Renunciation of a Legacy or Devise as a Fraudulent Transfer Under the Bankruptcy Act

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NOTES

RENUNCIATION OF A LEGACY OR DEVISE AS A FRAUDULENT TRANSFER UNDER THE BANKRUPTCY ACT

When an insolvent debtor files a petition in bankruptcy under the federal Bankruptcy Act, a trustee is appointed to gather the debtor's assets and distribute the proceeds to his creditors. If the debtor acquires property as a beneficiary under a will prior to or during the bankruptcy proceedings, the property received can be claimed by the trustee. However, the common law rule is that the beneficiary of a will can renounce a devise or a legacy and that the renunciation relates back to the death of the testator making the gift void from the beginning. Thus, to prevent seizure of these assets by the trustee, the debtor might be inclined to renounce the testamentary gift and have it pass to the next successor in interest, particularly if the next successor is a relative or a member of the debtor's immediate family. The question addressed in this note is whether a renunciation by an insolvent debtor which has the effect of avoiding his creditors can be set aside by the trustee in bankruptcy as a fraudulent transfer.

FRAUDULENT TRANSFERS DEFINED

Section 67(d)(2) of the Bankruptcy Act deals with transfers made

5. Some courts have held that the title is presumed to vest at the death of the testator but the renunciation relates back to make the gift void from the beginning. See Strom v. Wood, 100 Kan. 556, 164 P. 1100 (1917); Bradford v. Calhoun, 120 Tenn. 53, 109 S.W. 502 (1908). Others have held that the testamentary gift never vested in the beneficiary so that relation back is not necessary. See Perkins v. Isley, 224 N.C. 793, 32 S.E.2d 588 (1945). See generally 6 W. Bowe & D. Parker, Page on Wills § 49.4 (1962) [hereinafter cited as Page on Wills].
6. 11 U.S.C. § 107(d)(2) (1970), which states in part:
   Every transfer made and every obligation incurred by a debtor within one year prior to the filing of a petition initiating a proceeding under this title by or against him is fraudulent (a) as to creditors existing at the time of such transfer or obligation, if made or incurred without fair consideration by a debtor who is or will be thereby rendered insolvent, without regard to his actual intent; . . . or (d) as to then existing and future creditors if made or incurred with actual intent as distinguished from intent presumed in law, to hinder, delay, or defraud either existing or future creditors.

Id. Property which vests in the bankrupt by inheritance, legacy, or devise after the bankruptcy petition is filed is covered by § 70(a), 11 U.S.C. § 110(a) (1970). See note 69 infra.
for the purpose of defeating creditors. This section states that if an insolvent debtor makes a fraudulent transfer of property or an interest in property within one year prior to the filing of a petition in bankruptcy, the transfer is voidable and the trustee can include the property in the bankrupt's estate for distribution to his creditors. The transfer is fraudulent under § 67(d)(2) if (1) it is made with actual intent to defraud creditors, or (2) the debtor receives no consideration for making the transfer and the debtor is insolvent at the time of the transfer or is rendered insolvent because of the transfer.7

The term "transfer," as defined for purposes of the Bankruptcy Act in § 1(30),8 includes nearly every method by which a person can dispose of property or an interest in property. The broad wording of this section leaves the meaning of the term virtually unrestricted. Further, in Pirie v. Chicago Title & Trust Co.,9 the United States Supreme Court refused to approve an interpretation which would narrow the scope of § 1(30). In Pirie, a creditor who had received monetary payments from an insolvent debtor argued that money was not "property" and thus could not be the subject of a transfer within the meaning of § 1(30). The Court held:

[A] transfer of property includes the giving or conveying [of] anything of value—anything which has debt-paying or debt-securing power.

... All technicality and narrowness of meaning is precluded. The word is used in its most comprehensive sense, and is intended to include every means and manner by which property can pass from the ownership and possession of another, and by


The four sections of § 67(d)(2) are virtually identical to the Uniform Fraudulent Conveyance Act §§ 4-7. This act has been adopted by statute in about half of the states. The Uniform Act has its origin in the Statute of Fraudulent Conveyances of 13 Elizabeth, 13 Eliz. ch. 5 (1570), which voided any conveyance made with "an intent to hinder, delay, and defraud creditors." 4 Collier, supra, § 67.29.

8. "Transfer" shall include the sale and every other and different mode, direct or indirect, of disposing of or of parting with property or with an interest therein or with the possession thereof or of fixing a lien upon property or upon an interest therein, absolutely or conditionally, voluntarily or involuntarily, by or without judicial proceedings, as a conveyance, sale, assignment, payment, pledge, mortgage, lien, encumbrance, gift, security, or otherwise; the retention of a security title to property delivered to a debtor shall be deemed a transfer suffered by such debtor.

which the result forbidden by the statute may be accomplished...10

Since a property interest must exist before a transfer can be made, however, a court may avoid the issue of whether a voidable transfer occurred by determining that the debtor never acquired any property interest. In Hoecker v. United Bank,11 the United States Court of Appeals for the Tenth Circuit used this approach in holding that a renunciation of a testamentary gift by an insolvent debtor was not a fraudulent transfer under § 67(d)(2).

Hoecker v. United Bank

In Hoecker, a father devised and bequeathed all of his property to his two sons, Joseph and Anthony. The will provided that if either of the two sons predeceased the father, then that son's share would pass to his children, per stirpes. Five months after the father's death, Anthony disclaimed irrevocably the share of the property he received under the will. He received no consideration for the renunciation. At the time of the disclaimer, there were creditors who had provable claims against Anthony, and without his share of the decedent's property he was insolvent. Within one year after renouncing, Anthony filed a voluntary petition in bankruptcy.12

The trustee in bankruptcy argued that Anthony's disclaimer met the requirements of a voidable fraudulent transfer under § 67(d)(2),13 and that his share of the testamentary property should be included in his bankruptcy estate. However, the court concluded that it was bound by the applicable state law on the testamentary disposition of property—a Colorado statute14 making the renunciation of a testamentary gift retroactive to the testator's death and distributing the property as though the disclaimant had predeceased the testator. The court inferred from this statute that the Colorado legislature intended that the property would not vest in the disclaimant but rather would pass directly from the testator to the next designated beneficiaries. Since the bankrupt thus had no vested interest in the property, the court concluded that his disclaimer did not operate as a transfer. There was, therefore, no violation of § 67(d)(2) of the Bankruptcy Act and the trustee was not allowed to claim the renounced property.15

10. Id. at 443-44 (emphasis added).
12. Id. at 839.
13. See text accompanying note 7 supra.
15. 476 F.2d at 839-41.
RENUNCIATION OF A LEGACY

Judge Holloway dissented. He considered the meaning of transfer to be a federal question since it involved a federal statute requiring uniform application throughout the United States. While he agreed that state law would control on the question of whether or not the property vested, he did not see this as the material issue. Regardless of the state rule on vesting, the right of the beneficiary to accept or renounce gave him the power to designate whether he or someone else would receive the property. Judge Holloway deemed this power over the disposition of property to be an interest in the property. He considered the exercise of the power by renunciation to be a “mode, direct or indirect,” of disposing of the interest and hence a transfer within the meaning of § 1(30) of the Act as expanded by Pirie v. Chicago Title & Trust Co. The trustee should, therefore, be allowed to claim the property under § 67(d)(2).

The distinction between the majority and dissent in Hoecker turned on the issue of whether the existence of a transferable interest in property is to be determined by federal bankruptcy law or by state property law. This issue constitutes the focus of the next section.

THE FEDERAL–STATE CONFLICT

As a general rule, federal courts will apply state law when the issues of a case do not present a substantial need for federal law to predominate. However, the Supreme Court has firmly established that state law is not always controlling. There are two interrelated reasons why a federal rule

16. Id. at 842. The necessity for a uniform application of the Bankruptcy Act was expressed by the Supreme Court in McKenzie v. Irving Trust Co., 323 U.S. 365, 369-70 (1945). See also text accompanying notes 41-43 infra.

17. Judge Holloway stated:

The Colorado statute recognizes that there is a limited power in the disclaimant to control the passing of his interest in the property during the six-months’ period after the will is admitted to probate, as well as later. And if the right of disclaiming is then exercised “... such property or beneficial interest so disclaimed shall pass ...” as if he had predeceased the decedent .... Thus under state law there is a power which seems to me to be a “mode, direct or indirect,” of disposing [of] or parting with his interest in the property and hence a transfer.

476 F.2d at 842.

18. 182 U.S. 438 (1901); see text accompanying notes 8-10 supra.


The laws of the several states, except where the Constitution or treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply.

Id. See also Hill, The Erie Doctrine in Bankruptcy, 66 HARV. L. REV. 1013 (1953), where the author strongly argues that bankruptcy courts should apply state law in dealing with actions under the federal Bankruptcy Act.

should be adopted to deal with a debtor's renunciation of a legacy or devise. The first is the necessity of preventing state law from frustrating the policies embodied in the Bankruptcy Act. The second is the need for nationwide uniformity in administering the provisions of the Act.

Protecting the Policies of the Bankruptcy Act from State Interference

There is no clear rule to determine whether a particular issue arising in bankruptcy is so central to the policies of the Bankruptcy Act that it must be resolved by federal law. The question appears to depend upon what section of the Act is involved and upon the specific facts of the case. Although the general rule followed by the Supreme Court in bankruptcy cases is to let state law control whenever possible, exceptions are made in cases where a state law frustrates the purposes or contradicts the express provisions of the Bankruptcy Act. In such cases, the state law is held unconstitutional under the supremacy clause of the Constitution.

For example, in Local Loan Co. v. Hunt, a leading bankruptcy case holding that federal law must prevail, the Supreme Court held that a pre-bankruptcy assignment of wages by the debtor could not be en-

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a Bankruptcy Act case, the Supreme Court stated:

It is a familiar doctrine that the prohibition of a federal statute may not be set at naught, or its benefits denied, by state statutes or state common law rules. In such a case our decision is not controlled by Erie R. Co. v. Tompkins. The Erie doctrine is inapplicable to those areas of judicial decision within which the policy of the law is so dominated by the sweep of federal statutes that legal relations which they affect must be deemed governed by federal law having its source in those statutes, rather than by local law. Id. at 176. This holding is consistent with other Supreme Court decisions. See, e.g., Heiser v. Woodruff, 327 U.S. 726 (1946); Prudence Realization Corp. v. Geist, 316 U.S. 89 (1941); Royal Indemnity Co. v. United States, 313 U.S. 289 (1941). See also Countryman, The Use of State Law in Bankruptcy Cases, 47 N.Y.U.L. Rev. 407, 409-11 (1972) [hereinafter cited as Countryman]. The author supports the application of federal law rather than state law in all areas of the Bankruptcy Act, arguing that Erie and the Rules of Decision Act, 28 U.S.C. § 1652 (1970), are not controlling where the Bankruptcy Act is involved.


23. This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

U.S. Const. art. VI.

forced by his creditor after he received a discharge in bankruptcy, despite a state court decision to the contrary. The Court stated that a discharge in bankruptcy abrogated all prior debts and rejected the state court’s decision "as being destructive of the purpose and spirit of the Bankruptcy Act."\(^{25}\) The Court also stated that "courts of bankruptcy are essentially courts of equity, and their proceedings inherently proceedings in equity."\(^{26}\) As such, the bankruptcy courts may use their equity powers to override state law where an equitable claim is established.

In 1971, the Supreme Court reinforced *Local Loan Co. v. Hunt* in *Perez v. Campbell*.\(^{27}\) In that case, the Court declared unconstitutional a state driver responsibility statute\(^ {28}\) because it allowed post-bankruptcy sanctions for debts discharged in bankruptcy. The statute permitted the restriction of driving privileges of people who had not paid automobile accident judgments against them even when the judgment debt had been discharged. The decision reversed two prior cases which had upheld similar statutes as furthering a valid state interest in promoting highway safety.\(^ {29}\) In *Perez*, the Court held that a valid state interest would no longer be sufficient to save the statute if it interfered with the full effectiveness of the federal Bankruptcy Act in providing complete nullification of pre-bankruptcy debts.\(^ {30}\) The Court added that this result would be the same even though the state's purpose in passing the statute was other than frustration of the Act.\(^ {31}\) It is helpful to apply the Supreme Court's analysis in *Local Loan* and *Perez* to the facts in the *Hoecker* case.

*Hoecker* presents a situation where state law frustrates the Bankruptcy Act policy of protecting the interests of creditors. The Act gives the trustee the power to collect the bankrupt's assets, including those which were transferred to avoid his creditors.\(^ {32}\) Since the state law in

\(^{25}\) *Id.* at 245.

\(^{26}\) *Id.* at 240.

\(^{27}\) 402 U.S. 637 (1971).


\(^{30}\) 402 U.S. at 651-52. The Court used a two-step process in determining whether a state law can stand when it covers the same area as a federal statute: (1) Ascertain the construction of both statutes; (2) Determine the constitutional question of whether they are in conflict. *Id.* at 644. Applying this test, the Court found, *id.* at 652, that Arizona's goal of protecting the highway-using public from financial hardship caused by irresponsible persons conflicted with the federal goal of giving debtors a "'new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.'" *Id.* at 648, quoting *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934).

\(^{31}\) 402 U.S. at 652.

Hoecker allowed the disclaimer to relate back and thus treated the property as having never vested, the disclaimant could use the state law to deplete the assets available to the creditors. By permitting this result, the state law frustrated the purpose embodied in § 67(d)(2) of preventing the debtor's pre-bankruptcy dissipation of assets. The Supreme Court clearly established in Local Loan\textsuperscript{33} and Perez\textsuperscript{34} that a state law which frustrates a purpose of the Bankruptcy Act cannot be allowed to stand in federal bankruptcy proceedings. Hence, a bankruptcy court is obliged to disregard the state law and to treat the issue as a federal question.

This conclusion is more specifically supported by two Supreme Court cases directly interpreting the terms "property" and "transfer" within the context of the federal-state conflict.\textsuperscript{35}

Usually the federal courts follow state law to determine what constitutes property and how it can be owned\textsuperscript{36} since there is no federal law of property. But in Board of Trade v. Johnson,\textsuperscript{37} the Supreme Court held that a seat on the Chicago Board of Trade was property within the meaning of the Bankruptcy Act despite a prior contrary decision by the Supreme Court of Illinois.\textsuperscript{38} The United States Supreme Court found the state rule to be inconsistent with other Supreme Court decisions regarding similar membership situations.\textsuperscript{39}

Where the bankrupt law deals with property rights which are regulated by the state law, the federal courts in bankruptcy will follow the state courts; \textit{but when the language of Congress indicates a policy requiring a broader construction of the . . . \[Bankruptcy Act\] than the state decisions would give it, federal courts can not be concluded by them}.\textsuperscript{40}

In the second case, McKenzie v. Irving Trust Co.,\textsuperscript{41} the Court had to determine if the bankrupt had given an unlawful preference under §

\begin{itemize}
    \item \textsuperscript{33} 292 U.S. 234 (1934).
    \item \textsuperscript{34} 402 U.S. 637 (1971).
    \item \textsuperscript{35} McKenzie v. Irving Trust Co., 323 U.S. 365 (1945); Board of Trade v. Johnson, 246 U.S. 1 (1924).
    \item \textsuperscript{36} McKenzie v. Irving Trust Co., 323 U.S. 365 (1945); Demorest v. City Bank Farmers Trust Co., 321 U.S. 36 (1944); Thompson v. Magnolia Petroleum Co., 309 U.S. 478 (1940).
    \item \textsuperscript{37} 246 U.S. 1 (1924).
    \item \textsuperscript{38} Barclay v. Smith, 107 Ill. 349 (1883).
    \item \textsuperscript{39} 264 U.S. at 9. The prior decisions were Sparhawk v. Yerkes, 142 U.S. 1 (1891) (memberships in the New York and Philadelphia stock exchanges); Hyde v. Woods, 94 U.S. 523 (1876) (ownership of a seat on the San Francisco Stock and Exchange Board).
    \item \textsuperscript{40} 264 U.S. at 10 (emphasis added).
    \item \textsuperscript{41} 323 U.S. 365 (1945).
\end{itemize}
60(a) of the Act to one of his creditors. The controlling issue was whether a transfer of money by check was complete at the time of receipt, pursuant to state law, or at the date of mailing, according to federal law as announced in the Supreme Court's interpretation of § 60(a). The Court held:

*What constitutes a transfer* and when it is complete within the meaning of § 60(a) of the Bankruptcy Act is necessarily a federal question, since it arises under a federal statute intended to have uniform application throughout the United States. Since § 1(30) defines the meaning of transfer for § 67(d)(2) as well as § 60(a), *McKenzie* supports the conclusion that the meaning of transfer is also a federal question under § 67(d)(2).

Thus, in a situation such as the one in *Hoecker*, the definitions of the terms "interest in property" and "transfer" should be considered as matters of federal law and should be dealt with in a manner that furthers the policies of § 67(d)(2).

**Need for Uniformity in Bankruptcy Law**

A second reason favoring a federal rule to deal with the renunciation problem is the need for a uniform application of the Bankruptcy Act throughout the United States. The Constitution requires uniformity and the importance of this requirement has been stressed by the Supreme Court. A number of policy considerations also support the use of federal law rather than state law in bankruptcy courts. State laws designed to affect debtor-creditor relations represent a wide variation in attitudes which are not consistent with a national bankruptcy law. Such laws may have been drafted without regard for federal bankruptcy policies or may even have been written with the specific intention of avoiding federal bankruptcy law. Other state laws, such as those concerning wills and property, have been developed for reasons totally unrelated to debtor-creditor relations and without concern for their im-

43. 323 U.S. at 369-70 (emphasis added).
44. U.S. Const. art. I, § 8 states in part: "The Congress shall have Power . . . To establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." *Id.*
46. This was the case with the driver responsibility statute in *Perez v. Campbell*, 402 U.S. 637 (1971). *Ariz. Rev. Stat. Ann.* § 28-1163(B) (1956) states: "A discharge in bankruptcy following the rendering of any such judgment shall not relieve the judgment debtor from any of the requirements of this article." *Id.*
plications in bankruptcy. Furthermore, state laws may be infrequently revised and thus ill-adapted to present-day bankruptcy situations. Reliance on differing state laws makes a person's rights dependent on where he lives. This may allow a party involved in a bankruptcy proceeding to seek out state rules which will give him a financial advantage over the other participants. The problem could be alleviated, and the requirements of the Constitution and the Supreme Court complied with, by a uniform application of federal bankruptcy law. 47

The precise issue here requiring uniform resolution is whether a renunciation is a transfer under § 67(d)(2) of the Bankruptcy Act. 48 State law cannot fulfill the need for uniformity because of the diversity in the statutes and common law of the various states regarding renunciation of property passing by will or by intestate succession.

Some states apply the common law rule that the beneficiary of a will may renounce the property to which he is entitled even where the purpose of the renunciation is to avoid creditors. 49 There are, however, several common exceptions to this rule. Renunciation to avoid creditors may be prohibited where there has been collusion between the debtor and those benefitting by the disclaimer, 50 or where the debtor has caused his creditors to extend credit in reliance on his apparent acceptance of the gift. 51 Furthermore, renunciation of a devise must be made within a reasonable time after the testator's death. If the devisee waits too long to renounce, he may thereafter be prevented from doing so, but the time limits vary from state to state. 52 Other states have chosen to reject the

47. Bankruptcy Act § 6, 11 U.S.C. § 24 (1970); see Countryman, supra note 20, at 475-76, where he argues for federal law even in the area of exemptions allowed to debtors, where state statutes have traditionally been followed.
48. Professor James A. McLachlan (who changed his name from its original spelling of McLaughlin), a leading authority on the Bankruptcy Act and one of the draftsmen of the Chandler Act of June 22, 1938, ch. 575, 52 Stat. 840, which substantially amended § 67(d)(2), now 11 U.S.C. § 107(d)(2) (1970), was particularly insistent that this section be applied as federal law and not according to the law of the individual states. See McLaughlin, Aspects of the Chandler Bill to Amend the Bankruptcy Act, 4 U. CHI. L. Rev. 369, 385-86 (1937). See also McLaughlin, Application of the Uniform Fraudulent Conveyance Act, 46 HARV. L. Rev. 404 (1933).
52. A delay of a few months has been held to be reasonable. Suverkrup v. Suverkrup, 106 Ind. App. 406, 18 N.E.2d 488 (1939); Schoonover v. Osborne, 193 Ia. 474, 187 N.W. 20 (1922). A delay of several years is usually too long. Strom v. Wood, 100 Kan. 556, 164 P. 1100 (1917). But at least one New York case has held that as little
common law rule entirely, holding that renunciations are never permitted where the effect is to defeat creditors.\footnote{53}

Not only do the various states differ in their rules for testamentary renunciation, but many states have different rules for renunciation of testamentary gifts than for renunciation of property acquired by intestacy. If a decedent dies intestate, the common law rule is that his heir cannot renounce the property that he receives by inheritance.\footnote{54} If the heir attempts to renounce, the property passes from him by release, contract, estoppel or actual conveyance, but he cannot prevent the property from vesting in him, at least for a short time.\footnote{55}

A further complication arises where the beneficiary of a will is also an heir and would have received the same share of the estate by succession had the testator died without a will.\footnote{56} In cases of this nature, where the beneficiary’s creditors have attempted to attach property passing by devise, it has been held that the devisee could not renounce the part of the property he would have received as an heir, but he could renounce any additional interest extended to him by the will beyond the amount of the intestate

as ten months was unreasonably long and renunciation was not allowed. \textit{In re Wilson’s Estate}, 298 N.Y. 398, 83 N.E.2d 852 (1949).

\footnote{53} The California Supreme Court has clearly ruled that an insolvent debtor cannot renounce a testamentary gift to avoid his creditors. \textit{In re Kalt’s Estate}, 16 Cal. 2d 807, 108 P.2d 401 (1940). A few other states seem to have taken a similar approach. \textit{See, e.g.}, \textit{Kearley v. Crawford}, 112 Fla. 43, 151 So. 293 (1933); \textit{Daniel v. Frost}, 62 Ga. 697 (1879); \textit{Estate of Buckius}, 4 Pa. Dist. 775 (1895). The California position has been adopted by statute in Indiana. \textit{IND. CODE} § 29-1-6-4 (1971), \textit{IND. ANN. STAT.} § 6-604 (1970). This statute states in pertinent part:

At any time within three (3) months after the appointment of a personal representative an heir or devisee may renounce his succession to all or any portion of the real or personal property of a decedent . . . except that no such renunciation shall be effective if it is objected to . . . by a creditor of the heir or devisee and if the court finds that the creditor is prejudiced thereby. \textit{Id.} (emphasis added).

\footnote{54} Coomes v. Finegan, 233 Ia. 448, 7 N.W.2d 729 (1943); Bostian v. Milens, 239 Mo. App. 555, 193 S.W.2d 797 (1946); Annot., 170 A.L.R. 424 (1947). \textit{See generally 6 PAGE ON WILLS, supra note 5, § 49.1.}

\footnote{55} Hardenbergh v. Commissioner, 198 F.2d 63 (8th Cir.), \textit{cert. denied}, 344 U.S. 836 (1952); \textit{Estate of Smith}, 103 Colo. 91, 83 P.2d 333 (1938).

In a case similar to \textit{Hoecker}, an insolvent debtor attempted to renounce an inheritance to keep it away from his creditors. The Court of Appeals for the Eighth Circuit referred the case to the state courts for a decision as to whether there had been a transfer by the debtor. Milens v. Bostian, 139 F.2d 282 (8th Cir. 1943). The Missouri state court held that the debtor could not renounce, since the property had passed by inheritance and not by will. Bostian v. Milens, 239 Mo. App. 555, 193 S.W.2d 797 (1946). Hence, the attempted renunciation constituted a conveyance by the debtor and could be set aside by the trustee under § 67(d) (2).

\footnote{56} When this occurs, the doctrine of “worthier title” treats the property devised as having passed by inheritance under the laws of intestacy rather than by will. Perkins v. Isley, 224 N.C. 793, 32 S.E.2d 588 (1945). \textit{See generally 6 PAGE ON WILLS, supra note 5, § 49.3.}
share. But sometimes this distinction is merely ignored.

In summary, the law of the various states governing renunciation follows no consistent pattern. Whether a renunciation constitutes a transfer may vary significantly from state to state for reasons seemingly arbitrary and irrelevant to bankruptcy proceedings. If it is determined, as in the Hoecker case, that the property must actually "vest" in the debtor under state law in order for there to be a transfer, the result may differ from state to state depending upon whether the debtor’s ancestor dies with or without a will, or whether the gift in the will is the same as the share which the heir would have received by intestacy, or whether the heir has waited seven months or ten months to renounce the gift to avoid his creditors. Hence, bankruptcy courts should develop a federal law in this area in order to achieve the necessary uniformity.

FEDERAL TREATMENT OF RENUNCIATION BY AN INSOLVENT DEBTOR IN BANKRUPTCY

The foregoing discussion indicates the need for a federal rule to resolve the issue of whether the renunciation of a legacy or devise by an insolvent debtor is a "transfer" under the Bankruptcy Act. Such a rule is necessitated by the obvious conflict of some state rules with the fundamental policies of the Act and by the desirability of uniformity in the application of the Act throughout the land. Consideration must now be given to what the federal rule should be.

Primarily, the federal rule should be designed to further the purposes of § 67(d)(2) by treating a renunciation by an insolvent debtor as a transfer. The renunciation can then be properly evaluated to determine whether the requisite elements are present to make it a fraudulent transfer and thus voidable by the trustee. Unless a transfer is found, the protection for creditors provided by § 67(d)(2) can never be utilized. There are at least two possible avenues available to achieve the desired result: (1) viewing the power over the disposition of property as an interest in property and hence capable of being the subject of a transfer within the definition of § 1(30); (2) disregarding state relation back rules in determining whether there was a transfer.

57. McGarry v. Mathis, 226 Ia. 37, 282 N.W. 786 (1938); Lehr v. Switzer, 213 Ia. 658, 239 N.W. 564 (1931).
59. If the transaction in Hoecker is defined by federal law to be a transfer, then it is necessarily a fraudulent transfer under § 67(d)(2) since the facts are established that the disclaimant received no consideration for the transfer and he was rendered insolvent by it. See 476 F.2d at 839.
RENUNCIATION OF A LEGACY

Power over Disposition as a Transferable Interest in Property

One possible approach is that of Judge Holloway's dissenting opinion in *Hoecker v. United Bank.* He viewed the power to control the disposition of the property as a form of vested property interest in the devisee, and considered the exercise of this power by renunciation to be a "mode, direct or indirect," of disposing of or parting with an interest in the property, and thus a transfer under the broad definition of § 1(30). This approach, unlike state rules allowing renunciation to relate back, would protect the interests of creditors while not directly contravening any state law. A federal determination that the right to accept or renounce is enough of a power to be considered an interest in property under the Bankruptcy Act may co-exist with state rules concluding that the debtor's possessory rights in the property have never vested. Thus, an exercise of the power may be deemed a transfer and can be set aside by the trustee if fraudulent.

A similar analysis has been utilized by the state courts in a number of cases where the exercise of an optional power by the debtor has been set aside as a fraudulent conveyance. Under the law of fraudulent conveyances, a release by the beneficiary of an equitable interest in a trust has been held void as against his creditors. Similarly, where a party released attachments on the property of a third party with an intent to defraud an attorney of his fee, the release was held fraudulent. It has also been held that a refusal to exercise a valid option contract was fraudulent and could be set aside. Some states hold that a creditor may exercise a debtor's right to contest a will even if the debtor does not wish to do so. In all of these examples, the conveyance involved a power which could be exercised at the option of the debtor, but not a possessory property interest. The power to accept or reject a devise is an option of a similar nature. It would be consistent with these state court decisions to conclude that the debtor's exercise of his option by renunciation may be considered a transfer and may be set aside in bankruptcy if fraudulent.

Additional support comes from provisions of the Bankruptcy Act

60. 476 F.2d 838, 842 (10th Cir. 1973).
61. Id. at 842.
64. Marsh v. Galbraith, 31 Tenn. App. 482, 216 S.W.2d 968 (1948).
65. Brooks v. Paine's Ex'r, 123 Ky. 271, 90 S.W. 600 (1906); In re Langevin's Will, 45 Minn. 429, 47 N.W. 1133 (1891); Bloor v. Platt, 78 Ohio St. 46, 84 N.E. 604 (1908).
dealing with optional rights in the debtor. In particular, the various provisions of § 70(a) of the Act vest in the trustee a number of powers which the debtor might exercise for his own benefit, such as rights of action upon contracts, rights of entry, and rights to patents, trademarks, and possibilities of reverter. Section 70(c) also gives the trustee the benefit of all meritorious defenses which the bankrupt might exercise against third persons. These provisions are indicative of a congressional policy to prevent the debtor from choosing an alternative which would be detrimental to the estate. Similarly, treating the renunciation of a legacy or devise by an insolvent debtor as a transfer furthers this policy since it also prevents the debtor from depleting the estate.

In conclusion, there is ample authority for a federal court to treat a renunciation by an insolvent debtor as a transfer. It clearly falls within the Supreme Court’s definition of transfer as including “every means and manner by which property can pass from the ownership and possession of another.” If the courts fail to interpret the Bankruptcy Act so as to achieve this result, Congress should amend the Act, either to explicitly include renunciation as a transfer or to give the trustee the debtor’s option to accept or renounce any inheritance, legacy or devise.

66. This section provides in part:
The trustee of the estate of a bankrupt . . . shall in turn be vested by operation of law with the title of the bankrupt . . . to all of the following kinds of property wherever located . . . (2) interests in patents, patent rights, copyrights, and trademarks . . . (3) powers which he might have exercised for his own benefit . . . (6) rights of action arising upon contracts, or usury, or the unlawful taking or detention of or injury to his property . . . (7) contingent remainders, executory devises and limitations, rights of entry for condition broken, rights or possibilities of reverter . . . .
67. The trustee shall have the benefit of all defenses available to the bankrupt as against third persons, including statutes of limitations, statutes of frauds, usury, and other personal defenses . . . .
68. Pirie v. Chicago Title & Trust Co., 182 U.S. 438, 444 (1901).
69. Although Congress has not specifically faced the problem of property received by inheritance, legacy or devise before bankruptcy, it has dealt with property so received after bankruptcy in the first full paragraph after clause (8) of § 70(a):
All property, wherever located . . . which vests in the bankrupt within six months after bankruptcy by bequest, devise or inheritance shall vest in the trustee . . . as of the date when it vested in the bankrupt, and shall be free and discharged from any transfer made or suffered by the bankrupt after bankruptcy.
11 U.S.C. § 110(a) (1970). While this provision faces the matter more directly than § 67(d)(2), it is not certain that the wording used would require that a renunciation be set aside. That issue would still depend on whether state law or federal law determined when the property vested in the bankrupt. There seem to be no cases which have faced this question. But see Annot., 11 A.L.R.2d 738 (1950).
RENUNCIATION OF A LEGACY

Prohibition of State Relation Back Rules in Federal Bankruptcy Proceedings

An additional approach to the resolution of the problem of renunciations by insolvent debtors is for the courts to adopt a policy of disregarding state relation back rules in the determination of whether a transfer occurred under § 67(d)(2). The entire issue of renunciation to avoid creditors could be settled more easily if it were not for such rules. Standing alone, the renunciation of a devise creates no particular problems. There is a generally accepted rule that a beneficial devise or bequest is presumed to be accepted until it is renounced. Given this presumption, if a renunciation meets the § 67(d)(2)(a) criteria of present or ensuing insolvency and absence of consideration and is made within one year prior to bankruptcy, it is a fraudulent conveyance and can be set aside. The problem is created by state rules which make the renunciation retroactive to the testator's death, with the effect that the property is treated as having never vested in the beneficiary so that he has nothing to transfer.

The concept of relation back has a number of useful and justifiable applications in property law. It is a legal fiction which is used mainly for administrative convenience or to achieve equity for a party who might otherwise be treated unfairly. In general, relation back is employed to provide equitable protection for one party, but not by imposing any unfair burdens on third parties. Renunciation of a testamentary gift to avoid creditors is not analogous. In this situation, relation back


71. For example, upon delivery of a deed from escrow, the conveyance may be related back to the date when the deed was first placed in escrow in order to protect the grantee's title where the grantor died while the deed was in escrow, Simpson v. McGlathery, 52 Miss. 723 (1876), Prutsman v. Baker, 30 Wis. 644 (1872), or to allow the grantee to convey legal title while the deed was in escrow, Tooley v. Dibble, 2 Hill 641 (N.Y. 1842). Testamentary letters and letters of administration may be related back to the testator's death in order to validate sales of the property of the estate made by the executor before the will is admitted to probate, Wilson v. Wilson, 54 Mo. 213 (1873), and to protect the executor from liability for acts committed in the interim for the benefit of the estate, Nance v. Gray, 143 Ala. 234, 38 So. 916 (1904), see Annot., 26 A.L.R. 1359 (1923). One court applied relation back to the renunciation by the beneficiary of an equitable interest in a trust in order to void the trust and prevent the property from being seized by the Alien Property Custodian. Stoehr v. Miller, 296 F. 414 (2d Cir. 1923). Another court allowed the renunciation of a devise to relate back to the testator's death so that the renouncing devisee would not be required to pay the state inheritance tax. People v. Flanagin, 331 Ill. 203, 162 N.E. 848 (1928).

72. In re Kalt's Estate, 16 Cal. 2d 807, 812, 103 P.2d 401, 403 (1940); Wilson v. Wilson, 54 Mo. 213, 216 (1873); Prutsman v. Baker, 30 Wis. 644, 649 (1872).

73. Some states have recognized the dissimilarity of the two situations and have
does not protect the renouncing beneficiary, since he will lose the property either to the creditors or to the other heirs or beneficiaries. But there is damage to the creditors, who are losing the opportunity to collect legitimate debts. The only ones benefiting from the relation back rule are the next heirs or beneficiaries, who are receiving a windfall gain at the expense of the creditors. Unfortunately, many courts apply the rule in this situation without noticing that its normal justifications are not present. As a result, a rule founded on mere convenience has been allowed to become an instrument of injustice to creditors. As one commentator has stated:

"It must be apparent... that the doctrine which causes a renunciation to relate back so as to be operative from the moment of the deceased's death is largely conceptual, and its indiscriminate application may frequently lead to an inequitable result." 75

Within the context of the Bankruptcy Act itself, there is authority for disregarding state relation back rules. Section 67(a) 76 deals with judicial liens, which are voidable if they attach to the debtor's property within four months prior to bankruptcy. 77 While state law is used to determine the date when the lien attaches, 78 it is generally held that state rules permitting relation back are not applicable. 79 An invalid lien attaching within the four-month period cannot be protected by having it relate back to the start of a proceeding 80 or the entry of a judgment 81

taken appropriate steps to prevent relation back rules from working an injustice to creditors. See authorities cited note 53 supra.

74. Admittedly, the devisee is not a disinterested party since he would probably prefer to have the property pass to his family members, but an overt desire to accomplish this could be construed as actual fraud and thus voidable under § 67(d) (2) (d), 11 U.S.C. § 107(d) (2) (d) (1970). Transfers among family members are usually suspect and sometimes prima facie fraudulent. See McWilliams v. Edmondson, 162 F.2d 454 (5th Cir. 1947).

A given situation may involve both a renunciation to avoid creditors and an intent to benefit family members, but the two issues are not identical. While a renunciation could be set aside because of actual fraud if the transaction was intended to benefit family members by avoiding creditors, this note provides more general methods for dealing with renunciations which apply regardless of whether the next takers are family members or total strangers.

75. Note, Renunciation of Testamentary Gift to Defeat Claims of Devisee's Creditors, 43 YALE L.J. 1030, 1032 (1934). See also 37 MICH. L. REV. 1168 (1939).


77. See generally 4 COLLIER, supra note 7, §§ 67.04.

78. See, e.g., McLeod v. Cooper, 88 F.2d 194 (5th Cir.), cert. denied, 301 U.S. 705 (1937); Reilly v. Sabin, 81 F.2d 259 (D.C. Cir. 1935).

79. In re Darwin, 117 F. 407 (6th Cir. 1902); In re Laskaris, 4 F. Supp. 652 (W.D.N.Y. 1933); In re Prunotto, 51 F.2d 602 (W.D.N.Y. 1931).


which occurred prior to the four-month period.

Similarly, § 60(a) deals with illegal preferences extended to favored creditors by the bankrupt within four months prior to bankruptcy. An early Supreme Court case had held that a debtor's pledge of stocks and bonds within four months prior to bankruptcy related back to his promise to pledge made prior to the four-month period. Hence, the pledge was not an illegal preference. By amendments in 1938 and 1950, Congress rejected this holding by specifically prohibiting the use of the relation back rule in § 60(a) cases. These amendments evidence a congressional policy against permitting relation back rules to frustrate the provisions of the Bankruptcy Act.

Relation back is a legal fiction which creates an injustice when it is used to permit a debtor's renunciation to avoid his creditors. Prohibiting the use of the rule under § 67(d)(2) does not contravene any compelling state interest, and there is congressional and judicial support for this approach.

CONCLUSION

In actions under the Bankruptcy Act, the renunciation of an inheritance, legacy or devise by an insolvent debtor should be treated as a matter of federal law, either by defining the power to control the disposition of property as a transferable property right to bring it within the purview of § 67(d)(2) or else by proscribing the application of the relation back rule to renunciations by insolvent debtors. Bankruptcy courts, if they are to perform their duty to uphold the spirit and purpose of the Bankruptcy Act, should adopt one of these solutions. There is ample authority for both under the case law as well as by analogy to other related areas of the Bankruptcy Act. However, if the courts are inclined to follow nonuniform and often inequitable state rules in this area, then the change should come through a congressional amendment to the Bankruptcy Act.

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84. Act of June 22, 1938, ch. 575, 52 Stat. 840; Act of Mar. 18, 1950, ch. 70, 64 Stat. 24; see H.R. Rep. No. 1293, 81st Cong., 1st Sess. (1949). However, congressional action is not necessarily required to achieve this result. The congressional attitude evidenced by the 1938 and 1950 amendments are supportive of judicial action in this area as well. See cases cited notes 79-81 supra, where the courts disregarded relation back rules without specific statutory authorization.