

**UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
JACKSONVILLE DIVISION**

In re:

Case No. 3:07-bk-05082-JAF
Chapter 7

ROBERT ARTHUR MORAIS and
JANET LORRAINE MORAIS

Debtors.

AARON R. COHEN, as Chapter 7 Trustee,)

Plaintiff,

v.

Adv. No. 3:08-ap-0037-JAF

RICHARD A. MORAIS and
PAMELA L. MORAIS,

Defendant

**FINDINGS OF FACT AND CONCLUSIONS
OF LAW**

This proceeding came before the Court upon a Complaint filed by Plaintiff, Aaron R. Cohen, Trustee, to avoid the transfer of property of Robert Arthur Morais and Janet Lorraine Morais ("Debtors") pursuant to 11 U.S.C. § 548 and to recover the property transferred or its value pursuant to 11 U.S.C. § 550 and for turnover pursuant to 11 U.S.C. § 542. The Court conducted a hearing on the matter on October 1, 2008. In lieu of oral argument, the Court instructed the parties to submit briefs in support of their respective positions. Upon the evidence and the arguments of the parties, the Court makes the following Findings of Fact and Conclusion of Law.

Findings of Fact

Debtors filed their Chapter 7 bankruptcy petition on November 8, 2007. (Pl.'s Ex. 1.)¹ Richard A. Morais and Pamela L.

¹ (Pl.'s Ex. ____) refers to Plaintiff's exhibit number. (Defs.' Ex. ____) refers to Defendants' exhibit number.

Morais ("Defendants") are Debtors' son and daughter-in-law. Beginning in 1977 Debtors lived at 918 Brockelman Road, Lancaster, Massachusetts (the "Property"). For many years Debtors wanted to move to Florida. Debtor Janet Morais testified that she suffered from rheumatoid arthritis and wanted to move to Florida to deal with her condition.

At some time during 2004, in preparation for a move to Florida, Debtors commissioned an unofficial Title 5 inspection of the Property. A Title 5 inspection is an inspection of a septic tank system. Debtor Robert Morais testified that in order for property to change hands in Massachusetts, a homeowner must obtain a Title 5 certificate.² The Property failed the Title 5 inspection. Debtor Robert Morais testified that the inspector told him the cost to repair the septic system would be \$50,000.00-\$75,000.00. Debtor Robert Morais testified that if the Property had passed the inspection, he probably would have put it on the market to sell. Debtor Robert Morais' understanding was that a house could be sold by a parent to a child without a Title 5 inspection certificate.

On June 24, 2004 Defendants moved in with Debtors at the Property. Between June 2004 and May 2005 Debtors and Defendants lived together at the Property. During that time Debtors and Defendants split the approximate \$1,600.00 mortgage payment (which included the escrow for the real property taxes), electricity, and food expenses. (Defs.' Ex. 12, p. 14.)

Debtors moved out of the Property during May 2005. At that time, Debtors purchased the real property where they currently live at 814 Oak Road, Ocala, Florida. (Defs.' Ex. 12, p. 5.) After Debtors moved out of the Property, Defendants paid the mortgage and real property taxes but not the insurance. Debtors paid the insurance because they owned the Property. Debtors stopped paying the insurance when the Property was transferred on July 13, 2007. (Defs.' Ex. 12, pp. 23-25.)

² Plaintiff did not rebut this assertion and Massachusetts' State Environmental Code 310 CMR 15.021 provides that "[n]o person shall discharge sewage into a new, upgraded or expanded system without first obtaining a Certificate of Compliance from the Approving Authority..."

At some point prior to the petition date, Debtors entered into a Standard Purchase and Sale Agreement (the "Contract") pursuant to which they agreed to sell the Property to Defendants. (Pl.'s Ex. 3.) The Contract, which is dated June 20, 2005, is signed by Debtors and Defendants. June 20, 2005 is also the date next to Debtors' and Defendants' signatures. The signatures are not notarized. (Pl.'s Ex. 3.)

Paragraph 3 of the Contract states that the purchase price is \$342,000.00 and that \$10,000.00 is payable as a deposit. \$332,000.00 is to be paid at the time of performance by a bank check, a cashier's check, a treasurer's check, a certified check or by wire transfer. (Pl.'s Ex. 3.) Paragraph 5 of the Contract states that Debtors shall deliver the deed to the Property and Defendants shall pay the balance of the purchase price at 2:00 on the 15th day of July 2007. (Pl.'s Ex. 3.) Paragraph 15 of the Contract states that if Defendants breach the Contract, all escrowed funds paid or deposited by Defendants shall be paid to Debtors as liquidated damages and that receipt of such payment shall constitute seller's sole remedy. (Pl.'s Ex. 3.) Paragraph 23 of the Contract states that Defendants agree to move into the premises and be responsible for the mortgage, principal and interest, taxes, and insurance. It also states that the buyers will be responsible for obtaining a Title 5 Certificate of Compliance. (Pl.'s Ex. 3.)

On August 1, 2005 Defendants paid \$10,000.00 to Debtor Robert Morais. (Pl.'s Ex. 4.) On November 3, 2005, Defendants paid another \$500.00 to Debtor Robert Morais, which Defendants testified was paid toward the purchase price. (Pl.'s Ex. 5.)

Debtors' financial problems began during 2005. Debtor Robert Morais, testified that during the year prior to the Petition Date, the sum total of the value of Debtors' assets was less than the sum total of their liabilities during the entire time. On their Schedule F, debtors listed debts totalling \$94,165.13. (Defs.' Ex. 12, p. 5-6.)

Debtors first met with their bankruptcy attorney, Richard Perry, about filing bankruptcy on April 13, 2007. A few weeks before meeting with Mr. Perry, Debtors met with a credit counselor because of the problems they were having paying their debts. (Defs.' Ex. 12, p. 7.) Debtors stopped paying the debts listed on their

Schedule F during April, May or June, 2007. (Id.)

On June 7, 2007, Debtors and Defendants signed a document (the "June 7, 2007 Document"), which was prepared by Debtor Janet Morais stating as follows:

We agree to sell the property at
918 Brockelman Road,
Lancaster, Massachusetts to
Richard and Pamela Morais for
the sum of Fifty Thousand
(\$50,000) and the payoff of the
Mortgage held by Webster
First Federal Credit Union.

\$10,500 Paid on
Account

\$20,000 At Closing

\$19,500 To Be Paid
by June 1, 2010*

* * *

* If not paid by June 1, 2010
Interest at 18% per annum

(Pl.'s Ex. 6; Defs.' Ex. 13, p. 27.)

On or about June 15, 2007, Central Mass Appraisals conducted an appraisal of the Property. The appraiser valued the Property at \$342,000.00 as of June 15, 2007. (Defs.' Ex. 15.) Defendant, Richard Morais, testified that he agreed with the appraiser that the fair market value of the Real Property was \$342,000.00 as of June 15, 2007. (Defs.' Ex. 13, pp. 13-14.) Although Defendant Richard Morais showed the appraiser around the Property, he testified at trial that he forgot to tell the appraiser about the Title 5 situation. Prior to the appraisal Defendants made the following repairs or improvements to the Property: 1) \$5,805.00 for a stove (Defs.' Ex. 5.); 2) \$2,600.00 for a water pump (Defs.' Ex. 6.); 3) \$1,200.00 for a chimney (Defs.' Ex. 7.); and 4) \$1,356.18 for the yard loam and plywood. (Defs.' Ex. 8.) Additionally, Defendants replaced the basement floor which had been infested with mold and renovated some rooms in the house which they claim cost them \$12,195.00.

The purchase price of \$342,000.00 in the June 20, 2005 Contract is identical to the value of \$342,000.00 set forth in the June 15, 2007 appraisal. Debtor Robert Morais, testified at trial that this was just a “coincidence”. Debtor Janet Morais testified at trial that she does not know when she signed the Contract but that it was not dated when she signed it. Debtor Janet Morais further testified that she thought the Contract was “backdated.” (Defs.’ Ex. 12, pp. 44-47.) At his deposition Debtor Robert Morais, testified that he was pretty sure he signed the Contract on June 20, 2005. (Defs.’ Ex. 12, pp. 44-48.) Defendants, when asked during their deposition whether the Contract was signed on June 20, 2005 or whether it was backdated, testified “I don’t recollect” and “I don’t recall”. (Defs.’ Ex. 13, pp. 48-50.)

On June 25, 2007, Debtors executed a quit-claim deed stating that in full consideration of \$342,000.00, they grant to Defendants the Property. (Pl.’s Ex. 7.) On July 9, 2007, Debtors and Defendants signed another document (the “July 9, 2007 Document”) stating as follows:

We agree to sell the property at
918 Brockelman Road,
Lancaster, Massachusetts to
Richard and Pamela Morais for
the sum of Fifty Thousand
(\$50,000) and the payoff of the
Mortgage held by Webster
First Federal Credit Union.

\$10,500 Paid on
Account

\$ 5,000 At Closing

\$34,500 To Be Paid
by June 1, 2015

* * *

All other documents are null
and void as of this above date.

(Pl.’s Ex. 8.)

Debtors had both the June 7, 2007 Document and the July 9, 2007 Document in their possession when they filed bankruptcy. They did not give either document to Mr. Perry

or to the Chapter 7 Trustee, Aaron Cohen. (Defs.’ Ex. 12, pp. 30, 34-37.) In response to question 10 on their Statement of Affairs filed with the Court, Debtors listed the transfer of the Property to Defendant Richard Morais. They described the value received as follows:

Debtors’ son refinanced the mortgage on this house and paid off existing lien in the amount of \$189,209. Debtors received \$5,000 and used the money to live on and to pay bills.

(Pl.’s Ex. 2.) Thus, Debtors did not identify on their bankruptcy Schedules or Statement of Affairs any consideration received for the transfer of the Property except the payoff of the existing mortgage and \$5,000.00. Debtors did not list any additional amounts owed to them on their bankruptcy Schedules or Statement of Affairs, either under the Contract, the June 7, 2007 Document or the July 9, 2007 Document. Debtor Robert Morais, testified that he did not list the \$34,500.00 shown on the July 9, 2007 Document on his bankruptcy Schedules or Statement of Affairs because:

That was an oversight on my part because I didn’t think I would get anything out of my son. And it was a contract written between us that I didn’t think was enforceable.

(Defs.’ Ex. 12, p. 22.)

Debtor Janet Morais testified that she prepared the June 7, 2007 Document just to “pacify her other children.” She testified “[i]t’s saying that Rick and Pam are going to pay us, even though we knew they weren’t.” (Defs.’ Ex. 12, p. 27.) Debtor Robert Morais, testified that Debtors agreed to extend the payment deadline set forth in the July 9, 2007 Document because Defendant Richard Morais is his son. (Defs.’ Ex. 12, pp. 37-38.) He further testified that Debtors agreed to remove any interest because his son was upset about it and did not want to pay it. (Id.)

On July 13, 2007, Debtors received from Defendants’ attorney, Vincent J. Campobasso, a fully executed copy of the Contract. (Pl.’s Ex. 11.) This letter was the first

time that Debtors received a fully executed copy of the Contract. (Defs.' Ex. 12, pp. 46-47.) The closing occurred and the deed to the Property was recorded in the Official Records of Worcester County, Massachusetts on July 13, 2007. (Pl.'s Ex. 7.)

The mortgage holder on the Property prior to the transfer on July 13, 2007 was Webster First Credit Union. The balance owed on the mortgage on the date of the transfer was \$190,187.43. Defendants paid off the mortgage on the date of the transfer. (Pl.'s Ex. 9.) In order to pay off the mortgage Defendants borrowed on the Property approximately \$240,000.00 from SunTrust Mortgage. (Defs.' Ex. 13, p. 52.) Thus, the difference between the first mortgage payoff and the amount borrowed was approximately \$50,000.00. \$5,000.00 was paid to defendants on July 13, 2007. Defendant, Richard Morais testified at trial that \$30,000.00 went to pay off his personal credit card debt.

The total consideration Defendants paid to Debtors for the Property was (i) \$10,000.00 paid on August 1, 2005; (ii) \$500.00 paid on November 3, 2005;

(iii) \$5,000.00 paid on the day of the transfer, July 13, 2007; and (iv) the payoff of the first mortgage on the Property (\$190,187.43). Defendants have made no further payments to Debtors. (Defs.' Ex. 12, pp. 21-22).

On August 24, 2007, Defendants refinanced the \$240,000.00 mortgage on the Property by borrowing \$265,000.00 After the payoff of the \$240,000.00 mortgage and closing costs, Defendants received cash of \$15,684.86. (Pl.'s Ex. 10; Defs.' Ex. 13, pp. 52-56.)

Debtor Robert Morais testified that Defendant Richard Morais was aware of Debtors' financial problems at the time Debtors transferred the deed to Defendants because prior to signing the deed he told him he would probably end up filing bankruptcy. (Defs.' Ex. 12, page 34.) Defendant Richard Morais testified that when the quitclaim deed was signed and at the closing, Debtor Robert Morais told Defendant Richard Morais that he was considering bankruptcy. (Defs.' 13, p. 29.) Debtor Robert Morais further testified that it was "more than likely" that Pamela Morais was aware of Debtors' financial problems and that they would probably be filing bankruptcy at the

time Debtor Robert Morais signed the deed. (Defs.' Ex. 12, page 34.) The Court finds that Defendants were aware of Debtors' financial problems prior to and at the time of closing.

Conclusions of Law

Plaintiff argues that the transfer of the Property is avoidable pursuant to 11

§ 548(a)(1)(A). Alternatively, Plaintiff argues that the transfer is avoidable pursuant to

§ 548(a)(1)(B). The Court finds it appropriate to first analyze the transfer under

§ 548(a)(1)(B). Section 548(a)(1)(B) provides in relevant part that the Trustee may avoid any transfer of an interest of the debtor in property that was made within two years of the petition date if the debtor (i) received less than a reasonably equivalent value in exchange for such transfer and (ii) was insolvent on the date that such transfer was made or became insolvent as a result of such transfer. Defendants concede that Debtors were insolvent on the date of the transfer of the Property. The disputed issue is whether Debtors received less than reasonably equivalent value when they sold the Property to Defendants.

A. Did Debtors receive less than reasonably equivalent value when they sold the Property to Defendants?

The question of whether reasonably equivalent value is given in exchange for a transfer of property is a question of fact. In re McDonald, 265 B.R. 632, 636 (Bankr. M.D. Fla. 2001). In McDonald the Court looked to the following three factors to determine whether the preservation of an opportunity for economic benefit constituted "reasonably equivalent" value under § 548(a)(1)(B): (1) the fair market value of the opportunity compared to the amount of the transfer; (2) the arms' length (or collusive) nature of the transaction; and (3) the good faith (or lack thereof) of the transferee. Id. at 636. The Court will address each element in turn.

1. Fair Market Value of Property Compared to Amount of Transfer

The Court finds that the fair market value of the Property at the time of the transfer was \$342,000.00, the Property's appraised value.³ The Court finds that Debtors received \$240,187.43 in exchange for the Property. That amount is calculated by adding the following allowable expenses: 1) the \$190,187.43 payoff of the mortgage; 2) the \$10,000.00 August 2005 payment; 3) the \$500.00 November 2005 payment; 4) the \$5,000.00 July 2007 payment; and 4) the \$34,500 balance owed by Defendants to Debtors.

Defendants' payment of half of the mortgage payment while they lived with Debtors from June 2004 to May 2005 and their payment of the entire mortgage payment between June 2005 and the transfer of the Property are not additional consideration. Those payments were rent (and in light of the fair market value of the Property, very inexpensive rent) for Defendants' use of the Property. Moreover, the Contract provided that Defendants were required to pay the mortgage, taxes and insurance in addition to the \$342,000.00. Additionally, in light of the identicalness of the June 20, 2005 Contract price and the June 15, 2007 appraisal value, there is no evidence before the Court that the improvements or repairs which Defendants made to the Property while it was still titled in Debtors' name increased its value. The Court finds that those expenses were not consideration given in exchange for the Property. Defendants' payment of \$ 240,187.43 for the Property is far less than its fair market value of \$342,000.00 at the time of the transfer.

2. The Arms Length (or Collusive) Nature of Transaction

The Court finds that the transfer of the Property was not an arms' length transaction.

³ Defendants assert that the evidence establishes that it would cost at least \$50,000.00 to make the system compliant with Title 5. The only evidence before the Court as to the cost to bring the Property into compliance with Title 5 is Debtor Robert Morais' testimony that an inspector informed him the cost would be at least \$50,000.00. Such testimony is based upon hearsay. Additionally, the Court finds that based upon its own knowledge and experience, such testimony is not credible. Furthermore, as Plaintiff points out, if the cost to make the system compliant with Title 5 was material, surely Defendant Richard Morais would have informed the appraiser of the problem.

Debtors and Defendants backdated the Contract. Debtors agreed to reduce, by virtue of the July 8, 2007 Document, the \$342,000.00 Contract price to just \$34,500.00 (payable in 2015) over the mortgage amount and the \$15,500.00 already paid and to eliminate interest on the \$34,500.00 because the buyer was their son and he did not want to pay more than \$34,500.00.

3. Good Faith (or lack thereof) of Defendants

A transferee who has knowledge or notice of the debtor's financial difficulties does not act in good faith. See In re World Vision Entertainment, 275 B.R. 641, 659 (Bankr. M.D. Fla. 2002) (holding that a party can rebut the § 548(c) good faith defense by showing that the transferee had knowledge or notice of the debtor's financial difficulties or fraudulent purpose); In re Revels, 2007 WL 1756987 * 7 (Bankr. M.D. Fla. January 31, 2007) (finding that debtor's brother was not a good faith transferee under Fla. Stat. § 726.109(1) because he was on notice through his father of debtor's financial problems); In re O'Connell, 119 B.R. 311, 317 (Bankr. M.D. Fla. 1990) (holding that transferees were not good faith transferees because they had knowledge of the debtor's poor financial condition at the time of transfer). Debtor Robert Morais testified that Defendant Richard Morais was aware of Debtors' financial problems when Debtors transferred the Property to Defendants because he told him Debtors would probably be filing bankruptcy. The Court finds this testimony to be credible. Additionally, the Court finds that Defendant Pamela Morais was on notice of Debtor's financial problems. The Court finds that Defendants are not good faith transferees.

B. Recovery pursuant to 11 U.S.C. § 550(a)(1)

Once the court determines that a transfer is avoidable under 11 U.S.C. § 548, the court must then look to 11 U.S.C. § 550 to determine the liability of the transferee. Section 550(a) states:

- (a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a) of this title, the trustee may

recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from--

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee;

The purpose of § 550 is “to restore the estate to the financial condition it would have enjoyed if the transfer had not occurred.” In re American Way Service Corp., 229 B.R. 496, 530-31 (Bankr. S.D. Fla. 1999). In this instance the Court finds that while the transfer of the Property is avoidable, voiding the transfer is not an appropriate remedy. Instead, the Court will enter a judgment, which will attach as a lien to the Property, against Defendants in the amount of \$101,812.57, the difference between the \$342,000.00 fair market value of the Real Property at the time of the transfer and \$240,187.43, the amount Defendants paid for the Property. The Court will enter a separate Judgment consistent with these Findings of Fact and Conclusions of Law.

DATED this 24 day of February, 2009
in Jacksonville, Florida.

/s/Jerry A. Funk
JERRY A. FUNK
United States Bankruptcy Judge

Copies furnished to:

Ray Magley, Attorney for Plaintiff
Albert Mickler, Attorney for Defendant