

1995

William C. Selvage and WM. C. Selvage, Inc., a  
Utah corporation v. J.J. Jonson and Associates, a  
Utah corporation, Sear-Brown Associates, P.C., a  
New York corporation, and the Sear Brown Group,  
Inc., a New York corporation : Reply Brief

Utah Court of Appeals

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Anthony L. Rampton; Robert Palmer Rees; Fabian & Clendenin; Attorneys for Appellants.

James A. Boevers; Prince, Yeates & Geldzahler; Attorneys for Appellees.

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## UTAH COURT OF APPEALS

WILLIAM C. SELVAGE and WM. C.  
SELVAGE, INC., a Utah  
corporation,

Plaintiffs-Appellants/  
Cross-Appellees,

vs.

J.J. JOHNSON & ASSOCIATES, a  
Utah corporation, SEAR-BROWN  
ASSOCIATES, P.C., a New York  
corporation, and THE SEAR-  
BROWN GROUP, INC., a New York  
corporation,

Defendants-Appellees/  
Cross-Appellants.

Case No. 950240-CA

Priority 15

---

APPELLANTS/CROSS-APPELLEES WILLIAM C. SELVAGE AND WM.C. SELVAGE,  
INC.'S RESPONSE TO BRIEF OF APPELLEES/CROSS-APPELLANTS SEAR-BROWN  
ASSOCIATES, P.C. AND THE SEAR-BROWN GROUP, INC.

---

APPEAL FROM AMENDED AND FINAL JUDGMENT OF THE THIRD JUDICIAL  
DISTRICT COURT  
THE HONORABLE PAT B. BRIAN, PRESIDING

---

Anthony L. Rampton, A2681  
Robert Palmer Rees, A4652  
FABIAN & CLENDENIN,  
A Professional Corporation  
Twelfth Floor  
215 South State Street  
P.O. Box 510210  
Salt Lake City, Utah 84151  
Telephone: (801) 531-8900

James A. Boevers, 2374  
PRINCE, YEATES & GELDZAHLER  
City Centre I, Suite 900  
175 East Fourth South  
Salt Lake City, Utah 84111  
Telephone: (801) 524-1000

Attorneys for Plaintiffs-  
Appellants/Cross-Appellees

Attorneys for Defendants-  
Appellees/Cross-Appellant

**FILED**

MAY 26 1995

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175 East Fourth South  
Salt Lake City, Utah 84111  
Telephone: (801) 524-1000

Attorneys for Plaintiffs-  
Appellants/Cross-Appellees

Attorneys for Defendants-  
Appellees/Cross-Appellants

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Appellants/Cross-Appellees William C. Selvage and Wm. C. Selvage, Inc. (collectively "Selvage") submit this response to the Brief of Appellees/Cross-Appellants Sear-Brown Associates, P.C. and The Sear-Brown Group, Inc. (collectively "Sear-Brown").

**SUPPLEMENTAL STATEMENT OF THE CASE CONCERNING CROSS-APPEAL**

**I. Course of Proceedings.**

The trial court directed verdict against defendant J.J. Johnson & Associates ("Johnson") on Selvage's breach of contract claims. Instruction No. 22 at R.800. The jury's answers to Special Interrogatories found that Sear-Brown was also liable to Selvage on four independent bases under Utah's Fraudulent Transfers Act and the "mere instrumentality" doctrine. R.819-827.

After trial, Selvage and Sear-Brown submitted, briefed and argued proposed findings and conclusions. The lower court's January 13, 1994 Memorandum Decision (i) specifically adopted the jury's findings as its own, (ii) concluded that Selvage is entitled to judgment against Sear-Brown on four independent grounds of fraudulent transfer and mere instrumentality, and (iii) awarded Selvage \$42,500 in attorneys fees.<sup>1/</sup> R.1124-1133A.

Sear-Brown filed a Motion for Judgment Notwithstanding the Verdict, For a New Trial and to Alter or Amend Judgment. R.1138-

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<sup>1/</sup> This award of only 20% of Selvage's attorney's fees is the subject of Selvage's appeal.

1158. On April 14, 1994 the lower court entered its Findings of Fact, Conclusions of Law and Order, (i) incorporating its prior Memorandum Decision, (ii) specifically finding that there is sufficient evidence in the record to support each of the four bases of Sear-Brown's liability, (iii) ruling that Selvage's "insider" preference claim is not time-barred, and (iv) denying Sear-Brown's motions. R.1290-1294.

On May 23, 1994 the lower court entered its Amended and Final Judgment in favor of Selvage and against both Sear Brown and Johnson in the principal amount of \$109,400, plus prejudgment interest of \$75,810.73, expenses of \$6,433.87, and attorneys' fees of \$42,500, for a total of \$234,144.60. R.1396-1399.

## **II. Statement of Facts Concerning Cross-Appeal.**

**A. Defendant Johnson.** Johnson purchased Selvage's architectural business. R.12. The sale occurred on August 28, 1986 and consisted of three separate agreements (Exhibits 6, 7 and 9). All three agreements provided for reasonable attorneys fees.

Selvage commenced this action on April 7, 1987, alleging that Johnson breached all three contracts, and seeking damages, costs and reasonable attorneys' fees. R.2-82. After four days of trial, the jury was directed that Johnson is liable under all

three contracts.<sup>2/</sup> R.800. The jury returned its verdict through answer to Special Interrogatory No. 1, finding Johnson liable to Selvage in the principal amount of \$109,400.32. R.819.

**B. Defendant Sear-Brown.** Sear-Brown is a national design, architectural and engineering firm, headquartered in Rochester, New York. R.1779, 1780. In late 1985 and early 1986, Sear-Brown commenced its relationship with Johnson. R.1781. At that time, Sear-Brown was aware that Johnson was in financial trouble. R.1785. On or about December 16, 1985 Sear-Brown "loaned" Johnson \$365,000. R.1788. However, no security was given, no interest was charged, and no demand for payment was ever made. R. 1788, 1789; 1819. In conjunction with that "loan," Sear-Brown acquired 40% of the outstanding stock in Johnson. R.1788. On January 26, 1986 two of Sear-Brown's officers and directors joined Johnson's five member board. R.1790, 1791.

On or about February 25, 1987, Sear-Brown acquired an additional 26.6% of Johnson's stock, thereby increasing Sear-Brown's stock ownership to 66.6%. R.1796, 1797. This additional stock was purchased for \$200,000. R.1796. Sear-Brown retained two seats on the Johnson board of directors that was reduced to a total of four. R.1797. By April 15, 1988, Sear-Brown officers and employees occupied three of the four Johnson board seats.

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<sup>2/</sup> Sear-Brown did not contest the directed verdict against Johnson. Until the first morning of trial, however, Sear-Brown's attorneys also represented Johnson.

R.1803. At a Johnson board meeting on April 15, 1988, Mr. Jack Johnson, the founder and president of Johnson company, was fired by the Sear-Brown-controlled board. R.1803, 1804.

Mr. Johnson's termination was shortly followed by a lawsuit by Mr. Johnson against Sear-Brown, and two lawsuits by Sear-Brown and the Johnson company against Mr. Johnson and his wife.

R.1806; Exhibit 76.

On September 30, 1988 Sear-Brown entered into an agreement settling the pending litigation with Jack Johnson and his wife, Gloria. R.1808; Exhibit 76. That settlement agreement:

- (1) dismissed the pending lawsuits between Mr. & Mrs. Johnson, the Johnson company and Sear-Brown;
- (2) conveyed the remaining Johnson company stock to Sear-Brown, thereby vesting 100% of the Johnson stock in Sear-Brown;
- (3) obligated Mr. & Mrs. Johnson to pay Sear-Brown the sum of \$230,000; and
- (4) permitted Sear-Brown to use the Johnson name until December 31, 1988. R.1809; Exhibit 76.

The \$230,000 was actually owed by Mr. & Mrs. Johnson to the Johnson company, not to Sear-Brown. Mr. Johnson's payment to Sear-Brown of that \$230,000 was therefore a transfer of a Johnson company's corporate asset to Sear-Brown. R.1810.

As of September 30, 1988 Johnson's liabilities exceeded its assets by approximately one-half million dollars. R.1816, 1817; 1887, 1888. On October 1, 1988 Johnson, the company, ceased

operation. Exhibit 67. Johnson no longer had any employees. R.2192. Commencing on October 1, 1988 and through February, 1989, all of Johnson's assets were transferred to Sear-Brown, down to the last paper clip. R.1814, 1815, 1829. Those transfers were directed by Johnson's board of directors which consisted entirely of officers or employees of Sear-Brown. R.1868, 1869, 1878, 1879, 1885; Exhibit WW. The transferred assets included Johnson's personal property, accounts receivable of \$442,765.95, clients, and work in progress. R.1820-1823; Exhibit 60.

Mr. Clary, Sear-Brown's president and a member of Johnson's board, referred to the transfer of assets as an "acquisition by default." R.1881. As early as January 1989, Sear-Brown's stationary had a return address "Sear-Brown Group Resort Design Division, formerly J.J. Johnson & Associates." Exhibit 78. Mr. Clary admitted previously describing the relationship as one of "merger," (R.1827), although he declined to do so at trial. R.1881.

The transfers included Johnson's assets and liabilities. R.1885. According to Sear-Brown, it was owed some \$797,000 by Johnson as of September 30, 1988. R.1890; Exhibit 55. Some \$415,000 of the debt owed by Johnson to Sear-Brown was settled by the transfer of assets. R.1891, 1892; Exhibit 55. Johnson's "bad" accounts receivable that had previously been written off in the amount of \$364,000 were reinstated as income on Johnson's

book (no cash was transferred), and transferred to Sear-Brown so that Sear-Brown could take the loss. R.1892; Exhibit 55.

No value was assigned by Sear-Brown to the client base or work-in-progress it received from Johnson. R.1913. There was no attempt made to value the ongoing business of Johnson (R.1913), even though Sear-Brown originally came to Utah to get into the resort design business. R.1718. Sear-Brown is still in the resort design business in Salt Lake. R.1913.

The \$230,000 paid by Mr. & Mrs. Johnson under the litigation settlement was paid directly to Sear-Brown instead of through the Johnson company. R.1905. That \$230,000 payment went toward recoupment of Sear-Brown's equity investment in the Johnson company, not toward payment of any indebtedness. R.1906.

After the transfers to Sear-Brown and resolution of other Johnson liabilities, the only liabilities left with Johnson were those owed to Selvage. R.1830, 1898, 1899. On July 6, 1990, Sear-Brown placed Johnson into bankruptcy. R.1828; Exhibit 67. Johnson's Chapter 7 filing showed no (\$0.00) assets, and listed \$332,000 in contingent liabilities owing to Selvage. R.1828, 1832; Exhibit 67. In response to a bankruptcy petition question regarding payments to "relatives" during the year preceding the filing, Johnson responded "None." R.2175, 2176; Exhibit 67. Sear-Brown paid the costs and fees associated with Johnson's bankruptcy (R.1828), and specifically timed the bankruptcy

petition take advantage of statutes of limitations for avoiding transfers. R.1878, 2182

#### **SUMMARY OF ARGUMENT**

1. Sear-Brown admits that, unless a statute of limitation bars Selvage's claim based upon "insider" transfers, it is liable to Selvage. Selvage's claim is not time-barred for the following reasons:

a. Sear-Brown did not properly plead the statute of limitations defense;

b. Sear-Brown cannot cure its failure to properly plead by asserting that this is a jurisdictional issue;

c. Sear-Brown's last minute motion for summary judgment did not cure its failure to plead the statute of limitations;

d. Even if the statute of limitations was properly pleaded, application of the discovery rule bars its application;

e. The asserted statute of limitations is not a statute of repose and, even if it was, it is still subject to the discovery rule.

2. The appellant must marshal the evidence supporting the findings in order to demonstrate that the evidence, including all reasonable inferences drawn therefrom, is insufficient. Sear-Brown failed to marshal the evidence pertaining to the time period during which the transfers from Johnson to Sear-Brown were



made. On this basis alone, Sear-Brown's appeal should be dismissed.

3. The evidence fully supports the jury's answers to special interrogatories, and the lower court's findings, that Johnson and Sear-Brown had the requisite intent to hinder, delay or defraud Selvage. Utah Code Ann. § 25-6-5 is not simply a restatement of common law fraud. The jury was properly instructed as to the statutory "factors" that may be considered. Of particular relevance (not marshalled in Sear-Brown's brief) was the transfer of \$230,000 of Johnson assets on account of Sear-Brown's stock interest in Johnson.

4. The jury in this case was properly instructed. Any error in the instructions was immaterial and harmless because the lower court adopted the jury's findings as its own.

5. The doctrine of "mere instrumentality" is a basis for holding one corporation liable for the debts of another corporation that it totally controls and strips of assets to the detriment of a creditor. Selvage suffered such a loss and injury due to Johnson's transfer of all its assets to Sear-Brown. The lead case of *Turner* from the Seventh Circuit has been cited with approval by the Utah Supreme Court in *Omnico*.

6. Selvage is entitled to all his attorneys fees from Sear-Brown under both the doctrine of mere instrumentality and Utah's Fraudulent Transfers Act. No allocation of fees was required by failure of the alter ego theory because it did not

affect Selvage's presentation of evidence, right to judgment, or amount of judgment.

### ARGUMENT

#### I. SELVAGE'S "INSIDER TRANSFER" CLAIM WAS NOT TIME-BARRED AND SEAR-BROWN ADMITS LIABILITY ON THE MERITS.

Appellant Sear-Brown does not dispute the merits of Selvage's insider transfer claim under *Utah Code Ann.* § 25-6-6(2).<sup>3/</sup> Sear-Brown argues that this claim was time-barred under § 25-6-10(3). The trial court, however, properly sustained Selvage's claim by invoking the judicial discovery rules set forth in *Klinger v. Kightly*, 791 P.2d 868, 872 (Utah 1990).

Sear-Brown does not contend Selvage failed to actually satisfy the *Klinger* tests. Sear-Brown's sole appeal is the erroneous blanket contention that *Klinger's* judicial discovery rules can never be applied in any case to extend § 25-6-10(3). As set forth herein, *Klinger* can be applied in an appropriate insider transfer case, so Selvage's judgment must be affirmed.

Before turning to the discovery rule, however, Selvage's judgment must be affirmed because Sear-Brown never pleaded § 25-6-10(3) under *Utah Rule of Civil Procedure* 9(h).<sup>4/</sup>

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<sup>3/</sup> Sear-Brown Brief at 18: "It is undisputed that Johnson Associate's transfers to Sear-Brown in partial satisfaction of antecedent debts met the elements of insider transfers under *Utah Code Ann.* § 25-6-6(2)."

<sup>4/</sup> Because the trial court applied the discovery rule, it never reached Selvage's argument under Rule 9(h). See R.00828.

**A. Section § 25-6-10(3) Was Never Pleaded Under Utah R. Civ. P. 9(h).**

Sear-Brown's Answer only generally alleged that "Plaintiffs' claims are barred by the applicable statute of limitations." The Answer never identified § 25-6-10(3), or any other governing statute, and never indicated which of Selvage's multiple claims were allegedly affected. Rule 9(h) expressly required Sear-Brown to plead its statute of limitations defense by:

... referring to or describing such statute specifically and definitely by section number, subsection designation, if any, or otherwise designating the provision relied upon sufficiently clearly to identify it.

A century of rulings by the Supreme Court under Rule 9(h) and its predecessors hold that Sear-Brown's failure to specify § 25-6-10(3) waived the benefit of that affirmative defense. *E.g.*, *Wasatch Mines Co. v. Hopkinson*, 465 P.2d 1007, 1010-11 & n.5 (Utah 1970).<sup>5/</sup>

**1. Rule 9(h) Controls, Even If § 25-6-10(3) Is A Statute of Repose.**

Historical examination precludes Sear-Brown's contention that Rule 9(h)'s reference to "statute of limitations" excludes

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<sup>5/</sup> *American Theatre Co. v. Glassman*, 80 P.2d 922, 923-34 (Utah 1938) (pleading identified wrong statute, so defense was unavailable in fraudulent conveyance action); *In re Lindford's Estate*, 207 P.2d 1033, 1034 (Utah 1949) (general allegation insufficient); *Nelden-Judsen Drug Co. v. Commercial National Bank of Ogden*, 74 Pac. 195 (Utah 1903); *Spanish Fork City v. Hopper*, 26 Pac. 293 (Utah 1891).

statutes of repose.<sup>6/</sup> Rule 9(h) was adopted in 1950, and restates more than a century of Utah law. *E.g.*, *Compiled Laws of Utah* § 3244 (1888). In contrast, the Supreme Court's express distinction between statutes of repose and statutes of limitation apparently originated in 1985 with *Berry ex rel. Berry v. Beech Aircraft Corp.*, 717 P.2d 670 (Utah 1985).<sup>7/</sup> As recently as 1984, the Supreme Court used "statute of limitation" and "statute of repose" interchangeably. *E.g.*, *Compare Perry v. Pioneer Wholesale Supply Co.*, 681 P.2d 214, 216, 219 (Utah 1984) (referring to § 70A-2-725 both as a statute of limitation and as a statute of repose) *with Davidson Lumber Sales, Inc. v. Bonneville Investment, Inc.*, 794 P.2d 11, 13 n.2 (Utah 1990) (carefully distinguishing § 70A-2-725 as a statute of repose, even though it is frequently called a statute of limitation).<sup>8/</sup>

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<sup>6/</sup> Section 25-6-10(3) is a statute of limitation, not repose, as set forth in Selvage's argument on the discovery rule. For purposes of Rule 9(h), however, the distinction is immaterial.

<sup>7/</sup> *Berry* states that *Allen v. Intermountain Health Care*, 635 P.2d 30 (Utah 1981) and *Good v. Christensen*, 527 P.2d 223 (Utah 1974) reviewed statutes of "repose". 717 P.2d at 683. Neither of those cases, however, use the term "repose".

<sup>8/</sup> See also *Peterson v. Callister*, 313 P.2d 814, 815 (Utah 1957) (describing § 78-12-5.1 both as statute of limitation and as a statute of repose); *Good v. Christensen*, 527 P.2d 223, 224 (Utah 1974) (incorrectly referring to § 78-12-25.5 as a statute of limitation); *Hirtler v. Hirtler*, 566 P.2d 1231, 1231 (Utah 1977) (describing § 78-12-23 both as a statute of limitation and as a statute of repose).

Similarly, the Utah Legislature has historically used "statutes of limitation" to refer to statutes of repose. *E.g.*, former *Utah Code Ann.* § 78-15-3(1), the quintessential statute of repose reviewed in *Berry*; title language in 1977 *Utah Laws* § 149; *Utah Code Ann.* § 78-14-4 (medical malpractice statute of repose entitled "statute of limitations"). The earliest instances located by Selvage of the Utah Legislature actually using the term "statute of repose" are the 1988 enactments of § 78-12-33.5(1) and § 78-12-48(1) ("no statute of limitation or repose").

The foregoing historical background demonstrates that Rule 9(h)'s 1950 language of "statute of limitations" did not distinguish between statutes of limitation and statutes of repose, and must be read broadly to include both.

**2. Sear-Brown Cannot Avoid Its Failure to Properly Plead by Characterizing § 25-6-10(3) as Jurisdictional**

Sear-Brown also contends that statutes of repose are jurisdictional, and therefore cannot be waived, regardless of Rule 9(h). No Utah case cited by Sear-Brown describes statutes of repose in terms of "subject matter jurisdiction."<sup>2/</sup>

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<sup>2/</sup> Sear-Brown's only cases mentioning "jurisdiction" concern mechanics liens: *AAA Fencing Co. v. Raintree Dev. and Energy Co.*, 714 P.2d 289 (Utah 1986) and *Diehl Lumber Transp., Inc. v. Mickelson*, 802 P.2d 739 (Utah App. 1990). See also *Projects Unlimited v. Copper State Thrift & Loan Co.*, 798 P.2d 738, 751 n.13 (Utah 1990) which ruled that § 38-1-11 is a substantive restriction on mechanics liens rather than a statute of limitations. Obviously, after a lien has expired, there is nothing left for a court to order foreclosed. None of these cases, however, describe § 38-1-11

(continued...)

Accepting Sear-Brown's argument would allow any defendant to assert any statute of repose for the first time on appeal, thereby affecting such common litigation as sales disputes (§ 70A-2-725) and medical malpractice (§ 78-14-1).

Nor does § 25-6-10(3)'s language that "extinguishes" claims make it jurisdictional. Many affirmative defenses "extinguish" claims,<sup>10/</sup> but they must still be properly pleaded under *Utah R. Civ. P. 8(c)*. Sear-Brown's argument would excise all affirmative defenses that "extinguish" claims from Rule 8(c) on "jurisdictional" grounds. Finally, Sear-Brown offers no policy why statutes of repose should be treated as jurisdictional and nonwaivable.

**3. Sear-Brown's Motion for Summary Judgment Did Not Cure Its Defective Answer.**

Sear-Brown argues that its motion for summary judgment, filed one week before trial and heard on the first day of trial, should be deemed to satisfy Rule 9(h). General notice of potential affirmative defenses on the eve of trial, however, does not satisfy Rule 8(c) or Rule 9(h).

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<sup>2/</sup>(...continued)

as a statute of repose (or even mention statutes of repose). Those cases are simply not probative of the issues in this appeal.

<sup>10/</sup> See, e.g., *Robinson v. Hansen*, 594 P.2d 867, 870 (Utah 1979) (accord, "extinguishment"); *State v. Masciantonio*, 850 P.2d 492, 494 (Utah App. 1993) (payment, "extinguished"); *Quealy v. Anderson*, 714 P.2d 667, 669 (Utah 1986) (releases and accords, "extinguish").

Sear Brown cannot take refuge in *Utah R. Civ. P. 15(b)* because it never moved to amend as that rule requires. Sear-Brown failed to move to amend during the 7 months between Selvage's October 14, 1993 Memorandum raising Rule 9(h) (R.0828) and the May 23, 1994 Amended Final Judgment. Nor did Sear-Brown make a post-judgment motion as permitted by Rule 15(b).

Any motion to amend under Rule 15 would have to have been denied anyway. Having delayed identifying which claim was affected by which statute until the eve of trial, and having admitted liability on the merits,<sup>11/</sup> Sear-Brown could never satisfy Rule 15(b)'s requirement that the "merits of the action will be subserved thereby," or Rule 15(a)'s condition of "when justice so requires." See *Goeltz v. Continental Bank & Trust Co.*, 299 P.2d 832, 834-35 (Utah 1956); *Staker v. Huntington Cleveland Irrigation Co.*, 664 P.2d 1188, 1190 (Utah 1983).

Sear-Brown's brief offers no reason to deviate from a century of precedent strictly enforcing Rule 9(h). Any complaint that Rule 9(h) is a technicality is overshadowed by Sear-Brown's admission of liability "but for" the technicality of § 25-6-10(3)'s narrow one-year window. Under competing technicalities, the admitted merits must prevail.

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<sup>11/</sup> During argument on directed verdict (R.01979) Sear-Brown's counsel stated: Section 25-6-10(3) "is one of the single most important issues in this case, because if the plaintiffs are permitted to go ahead under this status kind of claim, they, in essence, win." See also Brief of Appellees/Cross-Appellant at 18.

**B. The Trial Court Was Not Precluded From Applying the Discovery Rule.**

Even if Rule 9(h) is not dispositive, Sear-Brown's arguments that the discovery rule should never be applied to § 25-6-10(3) are ill-founded.

**1. Statutory Construction of § 25-6-10 Does Not Preclude Use of Klinger's Judicial Discovery Rules.**

Section § 25-6-10 has three subsections setting limitations periods for different types of fraudulent transfers. Sear-Brown is correct that § 25-6-10(1)'s express discovery rule for "actual intent" cases precludes implying a statutory discovery rule for insider transfer cases under § 25-6-10(3). Sear-Brown's argument is an incomplete, however, because statutory provision is only one of three grounds in Klinger for invoking a discovery rule. Klinger also provides a judicial discovery rule if warranted by the particular facts of a specific case, i.e. where: (i) the defendant engaged in concealment or misleading conduct, or (ii) application of the general statute of limitation rule would be "irrational or unjust" while the equities and prejudice weigh in favor of the plaintiff. 791 P.2d at 872. See also Myers v. McDonald, 635 P.2d 84, 86-87 (Utah 1981).

Because Sear-Brown's brief never challenges Selvage's satisfaction of Klinger's criteria for invoking those judicial discovery rules in this case, the judgment must be affirmed. Moreover, the policies behind statutes of limitation are not



violated in this case because Sear-Brown's open admission of liability on the merits resolves any issue of surprise or stale evidence.

**2. Sear-Brown's Characterization of § 25-6-10(3) As A Statute Of Repose Does Not Bar Application of Klinger's Judicial Discovery Rules.**

Sear-Brown argues (i) that § 25-6-10(3) is a statute of repose, and (ii) that any discovery rule is antithetical to a statute of repose. Failure of either argument requires affirmation of Selvage's judgment.

**a. Section 25-6-10(3) Is Not A Statute Of Repose.**

The distinguishing feature of a statute of repose is that it commences from a date or event independent of the date the legal injury occurs. In comparison, a statute of limitations runs from the date a cause of action arises. *Berry ex rel. Berry v. Beech Aircraft Corp.*, 717 P.2d 670, 672 (Utah 1985); *Raithaus v. Saab-Scandia of America, Inc.*, 784 P.2d 1158, 1161 (Utah 1989).

Section 25-6-10(3)'s one-year period to file an insider transfer claim runs from the date property is transferred. A claim under § 25-6-6(2) accrues on that same date. The elements of an insider transfer claim are: (i) the plaintiff was a creditor "before the transfer" was made, (ii) the transferor "was insolvent at the time" of the transfer, (iii) the transfer satisfied an antecedent debt to the insider-transferee, and (iv)

the insider-transferee already "had reasonable cause to believe" the transferor was insolvent. Because § 25-6-6(2) and § 25-6-10(3) are triggered simultaneously, § 25-6-10(3) operates as a statute of limitation, not as a statute of repose. *Avis v. Board of Review of Industrial Comm.*, 837 P.2d 584, 587 (Utah App. 1992), cert. den., 853 P.2d 897 (Utah 1993) (§ 35-1-99 is a statute of limitation, not repose, because the limitation period begins when the claim arises).

Sear-Brown wrongly reasons that § 25-6-10(3) is a statute of repose because it "extinguishes" claims and UFTA Comment 9 says it is intended to "bar the right and not merely the remedy." Sear-Brown's brief ignores the remainder of UFTA's Comment 9 and UFTA's Prefatory Notes, however, which state that the legislation creates "statutes of limitation." 7A *Uniform Laws Ann*, Uniform Fraudulent Transfer Act, at pp. 642 and 666.

No Utah case<sup>12/</sup> makes the distinction that statutes of limitation "bar" remedies while statutes of repose "extinguish" claims. Berry uses the term "extinguish" to describe the

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<sup>12/</sup> Sear-Brown's citation to *United States v. Vellalos*, 780 F. Supp. 705 (D. Hawaii 1992) does not help its argument. First, the *Vellalos* court never refers to the Uniform Act as creating a statute of "repose". Second, to the extent the *Vellalos* court held the statute's "extinguished" language was legally significant, it also acknowledged it was diverging from rulings by the Fifth and Eighth Circuits. Third, *Vellalos* specifically noted that "the United States does not claim that it could not have reasonably discovered this recorded conveyance" by the statute's expiration date, thereby suggesting that a judicial discovery rule could have applied under the Uniform Act if the facts of the case warranted.

practical effect of a statute of repose expiring before a claim arises, 717 P.2d at 684, but also states that the purpose of a statute of repose "is to bar injured plaintiffs' judicial remedies." *Id.* at 673. Any difference between "extinguish" and "bar" is a red herring.<sup>13/</sup>

**b. Discovery Rules May Be Applied To Statutes Of Repose.**

Sear-Brown's argument that discovery rules are inherently antithetical to statutes of repose is erroneous. The Utah Legislature has determined that statutes of repose and discovery rules can coexist. *E.g.*, Utah Code Ann. § 78-12-25.5 (improvements to real property); § 78-12-48 (asbestos); § 78-14-4(1)(a) (medical malpractice). Sear-Brown even contradicts itself by arguing that all of § 25-6-10 is a statute of repose, while pointing out that § 25-6-10(1) contains a discovery rule. Sear-Brown's argument that tolling provisions can never apply to statutes of repose is also belied by *Lee v. Gaufin*, 867 P.2d 572, 589 (Utah 1993) ("§ 78-12-36 operates to toll ... the four-year statute of repose found in § 78-14-4(1)") (emphasis added); *Berry*, 717 P.2d at n.9 (application of tolling provisions by Nebraska court to statute of repose).

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<sup>13/</sup> *Cf. Berry*, 717 P.2d at 679, wherein the Supreme Court rejected any constitutional significance of semantic distinctions between "abrogating" a claim and defining a claim to be "temporally limited."

The above examples illustrate that discovery rules and other tolling provisions can coexist with statutes of repose. In contrast, Sear-Brown offers no policy reason why *Klinger* should never apply to such statutes. Justice is obviously best served by a judicial discovery rule in cases of concealment or misleading conduct -- otherwise a statute of repose would sanction such misconduct. Similarly, no purpose is served by barring claims when application of the general statute would be "irrational or unjust" and admission of liability belies any surprise or evidentiary prejudice.<sup>14/</sup>

Finally, Sear-Brown wrongly argues that *Utah Code Ann.* §§ 68-3-1 and 68-3-2 prevent a court from applying common law tolling principles to § 25-6-10(3). Section 25-6-11, however, expressly preserves and incorporates existing principles of law and equity not specifically displaced by the Act. E.g., UFTA's Comment 10 states that under § 25-6-11 laches may bar an otherwise timely claim. If § 25-6-11 is broad enough encompass laches, it is can also incorporate narrowly defined judicial discovery rules. Thus, even if judicial discovery rules are inapplicable to most statutes of repose, § 25-6-11 expressly preserves the courts' prerogative to apply *Klinger*, when

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<sup>14/</sup> Sear-Brown also argues that applying judicial discovery rules would be improper because § 25-6-6(2) is merely a "status-based violation". That contention is erroneous because, in addition to status, the statute also requires that the insider transferee "had reasonable cause to the believe that the debtor was insolvent."

appropriate, to cases under § 25-6-10(3). Sear-Brown's appeal does not challenge Selvage's satisfaction of the Klinger criteria, so the judgment must be affirmed.

**II. SEAR-BROWN FAILED TO MARSHAL THE EVIDENCE.**

The "clearly erroneous" standard governs appellate review of the sufficiency of evidence supporting findings of fact. A finding is clearly erroneous only if it is against the clear weight of the evidence. *Reinhold v. Utah Fun Shares*, 850 P.2d 487 (Utah App. 1993). The appellate court must review the evidence in a light most favorable to the trial court's findings and affirm if there is a reasonable basis for doing so. *Gillmore v. Gillmore*, 745 P.2d 461 (Utah App. 1987) cert. denied, 765 P.2d 1278 (Utah 1988). The appellant must marshal all the evidence in support of the findings in order to demonstrate that the evidence, including all reasonable inferences drawn therefrom, is insufficient. *Grayson Roper Ltd. v. Finlinson*, 782 P.2d 467 (Utah 1989).

Sear-Brown's "heavy burden" of marshaling the evidence was recently examined by this Court in *Oneida/SLIC v. Oneida Cold Storage*, 872 P.2d 1051 (Utah App. 1994):

To successfully appeal a trial court's findings of fact, appellate counsel must play the devil's advocate. "[Attorneys] must extricate [themselves] from the client's shoes and fully assume the adversary's position. In order to properly discharge the [marshaling] duty ..., the challenger must present, in comprehensive and fastidious order, every scrap of competent evidence introduced at trial which supports the very findings the appellant resists." [citations omitted]

Once appellants have established every pillar supporting their adversary's position, they then "must ferret out a fatal flaw in the evidence" and show why those pillars fail to support the trial court's findings. They must show the trial court's findings are "so lacking in support as to be 'against the clear weight of the evidence,' thus making them 'clearly erroneous.'" [citation omitted]

*Id.* at 1053. This Court concluded:

This rigorous standard reflects the doctrine that appellate courts "do not sit to retry cases submitted on disputed facts." [citation omitted] Accordingly, '[w]hen the duty to marshal is not properly discharged, we refuse to consider the merits of challenges to the findings and accept the findings as valid.' [citation omitted]

*Id.*

Sear-Brown did not attempt to marshal the evidence. Sear-Brown simply selected facts that support its position in an attempt to reargue the case before this Court. The most glaring failure in this respect is Sear-Brown's refusal to discuss the evidence of what occurred after September 30, 1988. Selvage's claims of fraudulent transfer and mere instrumentality did not arise until September 30, 1988 when Sear-Brown acquired total ownership and total control of Johnson, terminated Johnson's business, and transferred all of Johnson's assets. Selvage does not claim, and did not claim at trial, that Sear-Brown did anything improper before September 30, 1988. It was the evidence of events after that date that formed the basis and support of the jury's and lower court's findings and judgment. See discussion of this evidence under III. *infra.* at pp. 20-22; 27-29; 31-32.

Sear-Brown's failure to marshal the evidence regarding the critical period after September 30, 1988, let alone portray it in the light most favorable to Selvage, dictates dismissal of Sear-Brown's cross-appeal.

**III. THE FINDINGS THAT JOHNSON AND SEAR-BROWN ACTED WITH ACTUAL INTENT TO HINDER, DELAY OR DEFRAUD SELVAGE WERE FULLY SUPPORTED BY THE EVIDENCE.**

Sear-Brown's brief attacking the jury's verdict and the Court's findings rendered pursuant to Utah Code Ann. § 25-6-5(1)(a) (hinder, delay or defraud) disregards both the law and the facts. In short, Sear-Brown argues that this section is nothing more than common law fraud.

Section 25-6-5 provides in part as follows:

(1) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

(a) with actual intent to hinder, delay, or defraud any creditor of the debtor, or ....

The point of inquiry goes to the intent of the transferor.<sup>15/</sup> This basis of liability is a creature of statute, not of the common law. Consequently, it does not require findings on the various elements of common law fraud. See *Linden v. Lewis, Roca, et al.*, 333 P.2d 286 (Ariz. 1958).

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<sup>15/</sup> Johnson never appeared at trial to defend its intent. During the pertinent period from the transfers through the trial, Sear-Brown controlled Johnson and could have caused Johnson to appear and defend its intent. Indeed, Johnson shared Sear-Brown's counsel until the first day of trial.

The elements of § 25-6-5(1)(a) are simply a transfer and the proscribed intent. In addition, the statute states in the disjunctive the intent to hinder, delay, or to defraud. Courts have recognized that each element of the hinder, delay or defraud clause may independently supply a creditor with the elements of a *prima facie* actual intent case. Merely stalling for time at the expense of one's creditors can violate the actual intent provisions. P. Alces, *The Law of Fraudulent Transactions*, ¶ 5.03[3] (1989).

Section 25-6-5(2) lists several factors, "among other factors," that may be considered when finding actual intent; whether,

- (a) the transfer or obligation was to an insider;
- (b) the debtor retained possession or control of the property transferred after the transfer;
- (c) the transfer or obligation was disclosed or concealed;
- (d) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;
- (e) the transfer was of substantially all the debtor's assets;
- (f) the debtor absconded;
- (g) the debtor removed or concealed assets;
- (h) the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;
- (i) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred.
- (j) the transfer occurred shortly before or shortly after a substantial debt was incurred; and
- (k) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.



In determining actual intent, it is not necessary that all or even most of these factors be present. See *Dahnken, Inc. v. Wilmouth*, 726 P.2d 420 (Utah 1986). Obviously, based upon the language of 25-6-5(2), other factors may be taken into account by the fact finder as well.

The jury was properly instructed regarding Section 25-6-5(1)(a) and (2). Instruction 29 (R.807) was a virtual quote of the statute, including the listed nonexclusive factors.

The jury was then requested to answer two special interrogatories, one going to actual intent to hinder or delay (Special Interrogatory No. 2; R.820), and one going to actual intent to defraud (Special Interrogatory No. 3; R.821). The unanimous jury answered both of these questions in the affirmative.

As noted at the outset, Sear-Brown had a duty to marshal all the evidence going to these questions, but only identified selected portions.<sup>16/</sup> That failure dictates a dismissal of its cross-appeal. However, without relieving Sear-Brown of its duty, and *Selvae* cites the following illustrative evidence before the jury:

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<sup>16/</sup> Even the evidence identified in Sear-Brown's brief (pp. 28-31) support the verdict, although Sear-Brown attempts to downplay its significance.

1. The Transfer was to an Insider. At the time of the transfers, Sear-Brown owned 100% of the stock of Johnson.

R.1809.

2. The Transfer or Obligation was Disclosed or Concealed. Sear-Brown intentionally waited almost two years after the transfers before placing Johnson in bankruptcy. One of the express reasons for this delay was to avoid applicable statutes of limitation, including those of the Fraudulent Transfer Act. R.1828, 1875; 2172, 2182. The transfers were not disclosed in the bankruptcy schedules prepared for Johnson by attorney Curtis. R.1829; 2175, 2176; Exhibit 67. Sear-Brown paid Curtis's fees for preparing the schedules. R.1208-09; Exhibit 67.

3. Before the Transfer was Made or Obligation Incurred, the Debtor Had Been Sued. Johnson was sued by Selvage in the spring of 1987. R.2-82. While the transfers were being made, i.e., November 4, 1988, Selvage obtained summary judgment against Johnson on the promissory note. R.145.

4. The Transfer was of Substantially All of the Debtor's Assets. Between October 1, 1988 and February 17, 1989 all of Johnson's assets were transferred to Sear-Brown. R.1814, 1815.

5. The Value of the Consideration Received by the Debtor was Not Reasonably Equivalent to the Value of the Asset Transferred. The jury was presented with evidence that Johnson did not receive equivalent value for its assets. Sear-Brown alleged a debt owed by Johnson of \$797,000, and the transfer of

\$415,000 in assets. However, \$365,000 of this "debt" was accompanied by Sear-Brown's acquisition of 40% of Johnson's stock. The note supposedly reflecting this "loan" was never demanded, interest was never charged and security was never given. R.1788, 1789, 1819. The jury could infer that this was not a loan, but rather an acquisition of stock: it was pointed out that, two years later, Sear-Brown acquired another 26% of the stock for \$200,000. R.1796, 1797.

In addition, another \$230,000 of the cash transferred to Sear-Brown was admittedly applied to retire stock and had absolutely nothing to do with repayment of debt. R.1905, 1906; Exhibit 55. At that time, § 16-10-42 (now repealed) provided that distribution of assets to shareholders was allowed, provided: "No such distribution shall be made at the time when the corporation is insolvent or when such distribution would render the corporation insolvent." The \$230,000 transfer to Sear-Brown on account of a stock interest was, *ipso facto*, a fraudulent conveyance and probative evidence that all the transfers were made with proscribed intent.

No value whatsoever was assigned by Sear-Brown to Johnson's transfer of its existing client base, bad receivables tax write-off, or ongoing business contracts: yet Sear-Brown admitted its motive was to continue Johnson's resort design business in Salt Lake City. R.1913, 1914. Accordingly, the jury

was entitled to disregard Sear-Brown's valuations and was justified in inferring intent to hinder, delay or defraud.

6. The Debtor was Insolvent when the Transfers Occurred.

At the time of the transfers, Johnson's liabilities exceeded its assets by the amount of \$499,000. R.1887, 1888.

Considering these few listed statutory factors alone, there is more than ample evidence of defendants' actual intent. There was substantial additional evidence of Johnson's intent to hinder, delay and defraud Selvage, not the least of which was Johnson's waiting almost six years before conceding its obligations to Selvage at trial, and paying all other creditors except Selvage. From at least October 1988 onward, Sear-Brown was in control of Johnson's efforts to avoid payment to Selvage.

With or without viewing the evidence in a light most favorable to Selvage, there is ample evidence of Johnson's intent to hinder, delay or defraud Selvage, as well as Sear-Brown's complicity. The record precludes overturning the jury's verdict and the trial court's independent finding.

IV. INSTRUCTIONS 34 AND 35 WERE PROPER, OR HARMLESS ERROR.

A. Sear-Brown's Objections To Jury Instructions Were Not Preserved.

Sear-Brown placed certain objections to the jury instructions into the record (R.02060-61) shortly before the instructions were read to the jury, but neither the trial judge

nor Selvage's counsel was present.<sup>17/</sup> Selvage was thereby deprived of the opportunity to address those objections. More importantly, the private oration neither requested the court, nor gave it any opportunity, to correct any perceived error before the jury retired to deliberate. Objections serve no purpose if not brought to the Court's attention, and are not for solely setting up an appeal. See *Hill v. Cloward*, 377 P.2d 186 (Utah 1962).

In addition, the overly general and broad objections read into the record (R.02060) are inadequate to preserve the objections for appeal. *Beehive Medical Electric, Inc. v. Square D Company*, 669 P.2d 859 (Utah 1983).

**B. The Jury Was Correctly Instructed.**

Sear-Brown's brief (p.28 and pp. 2-3) erroneously challenges Instructions 34 and 35 with respect to finding actual intent to hinder, delay or defraud creditors. Instruction 35 (R.816), however, was correctly taken from the Utah Corporations Code<sup>18/</sup> which prohibits an insolvent corporation from distributing assets to its shareholders on account of their stock

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<sup>17/</sup> The transcript (R.02059A-61) does not expressly reflect who was present. It does show, however, that the objections were not acknowledged by the judge or Selvage's counsel. Selvage does not expect Sear-Brown to deny that its objections were read to the reporter in private. Selvage's counsel did notice Sear-Brown's private statements to the reporter by chance, but only in time to hear the last few sentences.

<sup>18/</sup> Section 16-10-42, as effective on the date of the transfer, now repealed.

*interests.* That instruction of statutory law was specifically warranted by admissions in Sear-Brown's trial testimony that

interests. That instruction of statutory law was specifically warranted by admissions in Sear-Brown's trial testimony that \$230,000 of Johnson's assets were transferred on account of Sear-Brown's "investment" and "not a repayment of debt." (Exhibit 55; R.01905-06, emphasis added). Sear-Brown's acceptance of transfers on account of its equity investment was significant evidence of actual intent to hinder and defraud, and was not a "mere preference." The jury could also infer that the \$365,000 unsecured, no interest, "loan" was actually equity.

Similarly, Instruction 34 (R.815) states that the fiduciary duty of directors of an insolvent corporation shifts from the stockholders to creditors, and that the directors cannot prefer themselves or other creditors. Under the Corporations Code, the duty of the directors in distributing assets clearly shifts to creditors ahead of stockholders. With respect to preferring Sear-Brown as one creditor over Selvage, the transfer (on the date thereof) was specifically proscribed by Utah Code § 25-6-6(2). Hence, Selvage's Proposed Additional Findings of Fact, Conclusions of Law and Order (R.01297) to the trial court stated:

Under the Utah Corporations Code and the Utah Fraudulent Transfer Act, Instructions 34 and 35 were properly given in the context of this case. While Utah law does not per se prohibit preferential transfers, such transfers are avoidable when they violate the specific provisions of the Utah Corporation Code and the Fraudulent Conveyance [sic Transfer] Act.

(Emphasis added). Shortly thereafter, the trial court issued its April 14, 1994 Findings and Conclusions (R.01293), agreeing that

"Instructions 34 and 35 were properly given **in the context of this case.**" (Emphasis added). The trial court was correct. Even though general preferences to outside creditors may not be avoidable, the jury wrestling with Sear-Brown's actual intent to hinder, delay or defraud Selvage was entitled to know that this particular transfer was statutorily proscribed on the date it was affected. Even if the preference claim under § 25-6-6(2) was time-barred, its statutory proscription at the time of transfer was material to the jury's determination of actual intent under § 25-6-5(1)(a). See also § 25-6-5(2)(a).

Moreover, Sear-Brown's brief omits the fact that Instruction No. 28 expressly instructed the jury that a transfer "is not fraudulent merely because the transferor prefers one creditor over another", and that Johnson's transfer to Sear-Brown "was not fraudulent merely because the company had insufficient assets to pay all creditors, including the plaintiffs." (R.806). Sear-Brown's suggestion that the jury ignored those express instructions is without foundation. The instructions must be read as a whole, and Sear-Brown's reference to Instruction Nos. 34 and 35, without Instruction No. 28, misstates the record.

**C. Any Error In Instructions 34 and 35 Were Immaterial and Harmless.**

Ultimately, the judgment below was rendered on the findings and conclusions of the trial court, not on the jury's verdict. The January 13, 1994 Memorandum Decision stated, "The foregoing



Findings of Fact were triable by the jury. To the extent any of the foregoing Findings of Fact were issues for the court, **the court adopts the findings of the jury as its own.**"

(R.01130) (emphasis added). In a later hearing, the trial court described the jury in this case as "advisory."<sup>19/</sup>

That ruling by the trial court itself, and the treatment of the jury as advisory, moots Sear-Brown's appeal on the jury instructions. Even if Instructions 34 or 35 could have confused a jury, prejudicial error does not occur when the jury is (or is treated as) advisory. *Kesler v. Rogers*, 542 P.2d 354 (Utah 1975). See also *Romrell v. Zions First National Bank*, 611 P.2d 392 (Utah 1980). While Sear-Brown's brief (p.28) contends that a jury may have been confused by Instructions 34 and 35, Sear-Brown never attempts to argue that the trial court failed to keep separate its respective analyses of the insider preference claim and the claims for actual intent to hinder, delay or defraud.

**V. JOHNSON WAS THE MERE INSTRUMENTALITY OF SEAR-BROWN WHEN SEAR-BROWN STRIPPED JOHNSON OF ITS ASSETS.**

Sear-Brown is liable for Selvage's judgment and claims against Johnson because, at the time all the assets of Johnson were transferred to Sear-Brown, Johnson was a mere

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<sup>19/</sup> Hearing of May 11, 1994 (R.02154-55). Selvage contends that all issues were triable by the jury because a money judgment was sought, and briefed that issue to the trial court. (R.00875-880). Nevertheless, given the trial court's independent concurrence with the jury's findings in all respects, the proper role of the jury in this case is moot.

instrumentality of Sear Brown. *Steven v. Roscoe Turner Aeronautical Corp.*, 324 F.2d 157 (7th Cir. 1963), cited with approval by the Utah Supreme Court in *Chatterly v. Omnico*, 485 P.2d 667, n.3 (Utah 1971). In *Bernardin, Inc. v. Midland Oil Corp.*, 520 F.2d 771, 774 (7th Cir. 1975), the court restated the well-established principle of law that "the parent corporation will be responsible for the obligations of its subsidiary when...the subsidiary has become its mere instrumentality." *Id.*

To establish liability through the mere instrumentality theory, three elements must be proved. First, the parent must control the subsidiary "to such a degree that the subsidiary has become its mere instrumentality." *Id.* at 774. Second, the parent must have perpetrated a wrong through its subsidiary such as by "stripping the subsidiary of its assets." *Id.* Finally, there must be an element of "unjust loss or injury to the claimant, such as insolvency of the subsidiary." *Id.* See also *Kelley v. American Precision Industries, Inc.*, 438 So.2d 29, 31 (Fla. App. 5 Dist. 1983); *CM Corp. v. Oberer Development Co.*, 631 F.2d 536, 538 (7th Cir. 1980); *Northern Illinois Gas Co. v. Total Energy Leasing Corp.*, 502 F.Supp. 412, 416 (N.D. Ill. 1980).

The record fulfills each of those elements: Sear-Brown had total control of Johnson on the transfer dates, Sear-Brown committed a wrong by stripping Johnson of its assets, and that wrong unjustly injured Selvage because it left Johnson with no

assets and no ability to pay its liabilities to Selvage. These three elements will be discussed in detail.

**A. Control.** Courts applying the mere instrumentality theory have listed several elements that indicate control of a subsidiary. The "proper combination" of these factors is controlling; each of them need not be met. *Northern Illinois Gas*, 502 F.Supp. at 419. As of the transfer dates, ten of the most relevant factors were clearly present:<sup>20/</sup>

(1) "The parent corporation owns all or most of the capital stock of the subsidiary." *Turner Aeronautical*, 324 F.2d at 161. When Johnson's assets were transferred to Sear-Brown, Sear-Brown owned all of the stock of Johnson.

(2) "The parent and subsidiary corporations have common directors or officers." *Id.* At the time of the transfer, all the directors of Johnson were agents of Sear-Brown.

(3) "The parent corporation finances the subsidiary." *Id.* Sear-Brown had financed Johnson through a "loan," stock purchase, and settlement agreement.

(4) "The parent corporation subscribes to all the capital stock of the subsidiary...." *Id.* At the time of the asset transfer, Sear-Brown owned all of Johnson's stock.

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<sup>20/</sup> The factors indicating control are quoted here from *Turner Aeronautical*, 324 F.2d at 161. *Turner Aeronautical's* recitation of these factors has been generally adopted by courts considering this theory. See *Bernardin*, 520 F.2d at 775; *Oberer Development*, 631 F.2d at 539.

(5) "The subsidiary has grossly inadequate capital." *Id.* From the moment of Sear-Brown's first involvement, Johnson was undercapitalized. Sear-Brown took all of Johnson's assets by assignment, leaving it without any capital at all, without any business operation, and ultimately in a liquidating Chapter 7 bankruptcy.

(6) "The parent corporation pays the salaries and other expenses or losses of the subsidiary." *Id.* During the transfer period all of Johnson's liabilities were paid, with the simple exception of the liabilities to Selvage. During the transfer period, Johnson had no employees.

(7) "In the papers of the parent corporation or in the statements of its officers, the subsidiary is described as a department or division of the parent corporation, or its business or financial responsibilities referred to as the parent corporation's own." *Id.* Prior to the asset transfer, Sear-Brown told the media that the Sear-Brown Group, Inc.'s relationship with Johnson was one of "merger." In January 1989, Sear-Brown used letterhead describing itself "formerly J.J. Johnson and Associates." At trial, Sear-Brown's president described an "acquisition by default."

(8) "The parent corporation uses the property of the subsidiary as its own." After September 30, 1988 Sear-Brown treated all of Johnson's assets as its own.

(9) "The directors or executives of the subsidiary do not act independently in the interest of the subsidiary but take their orders from the parent corporation in the latter's interest." *Id.* The directors and officers of Johnson acted in the interest of Sear-Brown rather than Johnson. Johnson's directors and officers stripped Johnson of all of its assets to pay Sear-Brown (some on account of stock rather than debt), waited a year to avoid preferential transfer liability, then put Johnson in Chapter 7. These actions of Johnson's officers and directors can hardly be characterized as "act[ing] independently in the interest of" Johnson. *See id.*

(10) "The formal legal requirements of the subsidiary are not observed." *Id.* Sear-Brown admitted taking some of the transfers on account of stock rather than debt.

Those ten factors are manifestly sufficient to support the finding that, at the time of the asset transfers, Sear-Brown had complete control to the point that Johnson had become its mere instrumentality. *See Northern Illinois Gas*, 502 F.Supp. at 419 & n. 12 (not all factors need be present to support finding of control; nine out of eleven is sufficient); *Bernardin*, 520 F.2d at 775 (eight is enough). Thus, the first prong of the mere instrumentality theory was supported by the evidence in this case.

**B. Wrong by Stripping Assets.** The second prong of the mere instrumentality theory is the presence of a "fraud or wrong

by the parent through its subsidiary, e.g., torts, violation of a statute or stripping the subsidiary of its assets." *Turner Aeronautical*, 324 F.2d at 160 (emphasis added). Obviously, this prong of the test is met in this case. By the time Sear-Brown was finished with Johnson, everything from work in progress to paper clips had been stripped clean.

C. **Unjust Loss or Injury.** The final prong is "unjust loss or injury to the claimant, such as insolvency of the subsidiary." *Id.* (emphasis added). Johnson's insolvency is undisputed, and Johnson's bankruptcy petition listed its assets at zero. As part of the asset stripping, Sear-Brown received at least \$230,00 on account of its stock investment. In contrast, Selvage as a creditor received nothing.

The facts of this case squarely fit the legal requirements for the application of the mere instrumentality theory. At the time of the asset transfers which created the wrong (i.e., asset stripping), and during the bankruptcy which created the unjust loss to Selvage, Sear-Brown was in complete control of Johnson. In the factually similar case of *Bernardin v. Midland Oil Corporation*, 520 F.2d 771, 775 (7th Cir. 1975), the United States Court of Appeals for the Seventh Circuit reached the following conclusion:

The question then becomes, against whom should judgment be entered? Midland [the parent corporation] and Zestee [the subsidiary] are both corporations, but all of Zestee's stock is owned by Midland...The evidence introduced at the trial of this cause demonstrates that Zestee is no longer a

viable corporation. Midland, as the sole shareholder, directed one of its own officers to collect the insurance proceeds and sell the assets of Zestee. This was done, and the cash received on liquidation of the assets has been paid to other creditors. To permit Midland to escape Zestee's creditors by retaining Zestee as a shell would clearly be inequitable and unjust. Factors such as the stock ownership and the decision to liquidate and maintain a shell establish a situation where the corporate veil should be pierced...Therefore, the Court finds that Midland and Zestee are in essence one and the same, and that each [is] liable for the amount due Bernardin.

*Id.* (quoting the opinion of the district court).

That passage from *Bernardin*, with a few name changes, could have been written about the case before this Court. Sear-Brown, as the sole shareholder of Johnson, directed its officers, who also were officers of Johnson, to liquidate Johnson's assets and pay them to itself and to Johnson's other creditors with the sole exception of Selvage. This left Johnson as an empty, bankrupt shell from whom Selvage could get no satisfaction on his contractual claim or his judgment. Sear-Brown's "stock ownership [of Johnson] and the decision to liquidate and maintain a shell establish a situation where the corporate veil should be pierced." *Id.* Therefore, just as the *Bernardin* court found, the jury and trial court were justified by the evidence in finding Sear-Brown and Johnson were "in essence one and the same and that each [is] liable for the amount due" Selvage. *Id.*

Sear-Brown argues that the jury's responses to Special Interrogatories Nos. 6 and 7 (R.824, 825) under Instruction 36 (R.817) on alter ego somehow absolved it of liability under mere

instrumentality. Jury Instruction No. 33 (R.814) separately advised the jury of the mere instrumentality doctrine, and Special interrogatory No. 5 (R.823) separately asked the jury whether "at the time the assets were transferred" Johnson had become a mere instrumentality of Sear-Brown, whether Sear-Brown stripped Johnson of its assets, and whether this created an unjust loss or injury to Selvage. The unanimous jury said yes.<sup>21/</sup>

Unlike the mere instrumentality directions, the instruction and special interrogatory on alter ego did not direct the jury to "the time the assets were transferred, or, for that matter, to any time period." Rather blatantly, Sear-Brown's evidence and argument explicitly dealt only with the period before the transfers occurred. Perhaps the best example of this dichotomy was Sear-Brown's counsel's statement to Sear-Brown's president, Mr. Clary, while inquiring into the association between Johnson and Sear-Brown:

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<sup>21/</sup> Although not addressed in Sear-Brown's brief, the jury reached its verdict in light of Instruction No. 32 (R.811) which required the jury to find "total domination" before it could find Sear-Brown liable under the mere instrumentality doctrine. Instruction No. 32 specified facts which "standing alone" would not establish sufficient control. (See also Instruction No. 27, R.805). Thus, the jury was appropriately instructed. Moreover, at trial, Sear-Brown objected to Instruction No. 33 on the basis that the mere instrumentality doctrine is not a basis for liability, but Sear-Brown did not object to how Instructions Nos. 32 and 33 were worded and put to the jury. See R.2060.



Q. Prior to the time the assets were transferred -- and all my questions are directed to this -- did Sear-Brown, for example, impose its vehicle policy on J.J. Johnson and Associates?

(R.1873) (emphasis added).

Later in the testimony, Sear-Brown's counsel inquired of Mr. Bruce Erickson as to his employment by Johnson. But again these questions only went through September 30, 1988, before any transfers occurred and before Sear-Brown had total control of Johnson. On cross-examination, Mr. Erickson admitted that during the period of transfers, he was an employee of Sear-Brown (rather than of Johnson). R.2192, 2193.

Special Interrogatory No. 5 and Instruction No. 33 for the mere instrumentality theory on which Salvage prevailed were both expressly directed to the period when the transfers occurred. In contrast, neither Instruction No. 36 nor Special Interrogatories Nos. 6 or 7 on alter ego directed the jury to the period when the transfers occurred. Based on the different time periods and cases presented, the verdicts and court findings on alter ego and mere instrumentality were not inconsistent or contradictory. The jury and court found that during the pre-September 30, 1988 period that Sear-Brown's counsel tried, Johnson was not Sear-Brown's alter ego. Separately, the court and jury found that during the post-September 30, 1988 period that Salvage's counsel tried, Johnson was Sear-Brown's mere instrumentality.

VI. SELVAGE IS ENTITLED TO ALL OF ITS ATTORNEYS FEES AGAINST SEAR-BROWN

Sear-Brown's brief does not dispute the reasonableness or amount of Selvage's attorneys fees, but rather only challenges Selvage's entitlement to any attorneys fees. During seven and one-half years of litigation, Selvage incurred substantial legal fees in first pursuing breach of contract claims against J.J. Johnson, and then pursuing those same claims against Sear-Brown under mere instrumentality and fraudulent transfer.

Pursuant to the three contracts that were conceded at trial to have been breached, Selvage is entitled to attorneys fees incurred in any action "brought for the enforcement of [the agreements], or because of an alleged dispute, breach, default or misrepresentation in connection with any of the provisions of the [the agreements]." Sear-Brown incorrectly argues that liability for fees is limited to Johnson on the contract claims and does not extend to Sear-Brown.

Selvage is entitled to have his attorneys fees awarded against Sear-Brown, because:

- Recovery under the mere instrumentality doctrine (Special Interrogatory No. 5) places Sear-Brown directly in Johnson's shoes. Sear-Brown therefore is directly and contractually liable for those fees.
- Independently, Utah's Fraudulent Transfer Act, makes Sear-Brown statutorily liable for "**the amount necessary**

to satisfy the creditor's [Selvage's] claim" against Johnson. Utah Code Ann. § 25-6-9(2) (emphasis added).<sup>22/</sup> Selvage's claim against Johnson includes his attorneys fees, and was less than the amount of the fraudulent transfers. See *Id.* Moreover, given Johnson's fraudulent transfers of all its assets, the costs of prosecuting the fraudulent transfer claim were "necessary to satisfy" Selvage's claim.

In *W. Marvin Radney, et al. v. Clean Lake Forest Community Association, Inc.*, 681 S.W.2d 191 (Tex.App.Ct. 1984), the court awarded attorneys fees for both the underlying claim and establishing a fraudulent transfer. Radney involved a violation of a restrictive covenant for which a statute provided for attorneys fees. Just prior to trial, the defendant conveyed the subject property to a third party. The trial was continued to allow the plaintiffs to join the transferee of the property and

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<sup>22/</sup> Counsel for Sear-Brown argued below that if the actions against Johnson and Sear-Brown had been separate, entitlement to attorneys fees would have been terminated at the conclusion of the case against Johnson. Nothing could be further from the truth. Fees incurred in collection or satisfaction of a judgment are also recoverable. This is recognized not only by § 25-6-9(2), but also by Rule 4-505 of the Code of Judicial Administration [attorneys' fees affidavits] which provides for the following language in default judgments:

"And it is further ordered that this judgment shall be augmented in the amount of reasonable costs and attorney's fees expended in collecting said judgment by execution or otherwise as shall be established by affidavit."

to state claims under the fraudulent conveyance act. The jury found that the conveyance was intended to "hinder or delay" plaintiffs from obtaining the requested relief. Attorneys fees were awarded against both the transferor and the transferee.

On appeal, the defendants argued that plaintiffs had to distinguish between the attorneys fees incurred on the fraudulent conveyance cause of action and those incurred on the underlying action on the restrictive covenant. Rejecting this argument, the court ruled as follows:

Appellants believe that, under the statute, appellees could not recover for legal services rendered in relation to the fraudulent conveyance cause of action. We disagree.

The statute allows the recovery of attorney's fees in an action based on a restrictive covenant. We believe that the fraudulent conveyance action was in part based on and related to the breach of the restrictive covenant. The home had been conveyed by appellants, shortly prior to trial, to a foreign corporation. **In order to obtain the complete relief to which they were entitled because of the breach, it was necessary for appellees to have the fraudulent conveyance voided. The fraudulent conveyance action would not have been necessary if appellants had not conveyed the property in order to avoid the suit to enforce the restriction. In this situation, the entire suit was based on the breach of the restriction.**

681 S.W.2d at p. 199 (emphasis added).

Sear-Brown's citation to *Cottonwood Mall Co. v. Sine*, 830 P.2d 266 (Utah 1992) is not to the contrary. *Cottonwood Mall* stands only for the proposition that a request for fees must distinguish between work that was subject to a fee award and work that was not:

"One who seeks an award of attorney fees must set out the time and fees expended for (1) successful claims for which there may be an entitlement to attorney fees, (2) unsuccessful claims for which there would have been an entitlement to attorney fees had the claims been successful, and (3) claims for which there is no entitlement to attorney fees."

at. p. 269, 270. *Cottonwood Mall* does not address whether fees incurred in avoiding a fraudulent transfer in satisfying a breach of contract claim are recoverable. Thus, there is simply no inconsistency between *Radney* and *Cottonwood Mall*. *Radney* addresses the question of what fees are recoverable; *Cottonwood Mall* addresses the question of allocation if it has already been determined that all fees are not recoverable.

After trial, both the jury and the court found for Selvage on every theory except alter ego. (Unconscionability was originally pleaded but not litigated.) That unsuccessful alter ego theory, however, involved the same operative facts, evidence and damages that were actually awarded under the successful theories of mere instrumentality and fraudulent transfer. Hence, failure of the alter ego theory did not require allocation of fees as contended by Sear-Brown because it did not affect the presentation of Selvage's case, Selvage's right to judgment, or the amount of judgment. Furthermore, to the extent the jury did not award one item of damage that was claimed under all of his theories (compare Instruction No. 26, R.804 with Interrogatory No. 1, R.819), Selvage offered to put on testimony for any needed allocation. The trial court, however, ruled without granting the

requested hearing. (The effort to claim that single damage item represented less than 1/10th of 1% of the fees incurred.) Selvage's request for, and right to, that hearing are discussed in his opening brief.

Sear-Brown speculates that the trial court reached the grossly reduced fee award of \$42,500 by estimating the amount expended by Selvage on the contract claim alone. That speculation, however, does violence to the actual judgment that both Johnson and Sear-Brown are liable for the \$42,500 fee award. Particularly in light of the trial court's failure to enter findings and conclusions on the fee award, the only reasonable interpretation of the trial court's rulings is that Selvage's \$175,000.00 fee request was slashed to \$42,500 for unexplained reasons. See *Regional Sales Agency, Inc. v. Reichert*, 784 P.2d 1210 (Utah App. 1989), vacated on other grounds, 830 P.2d 252 (Utah 1992) same counsel; same judge; same reduction).

#### **RELIEF SOUGHT**

Sear-Brown's cross-appeal on liability should be dismissed. The attorneys fee portion of the judgment should be remanded in the manner requested in Selvage's opening brief.

DATED this 26<sup>th</sup> day of May, 1995.



Anthony L. Rampton  
Robert Palmer Rees  
FABIAN & CLENDENIN,  
a Professional Corporation  
Attorneys for Appellants/Cross-  
Appellees

**CERTIFICATE OF SERVICE**

I hereby certify that on this 26<sup>th</sup> day of May, 1995, I caused to be hand delivered a true and correct copy of the APPELLANTS/CROSS-APPELLEES WILLIAM C. SELVAGE AND WM.C. SELVAGE, INC.'S RESPONSE TO BRIEF OF APPELLEES/CROSS-APPELLANTS SEAR-BROWN ASSOCIATES, P.C. AND THE SEAR-BROWN GROUP, INC. to the following:

James A. Boevers, Esq.  
Prince, Yeates & Geldzahler  
City Centre I, Suite 900  
175 East 400 South  
Salt Lake City, Utah 84111



## **ADDENDUM**



Tab A

## Rule 9. Pleading special matters

(h) **Statute of limitations.** In pleading the statute of limitations it is not necessary to state the facts showing the defense but it may be alleged generally that the cause of action is barred by the provisions of the statute relied on, referring to or describing such statute specifically and definitely by section number, subsection designation, if any, or otherwise designating the provision relied upon sufficiently clearly to identify it. If such allegation is controverted, the party pleading the statute must establish, on the trial, the facts showing that the cause of action is so barred.

**Tab B**

Jury Instruction 22

The jury is instructed that defendant J. J. Johnson & Associates failed to appear in this lawsuit and failed to mount a defense in this lawsuit. The court, therefore, directs that defendant J. J. Johnson & Associates is liable to plaintiffs for breach of the Asset Purchase Agreement, Independent Consulting Agreement, and the Addendum to the Independent Consulting Agreement. It is, however, within the province of the jury to determine the amount of damages to be awarded plaintiffs arising from defendant J. J. Johnson & Associates breach of those agreements.

The court also wishes to inform the jury that counsel for Sear-Brown did not represent J. J. Johnson & Associates in this lawsuit and is in no way responsible for the court's entry of a directed verdict as to J. J. Johnson & Associates liability for the breach of the agreements.

Jury Instruction 26

The plaintiffs claim that as a result of the defendants' failure to perform the defendants obligation under the contract, the plaintiffs suffered loss in one or more of the following respects:

UNPAID TIME AND EXPENSES UP TO FEB. 1, 1987	\$22,015.82
ADDITIONAL UNPAID REIMBURSEABLES / COSTS AFTER FEB.1, 1987	\$ 1,865.50
BALANCE OF UNPAID CONSULTING AGREEMENT:	
CONSULTING SERVICES	\$37,500.00
FIVE MONTHS RENT	\$ 2,500.00
FIVE MONTHS OFFICE EXPENSES	\$ 2,500.00
SIX MONTHS MED. INSURANCE	\$ 1,500.00
UNPAID ASSET PURCHASE NOTE	\$25,000.00
UNREIMBURSED AUGUST EXPENSES	\$ 9,650.00
LOSS ON SALE OF IBM STOCK	\$22,500.00
TAXES ON STOCK "GAIN"	\$ 7,000.00
	<hr/>
TOTAL	\$132,031.32

Jury Instruction 27

The degree to which a parent owns stock in its subsidiary or shares officers or directors with it, or files a joint tax return, or loans money to the subsidiary do not, in and of themselves, defeat the separate existence of the corporations so as to allow a parent corporation to be held liable for the debts of a subsidiary.

Jury Instruction 28

A transfer of property is not fraudulent merely because the transferor prefers one creditor over another. In this case, the transfer of J. J. Johnson & Associate's assets to the Sear-Brown Group and/or Sear-Brown Associates was not fraudulent merely because the company had insufficient assets to pay all creditors, including the plaintiffs. It is not the intent of the fraudulent transfer laws to provide equal distribution of the assets to creditors nor to compel a debtor to choose among its creditors.

This general rule does not apply, however, if the transfer was a fraudulent transfer.

## Jury Instruction 29

Under the Utah Uniform Fraudulent Transfer Act, a transfer of assets from a debtor corporation is fraudulent if it is shown, by a preponderance of the evidence, that the transfer was made with actual intent to hinder or delay any creditor of the debtor corporation, or when it is shown by clear and convincing evidence that the transfer was made with actual intent to defraud any creditor of the debtor corporation.

To determine whether the transfer was made with "actual intent to hinder, delay, or defraud," consideration may be given, among other factors, to whether:

- yes A. the transfer was to an insider (for purposes of the Utah Fraudulent Transfer Act, the term "insider" includes any shareholder who owns 20% or more of the outstanding voting securities of the debtor, or a corporation in control of the debtor);
- B. the debtor retained possession or control of the property transferred after the transfer;
- for transfer 1/2 C. the transfer or obligation was disclosed or concealed;
- yes D. before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;
- yes E. the transfer was of substantially all the debtor's assets;
- no F. the debtor absconded;
- ? G. the debtor removed or concealed assets;
- ? H. the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;



- I. <sup>yes</sup> the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;
- J. ~~yes~~ <sup>no</sup> the transfer occurred shortly before or shortly after a substantial debt was incurred; and
- K. <sup>no</sup> the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

Not all of these factors need to be present to prove actual intent to hinder, delay, or defraud. These factors are only guidelines, and you may consider other factors present in the case.

Jury Instruction 30

Under the Utah Uniform Fraudulent Transfer Act, a transfer of assets from a debtor corporation is fraudulent if it is shown, by a preponderance of the evidence, that:

- the assets were transferred to an insider for the purpose of satisfying a debt which the debtor owed to the insider (for purposes of the Utah Fraudulent Transfer Act, the term "insider" includes any shareholder who owns 20% or more of the outstanding voting securities of the debtor, or a corporation in control of the debtor corporation);

- and that, at the time the assets were transferred, the debtor was insolvent;

- and that the insider had reasonable cause to believe that the debtor was insolvent at the time of the transfer.

For purposes of this instruction, a debtor is "insolvent" if, at the time of the transfer, the debtor's liabilities exceeded its assets.

Jury Instruction 31

If a transfer is found to be fraudulent under the Utah Uniform Fraudulent Transfer Act, the plaintiff may recover damages from the transferee up to the amount of the value of the assets which were transferred.

For purposes of setting a value on the assets that were transferred, you may include the transferor's physical assets, cash, work in progress, accounts receivable, good will, and client lists.

Jury Instruction 32

Sear-Brown Associates and/or Sear-Brown Group may be held liable for the debts of J. J. Johnson & Associates, if you find that it misused J. J. Johnson & Associates by treating it, and by using it, as a mere business conduit for its own purposes. In making the determination of whether Sear-Brown Associates and/or Sear-Brown Group are liable to the plaintiff, you must consider two elements.

First, did Sear-Brown Associates and/or Sear-Brown Group control J. J. Johnson & Associates to the degree necessary to make J. J. Johnson & Associates a mere instrumentality as defined in these instructions, and

Second, Sear-Brown Associates and/or Sear-Brown Group must have proximately caused plaintiff harm through misuse of that control.

The fact that Metro Equipment held an ownership interest in J. J. Johnson & Associates does not, standing alone, resolve the question of whether Sear-Brown Associates and/or Sear-Brown Group had control of J. J. Johnson & Associates.

Similarly, the fact that a creditor/debtor relationship existed between J. J. Johnson & Associates and Metro Equipment and Sear-Brown Associates does not, standing alone, constitute control necessary to establish liability.

Generally, the mere loan of money from one corporation to another does not automatically make the lender liable for actions and omissions of the borrower.

In order for Sear-Brown Associates and/or Sear-Brown Group to be liable for the debts or obligations of J. J. Johnson & Associates, you must find proof that Sear-Brown Associates and/or Sear-Brown Group assumed actual, participatory, total control of J. J. Johnson & Associates; its merely taking an active part in the management of J. J. Johnson & Associates does not automatically constitute such control.

The degree of control required before Sear-Brown Associates and/or Sear-Brown Group can be found liable for the debts or obligations of J. J. Johnson & Associates amounts to total domination of J. J. Johnson & Associates, to the extent that J. J. Johnson & Associates manifests no separate corporate interest of its own and functioned solely to achieve the purposes of Sear-Brown Associates and/or Sear-Brown Group.

Jury Instruction 33

A successor corporation is liable for the debts and obligations of a predecessor corporation if it is shown, by a preponderance of the evidence, that the predecessor corporation was a "mere instrumentality" of the successor corporation and that the successor stripped the predecessor of its assets, causing an unjust injury or loss to the plaintiff.

A predecessor corporation is the "mere instrumentality" of the successor if it is shown by a preponderance of the evidence that, at the time of the asset transfer, that most, but not all, of the following factors were present:

- A. That the successor corporation owned all or most of the capital stock of the predecessor corporation; *yes*
- B. That the two corporations had common directors or officers; *yes*
- C. That the successor corporation financed the predecessor corporation; *yes*
- D. That the parent corporation subscribed to all the capital stock of the subsidiary or otherwise caused its incorporation; *yes*
- E. That the predecessor corporation had grossly inadequate capital so that it was unable to continue operation; *yes*
- F. That the successor corporation paid the salaries and other expenses or losses of the predecessor corporation; *yes*
- G. That in the statements and writings of the successor corporation's officers, the predecessor corporation was described as a department or division of the successor corporation or the predecessor corporation's business or financial responsibilities were referred to as belonging to the successor; *no*

- H. That the successor used the property of the predecessor as its own; and, *yes*
- I. That the executives of the predecessor did not act independently ~~in the independently~~ in the interest of the predecessor, but rather took their orders from the successor. *yes*
- J. J.J. Johnson had substantially no business except with the Sear-Brown Group and/or Sear-Brown Associates or no assets except those conveyed to it by the Sear-Brown Group and/or Sear-Brown Associates. *No*

Jury Instruction 34

When a corporation becomes insolvent, the fiduciary duty of the directors shifts from the stockholders to the creditors of the corporation. When a corporation becomes insolvent, or in a failing condition, the officers and directors no longer represent the stockholders, but by the fact of insolvency, become trustees for the creditors. The officers and directors of the insolvent corporation cannot by transfer of the corporation's property prefer themselves or other creditors.



Jury Instruction 35

A corporation may not distribute all or a portion of its assets to shareholders, on account of their stock interests, if the corporation (i) is then insolvent, or (ii) would thereby be rendered insolvent.

A corporation's distribution of assets to shareholders on account of their stock interest during insolvency is a fraudulent transfer.

Jury Instruction 36

Ordinarily, a corporation is regarded as a separate and distinct entity from its stockholders. This is true whether the corporation has many stockholders or only one. Consequently, the corporate veil which protects stockholders from liability for corporate debt will only be pierced reluctantly and cautiously.

To disregard the corporate entity under the equitable "alter ego" doctrine, two circumstances must be shown:

1. Such a unity of interest and ownership that the separate personalities of the corporation and the shareholder(s) no longer exists, but the corporation is, instead, the alter ego of its stockholder(s); and
2. If observed, the corporate form would sanction a fraud, promote injustice, or result in an inequity.

The plaintiff need not prove actual fraud, but must only show that failure to pierce the corporate veil would result in an injustice.

Certain factors are deemed significant, but not conclusive, in determining whether the foregoing test has been met, including:

- a. undercapitalization of a one-man corporation,
- b. failure to observe corporate formalities,
- c. nonpayment of dividends,
- d. siphoning of corporate funds by the dominant shareholder,
- e. nonfunctioning of other officers or directors,

- f. the use of the corporation as a facade for operations of the dominant stockholder or stockholders,
- g. the use of the corporate entity in promoting injustice or fraud.

Tab C

OCT 08 1993

Special Interrogatory 1

By Mary G. Badian  
SALT LAKE COUNTY  
Deputy Clerk

Indicate the amounts, if any, of damages you find plaintiffs incurred as a result of J. J. Johnson & Associates' breach of the Asset Purchase Agreement, the Independent Consulting Agreement and its Addendum.

A. UNPAID TIME AND EXPENSES UP TO FEB. 1, 1987:	\$ <u>22015.82</u>
B. ADDITIONAL UNPAID REIMBURSEABLES & COSTS AFTER FEB. 1, 1987	\$ <u>1865.50</u>
C. BALANCE OF UNPAID CONSULTING AGREEMENT:	
CONSULTING SERVICES	\$ <u>37500.00</u>
FIVE MONTHS RENT	\$ <u>2500.00</u>
FIVE MONTHS OFFICE EXPENSES	\$ <u>2500.00</u>
SIX MONTHS MED. INSURANCE	\$ <u>1500.00</u>
D. UNPAID ASSET PURCHASE NOTE	\$ <u>25000.00</u>
E. UNREIMBURSED AUGUST EXPENSES	\$ <u>9650.00</u>
F. LOSS ON SALE OF IBM STOCK	\$ <u>0</u>
G. TAXES ON STOCK "GAIN"	\$ <u>7000.00</u>

TOTAL DAMAGES: \$ 109400.32

DATED this 8<sup>th</sup> day of October, 1993.

Harold W. Ray  
Foreperson

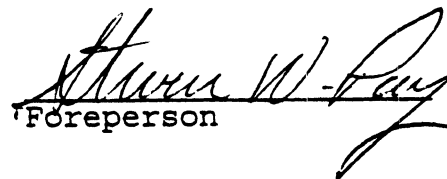
Special Interrogatory 2

Was it shown, by a preponderance of the evidence, that the transfer of J. J. Johnson & Associates' assets to Sear-Brown was made with actual intent to hinder or delay any creditor of J. J. Johnson & Associates?

Yes X

No \_\_\_\_\_

DATED this 8<sup>th</sup> day of October, 1993.

  
Foreperson

Special Interrogatory 3

Was it shown, by clear and convincing evidence, that the transfer of J.J. Johnson & Associates' assets to Sear-Brown was made with actual intent to defraud any creditor of J.J. Johnson & Associates?

Yes X

No \_\_\_\_\_

DATED this 8<sup>th</sup> day of October, 1993.

Steven W. Gay  
Foreperson

Special Interrogatory 4

Was it shown by a preponderance of the evidence that

- the transfer of J. J. Johnson & Associates, Inc.'s assets to Sear-Brown was made for the purpose of satisfying a debt which J. J. Johnson & Associates, Inc. owed to Sear-Brown;

-and, at the time the assets were transferred, Sear-Brown was an insider of J.J. Johnson & Associates, Inc.,

- and, at the time the assets were transferred, J. J. Johnson & Associates, Inc. was insolvent (its liabilities exceed its assets);

- and, that Sear-Brown had reason to believe that J. J. Johnson & Associates, Inc. was insolvent at the time of the transfer?

Yes X

No \_\_\_\_\_

DATED this 8<sup>th</sup> day of October, 1993.

  
Foreperson



Special Interrogatory 5

Was it shown by a preponderance of the evidence that the following factors were present?

1. That at the time the assets were transferred, Sear-Brown controlled J.J. Johnson & Associates, Inc. to such a degree that J.J. Johnson & Associates, Inc. had become a mere instrumentality of Sear-Brown.
2. That Sear-Brown stripped J.J. Johnson & Associates, Inc. of its assets.
3. That this created an unjust loss or injury to plaintiffs by making J.J. Johnson & Associates, Inc. insolvent.

Yes X

No \_\_\_\_\_

DATED this 8<sup>th</sup> day of October, 1993.

Steven W. Pay  
Foreperson

Special Interrogatory 6

Was it shown, by a preponderance of the evidence, that J. J. Johnson & Associates was the alter ego of Sear-Brown and that observation of the corporate distinction between J. J. Johnson & Associates and Sear-Brown would sanction a fraud, or promote injustice, or result in an inequity?

Yes \_\_\_\_\_

No X \_\_\_\_\_

DATED this 8<sup>th</sup> day of October, 1993.

Arthur W. Lay  
Foreperson

Special Interrogatory 7

Please answer the following questions based on a preponderance of the evidence, unless otherwise indicated. If you find the evidence preponderates in favor of the issue presented, answer "Yes." If you find the evidence is so equally balanced that you cannot determine a preponderance of the evidence, or if you find that the evidence preponderates against the issue presented, answer "No."

Taking into consideration all the evidence in this case, which if any, of the following propositions have been proved by a preponderance of the evidence? If a matter has been proven, answer "Yes," if it has not been proven, answer "No."

a) The Sear-Brown Group and/or Sear-Brown Associates owned all or most of the capital stock of J. J. Johnson.

Yes: X No: \_\_\_\_\_

b) The Sear-Brown Group or Sear-Brown Associates employed common directors or officers with J. J. Johnson.

Yes: X No: \_\_\_\_\_

c) The Sear-Brown Group and/or Sear-Brown Associates financed J. J. Johnson.

Yes: X No: \_\_\_\_\_

d) The Sear-Brown Group and/or Sear-Brown Associates created or caused the incorporation of J. J. Johnson.

Yes: \_\_\_\_\_ No: X

e) J. J. Johnson had grossly inadequate capital during its affiliation with the Sear-Brown Group and/or Sear-Brown Associates.

Yes: X No: \_\_\_\_\_

f) The Sear-Brown Group and/or Sear-Brown Associates paid the salaries and other expenses or losses of J. J. Johnson.

Yes: \_\_\_\_\_ No: X

g) J. J. Johnson had substantially no business except with the Sear-Brown Group and/or Sear-Brown Associates or no assets except those conveyed to it by the Sear-Brown Group and/or Sear-Brown Associates.

Yes: \_\_\_\_\_ No: X

h) In the papers of the Sear-Brown Group and/or Sear-Brown Associates, J. J. Johnson was described as a department or division of the Sear-Brown Group and/or Sear-Brown Associates.

Yes: \_\_\_\_\_ No: X

i) The directors and executives of J. J. Johnson did not act independently in the interest of J. J. Johnson but took their orders from the Sear-Brown Group and/or Sear-Brown Associates.

Yes: \_\_\_\_\_ No: X

j) The formal legal requirements of J. J. Johnson were not observed.

Yes: ~~\_\_\_\_~~ \_\_\_\_

No: X \_\_\_\_

DATED this 8<sup>th</sup> day of October, 1993.

Steven W. Ray  
Foreperson

Tab D

## COLLATERAL REFERENCES

Utah Law Review. — The Doctrine of Part Performance as Applied to Oral Land Contracts in Utah, 9 Utah L. Rev. 91.

Am. Jur. 2d. — 71 Am. Jur. 2d Specific Performance §§ 19, 20.

C.J.S. — 81 C.J.S. Specific Performance §§ 44, 45.

Key Numbers. — Specific Performance — 39 et seq.

**25-5-9. Agent may sign for principal.**

Every instrument required by the provisions of this chapter to be subscribed by any party may be subscribed by the lawful agent of such party.

History: R.S. 1898 & C.L. 1907, § 2478; C.L. 1917, § 5825; R.S. 1933 & C. 1943, 23-5-9.

## NOTES TO DECISIONS

Authorization from only one joint tenant.

Husband could not bind wife, who was joint tenant, by contract to purchase the common property since she had not signed the contract

nor given written authority to agent to sign for her. Williams v. Singleton, 723 P.2d 421 (Utah 1986).

## COLLATERAL REFERENCES

Am. Jur. 2d. — 72 Am. Jur. 2d Statute of Frauds § 379 et seq.

Key Numbers. — Frauds, Statute of — 116(1).

## CHAPTER 6

# UNIFORM FRAUDULENT TRANSFER ACT

Section		Section	
25-6-1.	Short title.	25-6-7.	Transfer — When made.
25-6-2.	Definitions.	25-6-8.	Remedies of creditors.
25-6-3.	Insolvency.	25-6-9.	Good faith transfer.
25-6-4.	Value — Transfer.	25-6-10.	Claim for relief — Time limits.
25-6-5.	Fraudulent transfer — Claim arising before or after transfer.	25-6-11.	Legal principles applicable to chapter.
25-6-6.	Fraudulent transfer — Claim arising before transfer.	25-6-12.	Construction of chapter.
		25-6-13.	Applicability of chapter.

**25-6-1. Short title.**

This chapter is known as the "Uniform Fraudulent Transfer Act."

History: C. 1953, 25A-1-1, enacted by L. 1988, ch. 59, § 1; recompiled as C. 1953, 25-6-1.

Comparable Provisions. — Other jurisdictions that have adopted the Uniform Fraudulent Transfer Act include: Arkansas, California, Florida, Hawaii, Idaho, Maine, Minnesota,

Nevada, New Hampshire, North Dakota, Oklahoma, Oregon, Rhode Island, South Dakota, Texas, Washington, and West Virginia.

Compiler's Notes. — This chapter was enacted as §§ 25A-1-1 to 25A-1-13; it has been renumbered and all internal references corrected accordingly under instruction from the

Office of Legislative Research and General Counsel.

**Effective Dates.** — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

**Cross-References.** — Uniform Commercial Code — Sales, § 70A-2-101 et seq.

Uniform Commercial Code — Bulk Transfers, § 70A-6-101 et seq.

Defrauding creditors as a misdemeanor, § 76-6-511.

Statute of limitations, § 78-12-26(3).

## 25-6-2. Definitions.

In this chapter:

(1) "Affiliate" means:

(a) a person who directly or indirectly owns, controls, or holds with power to vote, 20% or more of the outstanding voting securities of the debtor, other than a person who holds the securities:

(i) as a fiduciary or agent without sole discretionary power to vote the securities; or

(ii) solely to secure a debt, if the person has not exercised the power to vote;

(b) a corporation 20% or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by the debtor or a person who directly or indirectly owns, controls, or holds, with power to vote, 20% or more of the outstanding voting securities of the debtor, other than a person who holds the securities:

(i) as a fiduciary or agent without sole power to vote the securities; or

(ii) solely to secure a debt, if the person has not exercised the power to vote;

(c) a person whose business is operated by the debtor under a lease or other agreement, or a person substantially all of whose assets are controlled by the debtor; or

(d) a person who operates the debtor's business under a lease or other agreement or controls substantially all of the debtor's assets.

(2) "Asset" means property of a debtor, but does not include:

(a) property to the extent it is encumbered by a valid lien;

(b) property to the extent it is generally exempt under nonbankruptcy law; or

(c) an interest in property held in tenancy by the entireties to the extent it is not subject to process by a creditor holding a claim against only one tenant.

(3) "Claim" means a right to payment, whether or not the right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.

(4) "Creditor" means a person who has a claim.

(5) "Debt" means liability on a claim.

(6) "Debtor" means a person who is liable on a claim.

(7) "Insider" includes:

(a) if the debtor is an individual:

(i) a relative of the debtor or of a general partner of the debtor;

(ii) a partnership in which the debtor is a general partner;



- (iii) a general partner in a partnership described in Subsection (7)(a)(ii); or
  - (iv) a corporation of which the debtor is a director, officer, or person in control;
  - (b) if the debtor is a corporation:
    - (i) a director of the debtor;
    - (ii) an officer of the debtor;
    - (iii) a person in control of the debtor;
    - (iv) a partnership in which the debtor is a general partner;
    - (v) a general partner in a partnership described in Subsection (7)(b)(iv); or
    - (vi) a relative of a general partner, director, officer, or person in control of the debtor;
  - (c) if the debtor is a partnership:
    - (i) a general partner in the debtor;
    - (ii) a relative of a general partner in, a general partner of, or a person in control of the debtor;
    - (iii) another partnership in which the debtor is a general partner;
    - (iv) a general partner in a partnership described in Subsection (7)(c)(iii); or
    - (v) a person in control of the debtor;
  - (d) an affiliate, or an insider of an affiliate as if the affiliate were the debtor; and
  - (e) a managing agent of the debtor.
- (8) "Lien" means a charge against or an interest in property to secure payment of a debt or performance of an obligation, and includes a security interest created by agreement, a judicial lien obtained by legal or equitable process or proceedings, a common-law lien, or a statutory lien.
- (9) "Person" means an individual, partnership, corporation, association, organization, government or governmental subdivision or agency, business trust, estate, trust, or any other legal or commercial entity.
- (10) "Property" means anything that may be the subject of ownership.
- (11) "Relative" means an individual or an individual related to a spouse, related by consanguinity within the third degree as determined by the common law, or a spouse, and includes an individual in an adoptive relationship within the third degree.
- (12) "Transfer" means every mode, direct or indirect, absolute or conditional, or voluntary or involuntary, of disposing of or parting with an asset or an interest in an asset, and includes payment of money, release, lease, and creation of a lien or other encumbrance.
- (13) "Valid lien" means a lien that is effective against the holder of a judicial lien subsequently obtained by legal or equitable process or proceedings.

History: C. 1953, 25A-1-2, enacted by L. 1988, ch. 59, § 2; recompiled as C. 1953, 25-6-2.

Effective Dates. — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

## NOTES TO DECISIONS

## ANALYSIS

Creditors.  
Construction and application.  
Intent.

## Creditors.

Persons having claim in tort against grantor which was not reduced to judgment at time of alleged fraudulent conveyance held "creditor" within meaning of this section. *Zuniga v. Evans*, 87 Utah 198, 48 P.2d 513, 101 A.L.R. 532 (1935).

## Construction and application.

This section should be construed with liber-

ality so as to reach all artifices and evasions designed to rob the act of its full force and effect in preventing debtors from paying the just claims of their creditors. *Butler v. Wilkinson*, 740 P.2d 1244 (Utah 1987).

## Intent.

Where debtors engaged in a Ponzi scheme, the debtors' fraudulent intent was established as a matter of law, notwithstanding the bankruptcy trustee's burden of proving each element of a fraudulent conveyance by clear and convincing evidence under this chapter. *Merrill v. Abbott* (In re Independent Clearing House Co.), 77 Bankr. 843 (D. Utah 1987).

## COLLATERAL REFERENCES

Utah Law Review. — The Bankrupt's Spouse: The Forgotten Character in the Bankruptcy Drama, 1974 Utah L. Rev. 709, 722.

A.L.R. — Future tort, conveyance as fraudulent where made in contemplation of possible liability for, 38 A.L.R.3d 597.

Rule denying recovery of property to one who conveyed to defraud creditors as applicable where the claim which motivated the conveyance was never established, 6 A.L.R.4th 862.

Right of secured creditor to have set aside fraudulent transfer of other property by his debtor, 8 A.L.R.4th 1123.

Conspiracy, right of creditor to recover damages for conspiracy to defraud him of claim, 11 A.L.R.4th 345.

Key Numbers. — Fraudulent Conveyances — 5.

## 25-6-3. Insolvency.

(1) A debtor is insolvent if the sum of the debtor's debts is greater than all of the debtor's assets at a fair valuation.

(2) A debtor who is generally not paying his debts as they become due is presumed to be insolvent.

(3) A partnership is insolvent under Subsection (1) if the sum of the partnership's debts is greater than the aggregate, at a fair valuation, of all of the partnership's assets and the sum of the excess of the value of each general partner's nonpartnership assets over the partner's nonpartnership debts.

(4) Assets under this section do not include property that has been transferred, concealed, or removed with intent to hinder, delay, or defraud creditors or that has been transferred in a manner making the transfer voidable under this chapter.

(5) Debts under this section do not include an obligation to the extent it is secured by a valid lien on property of the debtor not included as an asset.

History: C. 1953, 25A-1-3, enacted by L. 1988, ch. 59, § 3; recompiled as C. 1953, 25-6-3.

Effective Dates. — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

## NOTES TO DECISIONS

## ANALYSIS

**Allegation of insolvency**  
**Determination of insolvency.**

**Allegation of insolvency.**

Allegation of insolvency in a complaint in an action to set aside a conveyance was sufficient as against contention that it was a conclusion. *Zuniga v. Evans*, 87 Utah 198, 48 P.2d 513, 101 A.L.R. 532 (1935).

**Determination of insolvency.**

The determination of insolvency under this section is not the same as the determination of

insolvency in the bankruptcy sense, as this section requires merely a showing that the party's assets are not sufficient to meet liabilities as they become due. *Meyer v. General Am. Corp.*, 569 P.2d 1094 (Utah 1977).

In an action by a creditor to set aside an allegedly fraudulent conveyance of real estate by a debtor, the plaintiff did not demonstrate that the debtor was insolvent where the only evidence was that the debtor submitted two checks that were returned unpaid. *Furniture Mfrs. Sales, Inc. v. Deamer*, 680 P.2d 398 (Utah 1984).

## COLLATERAL REFERENCES

**A.L.R. — Imputation of insolvency as defamatory**, 49 A.L.R.3d 163.

**Key Numbers. — Fraudulent Conveyances** — 57(1).

**25-6-4. Value — Transfer.**

(1) Value is given for a transfer or an obligation if, in exchange for the transfer or obligation, property is transferred or an antecedent debt is secured or satisfied. However, value does not include an unperformed promise made other than in the ordinary course of the promisor's business to furnish support to the debtor or another person.

(2) Under Subsection 25-6-5(1)(b) and Section 25-6-6, a person gives a reasonably equivalent value if the person acquires an interest of the debtor in an asset pursuant to a regularly conducted, noncollusive foreclosure sale or execution of a power of sale for the acquisition or disposition of the interest of the debtor upon default under a mortgage, deed of trust, or security agreement.

(3) A transfer is made for present value if the exchange between the debtor and the transferee is intended by them to be contemporaneous and is in fact substantially contemporaneous.

**History:** C. 1953, 25A-1-4, enacted by L. 1988, ch. 59, § 4; recompiled as C. 1953, 25-6-4.

**Effective Dates.** — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

**25-6-5. Fraudulent transfer — Claim arising before or after transfer.**

(1) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

(a) with actual intent to hinder, delay, or defraud any creditor of the debtor; or

(b) without receiving a reasonably equivalent value in exchange for the transfer or obligation; and the debtor:

- (i) was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
  - (ii) intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they became due.
- (2) To determine "actual intent" under Subsection (1)(a), consideration may be given, among other factors, to whether:
- (a) the transfer or obligation was to an insider;
  - (b) the debtor retained possession or control of the property transferred after the transfer;
  - (c) the transfer or obligation was disclosed or concealed;
  - (d) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;
  - (e) the transfer was of substantially all the debtor's assets;
  - (f) the debtor absconded;
  - (g) the debtor removed or concealed assets;
  - (h) the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;
  - (i) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;
  - (j) the transfer occurred shortly before or shortly after a substantial debt was incurred; and
  - (k) the debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

History: C. 1953, 25A-1-5, enacted by L. 1988, ch. 59, § 5; recompiled as C. 1953, 25-6-5.

Effective Dates. — Laws 1988, Chapter 59

became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25

Cross-References. — Defrauding creditors as a misdemeanor, § 76-6-511.

#### NOTES TO DECISIONS

##### ANALYSIS

Assignments  
Badges of fraud.  
Construction and application.  
Constructive trust  
Conveyances between relatives.  
Evidence.  
Fair consideration.  
"Good faith" transfer.  
Mortgagor remaining in possession.  
Parent and child.

##### Assignments.

Rule that sale or assignment of chattels, unaccompanied by change of possession, is fraudulent per se as to execution creditors of, or subsequent purchasers from, seller or assignor does not necessarily apply to assignments for benefit of creditors, but long delay in taking possession is circumstance from which fraud may be prima facie inferred. *Snyder v. Murdock*, 20 Utah 419, 59 P. 91 (1899).

Whether an assignment of an interest in an estate was in good faith and not to hinder, delay or defraud creditors, or was made for such purpose, depends upon the facts and circumstances surrounding the transaction, as gathered from the badges of fraud present. *Boccalero v. Bee*, 102 Utah 12, 126 P.2d 1063 (1942).

##### Badges of fraud.

Although actual fraudulent intent must be shown to hold a conveyance fraudulent, its existence may be inferred from the presence of certain indicia of fraud or "badges of fraud." *Dahnken, Inc. v. Wilmarth*, 726 P.2d 420 (Utah 1986).

"Badges of fraud," from which actual intent may be inferred, include, inter alia, a debtor's (1) continuing in possession and evidencing the prerequisites of property ownership after having formally conveyed all his interest in the property, (2) making a conveyance in antici-

tion of litigation, and (3) making a conveyance to a family member without receiving fair consideration *Dahnken, Inc. v. Wilmarth*, 726 P.2d 420 (Utah 1986).

#### Construction and application.

Statute was not intended to prevent debtor from paying or securing his honest debts, or from doing equity and exact justice to all of his creditors by placing his means at their disposal *Billings v. Parsons*, 17 Utah 22, 53 P. 730 (1898).

#### Constructive trust.

A constructive trust was properly imposed to prevent unjust enrichment, where the proceeds from the sale of fraudulently conveyed land, which were in excess of the purchase price, had been paid into court, and a subsequent conveyance to a third-party purchaser for value without notice could not be voided *Butler v. Wilkinson*, 740 P.2d 1244 (Utah 1987).

#### Conveyances between relatives.

Conveyances between near relatives, calculated to prevent a creditor from realizing on his claim against one of such relatives, are subject to rigid scrutiny *Paxton v. Paxton*, 80 Utah 540, 15 P.2d 1051 (1932).

The mere fact that the transaction is among close relatives does not necessarily mean that it is invalid, but the true facts are subject to proof *Givan v. Lambeth*, 10 Utah 2d 287, 351 P.2d 959 (1960).

A note and mortgage executed by son in good faith to secure a preexisting obligation which the son owed his father was not a fraudulent conveyance *Ned J. Bowman Co. v. White*, 13 Utah 2d 173, 369 P.2d 962 (1962).

Conveyances between close relatives are subject to rigid scrutiny, but the fact that close relatives are involved does not render the conveyance fraudulent *Ned J. Bowman Co. v. White*, 13 Utah 2d 173, 369 P.2d 962 (1962).

#### Evidence.

Whether an assignment of an interest in an estate was in good faith and not to hinder, delay or defraud creditors depends upon the facts and circumstances surrounding the transaction, as gathered from the badges of fraud present *Boccalero v. Bee*, 102 Utah 12, 126 P.2d 1063 (1942).

In an action on notes executed by the defendants and to establish a lien on property conveyed by one of the defendants to his children, the evidence was sufficient to sustain the lower court's findings that the conveyances were not fraudulent and to sustain a judgment denying a lien *Givan v. Lambeth*, 10 Utah 2d 287, 351 P.2d 959 (1960).

Whether a conveyance is fraudulent as to creditors must be determined from the facts of each case and from the circumstances surrounding the transaction, keeping in mind that

the purpose of the Fraudulent Conveyance Act (now see the Uniform Fraudulent Transfer Act) is not to prevent a debtor from securing his honest debt. *Ned J. Bowman Co. v. White*, 13 Utah 2d 173, 369 P.2d 962 (1962).

#### Fair consideration.

Where there is a valuable consideration which is stated to be fair, equivalent for, and not disproportionate to the value of the property conveyed, the requirement as to allegations and proof of fraud is more exacting. *Smith v. Edwards*, 81 Utah 244, 17 P.2d 264 (1932).

Where wife owned a substantial interest in a joint bank account and husband executed a note to the wife at her request upon withdrawing a substantial sum from such account to invest in a hazardous business, and when it became due, husband executed renewal note secured by mortgage on undivided one-half interest in property owned by them jointly, the original interest note was supported by valuable consideration, and, hence, the mortgage was not fraudulent as to creditors *Williams v. Peterson*, 86 Utah 526, 46 P.2d 674 (1935).

Conveyance of property worth \$14,000 to \$15,000, which netted only about \$180 a year, to party in satisfaction of preexisting debt of \$10,000 was not a fraudulent conveyance. *Utah Assets Corp. v. Dooley Bros. Ass'n*, 92 Utah 577, 70 P.2d 738 (1937).

A debt barred by the statute of limitations may nevertheless be consideration for the assignment of an interest in an estate, even as between close relatives *Boccalero v. Bee*, 102 Utah 12, 126 P.2d 1063 (1942).

In suit to set aside conveyance from husband to wife, no actual fraudulent intent will be required, when there was no fair value or consideration given, and the effect of the transfer is to render the grantor insolvent *Cardon v. Harper*, 106 Utah 560, 151 P.2d 99, 154 A.L.R. 906 (1944).

A conveyance was not made in good faith, and there was a failure of fair consideration, where purchaser knew that the purchase price of an item was approximately only one-tenth the value of the item *Meyer v. General Am. Corp.*, 569 P.2d 1094 (Utah 1977).

Satisfaction of an obligation owed the transferee by a third party did not qualify as fair consideration under former § 25-1-4. *Dahnken, Inc. v. Wilmarth*, 726 P.2d 420 (Utah 1986).

An otherwise fraudulent transfer is not made nonfraudulent because transfer is made to satisfy a third party's obligation to the transferee even if the third party is a corporation set up by the transferor *Dahnken, Inc. v. Wilmarth*, 726 P.2d 420 (Utah 1986).

#### "Good faith" transfer.

Proof that a transferee of property knows

that the transferor-debtor has preferred the transferee over other creditors or that the transferee actively sought the preference from the debtor does not support the conclusion that the transferee lacks good faith under former § 25-1-7. *Butler v. Wilkinson*, 740 P.2d 1244 (Utah 1987).

**Mortgagor remaining in possession.**

Mortgage on stock of merchandise was fraudulent as to judgment creditor of mortgagor, where mortgagor remained in possession of mortgaged property and continued to sell it in usual course of business pursuant to merely verbal agreement with mortgagee, which agreement contemplated that mortgage

was not to be paid on its due date but was to be extended from time to time. *McKibbin v. Brigham*, 18 Utah 78, 55 P. 66 (1898).

**Parent and child.**

Labor performed for parents by children during their minority will not entitle such children to compensation, so as to establish relation of debtor and creditor and permit parents lawfully to prefer children, convey their property to them, and thus place property out of reach of parents' creditors whose claims were in existence at time of deed's execution. *Ogden State Bank v. Barker*, 12 Utah 13, 40 P. 765 (1895).

**COLLATERAL REFERENCES**

**A.L.R.** — Future tort, conveyance as fraudulent where made in contemplation of possible liability for, 38 A.L.R.3d 597.

**Key Numbers.** — Fraudulent Conveyances — 24(2), 71, 76(1).

**25-6-6. Fraudulent transfer — Claim arising before transfer.**

(1) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made or the obligation was incurred if:

(a) the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at the time; or

(b) the debtor became insolvent as a result of the transfer or obligation.

(2) A transfer made by a debtor is fraudulent as to a creditor whose claim arose before the transfer was made if the transfer was made to an insider for an antecedent debt, the debtor was insolvent at the time, and the insider had reasonable cause to believe that the debtor was insolvent.

**History:** C. 1953, 25A-1-6, enacted by L. 1988, ch. 59, § 6; recompiled as C. 1953, 25-6-6.

**Effective Dates.** — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

**NOTES TO DECISIONS**

**Mortgage.**

A mortgage made without fair consideration, which will render the person making it insolvent, constitutes statutory fraud, and the exis-

tence of a subjective intention to defraud is not required. *Ned J. Bowman Co. v. White*, 13 Utah 2d 173, 369 P.2d 962 (1962).

**COLLATERAL REFERENCES**

**Key Numbers.** — Fraudulent Conveyances — 74(1).

**25-6-7. Transfer — When made.**

In this chapter:

(1) A transfer is made:

(a) with respect to an asset that is real property other than a fixture, but including the interest of a seller or purchaser under a contract for the sale of the asset, when the transfer is so far perfected that a good-faith purchaser of the asset from the debtor against whom applicable law permits the transfer to be perfected cannot acquire an interest in the asset that is superior to the interest of the transferee; and

(b) with respect to an asset that is not real property or that is a fixture, when the transfer is so far perfected that a creditor on a simple contract cannot acquire a judicial lien other than under this chapter that is superior to the interest of the transferee.

(2) If applicable law permits the transfer to be perfected as provided in Subsection (1) and the transfer is not so perfected before the commencement of an action for relief under this chapter, the transfer is deemed made immediately before the commencement of the action.

(3) If applicable law does not permit the transfer to be perfected as provided in Subsection (1), the transfer is made when it becomes effective between the debtor and the transferee.

(4) A transfer is not made until the debtor has acquired rights in the asset transferred.

(5) An obligation is incurred:

(a) if oral, when it becomes effective between the parties; or

(b) if evidenced by a writing, when the writing executed by the obligor is delivered to or for the benefit of the obligee.

History: C. 1953, 25A-1-7, enacted by L. 1988, ch. 59, § 7; recompiled as C. 1953, 25-6-7.

became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

Cross-References. — Secured transactions,

Effective Dates. — Laws 1988, Chapter 59 Chapter 9 of Title 70A.

**25-6-8. Remedies of creditors.**

(1) In an action for relief against a transfer or obligation under this chapter, a creditor, subject to the limitations in Section 25-6-9, may obtain:

(a) avoidance of the transfer or obligation to the extent necessary to satisfy the creditor's claim;

(b) an attachment or other provisional remedy against the asset transferred or other property of the transferee in accordance with the procedure prescribed by the Utah Rules of Civil Procedure;

(c) subject to applicable principles of equity and in accordance with applicable rules of civil procedure:

(i) an injunction against further disposition by the debtor or a transferee, or both, of the asset transferred or of other property;

(ii) appointment of a receiver to take charge of the asset transferred or of other property of the transferee; or

(iii) any other relief the circumstances may require.

(2) If a creditor has obtained a judgment on a claim against the debtor, the creditor, if the court orders, may levy execution on the asset transferred or its proceeds.

**History:** C. 1953, 25A-1-8, enacted by L. 1988, ch. 59, § 8; recompiled as C. 1953, 25-6-8.

**Effective Dates.** — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

#### NOTES TO DECISIONS

##### ANALYSIS

Garnishment proceeding.

Pleadings.

Presumptions and burden of proof.

Garnishment proceeding.

Fact that pleadings in garnishment proceedings revealed that indebtedness sued upon was that of individuals and that those individuals had no account with garnishee bank, the only account being with corporation owned by individuals, did not make cause of action one, under this section, to set aside conveyance, and thus argument that court had never obtained jurisdiction of corporate defendant or of res since no service of summons was made upon corporation could not be maintained; the pleading sufficiently averred a sham transaction between the individuals and the corporation so that they should be considered as identical for purpose of garnishment proceedings. *Stine v. Girola*, 9 Utah 2d 22, 337 P.2d 62 (1959).

Transfer of stock could be set aside as a fraudulent conveyance on motion in garnishment proceeding, and it was not necessary to file a separate action to obtain such relief. *Jensen v. Eames*, 30 Utah 2d 423, 519 P.2d 236 (1974).

Pleadings.

Allegations in an action to set aside convey-

ances that the conveyances were made for the purpose of placing the property beyond the reach of creditors and were made as part of a scheme, without a statement of the facts from which the purpose could be inferred, and without stating facts constituting the scheme, amounted to no more than the mere statement that the conveyances were fraudulent. *Smith v. Edwards*, 81 Utah 244, 17 P.2d 264 (1932).

Complaint in an action to set aside a conveyance was not objectionable for failure to allege that the property involved in the conveyance was not exempt. *Zuniga v. Evans*, 87 Utah 198, 48 P.2d 513, 101 A.L.R. 532 (1935).

Presumptions and burden of proof.

Where grantees were in possession of premises pursuant to a duly recorded deed and were paying taxes thereon, it was incumbent upon plaintiffs, in an action to set aside conveyance, to allege and prove that grantees as such did certain acts held themselves out in a way that misled plaintiffs and that plaintiffs had knowledge and relied thereon. *Smith v. Edwards*, 81 Utah 244, 17 P.2d 264 (1932).

Burden of proof is not on plaintiff to show that property alleged to have been fraudulently conveyed is not exempt from execution. *Cardon v. Harper*, 106 Utah 560, 151 P.2d 99, 154 A.L.R. 906 (1944).

#### COLLATERAL REFERENCES

**Key Numbers.** — Fraudulent Conveyances  
— 217, 226 et seq.

#### 25-6-9. Good faith transfer.

(1) A transfer or obligation is not voidable under Subsection 25-6-5(1)(a) against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

(2) Except as otherwise provided in this section, to the extent a transfer is voidable in an action by a creditor under Subsection 25-6-8(1)(a), the creditor may recover judgment for the value of the asset transferred, as adjusted under Subsection (3), or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered against:

(a) the first transferee of the asset or the person for whose benefit the transfer was made; or

(b) any subsequent transferee other than a good faith transferee who took for value or from any subsequent transferee.

(3) If the judgment under Subsection (2) is based upon the value of the asset transferred, the judgment must be for an amount equal to the value of the



asset at the time of the transfer, subject to an adjustment as equities may require.

(4) Notwithstanding voidability of a transfer or an obligation under this chapter, a good-faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to:

- (a) a lien on or a right to retain any interest in the asset transferred;
- (b) enforcement of any obligation incurred; or
- (c) a reduction in the amount of the liability on the judgment.

(5) A transfer is not voidable under Subsection 25-6-5(1)(b) or Section 25-6-6 if the transfer results from:

- (a) termination of a lease upon default by the debtor when the termination is pursuant to the lease and applicable law; or
- (b) enforcement of a security interest in compliance with Chapter 9, Title 70A, the Uniform Commercial Code.

(6) A transfer is not voidable under Subsection 25-6-6(2):

- (a) to the extent the insider gave new value to or for the benefit of the debtor after the transfer was made unless the new value was secured by a valid lien;
- (b) if made in the ordinary course of business or financial affairs of the debtor and the insider; or
- (c) if made pursuant to a good-faith effort to rehabilitate the debtor and the transfer secured present value given for that purpose as well as an antecedent debt of the debtor.

History: C. 1953, 25A-1-9, enacted by L. 1988, ch. 59, § 9; recompiled as C. 1953, 25-6-9.

Effective Dates. — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

#### NOTES TO DECISIONS

##### ANALYSIS

Consideration  
Constructive trust  
Good faith  
Previous notice of fraud.  
Purchaser.

##### Consideration.

The term "consideration" as used in former § 25-1-13 includes both a conveyance of "property" and satisfaction of an antecedent debt. *Merrill v. Abbott* (In re Independent Clearing House Co.), 77 Bankr. 843 (D. Utah 1987).

An investor in a Ponzi scheme gave "valuable consideration" for the transfers he received to the extent the transfers did not exceed his undertaking, but did not give valuable consideration for a transfer to the extent the transfer exceeded the amount of his undertaking. Therefore, for such transfers, former § 25-1-13 was no defense. *Merrill v. Abbott* (In re Independent Clearing House Co.), 77 Bankr. 843 (D. Utah 1987).

##### Constructive trust.

A constructive trust was properly imposed to prevent unjust enrichment, where the proceeds

from the sale of fraudulently conveyed land, which were in excess of the purchase price, had been paid into court, and a subsequent conveyance to a third-party purchaser for value without notice could not be voided. *Butler v. Wilkinson*, 740 P.2d 1244 (Utah 1987).

##### Good faith.

A conveyance will fail for lack of "fair consideration" if the party seeking to avoid the conveyance can show that the transferee did not take "in good faith." *Merrill v. Abbott* (In re Independent Clearing House Co.), 77 Bankr. 843 (D. Utah 1987).

##### Previous notice of fraud.

The mere fact that an investment promises to pay a high rate of return may not, without more, put one on notice that it is fraudulent. Therefore, that fact alone may not mean that the investors in a Ponzi scheme had previous notice of the debtors' fraud, especially when the debtors actually paid the promised returns until the scheme collapsed. *Merrill v. Abbott* (In re Independent Clearing House Co.), 77 Bankr. 843 (D. Utah 1987).

**Purchaser.**

The term "purchaser" as used in former § 25-1-13 includes anyone who acquires title to

property through a voluntary transfer *Merrill v. Abbott* (In re Independent Clearing House Co.), 77 Bankr. 843 (D. Utah 1987).

**COLLATERAL REFERENCES**

**Key Numbers. — Fraudulent Conveyances**  
— 192.

**25-6-10. Claim for relief — Time limits.**

A claim for relief or cause of action regarding a fraudulent transfer or obligation under this chapter is extinguished unless action is brought:

- (1) under Subsection 25-6-5(1)(a), within four years after the transfer was made or the obligation was incurred or, if later, within one year after the transfer or obligation was or could reasonably have been discovered by the claimant;
- (2) under Subsection 25-6-5(1)(b) or 25-6-6(1), within four years after the transfer was made or the obligation was incurred; or
- (3) under Subsection 25-6-6(2), within one year after the transfer was made or the obligation was incurred.

**History:** C. 1953, 25A-1-10, enacted by L. 1988, ch. 59, § 10; recompiled as C. 1953, 25-6-10.

**Effective Dates. —** Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25

**25-6-11. Legal principles applicable to chapter.**

Unless displaced by this chapter, the principles of law and equity, including merchant law and the law relating to principal and agent, equitable subordination, estoppel, laches, fraud, misrepresentation, duress, coercion, mistake, insolvency, or other validating or invalidating cause, supplement this chapter's provisions.

**History:** C. 1953, 25A-1-11, enacted by L. 1988, ch. 59, § 11; recompiled as C. 1953, 25-6-11.

**Effective Dates. —** Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

**25-6-12. Construction of chapter.**

This chapter shall be applied and construed to effectuate its general purpose to make uniform the law with respect to the subject of this chapter among states enacting it.

**History:** C. 1953, 25A-1-12, enacted by L. 1988, ch. 59, § 12; recompiled as C. 1953, 25-6-12.

**Effective Dates. —** Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.

**25-6-13: Applicability of chapter.**

This act applies when any transfer occurs after the effective date of this act.

History: C. 1953, 25A-1-13, enacted by L. 1988, ch. 59, § 13; recompiled as C. 1953, 25-6-13.

Compiler's Notes. — The term "this act" means Laws 1988, Chapter 59, which appears as §§ 25-6-1 to 25-6-13, 78-12-25, and

78-12-29, and which was effective April 25, 1988. The reference probably should be to "this chapter."

Effective Dates. — Laws 1988, Chapter 59 became effective on April 25, 1988, pursuant to Utah Const., Art. VI, Sec. 25.