Volume 97 | Issue 1 Article 10

September 1994

BFP v. Resolution Trust Corporation: Supreme Court Shifts Focus onto State Law in Ruling on Mortgage Foreclosure Sales

Audy M. Perry Jr.
West Virginia University College of Law

BFP v. RESOLUTION TRUST CORPORATION: SUPREME COURT SHIFTS FOCUS ONTO STATE LAW IN RULING ON MORTGAGE FORECLOSURE SALES

I. INTRODUCTION

In a recent victory for mortgage lenders, the United States Supreme Court made it more difficult for debtors and junior creditors to set aside foreclosure sales of property when a property owner is forced to sell the property at a foreclosure sale and then files bankruptcy within a year of the sale.[1] Federal courts had formulated a variety of methods to ascertain when a debtor may avoid a mortgage foreclosure sale when the debtor had "received less than a reasonably equivalent value in exchange for such transfer or obligation."[2] Courts had struggled to find a balance between protecting foreclosure sale purchasers from losing their purchase and protecting debtors from fraudulent transactions. A divided United States Supreme Court tried to give "sensible content" to 11 U.S.C. § 548 in *BFP v. Resolution Trust Corp.*[3]

The 5-4 majority[4] held that as long as the state's foreclosure law requirements were met, the price received at a noncollusive foreclosure sale conclusively establishes "reasonably equivalent value" of mortgage property.[5] Moreover, the majority held that "fair market value" was not the benchmark for evaluating mortgage foreclosure sales.[6] In fact, they found fair market value to be "the very *antithesis*" of a forced-sale value.[7] Thus, the Court, specifically rejecting the *Durrett* or *Bundles* approach,[8] found there to be no benchmark other than the price received at the properly conducted foreclosure sale.

The dissent argued that the majority, by not following the intent of Congress, was allowing a "peppercorn" to be the reasonably equivalent

1. 11 U.S.C. § 548 (1988).
2. 11 U.S.C. § 548(a)(2)(A) (1988).
3. 114 S. Ct. 1757, 1766 (1994).
4. Scalia, J. delivered the opinion of the Court, in which Rehnquist, C.J., O'Connor, Kennedy, and Thomas, JJ., joined. Souter filed the dissenting opinion, in which Blackmun, Stevens, and Ginsburg, JJ., joined.
5. *BFP*, 114 S. Ct. at 1765.
6. *Id.* at 1761.
7. *Id.*
8. For a discussion of the *Durrett* approach, *see infra* text accompanying notes 29-36; for a discussion of the *Bundles* approach, *see infra* text accompanying notes 48-54.

value for California beachfront property.[9] However, the dissent, by not endorsing any other particular valuation method, seemed to prefer that each Bankruptcy Court decide on a case-by-case basis.[10]

Despite the concerns of the dissent, the *BFP* decision will help to bring more certainty to real estate title and foreclosure sales. Although not answering all of the questions concerning the avoidance of foreclosure sales, the decision does rule against overturning a sale for price insufficiencies. However, now debtors and bankruptcy trustees will focus upon any irregularities in the foreclosure sale process and not on the property's fair market value. Therefore, it is imperative that lenders know the applicable state law, and surpass the law's minimum provisions in some instances, to help prevent the avoidance of a foreclosure sale. The purpose of this Note is to review foreclosure sale law in light of the *BFP* decision and to provide guidance to lenders on the foreclosure sale process in West Virginia.

II. BACKGROUND OF THE LAW

There are two theories on which a real estate foreclosure sale can be challenged: fraudulent conveyance law and state foreclosure law. This part of the Note discusses the history of fraudulent conveyance and state foreclosure law, the specific aspects of the federal fraudulent conveyance law[11] at issue in *BFP*, and the various circuit courts' interpretations of that section.

A. Fraudulent Transfer Law

The foundation for our federal fraudulent transfer law can be traced to sixteenth century England. The Statute of 13 Elizabeth prohibited "covinous and fraudulent" transfers intended "to delay, hinder or defraud creditors and others."[12] As debtors learned to avoid the

9. *BFP*, 114 S. Ct. at 1767.
10. *Id.* at 1772-73.
11. 11 U.S.C. § 548(a)(2)(A) (1988).
12. *BFP*, 114 S. Ct. at 1763 (citing 13 Eliz. ch. 5 (1570)).

statute by hiding their intent, the English courts began to allow a creditor to prove fraudulent intent objectively.[13] These objective indices of intent, or "badges of fraud," were used to raise a rebuttable presumption of fraudulent intent.[14]

The idea of constructively proving fraud was incorporated into American bankruptcy law. The Bankruptcy Act of 1898 specifically adopted the language of the Statute of 13 Elizabeth[15] and these basic principles were recognized in the Uniform Fraudulent Transfer Act in 1984.[16]

B. Foreclosure Law

The English Courts of Chancery developed the law of foreclosure with the "equity of redemption," which allowed the debtor to buy back his property after the original due date, or "law day."[17] Because title to forfeited property could remain clouded for years after law day, the expanded period of redemption left lenders in a quandary.[18] The courts responded by creating the equitable remedy of foreclosure, whereby the borrower was forever foreclosed from exercising his equity of redemption after a certain date.[19] With this remedy, known as "strict foreclosure," "the borrower's entire interest in the property was forfeited, regardless of any accumulated equity."[20]

The next major change in the development of foreclosure law occurred in 19th century America. To avoid the harsh consequences of strict foreclosure, the "foreclosure by sale" was created which provided

---

13. *BFP*, 114 S. Ct. at 1763. For example: a transfer to a close relative, a transfer of title without a change of possession, or grossly inadequate consideration. *Id.*

14. *Id.* (citing Twyne's Case, 3 Coke Rep. 80b, 76 Eng. Rep. 809 (K.B. 1601); ORLANDO F. BUMP, FRAUDULENT CONVEYANCES: A TREATISE UPON CONVEYANCES MADE BY DEBTORS TO DEFRAUD CREDITORS 31-60 (1882)).

15. *Id.* (citing Bankruptcy Act of July 1, 1898, ch. 541, § 67(e), 30 Stat. 564-65).

16. UNIF. FRAUDULENT TRANS. ACT, 7A U.L.A. 639 (1985).

17. *BFP*, 114 S. Ct. at 1763.

18. *Id.*

19. *Id.*

20. *Id.* (citing G. GLENN, 1 MORTGAGES 3-18, 358-62, 395-406 (1943); G. OSBORNE, MORTGAGES 144 (2d ed. 1970)).

that any surplus over the debt be given to the debtor.[21] Following the "foreclosure by sale" principle, each state created diverse networks of judicially and legislatively crafted rules governing the foreclosure process to achieve what each state considered the proper balance between the needs of lenders and borrowers.[22] Currently, all states permit judicial foreclosure conducted under direct judicial oversight; approximately half of the states also permit foreclosure through a private power of sale provided in the mortgage documents.[23]

Currently, although the foreclosure laws differ from state to state, most require: notice to the borrower; a substantial period of time before the foreclosure proceedings can begin; publication of the notice of sale; and adherence to the prescribed bidding rules and auction procedures.[24]

C. *Section 548 of the Bankruptcy Code*

BFP challenged the foreclosure sale under the fraudulent transfer provision of the Federal Bankruptcy Code, 11 U.S.C. § 548 (section 548).[25] Under section 548, the trustee in bankruptcy, or the debtor in

---

21. *Id.* (citing GLENN, *supra* note 20, at 460-62, 622; OSBORNE, *supra* note 20, at 661-63).

22. *Id.*

23. *Id.* (citing Robert M. Zinman et al., *Fraudulent Transfers According to Alden, Gross and Borowitz: A Tale of Two Circuits,* 39 BUS. LAW. 977, 1004-05 (1984)).

24. *Id.* (citing Zinman, *supra* note 23, at 1002, 1004-05; G. OSBORNE, *supra* note 20, at 683, 733-35); G. Osborne et al., REAL ESTATE FINANCE LAW 9, 446-47, 475-77 (1979).

25. Title 11 U.S.C. § 548 (1988) provides in relevant part:

> (a) The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily- (1) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted; or (2)(A) received less than a reasonably equivalent value in exchange for such transfer or obligation; and (B)(i) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation . . . .

Id.

possession in a Chapter 11 case, has the power to avoid both actual and constructively fraudulent transfers.[26] A transfer is deemed actually fraudulent and can be set aside if the trustee establishes that there was "actual intent to hinder, delay, or defraud."[27] A transfer can be set aside for constructive fraud if the trustee can establish:

> (1) that the debtor had an interest in the property; (2) that a transfer of that interest occurred within one year of the filing of the bankruptcy petition; (3) that the debtor was insolvent at the time of the transfer or became insolvent as a result thereof; and (4) that the debtor received "less than a reasonably equivalent value in exchange for such transfer."[28]

The focus of *BFP* was on the requirement of "reasonably equivalent value" found in 11 U.S.C. § 548(a)(2)(A). This phrase, undefined in the code, had resulted in a split among the circuits as to its meaning and applicability.

D. Determining "Reasonably Equivalent Value"

Prior to the *BFP* decision, the courts had formulated several approaches to determine what constituted a "reasonably equivalent value" under section 548(a)(2)(A) of the Bankruptcy Code. However, most courts followed one of three approaches for determining whether a transfer was voidable for receiving less than a reasonably equivalent value. These three predominant approaches were *Durrett*, *Bundles*, and *Madrid*, which are discussed in detail below.

1. The *Durrett* Approach

One approach used to determine if reasonably equivalent value was received at a foreclosure sale of real estate was the "*Durrett* approach" or the "seventy-percent test." This test established that a foreclosure sale yielding less than seventy-percent of the fair market value of the

---

26. *BFP* was concerned with the constructive fraud provision regarding transfers by insolvent debtors. *BFP*, 114 S. Ct. at 1760.

27. 11 U.S.C. § 548(a)(1) (1988).

28. *BFP*, 114 S. Ct. at 1760 (interpreting 11 U.S.C. § 548(a)(2) (1988)).

property was a fraudulent transfer for lack of reasonably equivalent value.[29] The *Durrett* approach was derived from dicta in *Durrett v. Washington National Insurance Co.*[30] In *Durrett*, the Court stated that it had been unable to locate any decision by a court that did not avoid a foreclosure sale of real estate yielding less than seventy-percent of the property's fair market value. Although the court's statements were dicta, these statements were construed to establish a seventy-percent test.[31] The *Durrett* approach had been followed in the Eleventh and Fifth Circuits,[32] and had also been approved by a Bankruptcy Court in at least one federal district where the Court of Appeals of that circuit had not expressly decided the issue.[33]

The *Durrett* approach, more so than the other approaches, potentially preserved more of the debtor's assets for distribution to the unsecured creditors.[34] However, the approach was criticized as creating a *de facto* federal right of redemption in the trustee for a one-year peri-

---

29. *E.g.*, First Fed. Sav. & Loan Ass'n v. Standard Bldg. Assocs., Ltd., 87 B.R. 221, 223 (Bankr. N.D. Ga. 1988).

30. Durrett v. Washington Nat'l. Ins. Co., 621 F.2d 201, 203 (5th Cir. 1980).

31. *E.g.*, *In re* General Indus., Inc., 79 B.R. 124 (Bankr. D. Mass. 1987); *In re* Willis, 48 B.R. 295 (Bankr. S.D. Tex. 1985); First Fed. Sav. & Loan Ass'n v. Standard Bldg. Assocs., Ltd., 87 B.R. 221 (Bankr. N.D. Ga. 1988); *In re* Wheeler, 34 B.R. 818 (Bankr. N.D. Ala. 1983); *In re* Park N. Partners, Ltd., 72 B.R. 79 (Bankr. N.D. Ga. 1987), *vacated on other grounds*, 80 B.R. 551 (Bankr. N.D. Ga. 1987). *See* 9A AM. JUR. 2D *Bankruptcy* § 1857 (1991), for a general overview.

32. *In re* Willis, 48 B.R. 295 (Bankr. S.D. Tex. 1985); First Fed. Sav. & Loan Ass'n. v. Standard Bldg. Assocs., Ltd., 87 B.R. 221 (Bankr. N.D. Ga. 1988); *In re* Coleman, 21 B.R. 832 (Bankr. Tex. 1982); *In re* Ocean Dev. of America, Inc., 22 B.R. 834 (Bankr. S.D. Fla. 1982), *reh'g. denied*, 24 B.R. 51 (Bankr. S.D. Fla.); *In re* Perdidio Bay Country Club Estates, Inc., 23 B.R. 36 (Bankr. S.D. Fla. 1982); *In re* Wheeler, 34 B.R. 818 (Bankr. N.D. Ala. 1983); *In re* Park North Partners, Ltd., 72 B.R. 79 (Bankr. N.D. Ga. 1987), *vacated on other grounds*, 80 B.R. 551 (Bankr. N.D. Ga.). *See* 9A AM. JUR. 2D *Bankruptcy* § 1857 (1991).

33. *In re* Berge, 33 B.R. 642 (Bankr. W.D. Wis.), *motion granted in part, modified on other grounds*, 37 B.R. 705 (Bankr. W.D. Wis. 1983).

34. Martha Lassiter Sewell, *Avoidance of Foreclosure Sales Under Section 548 of the Bankruptcy Code: A Balancing of Interests*, 27 WAKE FOREST L. REV. 1011, 1025 (1992).

od[35] and of inviting "federal intrusion into an area of law traditionally controlled by the States."[36]

2. The *Madrid* Approach

A second approach to reasonably equivalent value is the "*Madrid* approach." This approach was derived from *In re Madrid*,[37] in which the court held that the price received at a noncollusive and regularly conducted foreclosure sale is conclusively presumed to be a reasonably equivalent value for the property sold. The *Madrid* approach is based primarily on the policy consideration that subjecting properly conducted foreclosure sales to attack as fraudulent transfers would, in effect, create a "*de facto* right of redemption" in the trustee.[38] Such a right would significantly chill participation at foreclosure sales, depress prices obtained at the sales, and increase deficiency judgments.[39] Additionally, courts following the *Madrid* approach reasoned that to hold otherwise would create "negative repercussions" in the lending arena because "creditors would be less willing to lend funds on the security of a mortgage or deed of trust."[40] The Ninth Circuit continues to follow the *Madrid* approach.[41] The Sixth Circuit, in dictum, adopted the reasonably equivalent value presumption,[42] and several Bankruptcy Courts in circuits where the question had not been answered approved of the *Madrid* approach.[43]

---

35. William H. Henning, *An Analysis of Durrett and Its Impact on Real and Personal Property Foreclosures: Some Proposed Modifications*, 63 N.C. L. REV. 257, 265 (1985).

36. Johnny L. Woodruff, *Certiorari to In re BFP: The Eve of Decision to a Dozen Years of Durrett Conflict — Will Resolution of the Issue Solve the Real Problem?*, 24 MEM. ST. U. L. REV. 773, 787 (1994).

37. *In re* Madrid, 21 B.R. 424, 427 (Bankr. 9th Cir. 1982), *aff'd on other grounds*, 725 F.2d 1197 (9th Cir.), *cert. denied*, 469 U.S. 833 (1984).

38. *In re* New Yorketown Assocs., 40 B.R. 701 (Bankr. E.D. Pa. 1984); *In re* Robinson, 80 B.R. 455 (Bankr. N.D. Ill. 1987).

39. 9A AM. JUR. 2D *Bankruptcy* § 1858 (1991).

40. *Id.* at § 1858. *See also In re* Winshall Settlor's Trust, 758 F.2d 1136 (6th Cir. 1985); *In re* Ristich, 57 B.R. 568 (Bankr. N.D. Ill. 1986); *In re* Madrid, 725 F.2d 1197 (9th Cir. 1984); *In re* Verna, 58 B.R. 246 (Bankr. D. Cal. 1986).

41. *In re* BFP, 974 F.2d 1144, 1148 (9th Cir. 1992).

42. *In re* Winshall Settlor's Trust, 758 F.2d 1136, 1139 (6th Cir. 1985).

43. *See, e.g.*, *In re* Upham, 48 B.R. 695, 697 (Bankr. W.D.N.Y. 1985); *In re* Ristich,

The *Madrid* approach provides finality and stability to real estate foreclosure sales[44] and preserves the integrity of state real estate law.[45] However, it has been criticized for giving too much deference to state foreclosure law[46] and allowing the purchaser at a sale to receive a windfall at the expense of unsecured creditors.[47]

3. The *Bundles* Approach

The third major approach, from the Seventh Circuit decision *In re Bundles*,[48] determined that the decision of reasonably equivalent value must be reached on a case-by-case basis. According to the *Bundles* approach, the court must examine the facts surrounding the sale after an evidentiary hearing, with a rebuttable presumption that the foreclosure sale price is sufficient. Courts following this case-by-case approach, found "reasonably equivalent value" to be an elusive concept which could not be determined, as with the *Durrett* approach, solely on the basis of whether a foreclosure sale yielded a given percentage of market value.[49] The case-by-case approach had been adopted by the Seventh[50] and Eighth[51] Circuits, as well as by several federal district and bankruptcy courts in other circuits.[52] In fact, at one time the case-

---

57 B.R. 568, 577 (Bankr. N.D. Ill. 1986); *In re* Verna, 58 B.R. 246, 252 (Bankr. D. Cal. 1986). *See* 9A AM. JUR. 2D *Bankruptcy* § 1858 (1991).

44. Scott B. Ehrlich, *Avoidance of Foreclosure Sales as Fraudulent Conveyances: Accommodating State and Federal Objectives*, 71 VA. L. REV. 933, 955 (1985).

45. Woodruff, *supra* note 36, at 789.

46. Sewell, *supra* note 34, at 1027.

47. Woodruff, *supra* note 36, at 790.

48. *In re* Bundles, 856 F.2d 815, 824 (7th Cir. 1988).

49. 9A AM. JUR. 2D *Bankruptcy* § 1860 (1991).

50. *In re* Bundles, 856 F.2d 815 (7th Cir. 1988).

51. *In re* Hulm, 738 F.2d 323, 327 (8th Cir. 1984).

52. *See, e.g., In re* Richard, 26 B.R. 560 (Bankr. D.R.I. 1983); *In re* Ruebeck, 55 B.R. 163 (Bankr. D. Mass. 1985); *In re* General Indus., Inc., 79 B.R. 124 (Bankr. D. Mass. 1987); *In re* Carr, 40 B.R. 1007 (Bankr. D. Conn. 1984); *In re* Adwar, 55 B.R. 111 (Bankr. E.D.N.Y. 1985); *In re* Pruitt, 72 B.R. 436 (Bankr. E.D.N.Y. 1987); *In re* Jones, 20 B.R. 988 (Bankr. E.D. Pa. 1982); *In re* New Yorketown Assocs., 40 B.R. 701 (Bankr. E.D. Pa. 1984); *In re* Smith, 24 B.R. 19 (Bankr. W.D.N.C. 1982); *In re* Garrison, 48 B.R. 837 (Bankr. D. Colo. 1985); Lower Downtown Assocs., L.P. v. Brazosbanc Sav. Ass'n, 52 B.R.

by-case approach seemed to be the "emerging majority view."[53] Although a balance between the extremes of *Durrett* and *Madrid*, the *Bundles* approach had been criticized for creating uncertainty in foreclosure sales.[54]

4. After *BFP*

The *BFP* decision specifically rejected the *Durrett* and *Bundles* approaches[55] while affirming the Ninth Circuit's *Madrid* approach.[56] Because the Court in *BFP* specifically limited its ruling to mortgage foreclosures of real estate,[57] it may not be applicable to other types of foreclosure or forced sales. It is clear, however, that in determining the reasonably equivalent value for a mortgage foreclosure of real estate, the *Madrid* approach is the law of the land.

III. STATEMENT OF THE CASE

In 1987, Wayne and Marlene Pedersen and Russell Bartone formed a partnership, BFP, for the purpose of buying a home in Newport Beach, California. They had hoped to renovate and sell the property for a quick profit.[58] BFP acquired title to the house, subject to a first deed of trust in favor of Imperial Savings Association for $356,250[59] and a second deed of trust to the sellers, Sheldon and Ann Foreman for $200,000.[60] When BFP failed to make the monthly payments to Imperial Savings, a notice of foreclosure was issued. The foreclosure proceedings were temporarily delayed when Imperial was declared insolvent. The Resolution Trust Corporation was appointed as the re-

662 (Bankr. D. Colo. 1985). *See also* 9A AM. JUR. 2D *Bankruptcy* § 1860 (1991).

53. 9A AM. JUR. 2D *Bankruptcy* § 1860 (1991).

54. Sewell, *supra* note 34, at 1030.

55. *BFP*, 114 S. Ct. at 1761-62.

56. *Id.* at 1767.

57. *Id.* at 1761 n.3.

58. For a further explanation of the circumstances behind *BFP*, *see* James S. Granelli, *Partners Take Gamble — and Lose*, L.A. TIMES, May 24, 1994, at D1.

59. This amount represents a loan to the Pedersons for the purchase of the home. *BFP*, 114 S. Ct. at 1759.

60. This amount represented a promissory note. *Id.*

ceiver of Imperial. At the foreclosure sale of the BFP property on July 12, 1989, Paul Osborne purchased the home for $433,000.[61]

Three months after the foreclosure sale, BFP filed for Chapter 11 bankruptcy and petitioned the bankruptcy court to set aside the sale to Osborne as a fraudulent transfer. BFP argued that the home was worth over $725,000 at the time of the sale, and that $433,000 was not a "reasonably equivalent value" and thus constituted a fraudulent conveyance under 11 U.S.C. § 548.[62] Finding that the foreclosure sale had been properly conducted under California law without collusion or fraud, the bankruptcy court dismissed the complaint against Osborne and granted summary judgment in favor of Imperial.[63] The district court affirmed Osborne's motion to dismiss,[64] and a divided bankruptcy appellate panel affirmed Imperial's motion for summary judgment.[65] Utilizing the *Madrid* approach,[66] the panel majority found that a "non-collusive and regularly conducted nonjudicial foreclosure sale . . . cannot be challenged as a fraudulent conveyance because the consideration received in such a sale establishes 'reasonably equivalent value' as a matter of law."[67] The Ninth Circuit Court of Appeals consolidated the two BFP appeals and affirmed both.[68] BFP then filed a petition for certiorari, which the United States Supreme Court granted in May, 1993.[69]

IV. THE DECISION

The United States Supreme Court agreed to review the case in order to settle a dispute between the circuits as to the meaning of

---

61. *Id.*
62. *Id. See supra* note 25 for text of statute.
63. *BFP*, 114 S. Ct at 1759.
64. *Id.*
65. BFP v. Imperial Sav. & Loan Ass'n, 132 B.R. 748 (Bankr. 9th Cir. 1991).
66. *See In re* Madrid, 21 B.R. 424 (Bankr. 9th Cir. 1982), *aff'd on other grounds*, 725 F.2d 1197 (9th Cir.), *cert. denied*, 469 U.S. 833 (1984).
67. *BFP*, 132 B.R. at 750 (citing *Madrid*, 21 B.R. at 424).
68. *In re* BFP, 974 F.2d 1144 (9th Cir. 1992).
69. 113 S. Ct. 2411 (1993).

"reasonably equivalent value" in the context of fraudulent transfer law. Specifically, the Court considered whether the 11 U.S.C. § 548 requirement that transfers of property by insolvent debtors within one year prior to the filing of a bankruptcy petition be in exchange for "a reasonably equivalent value," was satisfied by the price received at a properly conducted, noncollusive, real estate mortgage foreclosure sale.[70] The Court affirmed the decisions of the three lower courts and held that the consideration received at a properly conducted sale conclusively establishes "reasonably equivalent value" for purposes of 11 U.S.C. § 548(a)(2).[71]

Justice Scalia wrote the majority opinion, joined by Chief Justice Rehnquist, Justice O'Connor, Justice Kennedy, and Justice Thomas. Justice Souter, joined by Justice Blackmun, Justice Stevens, and Justice Ginsburg, wrote the indignant dissent. The two high-spirited opinions reflect the difficulty that a court faces when it attempts to balance the rights of lenders, debtors, and purchasers in the foreclosure sale process.

A. The Majority Opinion: Foreclosure Sale Price is Conclusive

The majority first looked at the code section in question: 11 U.S.C. § 548(a)(2).[72] After determining that "transfer" includes a foreclosure sale,[73] the Court sought to define the Code term "reasonably equivalent value." Since only the word "value" is defined within the code section,[74] the Court reviewed the definitions of "reasonably equivalent" used by the circuit courts.

The discussion began with *Durrett v. Washington National Insurance Co.*[75] and the seventy-percent approach. The Court then compared the *Durrett* approach to the *In re Bundles*[76] line of cases,

70. 11 U.S.C. § 548(a)(2) (1988).
71. *BFP*, 114 S. Ct. at 1765.
72. *See supra* note 25 for the text of the statute.
73. *BFP*, 114 S. Ct. at 1760.
74. 11 U.S.C. § 548(d)(2)(A) (1988).
75. 621 F.2d 201 (5th Cir. 1980).
76. 856 F.2d 815 (7th Cir. 1988).

wherein the Seventh Circuit rejected the *Durrett* approach in favor of a case-by-case, "all facts and circumstances" approach to the question of reasonably equivalent value.[77] The opinion listed several other alternative approaches,[78] but concentrated primarily on *Durrett* and *Bundles* since both measured reasonably equivalent value against fair market value in determining the propriety of the sale.[79] The majority opined that the use of fair market value as determinative of reasonably equivalent value was inconsistent with the text of the Bankruptcy Code.[80] Because the term "fair market value" does not appear in section 548, while the term does appear in other sections of the Code,[81] the majority reasoned, therefore, that Congress went "out of its way" to avoid that standard term and instead chose the "entirely novel phrase 'reasonably equivalent value.'"[82]

Furthermore, the majority reasoned that market value has no applicability in the forced-sale context[83] because "'[f]air market value' presumes market conditions that, by definition, simply [cannot be obtained] in the context of a forced sale."[84] Both *Durrett* and *Bundles* failed to "come to grips with this glaring discrepancy between the factors relevant to an appraisal of a property's market value, on the one hand, and the strictures of the foreclosure process on the other."[85] The majority asserted that when all of these factors were considered, property that must be sold within the time and manner strictures of state-prescribed foreclosures are "simply *worth less*."[86] Furthermore, the majority remarked that "no one would pay as much to own such

77. *BFP*, 114 S. Ct. at 1760; *see supra* text accompanying notes 29-54.
78. *Id.* at 1760.
79. *Id.* at 1761.
80. *Id.*
81. *E.g.*, 11 U.S.C. § 522 (1988).
82. *BFP*, 114 S. Ct. at 1761.
83. *Id.*
84. *Id.*
85. *Id.*
86. *Id.* at 1762.

property as he would pay to own real estate that could be sold at leisure and pursuant to normal marketing techniques."[87]

The majority then looked at other possible constructions of reasonably equivalent value. They considered whether there could be a "reasonable" forced-sale price.[88] The majority thought that perhaps this was the source of *Durrett* and *Bundles*' reasoning.[89] However, the majority found that a "reasonable" forced-sale price construction represented "policy determinations which the Bankruptcy Code gives no apparent authority to make."[90]. The majority reasoned that how closely a price received at a foreclosure sale approximated its fair market value was dependent upon the terms of the forced sale.[91] However, because the terms of foreclosure sales differ from state to state, establishing a federal "reasonable" foreclosure-sale price would "extend federal bankruptcy law well beyond the traditional field of fraudulent transfers, into realms of policy where it has not ventured before."[92]

The majority asserted that to hold that the "reasonably equivalent value" language in section 548(a)(2) required a certain minimum price beyond state foreclosure law would be to claim that the Bankruptcy Code had adopted *Durrett* or *Bundles*.[93] The majority refused to presume such a "radical departure" from the Code's plain language without clearer textual guidance.[94]

The majority found an essential state interest at issue in that "the general welfare of society is involved in the security of the titles to real estate"[95] and to hold otherwise would cause a "federally created cloud" over every title of realty purchased at a foreclosure sale.[96] Finding no federal statutory purpose for displacing state regulation, the

87. *Id.*
88. *Id.*
89. *Id.*
90. *Id.* at 1762-63.
91. *Id.*
92. *Id.* at 1763.
93. *Id.* at 1764.
94. *Id.*
95. *Id.* at 1764 (quoting American Land Co. v. Zeiss, 219 U.S. 47, 60 (1911)).
96. *Id.* at 1765.

majority held that the Bankruptcy Code should be interpreted to adopt the pre-existing state law.[97]

The majority declined to read the phrase "reasonably equivalent value" in section 548(a)(2) to mean, as applied to mortgage foreclosure sales, either "fair market value" or "fair foreclosure price," whether calculated as a percentage of fair market value or otherwise.[98] Instead, the Court held that the price received at a foreclosure sale conforming to the applicable state foreclosure laws conclusively establishes "reasonably equivalent value" for the purposes of section 548 of the Bankruptcy Code.[99]

The majority insisted that this conclusion did not render section 548 superfluous, as the dissent argued,[100] because the "reasonably equivalent value" criterion would continue to have independent meaning outside the foreclosure context.[101] In other words, section 548(a)(2) would continue to be an exclusive means of invalidating some foreclosure sales because, if the sale was set aside for violating state procedural laws, then the price at the sale loses its conclusive force.[102]

The last portion of the majority's opinion was dedicated to a general response to the dissent. After pointing out that "one searches Justice Souter's opinion in vain for any alternative response to the question of the transferred property's worth,"[103] the majority noted that it was the "proper function of *this* Court to give 'sensible content' to the provisions of the United States Code."[104] The majority opinion concluded with a summary argument for their decision: The "reasonably equivalent value" inquiry is applicable to all transfers, but the strictures of foreclosure sales affect a property's worth by "completely redefining

97. *Id.*
98. *Id.*
99. *Id.* at 1765.
100. *Id.* at 1770. *See infra* text accompanying notes 116-17.
101. *Id.* at 1765.
102. *Id.*
103. *Id.* at 1766.
104. *Id.*

the market in which the property is offered for sale."[105] Therefore, the usual benchmark of a property's worth (fair market value) is inapplicable and "the only legitimate evidence of the property's value at the time it is sold is the foreclosure sale price itself."[106]

B. The Dissent: An Implausible Proposition

The dissent argued that the majority's reasoning was implausible and in "derogation of the straightforward language used by Congress."[107] The dissent noted that Congress, in the course of amending the Bankruptcy Code in 1984, considered, but did not enact, an amendment that said "precisely what the majority now says the current provision means."[108] The dissent noted that, "even if one is careful not to attach too much significance to such a legislative nonoccurrence, it surely cautions against undue reliance on a different, entirely speculative congressional 'omission.'"[109] Furthermore, the dissent urged that the words and meaning of section 548(a)(2) were clear.[110] The dissent asserted that an ordinary person conversant with the English language would conclude that the provision required the court to compare the price received with the worth of the item and to set aside the transfer if the former was unreasonably less than the latter.[111]

Moreover, the dissent complained that the majority was creating a foreclosure-sale exception in section 548(a)(2), through the use of a narrowed construction of the section.[112] Although the dissent agreed with the majority that foreclosure sales usually do obtain comparatively lower prices than other transfers and that every such sale should not be set aside,[113] the dissent argued that rejection of this option did not necessarily lead to the majority's alternative that avoidance be allowed

105. *Id.* at 1767.
106. *Id.*
107. *Id.*
108. *Id.* at 1767 n.1. *See* S. 445, 98th Cong., 1st Sess. § 360 (1983).
109. *Id.* at 1767 n.1.
110. *Id.* at 1768.
111. *Id.* at 1768-69.
112. *Id.* at 1767.
113. *Id.* at 1767-68.

only where the foreclosure sale was collusive or had failed to comply with state foreclosure laws.[114] The dissent argued that simply meeting the majority's criteria did not guarantee that the sale has produced a price "reasonably equivalent" to the value of the property.[115]

The dissent also argued that if the majority view was correct, there would be no need for the 1984 amendments[116] because, if a property's value is conclusively presumed to be whatever it is sold for, then the question of "less than reasonably equivalent value" would never be worth asking in a real estate foreclosure context.[117]

Furthermore, the dissent expressed confidence that bankruptcy courts were competent to determine whether "reasonably equivalent value" was received.[118] The dissent noted that the bankruptcy courts "regularly make comparably difficult (and contestable) determinations about the 'reasonably equivalent value' of assets transferred through other means than foreclosure sales."[119]

The dissent focused in on what they believed to be the underlying principle of the Bankruptcy Code: fair balance between rights of creditors and debtors.[120] They noted that avoiding procedurally regular foreclosure sales for inadequate prices was "consistent with those policies of obtaining a maximum and equitable distribution for creditors . . . which the Court has often said are at the core of federal bankruptcy law."[121]

In conclusion, the dissent agreed with the majority that *BFP* involved a choice between two possible statutory provisions:

---

114. *Id.* at 1768.
115. *Id.* at 1767-68.
116. The 1984 Bankruptcy Amendments include involuntary transfers within a trustee's section 548 avoidance powers and provide that the foreclosure of a debtor's equity of redemption is a "transfer." Martin I. Klein, *The Demise of "Durrett,"* N.Y.L.J., June 13, 1994, at 1 [hereinafter Klein].
117. *BFP*, 114 S. Ct. at 1770.
118. *Id.* at 1772.
119. *Id.*
120. *Id.* at 1774.
121. *Id.*

> [O]ne authorizing the trustee to avoid involuntary transfers for less than a reasonably equivalent value,[122] and another precluding such avoidance when a secured party or third party purchaser obtains title to an interest of the debtor in property pursuant to a good faith prepetition foreclosure proceeding permitting the realization of security upon default of the borrower.[123]

However, the dissent argued that the choice was made by Congress in 1984 when it enacted the former alternative rather than the latter. The dissent concluded that the court, therefore, should apply the statute "as Congress wrote it."[124]

V. ANALYSIS OF THE CASE

The United States Supreme Court denied the debtor's petition for rehearing,[125] therefore, one must evaluate mortgage foreclosure law in light of the *BFP* decision. This part of the Note addresses *BFP*'s applicability and impact on mortgage lenders in general and then specifically focuses on what *BFP* will mean to mortgage lenders in West Virginia.

A. BFP's Applicability to Bids by Mortgagees

The *BFP* decision was decided in the context of a third-party purchaser, therefore, there may be some question as to its applicability to foreclosure bids by mortgagees. The majority in *BFP* reasoned that since the price of foreclosed property is "simply worth less" than property in a free market context, then the price received at the sale must represent the property's reasonably equivalent value. However, as explained below, when a foreclosure sale is simply the mortgagee bidding on its own collateral, this argument may lose some of its force.[126]

---

122. 11 U.S.C. § 548(a)(2)(A) (1988). *See also supra* note 25.

123. *BFP*, 114 S. Ct. at 1777-78 (quoting S. 445, 98th Cong., 1st Sess., § 360 (1983)) (citations omitted).

124. *Id.* at 1778.

125. 114 S. Ct. 2771 (1994).

126. Kenneth M. Block & Jeffrey B. Steiner, *Ending the Threat of "Durrett,"* N.Y.L.J., July 20, 1994, at 5 [hereinafter Block].

The economic interests of a foreclosing mortgagee are in opposition to those of the debtor and his other creditors:[127] first, the mortgagee lacks incentive to bid more than the amount of the indebtedness because any surplus will be turned over to the debtor or junior creditors and second, if the mortgagee can purchase the property for the amount of the indebtedness and resell the property, any profits can be kept as a windfall.[128] Considering these factors, courts may find the majority's "free market" rationale difficult to accept. Indeed, some courts prior to *BFP* only allowed the conclusive presumption of reasonably equivalent value if a third party purchaser was the successful bidder at the foreclosure sale.[129] Additionally, closer scrutiny may occur in "mortgagee-only-bidder" sales because the bankruptcy trustees will now argue that such sales are collusive, whereas before, the trustee may have been content with the "inadequate" price argument to set aside the sale.

Fortunately for the mortgagee, the free market theory was not the only rationale the Supreme Court gave for its decision in *BFP*. The Court also held that states, having a legitimate interest in protecting the titles of real estate, should set all parameters on forced sale prices. The majority held that without clearer textual guidance from Congress, federal courts could not displace state law. Clearly then, if the sale could have only been challenged under state law in the context of a third-party purchaser, it is unlikely that federal law would apply in cases where the mortgagee is the purchaser.[130] Thus, the *BFP* decision should apply to foreclosing mortgagees with equal effect as to third-party bidders. Therefore, mortgagees should be allowed to take

127. *BFP*, 114 S. Ct. at 1775.

128. Block, *supra* note 126, at 5.

129. Robert A. Glaves, *The Controversy Over Section 548 of the Bankruptcy Code in the Mortgage Arena: Making the Case for a Federal Statute Reforming the Foreclosure Process*, 23 J. MARSHALL L. REV. 683, 698 (1990).

130. Block, *supra* note 126, at 6.

advantage of the conclusive presumption of "reasonably equivalent value."

B. BFP's Impact on Mortgage Lenders

The Supreme Court's decision in *BFP* restored confidence in the finality of forced sales and freed mortgagees from the burden of obtaining a certain percentage of fair market value in order to sell foreclosed property.[131] Prior to *BFP*, security of title was placed in jeopardy by providing unhappy debtors the weapon of bankruptcy litigation even after all state remedies were utilized. However, *BFP* does not ensure finality to the process. Although lenders and purchasers at foreclosure sales now have another arrow in their defensive arsenal, there are still ways for an unhappy debtor or junior creditor to attack the validity of the sale. *BFP* shifts the disgruntled debtor or junior creditor's attention from the foreclosure sale price to the foreclosure procedure. Trustees in bankruptcy will now focus their efforts on finding fault with the foreclosure sale procedure and on using state foreclosure law as their weapon.[132] Also, it is important to remember that *BFP* dealt only with the Bankruptcy Code; challenges under state foreclosure law (suits in equity) may remain unaffected by the *BFP* decision.[133]

Nevertheless, *BFP* is a definite victory for the mortgage lender. It provides Supreme Court authority that the Bankruptcy Code does not provide for a challenge of inadequate price at a foreclosure sale.[134] However, since the focus will now be upon whether the sale was conducted according to state foreclosure law,[135] it is imperative that the

131. Block, *supra* note 126, at 7.

132. *See* Barr v. Allen, 170 B.R. 772, 776 (Bankr. E.D.N.Y. 1994) (because of the *BFP* decision, the only issue was whether the foreclosure sale was "accordant procedurally and substantively with applicable South Carolina state foreclosure law"). Price may still become a factor in determining whether a sale should be set aside, but the challenge is under state foreclosure law, not federal bankruptcy law. *Id.*

133. The holding of *BFP* regarding "reasonably equivalent value" only applies to the Federal Bankruptcy Code, and thus challenges under state foreclosure law that the price received at a foreclosure sale was so low as to "shock the conscience" of the court are still viable, but are beyond the scope of this Note.

134. When state foreclosure sale procedures have been met, a challenge for inadequacy of sale price can only be brought under state foreclosure and not under the fraudulent transfer law of the Bankruptcy Code. *BFP*, 114 S. Ct. at 1763.

135. *See supra* note 132.

lender know the applicable state foreclosure laws to help ensure that the foreclosure sale will withstand procedural attack.

C. Foreclosure Sale Requirements in West Virginia

The conclusive presumption of "reasonably equivalent value" provided by *BFP* is contingent upon the requirement that the sale must satisfy the state's foreclosure law. Thus, mortgage lenders and their lawyers must review the applicable state law. For simplification, the foreclosure sale process in West Virginia will be divided into three steps: notice, sale, and recording of documents.

1. Notice

Adequate notice is crucial in preventing the avoidance of a foreclosure sale because the notice undertaken represents the best opportunity with which the mortgage lender can show to the court that reasonable measures were taken to try to ensure that third parties were notified of the sale. The West Virginia Code provides that:

> Every notice of sale by a trustee under a trust deed shall show the following particulars: (a) the time and place of sale; (b) the names of the parties to the deed under which it will be made; (c) date of the deed; (d) the office and book in which it is recorded; (e) the quantity and description of the land or other property or both conveyed thereby; and (f) the terms of sale.[136]

---

136. W. VA. CODE § 38-1-4 (Supp. 1994).

If a title search has revealed any federal or state tax liens, then special notice procedures must be followed. Concerning tax liens, the *BFP* majority expressly stated that it was only determining "reasonably equivalent value" in the context of mortgage foreclosure sales and that other forced sales may be different. *BFP*, 114 S. Ct. at 1761 n.3. However, some courts have held that the *BFP* decision does apply with equal force to tax foreclosures. *See In re* McGrath, 170 B.R. 78 (Bankr. D.N.J 1994); *In re* T.F. Stone Co., Inc., 1994 WL 456767 (Bankr. N.D. Tex. 1994). *But see In re* Butler, 1994 WL 446044 (Bankr. N.D. Ill. 1994) ("*BFP* may not be applicable with respect to tax sales . . . this question can be revisited at and following trial").

Regarding the terms of sale, the West Virginia Code requires that the sale be conducted upon the terms set forth in the deed of trust, or by the terms set forth in Section 38-1-5.[137] Case law construing Section 38-1-5 suggests that generally, flexibility is allowed in the terms of sale specified in the deed of trust, but whatever the terms, they must be strictly followed.[138] The most frequent term of sale used is cash in hand on the day of the sale.

a. Publication

After the notice of sale has been prepared, the West Virginia Code requires that it be published and served.[139] The Code currently mandates that the notice be published as a Class II legal advertisement in an authorized publication for the county in which the property is located.[140] If the publication or the service requirements in the deed of trust are greater than those imposed by statute, then the deed controls.[141] Additionally, the Code requires that the publisher provide an affidavit of publication evidencing publication of the notice of sale.[142]

---

137. W. VA. CODE § 38-1-5 (1985), terms of sale for real property if none are mentioned in the deed:

> [O]ne third of the purchase money cash in hand, one third thereof, with interest, in one year, and the residue thereof, with interest, in two years from the day of sale, taking from the purchaser his notes, with good security, for the deferred payments, and either retaining the legal title as further security or conveying the legal title and reserving in the deed of conveyance a lien for the deferred purchase money, or otherwise securing the same.

Id.

138. *See* Lallance v. Fisher, 2 S.E. 775 (W. Va. 1887) (if deed provided for a sale by cash, a sale by credit is invalid).

139. W. VA. CODE § 38-1-4 (Supp. 1994); W. VA. CODE §§ 59-3-1 et seq. (1985).

140. A class II legal advertisement is an advertisement published once a week for two consecutive weeks prior to the sale. W. VA. CODE § 59-3-2 (Supp. 1994). Under recent amendments, posting of the notice on the courthouse door is no longer adequate. *See* State *ex rel.* Thomas v. Neal, 299 S.E.2d 23 (W. Va. 1982) (holding that such service was insufficient notice).

141. W. VA. CODE § 38-1-4 (Supp. 1994).

142. W. VA. CODE § 59-3-4(a) (Supp. 1994).

b. Service

The West Virginia Code requires that a copy of the notice of sale be served upon the grantor and upon any subordinate lienholder who has previously notified the primary lienholder of its claim at least twenty days prior to the sale.[143] Again, if the deed of trust or other related loan documents provide for greater notice or publication requirements than the statute, then the documents will control.[144] The notice is deemed complete when mailed by certified mail, return receipt requested, directed to the grantors at the address shown in the deed of trust or in a writing delivered to the beneficiary of the deed of trust subsequent to the execution and delivery of the trust deed.[145]

2. The Sale

The actual foreclosure sale is a relatively simple process. It must be conducted on the date, and at the time and place specified in the notice of sale (which in turn must be in accordance with the agreements of the parties as set forth in the deed of trust or other related documents).[146]

At the appointed time and place, the trustee begins the sale by reading a copy of the notice of sale. The trustee then offers the property for sale to the highest bidder.[147] At the conclusion of the bid-

143. W. VA. CODE § 38-1-4 (Supp. 1994). *But see* Joy v. Chessie Employees Fed. Credit Union, 411 S.E.2d 261 (W. Va. 1991) (eighteen days notice to grantor was found reasonable).

144. W. VA. CODE § 38-1-4 (Supp. 1994).

145. W. VA. CODE § 38-1-4 (Supp. 1994). Other methods of service are permitted but they are expressly stated to be "in addition to, but not in lieu of" service by certified mail. *Id.*

146. W. VA. CODE § 38-1-3 (1985).

147. The trustee may obtain the assistance of an auctioneer to cry the sale although the trustee must actually ring down the sale. *See* Copelan v. Sohn, 82 S.E. 1016 (W. Va. 1912).

ding, the trustee announces that the bidding is closed, as well as the name of the purchaser and the dollar amount of the bid.

After payment of the purchase price, the trustee must prepare, execute, and deliver a deed conveying the property sold to the successful bidder, properly apply the proceeds of sale, and make a report of the sale.[148] The West Virginia Code provides that the trustee's expenses of sale are entitled to be paid first from the proceeds,[149] including: (1) the cost of publishing the notice of sale; (2) the cost of certified mailing of the notice of sale or other service of the notice; (3) the trustee's fee;[150] (4) transfer stamps; (5) cost of deed preparation; and (6) auctioneer's expenses and costs.

After payment of the trustee's expenses, the balance is then applied to the indebtedness secured by the deed of trust under which the foreclosure has occurred. If there is a surplus, the Code directs that the trustee pay the surplus "to the grantor, his heirs, personal representatives or assigns, as their interests may appear."[151]

Thomas H. Gilpin,[152] a West Virginia seminar speaker on the subject of foreclosure sales, suggests that, although not required by statute, some additional precautions should be observed.[153] These extra steps may help prevent subsequent factual disputes and litigation. For example, immediately prior to conducting the foreclosure sale, the title to the subject property should be updated to rule out any new problems. Also prior to the sale, the trustee should confirm that the beneficiary (mortgagee) has received no notice of bankruptcy, injunction or the like, and that the beneficiary has received the publisher's affidavit. These final preparations help to reassure the lender that all

148. W. VA. CODE § 38-1-8 (1985). A sample form of the trustee's deed is found in W. VA. CODE § 38-1-6 (1985).

149. W. VA. CODE § 38-1-7 (1985).

150. W. VA. CODE § 38-1-7 (1985) provides that the trustee's fee shall be 5% on the first $300.00 and 2% on the residue.

151. *Id.*

152. Thomas H. Gilpin, Partner, Huddleston, Bolen, Beatty, Porter & Copen, Huntington, W. Va.

153. Thomas H. Gilpin, *Real Property Foreclosure Procedures*, Continuing Legal Education Address, Charleston, W. Va. (June 15, 1994) [hereinafter Gilpin].

the necessary steps have been taken and to reduce subsequent problems.

At the foreclosure sale, the trustee should make a record of the persons in attendance, the individuals making any bid, and the value of the bids. This extra effort in record keeping may prevent a later factual dispute about the sale. Also, once the bidding is closed, the purchaser and trustee should immediately meet to make arrangements for the payment of the purchase price.[154]

Finally, although as stated previously, the West Virginia Code directs that the trustee pay any surplus "to the grantor, his heirs, personal representatives or assigns," caution should be exercised. If there are subsequent lienholders and a surplus from the sale proceeds, it is risky for a trustee to make a determination as to which of the various parties is entitled to the surplus. In such circumstances, the safest course for the trustee may be to institute an interpleader action in the circuit court of the county where the property was sold and let the court determine who is entitled to the proceeds.[155]

3. Recording of Documents

The West Virginia Code requires that the trustee make a report of the sale within two months after the sale is completed.[156] The report of sale should include: (1) the publisher's affidavit certifying that the notice of sale had been published; (2) a recital by the trustee that notice was served upon the parties required to be served under West Virginia Code Section 38-1-4; and (3) a detailed accounting of the proceeds of the sale, including the amount of the proceeds paid to the holder of the lien upon which foreclosure was made.[157] The trustee

---

154. *See* Fleming v. Holt, 12 W. Va. 143, 156 (1877) (holding that trustee sale is complete when the trustee accepts the bid and signs the memorandum of sale).

155. *See* W. VA. CODE § 38-1-7 (1985); Banks-Miller Supply Co. v. Smallridge, 175 S.E.2d 446, 451 (W. Va. 1970).

156. W. VA. CODE § 38-1-8 (1985). If the trustee fails to record the proper account, his commission can be forfeited. *Id.*

157. W. VA. CODE § 38-1-8 (1985). If the beneficiary was the successful bidder of the

should execute this report and record it with the Clerk of the County Commission of the county where the deed of trust was first recorded.[158]

D. Real Estate Foreclosure Law in West Virginia

In West Virginia, suits challenging the price received at a real estate foreclosure sale can be raised under the Federal Bankruptcy Code,[159] the West Virginia's Uniform Fraudulent Transfer Act,[160] and suits in equity under the state's foreclosure laws. Since the Bankruptcy Code concerns the federal court system and is discussed in *BFP*, this part of the Note discusses only the Uniform Fraudulent Transfer Act and suits in equity as applicable to West Virginia.

1. Uniform Fraudulent Transfer Act

In an attempt to provide uniformity of law among the states, the National Conference of Commissioners on Uniform State Laws enacted the Uniform Fraudulent Transfer Act (UFTA) in 1984.[161] West Virginia adopted its version of UFTA in 1986.[162] The West Virginia UFTA provides for transfers which are fraudulent as to present and future creditors, remedies of the creditors, and defenses of the transferee. With regard to its provision for the price received at a transfer, the West Virginia UFTA uses the same phrase found in the Bankruptcy Code: "reasonably equivalent value." However, unlike the Bankruptcy Code, the West Virginia UFTA defines the phrase in the Code:

> [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 ac-

---

sale, then a statement that a credit to the amount owed for the remaining proceeds should be made.

158. W. VA. CODE § 38-1-8 to -9 (1985).

159. 11 U.S.C. § 548 (1988).

160. W. VA. CODE § 40-1A-1 to -12 (Supp. 1994).

161. UNIF. FRAUDULENT TRANSFERS ACT, 7A U.L.A. 639 (1985).

162. W. VA. CODE § 40-1A-1 to -12 (Supp. 1994).

> quisition or disposition of the interest of the debtor upon default under a mortgage, deed of trust or security agreement.[163]

Thus, the West Virginia UFTA is in agreement with the holding in *BFP* regarding "reasonably equivalent value."

2. Suits in Equity

Through case law, the Supreme Court of Appeals of West Virginia has applied a "shock the conscience" test to suits in equity challenging the validity of a foreclosure sale. This test is summarized as:

> A sale of real estate by a trustee will not be set aside upon the ground of inadequacy of price unless such inadequacy is so great as to shock the conscience of the chancellor. Such a sale will not be disturbed where the price realized is *approximately three fourths* of the estimated value of the property.[164]

This language has caused some West Virginia lenders not to bid less than seventy-five percent of the appraised value at a foreclosure sale for fear of having the sale set aside as a fraudulent conveyance. However, a more detailed review of the applicable cases reveals that the cited case merely upholds a sale of approximately three fourths of the estimated value, as opposed to establishing a seventy-five percent floor and, in fact, bases its decision upon an earlier case which found that a sale of approximately one half of the value did not "shock the conscience" of the court.[165]

---

163. W. VA. CODE § 40-1A-3(b) (Supp. 1994).

164. Rife v. Woolfolk, 289 S.E.2d 220, 223 (W. Va. 1982) (quoting Pence v. Jamison, 94 S.E. 383, 384, Syl. Pt. 9 (W. Va. 1917)) (emphasis added).

165. As discussed *supra* note 164, *Rife* was quoting from a syllabus point in *Pence*. *Pence* involved a challenge that the price paid at the foreclosure sale was grossly inadequate and that the sale should be set aside. The Court looked at Lallance v. Fisher, 2 S.E. 775 (W. Va. 1887) (upholding a sale for one half of the estimated value) and Copelan v. Sohn, 82 S.E. 1016 (W. Va. 1912) (upholding sale for one half of the estimated value) in concluding that a sale price of three fourths of the market value did not "shock the conscience."

The most recent Supreme Court of Appeals of West Virginia decision on this issue, *Benavides v. Shenandoah Federal Savings*,[166] does not refer to any set percentage, but does reaffirm the shock the conscience test. Thus, it could be argued that the "shock the conscience" test in West Virginia considers the facts and circumstances of the individual case, much like the *Bundles* approach, instead of a *Durrett* minimum percentage approach.

To summarize, in West Virginia, challenges of price at real estate foreclosure sales can be made under the Federal Bankruptcy Code, the West Virginia Uniform Fraudulent Transfer Act (WVUFTA), or suits in equity. After the United States Supreme Court's ruling in *BFP*, both the Bankruptcy Code and WVUFTA provide that the price received at a properly conducted, noncollusive sale conclusively establishes a "reasonably equivalent value." However, the rule is less clear in suits in equity in West Virginia, where the courts apply a "shock the conscience" test to the sales.[167]

E. Recommendations to West Virginia Lenders

With regard to mortgage foreclosures, the *BFP* decision supplied the same conclusive presumption of "reasonably equivalent value" to the Federal Bankruptcy Code as found in the WVUFTA. Thus, the fraudulent conveyance focus will now, more than ever, be upon whether the foreclosure sale was in accordance with the applicable state

166. 433 S.E.2d 528 (W. Va. 1993).

167. The holding of *BFP* regarding "reasonably equivalent value" only applies to the Federal Bankruptcy Code, and thus challenges under state foreclosure law that the price received at a foreclosure sale was so low as to "shock the conscience" of the court are still viable, but are beyond the scope of this Note.

For a review of West Virginia cases utilizing the "shock the conscience" test, the following are suggested: Lallance v. Fisher, 2 S.E. 775 (W. Va. 1887) (upholding sale for one-half of the estimated value); Copelan v. Sohn, 82 S.E. 1016 (W. Va. 1912) (upholding sale for one-half of the estimated value); Pence v. Jamison, 94 S.E. 383 (W. Va. 1917) (upholding sale for three-fourths of the estimated value); Rife v. Woolfolk, 289 S.E.2d 220 (W. Va. 1982) (setting aside sale for one-seventh of the estimated value); Tudor v. Tudor, 298 S.E.2d 108 (W. Va. 1982) (setting aside sale for more than one-seventh of the estimated value); Benavides v. Shenandoah Fed. Sav., 433 S.E.2d 528 (W. Va. 1993) (upholding sale for approximately 48% of the estimated value).

foreclosure laws or whether the sale "shocks the conscience" of a court in equity.

According to Thomas H. Gilpin,[168] some lenders in West Virginia had already been supplanting the West Virginia Code's minimum notice requirements in an attempt to attract as many bidders as possible to the sale.[169] Most commentators agree that inadequate notice of the sale is a major factor in realizing a low price at a foreclosure sale.[170] Unless potential bidders are aware of the sale, there will be no competitive bidding, and low prices will continue to be realized. The extra preparation costs may reduce the chance of litigation and save the expense and frustration of having a sale later invalidated.

An additional concern is that the Supreme Court of Appeals of West Virginia has, in certain cases, held that merely following an applicable statute does not always guarantee success when the applicable statute is deficient or the result is inequitable.[171] Therefore, lenders should anticipate close scrutiny of their foreclosure sale procedures if a debtor or an unsecured creditor believes the sale was unfair. Extra steps with regard to notice provide a good way to stifle such challenges by providing debtors and unsecured creditors with the opportunity to bid at the sale and lessening their challenge before the court.[172]

---

168. *See supra* note 152.

169. Gilpin, *supra* note 153.

170. Glaves, *supra* note 129, at 691; Steven Wechsler, *Through the Looking Glass: Foreclosure by Sale as De Facto Strict Foreclosure — An Empirical Study of Mortgage Foreclosure and Subsequent Resale*, 70 CORNELL L. REV. 850, 891 (1985); Woodruff, *supra* note 36, at 797.

171. *See* Lilly v. Duke, 376 S.E.2d 122 (W. Va. 1988) (involving statutory provision for forfeiture of delinquent lands); State *ex rel.* Thomas v. Neal, 299 S.E.2d 23 (W. Va. 1982) (holding statutory allowance of posting notice on the door insufficient); Cordell v. Jarrett, 301 S.E.2d 227 (W. Va. 1982) (setting aside otherwise valid and enforceable default judgment); State *ex rel.* Payne v. Walden, 190 S.E.2d 770, 777 (W. Va. 1972) (overruling statutory distress provision).

172. *See* Benavides v. Shenandoah Fed. Sav. Bank, 433 S.E.2d 528, 531 (W. Va. 1993) (contention of inadequate sale price was "slightly weakened" by failure of appellant to bid at the sale despite her presence there).

Completeness is the key to providing sufficient notice in a West Virginia foreclosure sale. The more information provided, the less likely a court will find collusion or a violation of the applicable statutes. Therefore, although notices frequently omit the name of the beneficiary (mortgagee) of the trust deed, it is a better practice to include the name of the beneficiary in the notice to fully comply with the statutory requirement of Section 38-1-4(b).[173] Additionally, depending on the various circumstances of each sale, statutory notice requirements may be supplemented with some of the following information regarding the authority to sell or the terms of sale: (1) a recital that relief from stay has been obtained, if applicable; (2) a statement that the trustee shall have the right to adjourn the sale by oral proclamation;[174] (3) any known prior liens; (4) any provisions necessary to handle the sale of multiple parcels under a single deed of trust, if applicable; (5) any exceptions for prior liens, whether known or unknown;[175] (6) disclosure of any IRS right of redemption.[176]

Regarding the West Virginia Code requirements of service,[177] although not specifically required by the statute, all guarantors or other persons obligated in any way on the debt in question should be served with a copy of the notice of sale. Additionally, all lienholders of record after the recording of the deed of trust in question should be served a copy of the notice of sale.[178]

Other commentators have suggested using the standard real estate advertising methods instead of the obscure and unattractive legal descriptions to attract more potential bidders.[179] Also, because few po-

173. Gilpin, *supra* note 153.

174. W. VA. CODE § 38-1-3 (1985). This right must have been given in the trust deed.

175. The following language is frequently used to make an exception for prior liens: "The terms of sale, cash in hand paid, but subject to any and all assessments and taxes against said property, and all prior liens and encumbrances of any nature whatsoever." Gilpin, *supra* note 153.

176. Language can be used to the effect that "the sale is subject to the right of the Internal Revenue Service to reserve the property by § 7425 of the Internal Revenue Code of 1986, as amended." Gilpin, *supra* note 153.

177. W. VA. CODE § 38-1-4 (Supp. 1994).

178. Gilpin, *supra* note 153.

179. Steven Wechsler, *Through the Looking Glass: Foreclosure by Sale as De Facto Strict Foreclosure — An Empirical Study of Mortgage Foreclosure and Subsequent Resale,*

tential buyers will be willing to bid on property they have not seen, the subject property could be made available for inspection with dates and times provided in the notice of sale.[180] Additionally, other commentators suggest that title information should be made available before the sale to afford potential buyers the opportunity to determine what, if any, encumbrances are against the property.[181]

The foregoing suggestions are not specifically required by the West Virginia Code. Given, however, that *BFP* will place an increased emphasis on the foreclosure sale procedure, and that the last revision to any part of the applicable state law was in 1987,[182] it may be beneficial for either the West Virginia legislature, the West Virginia Law Institute, or the West Virginia Bankers Association to look again at the statutory procedures for foreclosure of property. Absent this, a lender should consider the foregoing suggestions before each sale and determine which, if any, should be utilized. These additional steps may encourage competitive bidding and thereby avert a subsequent factual dispute or challenge of collusion or fraudulent conveyance.

VI. CONCLUSION

The Supreme Court's decision in *BFP* that the price received at a noncollusive, properly conducted foreclosure sale conclusively establishes "reasonably equivalent value" under 11 U.S.C. § 548(a)(2)(A), restored a sense of confidence in the finality of forced sales and freed mortgagees from the burden of requiring a specified percentage of fair market value in order to sell foreclosed property. The majority in *BFP* defined "reasonably equivalent value" as meaning something different than "fair market value." It coupled this focus with its view that in the

---

70 CORNELL L. REV. 850, 892 (1985).

180. Woodruff, *supra* note 36, at 799 (citing Wechsler, *supra* note 179, at 891-92; Glaves, *supra* note 129, at 691); *see also* ILL. ANN. STAT. ch. 735, para. 5/15-1507(c)(1)(E) (Smith-Hurd 1993).

181. Ehrlich, *supra* note 44, at 979.

182. In 1987, W. VA. CODE § 38-1-4, which deals with the notice of sale requirements under vendor and trust deed liens, was completely rewritten.

context of a forced sale, prices are routinely less than fair market value and that protecting the security of real estate title is an essential state interest. The dissent refused to depart from what it found to be the plain meaning of the statute and disputed the majority's view that "clearer textual guidance" is needed before state law can be preempted.[183]

While *BFP* will significantly increase the lender's freedom in bidding at forced sales, lenders may still encounter the efforts of trustees in bankruptcy to use state foreclosure law to set aside noncollusive foreclosure sales where procedures are not strictly followed. Therefore, it is imperative that lenders know and follow closely the state law foreclosure requirements, and in some cases surpass these minimum requirements to help ensure the finality of the sale.

*Audy M. Perry, Jr.**

183. Klein, *supra* note 116, at 6.

* *The author wishes to express his sincere thanks to Professor John W. Fisher, II, of the West Virginia University College of Law and Mr. Thomas H. Gilpin, Partner, of Huddleston, Bolen, Beatty, Porter & Copen, Huntington, W. Va., for their help and guidance in the preparation of this article.*