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## Kentucky's Obsolete Law on Gifts by Debtors

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punishment. The criminal punishment is not exclusive and a civil action may be maintained. It seems that this civil action can be maintained by third persons. Notice is necessary if the suit is brought by another child but may not be necessary if the action is brought by third persons. Future support should be allowed to prevent multiplicity of actions and should be similar to a decree for alimony.

GERALD ROBIN GRIFFIN

### KENTUCKY'S OBSOLETE LAW ON GIFTS BY DEBTORS

The Statute of Elizabeth,<sup>1</sup> progenitor of most modern statutes and case law concerning conveyances deemed fraudulent as to creditors, declared broadly that every conveyance and gift made with the "intent to delay, hinder or defraud creditors and others is void." Thus the sole criterion for declaring a conveyance within the operation of the statute was whether there was an intent on the part of the grantor to delay or defraud his creditors. Literally interpreted, the statute makes of no consequence the fact that a conveyance would have the effect of delaying or defrauding a creditor unless there is also present the requisite intent. Nevertheless the courts have uniformly held that a gift, or a voluntary conveyance without consideration, made while the financial position of the debtor is such that the payment of creditors is necessarily defeated, as where the debtor is insolvent or is rendered thereby insolvent, is fraudulent as a matter of law without regard to actual intent of the debtor.<sup>3</sup> From a practical standpoint there can be no quarrel with this holding. An irresponsible person should not be permitted to dissipate completely his assets by gifts leaving his creditors without any assets on which to realize their claims.

A more difficult problem is what effect mere indebtedness without near insolvency of the donor should have upon the validity of a gift as against contemporaneous creditors. Two views have been developed by courts interpreting the Statute of Elizabeth or its successors as to this problem. The holdings are that the voluntary conveyance (1) is presumed to be fraudulent with respect to the existing debt and no circumstance will suffice to repel the legal presumption of fraud,<sup>4</sup> and (2) is merely *prima facie* fraudulent.<sup>5</sup>

As early as 1836, Kentucky laid down without reservation the rule that voluntary conveyances were conclusively fraudulent as to antecedent creditors and the court has followed it undeviatingly until the present time.<sup>6</sup> In *Hanson v. Buckner s Devisees*,<sup>7</sup> the first case holding squarely on this point, the court said:

"And the presumption of law as to prior debts, does not depend upon the amount of the debts, the intentions, or circumstances of the party conveying, or the amount of property conveyed. The law

<sup>1</sup> 3 ELIZ., c. 5 (1540).

Although there were earlier statutes for the protection of creditors such as 50 EDW. III, c. 6 (1376) and 3 HEN. VII, c. 4 (1488), the statute of 13 ELIZ. is the starting point for most discussions of fraudulent conveyances.

<sup>2</sup> GLENN, *THE LAW OF FRAUDULENT CONVEYANCES* sec. 269 (1940).

<sup>3</sup> GLENN, *op. cit. supra*, note 3, at sec. 268.

<sup>4</sup> GLENN, *op. cit. supra*, note 3; 37 C. J. S. 935, 936.

<sup>5</sup> Daniels v. Goff, 192 Ky. 15, 232 S.W. 66 (1921); Townsend v. Wilson, 114 Ky. 504, 24 Ky. L. Rep. 1276, 71 S.W. 440 (1903); Miller v. Desha, 66 Ky. (3 Bush) 212 (1867); Trumble v. Ratcliff, 48 Ky. (9 B. Mon.) 511 (1849). The paucity of recent cases on this point is further evidence of the rigidity of this rule.

will not permit an inquiry to be made into these matters, or give to them any weight or influence. The law, has wisely cut off all enquiry (sic) and treated all voluntary conveyances and settlements founded upon no other consideration than that of natural affection or blood, as nullities, whenever they stand in the way of pre-existent debts."<sup>7</sup>

Earlier Kentucky cases<sup>8</sup> and statutes<sup>9</sup> could have been cited in support of this holding, but the court chose to rely mainly on the decision of Chancellor Kent in *Reade v. Livingston*.<sup>11</sup> It was in this famous case that Kent came to the conclusion that the fair deduction from the cases is that the Statute of 13 Elizabeth, which requires intent to delay, hinder, or defraud, should be interpreted to mean that if "the party be indebted at the time of the voluntary settlement, it is presumed to be fraudulent in respect to such debts, and no circumstances will permit those debts to be affected by the settlement, or repel the legal presumption of fraud."<sup>12</sup> In other words, fraudulent intent of the debtor is presumed as to existing creditors when any gifts are made by him. This interpretation of the statute was made notwithstanding the obvious fact that the intent of the parties is no more subject to inquiry under the statute when the conveyance is made to defraud subsequent creditors than when it is made to defraud antecedent creditors.

It was this Kent doctrine which was codified and embodied into the Ky. Rev. Stat. sec. 378.020 (1948) which provides that:

"Every gift, conveyance, assignment, transfer or charge made by a debtor, of or upon any of his estate without valuable consideration therefor, shall be void as to all his then existing creditors, but shall not, on that account alone, be void as to creditors whose claims are thereafter contracted, nor as to purchasers from the debtor with notice of the voluntary alienation or charge."<sup>13</sup>

This statute is open to the common sense objection of imputing a fraudulent intent, under circumstances repelling all possible imagination of fraud and invading the lawful dominion which a man should have over his own property while acting in good faith. If carried to its ultimate consequences even the most trivial indebtedness would be sufficient to avoid the voluntary conveyance. The easy credit and installment buying, which has descended upon us within the last generation, has made the unindebted person a rarity. With this premise it would perforce follow that not one donee could feel secure in the enjoyment of his bounty. Chief Justice Marshall expressed his fear of this outcome in *Hopkirk v. Randolph* by declaring, " a construction which should, under all circumstances, comprehend every gift (fraudulent), merely because it was voluntary, might derange the ordinary course of society, and produce much greater injustice than it would prevent."<sup>14</sup>

<sup>7</sup> 34 Ky. (4 Dana) 251, 29 Am. Dec. 401 (1836).

<sup>8</sup> *Id.* at 254, 29 Am. Dec. at 404.

<sup>9</sup> *Lyne, etc. v. Bank of Kentucky*, 28 Ky. (5 J. J. Marsh) 545 (1831); *see Cosby, etc. v. Ross Admr*, 26 Ky. (3 J. J. Marsh) 290 (1830).

<sup>10</sup> 1 STAT. LAW OF KY. (Littell, 1809) 371, approved Dec. 14, 1796.

<sup>11</sup> 3 Johns. Ch. Rep. (N. Y.) 481, 8 Am. Dec. 520 (1818).

<sup>12</sup> *Id.* at 500, 8 Am. Dec. at 532.

<sup>13</sup> The word "void" as used in this statute and the statute of 13 ELIZ. has been construed to mean "voidable," and "voidable" only at the instance and option of those who are within the purview of the statutes. 24 AM. JUR. 261.

<sup>14</sup> 12 Fed. Cas. 513, 515, No. 6, 698 (C.C.E.D. Va. 1824).

It was only a short time after Kent laid down his doctrine that New York realized its harshness and overruled his decision in *Jackson v. Seward*.<sup>15</sup> In this case the court was constrained to hold from its review of the cases that a voluntary conveyance by one indebted at the time, was only *prima facie*, and not conclusive, evidence of fraud. This decision was later followed by a statute.<sup>16</sup> Most of the states by now have accepted this more rational view, and they impute conclusive fraud only when the donor is insolvent.<sup>17</sup>

Other courts, unable wholly to discard the rule, strained to remove themselves from under its full impact by limiting it in whatever way possible. The amount of indebtedness and the amount of the gift necessary to bring the rule into effect were increased. Thus where the indebtedness is slight, as for the current expenses of the family, or the debts are inconsiderable as compared with the value of the donor's estate, the conveyance has been held valid.<sup>18</sup> Still other jurisdictions limited its application by declaring that a person holding mere contingent claims which would not mature until after the gift was not to be considered a preexisting creditor and hence not in a position to bring the rule into effect.<sup>19</sup> Kentucky, however, has expressly refused to go along with this latter holding.<sup>20</sup>

With a view toward remedying this obsolete doctrine, Kentucky should take notice that New Jersey which was labeled the "modern stronghold"<sup>21</sup> for the Kent rule, was one of the first to enact the Uniform Fraudulent Conveyance Act. The pertinent section of this Act relating to voluntary conveyances by debtors provides:

"Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration."<sup>22</sup>

Although this section does not in express words repeal the holding that all voluntary conveyances are fraudulent at law with respect to antecedent creditors, it may well be argued that it is so inconsistent therewith that the two should not be permitted to coexist.<sup>23</sup> The wording of the Uniform Act seems to indicate that the test for the imputation of conclusive fraud on a debtor is not mere indebtedness as provided in Kentucky's statute, but rather insolvency. However, even after the passage of that act, the New Jersey courts had difficulty in overcoming

<sup>15</sup> 8 Cow. 406 (N. Y. 1826).

<sup>16</sup> N. Y. REV. STAT. (1829) pt. II, c. 7, tit. 3. This statute went to the opposite extreme by declaring that the determination of what is a fraudulent conveyance was always a question of fact.

<sup>17</sup> See note 5 *supra*.

<sup>18</sup> *Buchanan v. McNinch*, 3 Rich 498 (S. C. 1872); *Hindes Lessee v. Longworth*, 11 Wheat 198 (U. S. 1826), see *Trimble v. Ratcliff*, 48 Ky. (9 B. Mon) 511, 514 (1849).

<sup>19</sup> *Severs v. Dodson*, 53 N. J. Eq. 633, 34 A. 7 (1895).

<sup>20</sup> *Damels v. Goff*, 192 Ky. 15, 20, 232 S.W. 66, 68 (1921) where the court said in reference to the wording of KY. REV. STAT. sec. 378.020 (1948), "The word 'liabilities' includes debts and indebtedness; but it is broader, and includes in addition existing obligations, which may or may not in the future eventuate in an indebtedness."

<sup>21</sup> *McLaughlin, The Uniform Fraudulent Conveyance Act*, 46 HARV. L. REV. 404, 408 (1933).

<sup>22</sup> Uniform Fraudulent Conveyance Act, sec. 4, 9 U. L. A.

<sup>23</sup> *McLaughlin, supra*, note 21, at 408.

the inertia that had kept the doctrine of *Reade v. Livingston* alive through the years. It was followed for nearly ten years before it was corrected in *Conway v. Raphael*.<sup>24</sup> In view of the reluctance which the courts of that state displayed in breaking away from the established rule, case-hardened through the years, even after the passage of the Uniform Act, it is inconceivable that Kentucky could change its equally well established rule by any means other than by statute.

Kentucky should therefore enact the pertinent section of the Uniform Act set out above. In addition Ky. Rev. Stat. sec. 378.020 (1948) should be modified so as to eliminate the inconsistency which arises from that statute as it now stands and the Uniform Act. This is the same inconsistency which New Jersey encountered. It can be removed by the substitution of the words "prima facie fraudulent" for the word "void" in the present statute. With this minor change the statute would read:

"Every gift, conveyance, assignment, transfer or charge made by a debtor, of or upon any of his estate without valuable consideration therefor, shall be (void) *prima facie fraudulent* as to his then existing creditors, but shall not, on that account alone, be (void) *prima facie fraudulent* as to creditors whose claims are thereafter contracted, nor as to purchasers from the debtor with notice of the voluntary alienation or charge." (Proposed additions in italics; present wording in brackets).

This change would incorporate into statutory form the prevailing judicial treatment of voluntary conveyances by solvent debtors. If this section were completely repealed the case law holding that gifts by debtors were fraudulent as to preexisting creditors might continue to exist. This would result in placing Kentucky in the same position as New Jersey immediately after it passed the Uniform Act. Therefore this section, as changed would require the courts of this state forthwith to sever themselves from the old line of decisions and thereby eliminate the possibility of an interim period, such as the one New Jersey endured, from the time of the passage of the Uniform Act until it becomes completely effective.

The enactment of these proposed statutes would remove the stigma of a doctrine early placed in Kentucky's laws by the blind following of the weighty name of Chancellor Kent, and which rests on no more than the highly dubious rationale "that a person must be just before he is generous."<sup>25</sup>

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<sup>24</sup> 102 N. J. Eq. 531, 141 Atl. 804 (1928).

<sup>25</sup> *Thomas v. Aldridge*, 241 Ky. 1, 43 S.W. 2d 179 (1931); *Lyne v. Bank of Kentucky*, 28 Ky. (5 J. J. Marsh) 545, 553, 554 (1831).