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Texas appears poised to abandon the Ponzi scheme presumption

By Michael Summerhill and Tevin Hopkins

On December 20, 2019, in a case arising out of the Stanford Bank Ponzi scheme, the Texas Supreme Court fired its second shot across the bow of the Ponzi scheme presumption in fraudulent transfer actions in *Janvey v. GMAG, L.L.C.*, *et al*., -- S.W.3d --, No. 19-0452, 2019 WL 6972237 (Tex. Dec. 20., 2019). The court fired its first shot in another fraudulent transfer action case arising out of the Stanford Bank Ponzi scheme more than three and a half years earlier in *Janvey v. Golf Channel, Inc*., 487 S.W.3d 560 (Tex. 2016). Texas now appears poised to follow the Minnesota Supreme Court's 2015 decision in *Finn v. Alliance Bank*, 860 N.W.2d 638 (Minn. 2015), and fire a shot below the waterline to sink the Ponzi scheme presumption once and for all. These decisions make clear that, regardless of the jurisdiction, defendants in fraudulent transfer litigation that involve a Ponzi scheme should challenge the application of the presumption and preserve any objections to it for appeal to the state supreme court.

The Ponzi scheme presumption

Although the United States is currently in its longest period of recorded economic growth, history teaches that when it ends, the end will bring to light something that hides well in a good economy: Ponzi schemes. The three largest Ponzi schemes in United States history—Madoff, Petters, and Stanford Bank—all came to light in 2008 and 2009 following the onset of the Great Recession. Ponzi schemes invariably bring with them fraudulent transfer litigation to claw back assets—the scheme transferred to third parties—for distribution to the scheme's victims. The Uniform Fraudulent Transfer Act (UFTA)—which has been adopted by forty-three states, the District of Columbia, and the U.S. Virgin Islands—provides defrauded creditors, and the receivers and trustees that represent them, the means to reach those assets. Under UFTA, any transfer of an asset is voidable if the transferor made it with the actual intent "to hinder, delay, or defraud any creditor," or if the transferor did not receive reasonably equivalent value in exchange and the transfer either rendered the transferor insolvent or nearly insolvent.

In a normal case, a plaintiff must rely on UFTA's so-called enumerated badges of fraud to plead and prove a transferor's actual intent to defraud or otherwise plead and prove facts showing a lack of reasonably equivalent value in exchange for the transfer. If the transferor is a Ponzi scheme, however, the plaintiff can rely on the judicially-created "Ponzi scheme presumption" to establish the requisite intent and lack of reasonably equivalent value, and thus, the plaintiff's prima facie

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case. Thus, rather than offering evidence related to the transferor's intent, a court will presume the transferor's fraudulent intent if the plaintiff establishes that the transferor was a Ponzi scheme and that the transfer was made in furtherance of the scheme. In other words, without any facts related to the actual transfer at issue in the case, a plaintiff can satisfy its entire burden merely upon proof that the transferor was operating a Ponzi scheme. The burden would then shift to the defendant to establish an affirmative defense. The only affirmative defense available to a defendant, however, requires proof that the transferee accepted the transfer in good faith and for reasonably equivalent value. Thus, the Ponzi scheme presumption, by presuming the lack of reasonably equivalent value, negates the affirmative defense as well.

The Texas Supreme Court questions the viability of the presumption

Although courts throughout the country have relied on the presumption in dozens of decisions over the past few decades, on December 20, 2019, the Texas Supreme Court questioned the continued existence of the presumption in *Janvey v. GMAG, L.L.C., et al.*, -- S.W.3d --, No. 19-0452, 2019 WL 6972237 (Tex. Dec. 20., 2019). *GMAG* presented a certified question from the Fifth Circuit Court of Appeals relating to the meaning of good faith under the "good faith transferee" defense. Although the Stanford Bank receiver exclusively relied on the Ponzi scheme presumption to prove that the transfer was made with the requisite fraudulent intent, the court ignored the presumption entirely and instead focused on the enumerated badges of fraud in its discussion of UFTA. The court stressed that the Texas version of UFTA "provides its own badges of fraud in a list of eleven, nonexclusive indicia of fraudulent intent," and that the "badges provide guidance on determining whether a transfer was made or obligation incurred with actual intent to hinder, delay, or defraud a creditor." In other words, the court focused on the text of UFTA as it relates to proof of fraudulent intent, and not the Ponzi scheme presumption. The court, however, was able to answer the certified question without actually deciding whether the presumption remains viable under Texas law.

Further illuminating the Texas court's view that the presumption does not exist, was the court's decision in *Janvey v. Golf Channel, Inc.*, 487 S.W.3d 560 (Tex. 2016). *Golf Channel* also presented a certified question from the Fifth Circuit arising out of the Stanford Bank Ponzi scheme. There, the court was asked to decide the meaning of "reasonably equivalent value" under the good-faith transferee defense. Although not directly related to its answer to the certified question, the court noted that in cases involving Ponzi schemes, "courts…have bypassed the statutory badges-of-fraud analysis in favor of a conclusive presumption that transfers in furtherance of [a Ponzi scheme] were made with actual intent to defraud." In a footnote, the court noted the inherent inconsistency between the text of UFTA and the Ponzi scheme presumption, stressing that UFTA "provides only one express presumption: 'A debtor who is generally not paying the debtor's debts as they become due is presumed to be insolvent.'" The court, however, refused to rule on "the [presumption's] validity" because "[n]either party briefed the issues before this Court or in the federal appellate proceeding; the issues are well beyond the certified question's scope; and we need not address the matter to answer the certified question."

The Texas Supreme Court's decisions are consistent with both the Minnesota Supreme Court's decision in *Finn v. Alliance Bank*, 860 N.W.2d 638 (Minn. 2015), and the text of UFTA. With respect to the latter, in 2014, the National Conference of Commissioners on Uniform Laws amended UFTA. In addition to renaming it the Uniform Voidable Transactions Act, the amendments added a new subsection to the operative provision of UFTA. That new section provides: "[a] creditor making a claim for relief under subsection (a) [actual intent to defraud] has the burden of proving the elements of the claim for relief by a preponderance of the evidence." The commentary to the

revisions makes clear that one of the purposes of the addition was to make clear that courts "should be wary of nonstatutory presumptions that would dilute" the burden of persuasion. The Commissioners state that the amendments are not designed to "forbid…any and all nonstatutory presumptions," but the commissioners similarly stress a preference only for those "judicially-crafted presumption[s] applied under this Act or its predecessors [that have] won such favor [as have been] codified as [] separate statutory creation[s]." The Ponzi scheme presumption is not listed as one of the acceptable presumptions, and it has not been codified in any jurisdiction.

In 2015, a year after the amendments, the Minnesota Supreme Court concluded that the Ponzi scheme presumption is inconsistent with the express language of UFTA. The court reasoned that the text of UFTA does not refer to the presumption, use the word Ponzi, or even refer to schemes generally. Instead, UFTA focuses on the facts and circumstances of the challenged "transfers, rather than a pattern of transactions that are part of a greater scheme." As a result, the court concluded that an UFTA plaintiff must "prove the elements of a fraudulent transfer with respect to each transfer, rather than relying on a presumption related" to the transferor. In so holding, the court rejected the receiver's argument that the "presumption is justified [because] the scheme's operator invariably intends to cheat all investors"—a common refrain in all Ponzi scheme litigation. The court stressed that UFTA "does not contain a provision allowing a court to presume fraudulent intent." To the contrary, the court emphasized that UFTA's enumeration of specific badges of fraud, "none of which are conclusive, precludes an interpretation that [the legislature] intended a non-enumerated badge of fraud to be conclusive."

Transferee-defendants should challenge the application of the Ponzi scheme presumption

The Ponzi scheme presumption is a nonstatutory presumption that is inconsistent with the very statutory framework under which it operates. UFTA speaks in terms of transfers, not transferors. Its focus is on the characteristics of a transfer, not the characteristics of a transferor. Thus, while the fact of a Ponzi scheme can be a badge of fraud useful to establish the requisite intent, it cannot be the sole fact upon which the entire claim is won and lost. For this reason, when the next extended bear market causes a Ponzi scheme to collapse, fraudulent transfer defendants should not abandon a challenge to the Ponzi scheme presumption merely because courts—especially federal courts—currently recognize the existence of this presumption. UFTA claims are a matter of state law, and efforts should be made to preserve this issue for appeal to the state supreme court.

Indeed, as the *Golf Channel* litigation makes clear, receivers aggressively use the presumption to claw-back payments to unwitting third parties. While the transferee eventually prevailed in *Golf Channel*, it did so on the basis of the affirmative defense. But, whether third parties—such as a utility provider that services a Ponzi scheme, a caterer that provides company meals to employees of a Ponzi scheme, or a janitorial service that cleans offices that happen to be used to operate a Ponzi scheme—get to keep payment for their services should not depend solely on their ability to satisfy the good faith transferee defense. On the contrary, the plaintiff should first, consistent with the language of UFTA, have to prove that the specific, challenged transfer at issue in the case was made with the actual intent to defraud.

For more information on the content of this alert, please contact your Nixon Peabody attorney or:

- Michael Summerhill at **msummerhill@nixonpeabody.com** or 312-977-9224
- Tevin Hopkins at **tlhopkins@nixonpeabody.com** or 312-977-4385