* note 14, ¶ 727.02[2], at 727-15. (arguing that for the purposes of section 727, the bona fide purchaser rule is the proper rule because this is the appropriate time to consider a transaction perfected).

46. See Amendments to the Bankruptcy Act of 1898, ch. 487, § 4, 32 Stat. at 798 (designating as a new ground for denying discharge the transfer of property with the intent to hinder, delay, or defraud without defining when a transfer was deemed “made” in section 14(c)(4)) cited in *Finalco, Inc. v. Roosevelt* (*In re Roosevelt*), 87 F.3d 311, 316 (9th Cir. 1996).

47. See Bankruptcy Act of 1938, Amendments, ch. 575, § 67(d)(5), 52 Stat. 840, 878 (1938) (deeming a transfer “made” at the time it was recorded for the purposes of fraudulent transfers) cited in *In re Roosevelt*, 87 F.3d at 316 n.8.

48. *In re McKane* used the bona fide purchaser analysis to state that a transfer was made for the purposes of section 14(c)(4) of the Bankruptcy Act when it was recorded. See *In re McKane*, 155 F. 674 (E.D.N.Y. 1907). *In re Plank*, however, held that the date of the deed (perfection between the parties) and not recordation controlled. See *In re Plank*, 289 F. 900 (D. Mont. 1923).

49. Bankruptcy Code, 11 U.S.C. § 548(d)(1) (1994).

50. See, e.g., *Longview Fibre Co. v. Rasmussen*, 980 F.2d 1307 (9th Cir. 1992). The court stated:

[T]he . . . specificity of section [1369(b)] in identifying what actions of EPA under the FWPCA would be reviewable in courts of appeals suggests that not all such actions are so reviewable. If Congress had so intended, it could have simply provided that all EPA action under the statute would be subject to review in courts of appeals, rather than specifying particular actions and leaving out others.

*Id.* at 1313 (quoting *Bethlehem Steel Corp. v. BPA*, 538 F.2d 513, 517 (2d Cir. 1976)).

51. See 2 SIR ARTHUR CONAN DOYLE, *Silver Blaze*, in THE ANNOTATED SHERLOCK HOLMES, 261, 277 (William S. Baring-Gould ed., 1967) (“‘You consider that to be important?’ he asked. ‘Exceedingly so.’ ‘Is there any other point to which you would wish to draw my attention?’ . . . ‘To the curious incident of the dog in the night time’ . . . ‘The dog did nothing in the night time. That was the

statutory construction that, “it is generally presumed that Congress acts intentionally and purposely when it includes particular language in one section of a statute but omits it in another.”<sup>52</sup> This maxim of statutory interpretation fits in with the “whole act rule” which interprets each section of a statute in the context of the whole enactment, and is:

the most realistic in view of the fact that a legislature passes judgment upon the act as an entity, not giving one portion of the act any greater authority than another. Thus any attempt to segregate any portion or to exclude any other portion from consideration is almost certain to distort the legislative intent.<sup>53</sup>

The Supreme Court did use such an analysis in *BFP v. Resolution Trust Corp.* There, the issue was whether “fair market value” was the benchmark against which reasonable equivalent value should be measured in section 548 of the Code.<sup>54</sup> In an opinion by Justice Scalia, the Court held that such an interpretation is inconsistent with the text of the Code. The logic, which can be analogized to the current discussion, progressed as follows: The term “fair market value” does not appear in the text of section 548,<sup>55</sup> just as a definition of when a transfer is deemed to have been made does not appear in the text of section 727(a)(2). In contrast, section 522 specifically provides that the term “value” means “fair market value” (just as section 548 deems a transfer to have been made for the purposes of that section when it is recorded).<sup>56</sup> The Court stated that section 548 seemingly goes out of its way to avoid the term fair market value<sup>57</sup> (just as section 727(a)(2) avoids using recording provision to determine when a transfer occurs). Using the canon of statutory construction above, the Court held that the language of section 548 precludes the use of fair market value as the benchmark against which reasonable equivalent value should be meas-

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curious incident,’ remarked Sherlock Holmes.”).

52. *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 537 (1994). *See also* *Chicago v. Environmental Defense Fund*, 511 U.S. 328, 338 (1994).

53. WILLIAM N. ESKRIDGE JR., PHILIP P. FRICKEY, *CASES AND MATERIALS ON LEGISLATION STATUTES AND THE CREATION OF PUBLIC POLICY* 643 (2d ed. 1995) (quoting SUTHERLAND, *STATUTES AND STATUTORY CONSTRUCTION*, § 47.02 at 139 (Norman Singer ed., 5th ed.)).

54. *See BFP*, 511 U.S. at 536-37 (a chapter 11 debtor brought a fraudulent transfer proceeding to avoid a mortgage foreclosure sale on the theory that the price received at the mortgage foreclosure sale was less than the “reasonably equivalent value” of the property). The Supreme Court, in an opinion written by Justice Scalia, held that the price received at the mortgage foreclosure sale conclusively established the “reasonably equivalent value” of the mortgage property, as long as the requirements of the state’s foreclosure law were met. *See id.*

55. *See id.* at 537.

56. *See id.* (citing 11 U.S.C. § 522(a)(2)).

57. *See BFP*, 511 U.S. at 537.

ured.<sup>58</sup> By analogy, the language of section 727(a)(2) thus suggests that a transfer cannot be deemed to have been made at the time it is recorded. This analysis on its face appears to be a strong argument. However, reference to this type of analogy does not resolve the issue definitively given that reliance on a canon of statutory construction can lead to alternative interpretations.<sup>59</sup>

In contrast, advocates of the BFP rule point to legislative history which says that, “any transfer of an interest in property is a transfer, including a transfer of possession, custody or control even if there is no transfer of title, because possession, custody, and control constitute interests in property.”<sup>60</sup> They further argue that recording title is definitive evidence of control.<sup>61</sup> This, however, is too absolute of a claim. Indeed, many bankruptcy cases exist wherein a person transferred record title of his assets and yet maintained constructive control over those assets.<sup>62</sup> Proponents of the BFP rule thus cannot contend that under these circumstances, Congress intended the transfer to have occurred at the time of recordation—such analysis could subvert the Bankruptcy Code altogether by allowing one to transfer property to a “straw man” in order to conceal assets.

Of course, there is a risk that, without a recordation requirement, a person will transfer assets while still maintaining virtual total control over those assets. In addition, notice to third parties could be just as important

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58. *See id.*

59. *See, e.g.,* Karl N. Llewellyn, *Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes are to be Construed*, 3 VAND. L. REV. 395, 401-06 (1950).

60. Petition for Writ of Certiorari at 7, *Finalco, Inc. v. Roosevelt*, 117 S. Ct. 1691 (1997) (No. 96-1183) (quoting *In re Lemley Estate Bus. Trust*, 65 B.R. 185, 189 (Bankr. N.D. Tex. 1986)).

61. *See id.* *But see* Douglas M. Garrou, Note, *The Potentially Responsible Trustee: Probable Target for CERCLA Liability*, 77 VA. L. REV. 113, 124 (1991) (“Possession of title, or the lack thereof, is not necessarily dispositive with respect to the questions of ownership or control.”).

62. *See United States v. One 1988 Prevost Liberty Motor Home*, 952 F. Supp. 1180 (S.D. Tex. 1996). The court stated:

In 1986 and 1987, aware that creditors could reach assets held in his name personally, [the debtor] knowingly and fraudulently transferred record title to his assets into LMC, to Banner and B & B, and to Ross in order to conceal his continuing interest in those assets from his creditors. As described in detail above, he retained virtually total control and dominion over these assets thereafter. The concealment of his beneficial interest in LMC and its subsidiaries’ assets was done in contemplation of a bankruptcy case under Title 11 of the United States Code.

*See id.* at 1207. *See, e.g.,* *FDIC v. Sullivan (In re Sullivan)*, 204 B.R. 919 (Bankr. N.D. Tex. 1997) (holding that the continuing concealment doctrine may be applied to extend the reach of the statutory exception to discharge to fraudulent transfers that occurred more than one year before a debtor’s bankruptcy filing, where the party seeking to deny the debtor’s discharge can prove that the debtor retained control over or held an equitable interest in the property even after the transfer); *Mazer v. Jones (In re Jones)*, 184 B.R. 377 (Bankr. D. N.M. 1995); *B.K. Med. Sys., Inc. Pension Plan v. Roberts (In re Roberts)*, 81 B.R. 354 (Bankr. W.D. Pa. 1987).

as control in determining when a transfer was made. These arguments, however, are negated by the fact that Congress left a recording element out of section 727(a)(2) when it wrote the Bankruptcy Code in 1978. If these concerns were paramount, Congress would not have made this omission.<sup>63</sup> Also, the risk that a person will fraudulently conceal his property in the manner described above is provided for by the concealment clause of section 727(a)(2).<sup>64</sup> Therefore, one cannot conclude that Congress intended the BFP rule to be determinative from this citation to legislative history.

In sum, neither the plain language nor the legislative history conclusively determine the proper rule. Although Congress specified when a transfer is deemed made for the purposes of other sections of the Code, it did not do so for the section dealing with the denial of discharge.<sup>65</sup> As a result, Congress presumably left it to the courts to determine when a transfer is made under section 727(a)(2). If Congress has not defined a term in a way that is helpful to construe a particular statute, and the legislative history does not help to determine the proper interpretation of the term, a court's best approach is to "interpret the words of these statutes in light of the purposes Congress sought to serve."<sup>66</sup> With this concept in mind, the courts have responded with two different timing rules: the bona fide purchaser rule and the party rule. The following will discuss the arguments for each.

#### IV. ARGUMENTS FOR THE BONA FIDE PURCHASER RULE

##### A. SECTION 548 DEFINES THE TIME OF TRANSFER AS THE TIME OF RECORDATION; SECTION 727(A)(2) SHOULD DO THE SAME

For the purposes of this section, a transfer is made when such transfer is so perfected that a bona fide purchaser from the debtor against applicable law permits such transfer to be perfected cannot acquire an interest in the property transferred that is superior to the interest in such property of the transferee . . . .<sup>67</sup>

Proponents of the BFP rule contend that, although Congress did not specifically write a similar provision for 727(a)(2), there is no reason it

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63. See *supra* notes 45-56 and accompanying text.

64. See discussion *infra* Part V.C.

65. See *Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 87 F.3d 311, 316 n.8 (9th Cir. 1996); *supra* note 6 and accompanying text.

66. *Chapman v. Houston Welfare Rights Org.*, 441 U.S. 600, 608 (1979).

67. Bankruptcy Code, 11 U.S.C. § 548(d)(1) (1994).

should not be accepted by analogy.<sup>68</sup> This argument rests on the premise that when the recording date is used, there is a smaller chance of dispute because that date is a matter of public record. Additionally, using the recording date serves the policy of protecting creditors by giving them notice.<sup>69</sup> In contrast, when the date of transfer is controlling, the issue ultimately turns on the credibility of the witnesses.

Thus, advocates of this interpretation argue that the reasoning behind looking at the recording date for section 548 is the same as doing so for section 727(a)(2).<sup>70</sup> After all, both sections of the Code are geared toward preventing the use of fraudulent transfers as an effective tool for debtors to avoid their obligations. Consequently, many similarities have developed within the courts in the application of the two sections. For example, at least one court has applied the doctrine of collateral estoppel to preclude a debtor from relitigating the issue of fraudulent intent under section 727(a)(2)(A) after finding that the debtor transferred property with the intent to hinder, delay or defraud his creditors in violation of section 548(a)(1).<sup>71</sup> Additionally, the burdens of proof for sections 548(a)(1) and 727(a)(2)(A) are the same. The same “convincing evidence” standard applies to lawsuits brought by a bankruptcy trustee to recover a fraudulent conveyance, and to lawsuits initiated by a creditor to deny a debtor’s discharge on the ground that he engaged in a fraudulent conveyance.<sup>72</sup> Courts have looked to section 548 in other contexts for guidance in interpreting section 727. For example, in *Reynolds v. Coggin*, the debtor argued that the bankruptcy court mistakenly found that a transfer to his son violated section 727(a)(2)(A) because the transfer was supported by “valuable consideration.”<sup>73</sup> The court then referred to section 548, which states that a

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68. As one court wrote:

[T]he old Act and the present Code define when a transfer occurs for the purpose of avoiding fraudulent transfers made within a year before bankruptcy: “For the purposes of this section, a transfer is made when such transfer becomes so far perfected that a bona fide purchaser from the debtor against whom such transfer could have become perfected cannot acquire an interest in the property transferred that is superior to the interest in such property of the transferee . . . .”

11 U.S.C. § 548(d)(1).

Although this provision is not explicitly made applicable to section 727(a)(2), there is no good reason why it should not be adopted by analogy.

*Young Contracting Co. v. Roy (In re Roy)*, 42 B.R. 102, 104 (Bankr. S.D. Fla. 1984).

69. Perhaps it is for this very reason that section 548 exists. Namely, section 548 serves to protect creditors, while section 727 serves to punish debtors who commit wrongful acts. This may be a reason for not requiring the same degree of certainty in section 727.

70. See *In re Roy*, 42 B.R. at 104.

71. See *Cohen v. Bucci*, 103 B.R. 927, 928 (Bankr. N.D. Ill. 1989).

72. See *Cohen v. Bucci (In re Bucci)*, 97 B.R. 954, 957 (Bankr. N.D. Ill. 1989).

73. *Reynolds v. Coggin*, No. CV-90-HM-1476-S, 1993 WL 738391, at \*7 (N.D. Ala. Sept. 30, 1993).

transfer may be set aside if it was for “less than a reasonably equivalent value,” and found that the bankruptcy court’s determination that the debtor had intended to defraud his creditors should stand.<sup>74</sup>

Another similarity between sections 727 and 548 exists in the use of the eleven “badges of fraud.” Courts have used the eleven “badges of fraud” since the time of Queen Elizabeth I to consider whether a debtor had the intent to hinder, delay, or defraud a creditor by transferring property, and they do so today in the context of both sections 727 and 548.<sup>75</sup> Courts have also concluded that, for the purposes of both sections, to sustain a finding of fraud, a plaintiff must prove actual intent<sup>76</sup>—constructive intent is insufficient.<sup>77</sup> As a result of these similarities, proponents of the BFP rule claim that the two statutes can be further analogized so that the time of transfer is determined when the transfer is recorded.

#### B. THE BONA FIDE PURCHASER RULE IS MORE PRACTICAL

By deeming a transfer under section 727(a)(2) made when it is recorded, courts avoid evidentiary disputes. Recordation becomes verifiable evidence of when deeds were executed or when agreements were signed, thereby avoiding potential frauds, such as the back dating of documents, by the debtor-transferor. If creditors are not protected from their debtors’ prior unrecorded transfers, debtors could thwart the legitimate expectations of those creditors.<sup>78</sup> One scholar has noted that, “[a]bsent a rule subordinating prior unrecorded transfers, [] fraudulent back dating scheme[s] would be particularly difficult to prevent.”<sup>79</sup> Even if the failure to record the transfer is due to some reason other than fraud, the creditor’s injury could still be substantial, as they may be unable to collect all of the obligations originally owed to them. Thus, commentators argue that courts

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74. *See id.*

75. *See* 718 Arch St. Assoc. v. Blatstein (*In re Main, Inc.*), 213 B.R. 67, 79 (Bankr. E.D. Pa. 1997) (“[Courts have considered] the eleven ‘badges of fraud’ . . . in determining whether a debtor possessed the requisite intent to hinder, delay, or defraud a creditor by transferring the property in several scenarios under the Bankruptcy Code, notably in interpreting [section] 548(a)(1).”) (citations omitted).

76. *See* Loeber v. Loeber (*In re Loeber*), 12 B.R. 669, 675 (Bankr. D. N.J. 1981) (“In order to sustain a finding of fraud under section 727(a)(2) and section 548, it is essential to prove actual intent to defraud; constructive intent is insufficient.”).

77. *See id.*

78. *See* Dan S. Schechter, *Judicial Lien Creditors Versus Prior Unrecorded Transferees of Real Property: Rethinking the Goals of the Recording System and Their Consequences*, 62 S. CAL. L. REV. 105, 107 (1988) (discussing a recording requirement prior to the creation of a judicial lien). On the other hand, the four-year reach back provision in the case of fraudulent transfers does offer some protection.

79. *Id.* at 140.

should not force creditors to bear the costs of the transferee's failure to comply with the recording statute, especially where the costs to the creditor outweigh the costs of the guarantee of preventing the problem by ensuring a fixed date for when a transfer is made.<sup>80</sup>

While section 727(a)(2) requires a transfer to be made, a transfer of real property is usually perfected when it is recorded.<sup>81</sup> This is because recording a deed results in either actual notice or inquiry notice being held against a bona fide purchaser. In some states, the perfection of a deed of trust occurs when the document is recorded in the office of the County Recorder.<sup>82</sup> Indeed, recording is held to be so valuable for evidentiary purposes in some jurisdictions that the first party to record prevails over prior unrecorded transferees as long as they give valuable consideration and have no knowledge of any prior conveyance.<sup>83</sup> Thus, "an additional advantage to using the recording date, as opposed to the inter se transfer date, is that it eliminates most disputes about the effective date."<sup>84</sup>

#### C. THE BONA FIDE PURCHASER RULE WOULD ENCOURAGE DEBTORS TO DISCLOSE THEIR TRANSFERS

Knowing that their transfers will not be made for the purposes of section 727(a)(2) unless they are recorded will encourage debtors to disclose their transfers. This will prevent a debtor from concealing a fraudulent transfer for more than a year to avoid the statute's one-year reach back period.<sup>85</sup> This assertion surrounds situations like those presented in *In re Kauffman*, where the bankruptcy court denied a debtor the discharge of his debts because there was sufficient evidence that the debtor's transfer of his house to his wife constituted a continuing concealment.<sup>86</sup> In *In re Kauffman*, the court found that the debtor retained a beneficial interest in the

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80. *See id.* at 107.

81. *See supra* notes 41-44 and accompanying text.

82. *See, e.g.*, CAL. CIV. CODE § 1213 (Supp. 1998); *Miller v. Schuman (In re Schuman)*, 81 B.R. 583, 587 (B.A.P. 9th Cir. 1987) ("In California, perfection of a deed of trust occurs upon the recording of the document with the county recorder.").

83. For example, the Idaho Code states: "Every conveyance of real property other than a lease for a term not exceeding one (1) year, is void as against any subsequent purchaser or mortgagee of the same property, or any part thereof, in good faith and for a valuable consideration, whose conveyance is first duly recorded." IDAHO CODE § 55-812 (1994).

84. *Dean Witter Reynolds, Inc. v. MacQuown (In re MacQuown)*, 717 F.2d 859, 863 (3d Cir. 1983).

85. This argument may not be as strong as it appears on its face. There may be no encouragement to debtors to disclose their transfers since the reach back provision for fraudulent transfers is four years in most states.

86. *Friedell v. Kauffman (In re Kauffman)*, 675 F.2d 127 (7th Cir. 1981).

property after he had conveyed the house more than a year before the bankruptcy filing.<sup>87</sup>

Finalco made a similar argument in the case *In re Roosevelt*.<sup>88</sup> At trial, the court found that the mortgage and maintenance expenses of the house were paid from the debtor's community property interest until August 1991, and that the house was treated by the debtor and his wife as community property.<sup>89</sup> This occurred despite the fact that in June 1989, the two executed the "marriage settlement agreement," and in April 1990, a quitclaim deed was executed by the debtor in his wife's favor. These facts, plus the fact that the debtor lived in the house right up to the time he filed for bankruptcy and borrowed<sup>90</sup> against the house in December 1989, gave grounds for Finalco to argue that "despite the conveyance via the Marital Agreement, the Debtor retained an interest in the property both factually, and as a matter of law."<sup>91</sup> Because Finalco did not raise this issue at trial, its attempt to raise it de novo was rebuffed. However, proponents of the BFP rule argue that, "[u]nder [the party rule], it must be recognized that some failures to record transfers are intentional and are in the nature of continuing concealments [so] the date of recordation may be used to determine whether the transfer occurred during the one-year period."<sup>92</sup>

In sum, proponents of the BFP rule argue that the recording requirement of section 548, which deems a transfer to be made when it is recorded, should be applied to section 727 since there are many other similarities in the judicial interpretations of the two sections. They also claim that deeming a transfer made under section 727(a)(2) when it is recorded

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87. *Id.* (finding that the evidence was sufficient to sustain objecting creditor's burden of proving that bankrupt's transfer of his house to his wife constituted a continuing concealment, that bankrupt retained a beneficial interest in the property, and that there was fraudulent intent on the part of bankrupt).

88. *Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 87 F.3d 311, 318 (9th Cir. 1996) ("Finalco opines that the BFP rule would encourage debtors to disclose their transfers, thereby preventing a dishonest debtor from concealing a fraudulent transfer for more than a year in order to avoid § 727(a)(2)'s one-year reach back. Finalco's concern is misplaced. Section 727(a)(2) already denies discharge to a debtor who conceals his property with the intent to hinder, delay, or defraud.").

89. *See id.* at 318. Despite the fact that the house was treated as community property, the court held that Judy had a joint tenancy. Otherwise, if the house had been community property, it would have been an asset of the bankruptcy estate. *See* Appellant's Brief at 2-3, *Finalco, Inc.*, 87 F.3d 311 (No. 95-55160).

90. This is an assertion made by Finalco. *See* Appellant's Brief at 16-17, *In re Roosevelt* (No. 95-55160). Dr. Roosevelt stated that he was required to sign the loan documents by the lender. *See* Interview with Donald E. Rinaldi, Attorney at Law, in Covina, Cal. (July 28, 1998).

91. Appellant's Brief at 13, *In re Roosevelt* (No. 95-55160) (Finalco did not raise the issue of a continuing concealment at trial, and, accordingly, it was not allowed to raise this issue de novo on appeal).

92. 4 COLLIER, *supra* note 14, ¶ 727.02[2][c] at 727-15.

will avoid evidentiary disputes during trials. Finally, these proponents contend that debtors will be encouraged to disclose their transfers if transfers are not deemed made until they are recorded, thereby decreasing the incentive for a debtor to conceal their transfers in an effort to avoid their debt obligations.

## V. REASONS FOR THE ADOPTION OF THE PARTY RULE

### A. SECTION 727(A)(2) FOCUSES ON THE DEBTOR'S WRONGDOING

Drawing an analogy between sections 727(a)(2) and 548 on the basis that they both involve situations of a fraudulent transfer is not a proper analysis because the two sections serve different purposes that can only be accomplished by employing two different timing rules.<sup>93</sup> One scholar has pointed out that, "where a court uses the technique of reasoning by analogy, it is methodologically mistaken not to consider whether the principles involved would be offended by drawing such an analogy."<sup>94</sup> By not considering the purpose of a provision when drawing an analogy, a court's analysis could lead to misinterpretation of a statute.

Section 727(a)(2) focuses on a debtor's wrongdoing in connection with a bankruptcy case.<sup>95</sup> As the Congressional report explained:

The . . . three grounds for denial of discharge [that] center on the debtor's wrongdoing . . . are derived from Bankruptcy Act § 14c. If the debtor, with intent to hinder, delay, or defraud his creditors or an officer of the estate, has transferred, removed, destroyed, mutilated, or concealed . . . property of the debtor within the year preceding the case . . . then the debtor is denied discharge.<sup>96</sup>

The main purpose of this provision is therefore to avoid rewarding a debtor for fraudulent acts by imposing the severe penalty of the denial of discharge when such acts occur.

Section 548, on the other hand, deals with the bankruptcy trustee's power to avoid transactions and bring them back into the estate of the

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93. Terms may have different meanings depending on the purpose. See *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 537 (1994) (holding that fair market value was not the benchmark against which reasonable equivalent value was to be measured because such an interpretation was not consistent with the text of section 548).

94. Howard Foss, *Interpreting the Uniform Commercial Code: Methodologies Used, Misused and Unused*, 20 GOLDEN GATE U. L. REV. 29, 87 (1990).

95. See S. REP. NO. 95-598, at 98 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5884.

96. H.R. REP. NO. 95-598, at 384, reprinted in 1978 U.S.C.C.A.N. 5963, 6340. Section 14(c) is the predecessor to section 727 in the old Bankruptcy Act.

debtor for the benefit of creditors. This power is not limited to cases where the debtor acted with a fraudulent intent.<sup>97</sup> There are five ways that a trustee may attack transfers under section 548, four of which have little to do with an intent to defraud creditors. These four include transfers made by a debtor for less than the reasonably equivalent value, transfers made by a business debtor for less than reasonably equivalent value at a time when the debtor was left with unreasonably small capital for carrying on its business, transfers made by a debtor for less than reasonably equivalent value at a time when the debtor believed that he would incur debts beyond his ability to pay, and transfers made by a debtor to a general partner of the debtor if, on the date of the transfer, the debtor was insolvent.<sup>98</sup> In fact, section 548 permits a trustee to avoid involuntary transfers made within one year before the bankruptcy as long as they are constructively fraudulent against creditors. In these circumstances, it surely cannot be said that the provision is focusing on the wrongdoing of the debtor. Section 548 seeks to aid creditors rather than punish debtors.

Another indication of section 548's focus on creditors' rights as opposed to debtor's wrongdoing is the fact that the trustee may avoid a fraudulent conveyance where the transferee takes in good faith and for fair consideration.<sup>99</sup> The purchaser in these cases retains only a lien for the original purchase price. Under these circumstances, creditors are thus protected more than the good faith transferee.

Denial of discharge is a very harsh result which may frustrate the ordinary fresh start policy of the Code. As one scholar has noted:

Even if a socially disfavored activity is so closely linked with bankruptcy or creditor collection efforts that some restriction of the debtor's financial fresh-start is justified, a complete denial of discharge is not necessarily an appropriate response. In determining the proper penalty, one

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97. See Bankruptcy Code, 11 U.S.C. § 548(a)(2)(A) (1994) (allowing avoidance of transfers because they were made for less than "reasonably equivalent value").

98. See Mary Letter Swick, *The Power of Avoidance: A Bankruptcy Perspective on the Developing Law of Fraudulent Transfers in Nebraska*, 25 CREIGHTON L. REV. 577, 592 (1992).

99. See Thomas E. Plank, *The Constitutional Limits of Bankruptcy*, 63 TENN. L. REV. 487, (1996). Plank writes:

Under both the Uniform Fraudulent Transfer Act and the Uniform Fraudulent Conveyance Act, creditors cannot avoid a transfer of property made with the actual intent to hinder, delay, or defraud creditors if the transferee took the property in good faith and for fair consideration or reasonably equivalent value. Under section 548 of the Code, however, the trustee may avoid such a fraudulent conveyance, and the purchaser retains only a lien for the original purchase price.

*Id.* at 579.

must weigh the benefits of the fresh-start policy against the effectiveness of using denial of discharge as a lever to enforce behavioral norms.<sup>100</sup>

Without the benefit of a fresh start, debtors will put off filing a bankruptcy petition which may lead to a draining of assets, leaving both the debtor and creditor worse off. “The two major purposes of the Code are to provide debtors with a ‘fresh start’ and to provide for a fair and equitable distribution of assets to creditors.”<sup>101</sup> Neither policy would be promoted if discharges were liberally denied.

Thomas Jackson accordingly argues that in determining the proper penalty, the benefits of the fresh-start policy must be weighed against the effectiveness of using denial of discharge as a means to induce behavioral norms.<sup>102</sup> Preventing debtors from attempting to transfer their assets in order to defraud creditors will be better served by the party rule, since that rule focuses on the time of the debtors fraudulent act, whereas the BFP rule focuses on the actions of a transferee. To effectively enforce a particular behavior, the person committing the act should be the focus of inquiry, lest the efficacy of the punishment will be lost. In addition, the party rule allows more debtors to be granted a discharge. Since recording always occurs simultaneous to or after the transfer, more discharges will be saved from the one-year reach back provision of the statute. Consequently, the party rule better serves the fresh start policy, and is more effective in inducing the behavioral norm of not committing fraudulent transfers. Section 548, on the other hand, focuses on another bankruptcy policy: the equitable distribution to creditors. The concerns of that section, as stated below, are better served by requiring a recordation before a transfer is deemed to have been made.

There is no doubt that a denial of discharge, even if done to punish the debtor, has the effect of protecting the creditors.<sup>103</sup> Moreover, some of the trustee’s avoidance powers laid out in section 548 may come about as a result of the debtor’s wrongdoing. Serving the goals of section 727 therefore often advances the goals of section 548, and vice versa.<sup>104</sup> However, the courts should focus on the main purpose of the two statutes, not their congruent effects, otherwise Congress would not have perceived a need for both sections.

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100. Thomas H. Jackson, *The Fresh Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393, 1442 (1985).

101. *In re Morrissey*, 37 B.R. 571, 573 (Bankr. E.D. Va. 1984).

102. *See supra* note 88 and accompanying text.

103. *See Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 87 F.3d 311, 317 n.12 (9th Cir. 1996).

104. *See id.*

Recording statutes are intended to create certainty in business transactions. "When creditors extend credit to [purchasers of property,] they must be able to rely on the accuracy of the filing and recording systems . . ." <sup>105</sup> Requiring public notice of a security interest may place burdens on people and could be a trap for the unwary—race jurisdiction for example. However, "the need to protect creditors from what otherwise was a misleading situation that could prejudice them was considered the paramount objective [of recording rules]." <sup>106</sup> Indeed, recording acts often state this purpose in the words of the Act itself. For instance, the Florida code states that "[n]o conveyance . . . of real property . . . shall be good . . . against *creditors* or subsequent purchasers for a valuable consideration and without notice, unless the same be recorded according to law . . ." <sup>107</sup>

Because recording statutes have the main purpose of protecting creditors, it is logical that section 548, which has a similar objective, should use the date of recording to accomplish its purpose. In contrast, section 727(a)(2):

[P]remises denial of discharge on certain conduct of the debtor in relation to his assets and creditors if done with "intent to hinder, delay or defraud." Thus, one of the principal points of focus in litigation involving that sub-section involves certain conduct coupled with an appropriate guilty state of mind. This suggests to me that the "transfer" which is contemplated by § 727(a)(2) focuses on the time of the debtor's activity and not when the activity is somehow fully-insulated from the claims of other creditors. <sup>108</sup>

Thus, the analogy between sections 548 and 727(a)(2) is misplaced, and a court using this approach will misinterpret the latter. The party rule is thus better suited to animate the purpose of § 727(a)(2) than the bona fide purchaser rule. <sup>109</sup>

105. Carlos J. Cuevas, *Bankruptcy Code Section 544(a) and Constructive Trusts: The Trustee's Strong Arm Powers Should Prevail*, 21 SETON HALL L. REV. 678, 753 (1991).

106. Morris G. Shanker, *The Trashing of Article 6: Isn't There a Better Alternative?*, 41 ALA. L. REV. 653, 659-60 (1990).

107. FLA. STAT. ANN. § 695.01(1) (West 1998) (emphasis added).

108. First Nat'l Bank and Trust Co. v. Shreves (*In re Kock*), 20 B.R. 453, 454 (Bankr. D. Neb. 1982).

109. Finalco, Inc. v. Roosevelt (*In re Roosevelt*), 87 F.3d 311, 317 (9th Cir. 1996).

B. IT IS THE FUNCTION OF LOWER COURTS TO DETERMINE FACTS AND  
ASSESS THE CREDIBILITY OF WITNESSES

Using the recording date to determine when a transfer is made under section 727 is undoubtedly more practical. It does eliminate disputes as to when deeds were executed or agreements signed.<sup>110</sup> However, concluding that one rule is the easier rule to implement does not compel the decision that it is the correct rule. Lower courts exist for fact-finding purposes and to assess the credibility of witnesses.<sup>111</sup> The Federal Rules of Civil Procedure provide that, “[f]indings of fact . . . shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of witnesses.”<sup>112</sup>

The trier of fact who hears the actual testimony of a case is competent to observe the appearance of witnesses and is in the best position to assess their credibility. At least one court has held that expert opinions on the veracity of a witness are suspect because they supplant the main function of the trier of fact to assess the credibility of each witness.<sup>113</sup> The immense deference the judicial system gives to trial courts should not be discredited because a rule such as the bona fide purchaser rule is easier to apply, especially when such a rule will not advance the main purpose of section 727(a)(2). Thus, as the Ninth Circuit concluded, “relieving the lower courts of a function which they are already competent to perform is not a reason unto itself to adopt the BFP rule.”<sup>114</sup>

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110. See *supra* Part IV.B.

111. In *United States v. Herrero*, the Seventh Circuit held: [W]e defer to the [trier of fact’s] determination of witnesses’ credibility. As we noted in *United States v. Ramirez*, 796 F.2d 212, 214 (7th Cir. 1986): “An appellate court will not weigh the evidence or assess the credibility of the witnesses.” Similarly, we have stated: “It is well settled law that a court of appeals does not stand in judgment of the credibility of witnesses. Rather that question is left to the sound discretion of the trier of fact.” Finally, “the credibility of witnesses is peculiarly within the province of the [trier of fact] and our review of credibility is prohibited absent extraordinary circumstances.”

*United States v. Herrero*, 893 F.2d 1512, 1533 (7th Cir. 1990) (alterations in original) (citations omitted) (quoting *United States v. Vega*, 860 F.2d 779, 794 (7th Cir. 1988)).

112. FED. R. CIV. P. 52.

113. See *United States v. Whitted*, 11 F.3d 782, 785-86 (8th Cir. 1993) (“A doctor also cannot pass judgment on the alleged victim’s truthfulness in the guise of a medical opinion, because it is the jury’s function to decide credibility.”).

114. *In re Roosevelt*, 87 F.3d at 318.

C. THE CONCERN ABOUT ENCOURAGING DEBTORS TO DISCLOSE THEIR TRANSFERS IS MISPLACED

Proponents of the BFP rule contend that it will encourage debtors to disclose their transfers, and will also prevent debtors from transferring property on the surface, while secretly maintaining an interest therein.<sup>115</sup> However, this argument is misplaced because another provision in section 727(a)(2) denies a discharge to a debtor who conceals his property with an intent to hinder, delay, or defraud his creditors.<sup>116</sup> In *In re Sanders*, for instance, a debtor donated valuable property to her children's trust for no consideration, but retained possession of the property.<sup>117</sup> The court found that the debtor had gratuitously transferred said property more than a year prior to the bankruptcy, but held that it was concealed with intent to hinder, delay, and defraud creditors.<sup>118</sup> Accordingly, the court denied discharge because the transferors retained a beneficial interest in the property that continued into the year prior to petitioning for bankruptcy.<sup>119</sup> The transfer of title, while retaining the benefits of ownership, may constitute "concealment" for purposes of determining whether a discharge should be granted.<sup>120</sup> In *In re Sanders*, the fact that the trust documents were recorded did not preclude the court from finding that the debtor had concealed her assets by making gratuitous transfers to her children's trusts, and thus that her discharge was denied.<sup>121</sup>

Finally, since fraud is punishable under section 727(a)(2), adoption of the BFP rule will not encourage recordation of potentially fraudulent transfers. Indeed, it is human nature that those who commit fraud do so in the belief that they will not be discovered. For these people then, whether or not a recording element is read into section 727(a)(2) makes no difference as there is still no incentive to record. These transfers are made with the belief that the fraudulent intent will not be detected. If anything, the BFP rule will make the incentive not to get caught much stronger, and will lead

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115. See *supra* Part IV.C. Again, it is a strain to claim that the timing of the transfer has any impact on the veracity of the parties involved.

116. See Bankruptcy Code, 11 U.S.C. § 727(a)(2) (1994).

117. *March v. Sanders (In re Sanders)*, 128 B.R. 963 (Bankr. W.D. La. 1991).

118. See *id.* at 968.

119. See *id.* at 969 ("Mr. and Mrs. Sanders for no consideration nominally donated valuable property to their children's trusts but retained possession or use of this property at a time when they were faced with a number of lawsuits later reduced to judgment.").

120. See *id.*

121. *Id.* at 970 ("Mrs. Sanders maintains that there could not have been concealment because the trust documents were recorded and therefore public knowledge. This misses the point. The debtors' continued use and enjoyment of property after it was transferred was not recorded and constituted a continuing concealment.").

to more subversive, and possibly less detectable, fraudulent transfers such as multiple transfers to dummy or shell corporations or other entities which act to launder the transfers.

Therefore, the situations described earlier in Part IV.C and relied upon by proponents of the BFP rule are addressed by the “concealment” provision in section 727(a)(2). The Ninth Circuit has agreed, commenting that, “[c]ourts following the ‘party rule’ would not discharge a debtor who failed to record if he did so for the purpose of concealing the transfer.”<sup>122</sup>

#### D. GREATER PROTECTION TO DEBTORS

Courts should construe section 727(a)(2) liberally in favor of the debtor and strictly against those objecting to the discharge.<sup>123</sup> Before a court can deny a discharge under section 727(a)(2), “it must be shown that there was an actual transfer of valuable property belonging to the debtor which reduced the assets available to [the] creditor and which was made with fraudulent intent.”<sup>124</sup> Creditors bear the burden of proving facts that are essential to their pleas for a denial of discharge.<sup>125</sup> Because of this general rule, constructive fraudulent intent cannot be a reason to deny a discharge.<sup>126</sup> In addition, actual intent to hinder or delay a creditor or the bankruptcy trustee can be negated by reliance upon advice of an attorney, as long as such reliance is in good faith.<sup>127</sup>

Section 727 discharges are construed strictly against creditors and liberally in favor of debtors in order to effectuate the fresh start purpose of

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122. *Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 87 F.3d 311, 318 (9th Cir. 1996).

123. *See Bernard v. Scheaffer*, 96 F.3d 1279, 1281 (9th Cir. 1996); *Gullickson v. Brown*, 108 F.3d 1290, 1292 (10th Cir. 1997). Unlike the rules of statutory construction discussed earlier in Part III.B. of this Note, this rule is universally applied to section 727(a)(2), and thus cannot be easily dismissed.

124. *Lee Supply Corp. v. Agnew (In re Agnew)*, 818 F.2d 1284, 1289 (7th Cir. 1987) (quoting 4 COLLIER, *supra* note 14, ¶ 727.02[2][5], at 727-21 to 727-22).

125. *See* BANKRUPTCY RULE 4005 (Rule 4005 governs the burden of proof. It does not govern the burden of going forward with the evidence).

126. *See First Beverly Bank v. Adeeb (In re Adeeb)*, 787 F.2d 1339, 1343 (9th Cir. 1986).

127. *See id.* (“Generally, a debtor who acts in reliance on the advice of his attorney lacks the intent required to deny him a discharge of his debts.”); *Hultman v. Tevis*, 82 F.2d 940 (9th Cir. 1936). In *Hultman*, the court said:

The bankrupt had . . . been advised by his attorney, to whom all the facts were fully disclosed, that money received from this trust could not be subjected to the claims of his creditors, even after it reached his hands. Whether this advice was correct or not is a question which the District Court did not, nor do we, deem it necessary to decide. The bankrupt, in good faith, believed and relied on his attorney’s advice and acted on it in making the transfer to his son.

*Id.* at 941.

the Bankruptcy Code.<sup>128</sup> A denial of discharge is an extremely harsh penalty: Not only is the debtor liable for fraudulently conveyed property, none of his debts are excused. Hence, the debtor is, in a sense, working for his creditors as he attempts to pay off his debts for what could be an extremely long period of time.

A debtor is entitled to the presumption of honesty and a presumption that most people do not engage in fraudulent transfers.<sup>129</sup> This idea attempts to balance the fresh start policy with the incentive to prevent a dishonest debtor from avoiding the consequences of pre- or post-petition conduct. The party rule, when compared to the BFP rule, allows the greater number of debtors to be granted a discharge since recording can never occur before the initial transfer.<sup>130</sup> In addition, forcing a creditor to prove that a transfer had been made within a year before filing a petition would conform more with the evidentiary burdens that Congress has placed on creditors for section 727(a)(2) lawsuits.

#### E. THE BONA FIDE PURCHASER RULE CAN UNFAIRLY EXTEND THE REACH BACK PERIOD

The debtor in *In re Roosevelt* argued that the BFP rule would put a debtor at the mercy of the transferee.<sup>131</sup> This is so because a debtor, who believed he was eligible for a discharge, could suddenly find out that he was ineligible if the transferee delayed recording the transfer until the one-year period had arrived.<sup>132</sup>

For example, as in *In re Roosevelt*, a marital settlement agreement was executed during a time of marital difficulty. The husband, a physician, had owned a medical practice several years before his bankruptcy filing. The medical practice was capitalized for the purposes of evaluation under a family law analysis in a fee-for-service environment, and had a certain value including, for marital dissolution purposes, a value for com-

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128. See *State Bank of India v. Chalasani (In re Chalasani)*, 92 F.3d 1300, 1310 (2d Cir. 1996) ("Clearly, § 727 imposes an extreme penalty for wrongdoing. As such, we have held that it must be construed strictly against those who object to the debtor's discharge and 'liberally in favor of the bankrupt.'").

129. See *Francis v. Riso (In re Riso)*, 74 B.R. 750 (Bankr. D. N.H. 1987) ("[T]he case law establishes that a debtor is entitled to a starting presumption that most people are honest and do not ordinarily engage in fraudulent activities.").

130. See *Finalco, Inc. v. Roosevelt (In re Roosevelt)*, 87 F.3d 311, 318 (9th Cir. 1996).

131. *Id.*

132. In fact, during the *In re Roosevelt* trial, Dr. Roosevelt's attorney testified under oath that he had advised Dr. Roosevelt that the transfer occurred when the agreement was signed. See Interview with Donald E. Rinaldi, Attorney at Law, Covina, Cal. (July 28, 1998).

munity property.<sup>133</sup> The parties subsequently reconciled without recording the transfer, but this fact did not void the transfer which was effective between the parties.<sup>134</sup> The important issue here, it must be remembered, is that once the transferee has possession of the deed, the transferor has no control over recordation.

When managed care came to be the reimbursement norm, however, the debtor experienced a severe reduction in earning capacity. As a result, the value of the wife's community property interest in the good will of the medical practice, which she had exchanged for his separate property interest in the house, was substantially reduced. The trial court concluded that the value given by the transferee wife was worthless, leading to the finding that the transfer was fraudulent because the value of the interest which the husband retained in his medical practice was, for the most part, not reachable by his creditors.<sup>135</sup> When the wife then recorded the marital settlement agreement several months after the parties made the agreement, the reach back provisions suddenly became effective to potentially strike the transferor physician.

Although the court in *In re Roosevelt* summarily dismissed this argument,<sup>136</sup> it is, nevertheless, worthy of consideration because it shows just how unfair the BFP rule can be, especially in light of the Bankruptcy Code's goal to give debtors a fresh start. Indeed, the repercussions of a denial of discharge for a debtor who violates section 727(a)(2) are so severe as to be nearly quasi-criminal in nature. A debtor should not be liable for such a sanction simply because the transferee recorded the transfer subsequent to the date when the transfer took effect.

The timing of the transfer is critical since a debtor is denied discharge for fraudulent conveyances which occur within one year prior to the filing for bankruptcy. In *In re Roosevelt*, if the transfer was deemed to have oc-

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133. See, e.g., CAL. FAM. CODE § 2550 (1994); *In re Marriage of Foster*, 117 Cal. Rptr. 49 (1974) (the value of the good will of spouse's professional medical practice as a sole practitioner was taken into consideration in determining the community property award to the other spouse).

134. See, e.g., *In re Marriage of Broderick*, 257 Cal. Rptr. 397 (1989) (a wife's quitclaim deed that transferred all of her interest in the family residence to her husband, which was executed during marital difficulties, was not annulled by the subsequent reconciliation of the parties).

135. See, e.g., *Ray v. Roosevelt (In re Roosevelt)*, 176 B.R. 200 (B.A.P. 9th Cir. 1994). The court stated:

The [trial] court proceeded to reject wife's defense to avoidance on grounds that, though wife was good faith transferee, from standpoint of creditors, debtor's wife gave zero value in exchange for property she received. The court reasoned that consideration received or retained by debtor in marriage settlement agreement had no value to his creditors.

*Id.* at 200.

136. *Id.*

curred at the time it was effective between the parties, namely when the marriage settlement agreement was effectuated, then the debtor would receive a discharge. On the other hand, if the transfer occurred when the deed was recorded, then the debtor would be denied a discharge since it occurred within one year before his filing for bankruptcy.

The debtor's wrongful act occurred seventeen months before the petition. That was when the debtor made a transfer which the trial court held had the purpose of defrauding the creditors. Congress enacted section 727(a)(2) to punish debtors who commit wrongful acts one year before the filing of a bankruptcy petition. In this case, if the court applied the BFP rule, the debtor would be severely punished, not from the date that he made his transfer but from the date when his good faith transferee recorded the deed. Although in this case it can be argued that the debtor maintained some control over his wife's actions,<sup>137</sup> in many cases, a debtor will not maintain such control. Thus, it would be unfair for that debtor to be punished for an act over which he had no control.

As an addendum, it should be noted that Finalco was not without a remedy in this case. In a separate action commenced against the debtor's wife under section 548 regarding the avoidance powers of a bankruptcy trustee, the bankruptcy trustee won a judgment exceeding \$100,000 for the same property sought in *In re Roosevelt*. Ironically, all of the funds recovered to date from the good faith transferee have gone to the Chapter 7 trustee's legal fees and administrative costs, with no distribution to the debtor's aggrieved creditors, including Finalco.

## VI. CONCLUSION

Absent a strong reason to do so, one circuit will not create a direct conflict with other circuits.<sup>138</sup> Despite this strong disincentive within the judicial system, the Ninth Circuit in *In re Roosevelt* has decided a rule that directly conflicts with the Third Circuit decision in *In re MacQuown*. For the purposes of section 727(a)(2), the Ninth Circuit has determined that a transfer should be deemed to have been made at the time it is valid between the parties to the transfer, while the Third Circuit had earlier determined that a transfer is deemed to have been made when it is valid as against a bona fide purchaser, which occurs upon the date of recording.

After analyzing the arguments for both rules, it appears that the Ninth Circuit's adoption of the party rule is the proper holding since it better

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137. See discussion *supra* Part IV.C.

138. See *United States v. Chavez-Vernaza*, 844 F.2d 1368, 1374 (9th Cir. 1988).

serves the goals of section 727(a)(2) than does the Third Circuit's adoption of the BFP rule. Although the plain language and the legislative history of the provision do not provide a clear answer as to which rule is required under the statute, an analysis of the arguments for each rule leads to the conclusion that the party rule better effectuates the purpose of that statute.

First, although another section of the Code that deals with fraudulent conveyances explicitly states that a transfer is not made under that section until it is valid as against bona fide purchasers, analogizing that section to section 727(a)(2) is inappropriate. Section 548 is mainly concerned with protecting creditors, while section 727(a)(2)'s main focus is on the wrongdoing of the debtor subject to discharge. The party rule is better suited to advance the goals of section 727(a)(2) than is the bona fide purchaser rule. Additionally, creating a rule that is more practical because it reduces evidentiary issues may be a legitimate way to create judicial rules but, when doing so would create a rule that does not further the main purpose of a statute, practicality should not dominate responsible jurisprudence. Third, concerns that the party rule will not encourage debtors to disclose their transfers are misplaced. The provision in section 727(a)(2) that addresses "concealments" of property will ensure that debtors do not transfer their property symbolically, while retaining real interests therein. The rule announced by the Ninth Circuit also conforms better with the rule of construction which states that statutes dealing with discharge are to be construed liberally in favor of the debtor and strictly against creditors in order to advance the fresh start goal of the Code. Finally, the party rule prevents debtors from being at the mercy of transferees who may delay recording to the point where a debtor is denied a discharge because the transfer occurred within the one-year reach back provision in section 727(a)(2).

The concern that the party rule will wreak havoc in bankruptcy law and other areas of the law by displacing the reliability and certainty of public record as proof of ownership is overstated for several reasons. First, the rule will apply only to discharges under section 727(a)(2). Other areas of the Code that deal with fraudulent transfers explicitly mandate the application of the BFP rule. Second, recording acts have the primary purpose of protecting creditors. Section 727(a)(2), however, centers around the wrongdoing of a debtor in connection with his bankruptcy case. There are many other areas of the Bankruptcy Code that serve to protect creditors, such as sections 544 and 548. Third, the reliability of public records is at best a questionable presumption. As any home purchaser knows, if they did create certainty, there would be no need for protective devices such as title insurance. Only costly monitoring or investigating mechanisms can guarantee the complete reliability of public records. Finally, tri-

ers of fact are charged with the task of fact finding which necessarily includes determining the credibility and the demeanor of witnesses. It seems a strange contention to state that relying on this fundamental aspect of the judicial system will create havoc in all areas of the law.

For all of these reasons, the rule adopted by the Ninth Circuit in *In re Roosevelt* is the better rule. A transfer under section 727(a)(2) should be deemed to have been made when it is valid between the parties, even if it is not valid as against a bona fide purchaser.