IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

WILLIAM J. SALLADIN,	)	
	)	
Plaintiff,	)	
	)	
v.	)	C.A. No. 2447-MG
	)	
DATAQUICK INFORMATION SYSTEMS, INC.,	)	
	)	
	)	
Defendant.	)	

MASTER'S FINAL REPORT
(Motion to Dismiss)

Date Submitted: April 4, 2008
Final Report Issued: August 8, 2008

Ronald J. Drescher, Esquire, of Drescher & Associates, P.A., Wilmington, Delaware; Attorney for Plaintiff.

John C. Phillips, Jr., Esquire, of Phillips Goldman & Spence, P.A., Wilmington, Delaware; Attorney for Defendant.

GLASSCOCK, Master

This action involves a complaint by plaintiff William J. Salladin seeking to void an arbitration award under the Maryland Uniform Fraudulent Conveyances Act (the "Act").[1] The matter is currently before me on the motion of defendant DataQuick Information Systems, Inc. ("DataQuick") to dismiss. The plaintiff is a creditor of Steele Software Systems Corporation and its successor, Three S Delaware, Inc. (collectively, "Steele"). Steele was obligated by an arbitration award to pay $6,126,171 to defendant DataQuick. The plaintiff makes the novel claim that the arbitration award amounts to a voidable fraudulent conveyance by an insolvent debtor under Section 15-204 of the Act.[2]

After DataQuick moved to dismiss under Rule 12(b)(6), the matter was briefed and argued. By that point, Steele, which is not a party to this action, had sought to set aside the arbitration award via a suit in the United States District Court for the District of Maryland. That court had affirmed the arbitration award, and Steele had appealed to the Fourth Circuit Court of Appeals. The decision of the Court of Appeals was pending when the motion to dismiss in this action was filed. On the reasoning that a decision by the Fourth Circuit setting aside the arbitration award would moot the issues before me, I stayed this action pending the decision in the Court of Appeals. That court ultimately affirmed the District Court decision, confirming the arbitration award. Three S Delaware,

[1]Md. Code Ann., Com. Law §§15-201 *et seq.*

[2]Md. Code Ann., Com. Law §15-204.

Inc. v. DataQuick Information Systems, Inc., 4th Cir., 492 F. 3d 520 (2007).[3] I then lifted the stay and permitted the parties additional briefing and argument. This is my final report on DataQuick's motion to dismiss.

Standard and Facts

In considering a motion to dismiss under Rule 12(b)(6), I must consider the facts as stated in the complaint and draw all reasonable inferences from those facts in favor of the plaintiff. Only if it appears that the plaintiff cannot prevail as a matter of law may the defendant's motion to dismiss be granted. *E.g.* Sprint Nextel Corp. v. iPCS, Inc., Del. Ch., No. 3746, Parsons, V.C. (July 14, 2008)(Mem. Op.) at 12.

According to the complaint, Steele is indebted to the plaintiff in the amount of $142,855. Steele's business is to provide residential real estate information to mortgage companies and other financial institutions. In January 1996, Steele entered an agreement (the "License Agreement") with DataQuick Information Systems ("DIS").[4] Under the License Agreement, DIS was to provide data from public records to Steele for its use in producing and selling information concerning the value of parcels of real estate to financial institutions. The License Agreement obligated Steele to pay DIS the greater of a

[3] I take judicial notice of the decisions of the various courts which have ruled on issues pertinent here.

[4] Despite the similarity of the names, DIS and DataQuick are separate entities: DataQuick is a Delaware corporation; DIS is incorporated in California.

monthly lump sum or an amount based upon the number of transactions in which Steele used DIS data. DataQuick is the assignee of DIS's rights under the License Agreement.

Steele had a contract with First Union National Bank ("First Union") to provide real estate information. First Union breached that contract and Steele sued First Union in Maryland state court. On December 17, 2003, the Maryland Court of Special Appeals upheld a jury verdict against First Union in favor of Steele in the amount of $37,476,342 as compensatory damages based on the breach of contract. First Union National Bank v. Steele Software Systems Corp., Md. App., 838 A.2d 404 (2003). According to the complaint here, that award was not based on services Steele provided to First Union using DIS's products, which would have obligated Steele to pay DataQuick (as DIS's assignee) under the terms of the License Agreement.

On December 9, 2003, DataQuick filed an action for breach of the License Agreement against Steele in California Superior Court. The action sought damages in an "amount of at least $170,000," together with an unspecified demand under a theory of unjust enrichment. The License Agreement contained a mandatory arbitration provision. Steele moved the California court to enforce the arbitration provision and prevailed: the Superior Court of California directed Steele to initiate an arbitration proceeding with the American Arbitration Association (the "AAA"). Steele filed the demand for arbitration which the AAA in September 2004, seeking a declaratory judgment and damages against DataQuick in the amount of $170,000. DataQuick responded to the arbitration demand

by filing with the arbitrator a copy of the complaint filed in the California Superior Court action against Steele, which the arbitrator deemed to be a counterclaim in arbitration by DataQuick against Steele. Steele withdrew its claim for damages against DataQuick in the arbitration. The arbitration hearing was held on May 23, 2005. Steele failed to participate in the hearing. Ultimately, on August 25, 2005, the arbitrator entered an order in favor of DataQuick, awarding $6,126,171, of which over $2 million was for breach of the License Agreement and almost $4 million for unjust enrichment resulting from the judgment Steele had obtained from First Union. According to the complaint here, the arbitrator's conclusions were "strange" and "unfounded," and the award was not rationally related to the terms of the License Agreement and exceeded the jurisdiction of the arbitrator.

As part of its appeal of the arbitration award before the Fourth Circuit, according to counsel, Steele was required to post a bond in favor of DataQuick. As a consequence of the failure of Steele's appeal, the bond has been made over to DataQuick, in satisfaction of the arbitration award.

According to the complaint, Steele is now insolvent. The plaintiff is a Maryland resident, the arbitration took place in Baltimore, and the parties agree that Maryland law applies to the plaintiff's attack on the arbitration. The plaintiff, as a creditor of Steele, seeks to set aside the arbitration award as a "fraudulent transaction" by Steele under the Act.

Discussion

The plaintiff seeks to demonstrate that the arbitration that lead to an award of over $6 million to DataQuick from Steele was fundamentally flawed in matters concerning the jurisdiction of the arbitrator, the notice to Steele, the arbitrator's decision with respect to facts, and the arbitrator's application of the law. These issues, in substantially similar form, were advanced by Steele in his attempt to vacate the arbitration award before the United States District Court for the District of Maryland and the Fourth Circuit Court of Appeals. The Fourth Circuit has rejected Steele's challenges to the arbitration award, albeit under a different standard of review than that which the plaintiff asks me to employ here. Three S Delaware, 492 F.3d 520. In his attempt to collaterally attack the arbitration proceeding in this action, the plaintiff invokes the Act, as a creditor of Steele, seeking to void a fraudulent transfer or obligation by a debtor. *See* Md. Code Ann., Com. Law § 15-209. The Act codifies the long-standing common law rule that a transfer by a debtor meant to defraud the rights of his creditor is voidable. *See* Schaferman v. O'Brien, Md. Spec. App., 1986 WL 2306 (1868) at 6; *see also* BFP v. Resolution Trust Corp., 511 U.S. 531,540-41 (1994)(tracing the history of the law of fraudulent transactions from A.D. 1570). Nothing in the complaint, however, alleges common-law fraud on the part of the plaintiff's debtor, Steele. Nowhere does the complaint suggest (nor does there appear to be any basis for plaintiff to suggest) that Steele fraudulently colluded with DataQuick in order to avoid the consequences of its indebtedness to the plaintiff. Instead, the

plaintiff argues that the arbitration award is voidable based on statutory fraud, relying solely on Sections 15-204 and 15-205 of the Act, which provide:

> Every conveyance made and every obligation incurred by a person who is or will be rendered insolvent by it is fraudulent as to creditors without regard to his actual intent, if the conveyance is made or the obligation incurred without a fair consideration.
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> * * *
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> Every conveyance made without fair consideration when the person who makes it is engaged or is about to engage in a business or transaction for which the property remaining in his hands after the conveyance is an unreasonably small capital, is fraudulent as to creditors and other persons who become creditors during the continuance of the business or transaction without regard to his actual intent.

Md. Commercial Law Code §§15-204, 15-205.

The syllogism advanced by the plaintiff therefore proceeds as follows: the arbitration proceeding and its resulting award were an analogous to a "conveyance" or an "obligation" under the Act. The arbitration award left Steele insolvent and was an obligation incurred without fair consideration, because the arbitration process was in fact detrimental to Steele. Therefore, regardless of Steele's actual intent, the arbitration and award amount to statutory fraud and must be set aside.[5] Because it is clear to me that the

[5] The plaintiff has been difficult to pin down on exactly what remedy he seeks. The complaint seeks to void the arbitration award. Later, counsel for the plaintiff indicated that the plaintiff wished to avoid only so much of the arbitration award as to allow him to recoup Steele's indebtedness to him from DataQuick. During supplemental argument on April 1, 2008, plaintiff's counsel indicated that, in his opinion, the correct remedy was to pull the arbitration award back into a "pot" for all creditors of Steele; to then try in this Court those issues that were before the arbitrator (that is, the liability of Steele to DataQuick); determine the value of plaintiff's and any other claims against Steele; and distribute the proceeds in the manner of a bankruptcy court.

arbitration award is neither a conveyance nor an obligation under Section 15-204, the complaint must be dismissed.

It is clear that the arbitration procedure itself was not a "conveyance" or "obligation;" what is objected to by the plaintiff here—to the extent it pertains to Section 15-204—is the award that arose from the arbitration, which has now been reviewed and upheld in both the District Court for the District of Maryland and the Fourth Circuit, and has been paid to DataQuick. Is this award an "obligation" of the kind addressed by Section 15-204? That Section is meant simply to eliminate the requirement that one seeking to avoid a transaction undertaken by an insolvent debtor as fraudulent must demonstrate that the challenged transaction was done by the debtor with the intent to defraud. Under the Act, an obligation incurred by a debtor without fair consideration, if that transaction results in his insolvency, is fraudulent as to creditors *regardless* of the intent of the debtor, because the uncompensated nature of the transaction is itself a badge of fraud. Section 15-204 allows creditors to attack transactions by the insolvent debtor that result in the removal of assets from the debtor—and thus from the reach of the creditor—without fair consideration flowing to the debtor in return. *See*, e.g., Cruikshank-Wallace v. County Banking and Trust Co., Md. App., 885 A.2d 403 (2004)(holding that transfer of proceeds of a tax refund from husband to wife without consideration was constructively fraudulent to husband's creditors); Colandrea v. Colandrea, Bnkrtcy. Md., 17 B.R. 568 (1982)(considering whether mortgage taken

against debtor's property without consideration may be fraudulent obligation undertaken to detriment of creditors); Molovinski v. Fair Employment Council of Greater Washington, Inc., Md. App., 839 A.2d 755 (holding that transfer of trust assets under debtor's control to debtor's wife without consideration was fraudulent conveyance with respect to creditor).

The plaintiff alleges that the arbitration process here was riddled with flaws and was unfairly unfavorable to the debtor, Steele. Therefore, argues the plaintiff, there was no "fair consideration" for the arbitration award and the resulting judgment.[6] But this argument proves too much. An unfavorable result from an arbitrator or court, whether justified or not, never returns "fair consideration" to the unfortunate litigant. That is because there is no conveyance, obligation, or transaction of any kind between the litigant and the arbitrator or court (setting aside arbitration fees or court costs, which are not at issue here) to which Section 15-204 may attach. I note that the plaintiff cites no law suggesting that the arbitration or award represents a conveyance or obligation under Section 15-204 of the Act. Of course, such an award often enforces an obligation that itself was undertaken for a fair consideration. The only obligation potentially pertinent to

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[6]"Fair consideration" is given under the act if:
(1) In exchange for the property or obligation, as a fair equivalent for it and in good faith, property is conveyed or an antecedent debt is satisfied; or (2) the property or obligation is received in good faith to secure a present advance or antecedent debt in an amount not disproportionately small as compared to the value of the property or obligation obtained.
Md. Code Ann., Comm. Law, § 15-203.

Section 15-204 here was that undertaken by Steele to DataQuick under the License Agreement entered into on January 23, 1996. That is the obligation that has ultimately lead to an arbitration and the resulting award (and, ultimately, a judgment) against Steele. Nowhere in the complaint does the plaintiff allege that the License Agreement itself represented a conveyance or obligation made without fair consideration. The obligations incurred by Steele under the License Agreement were what gave rise to the California litigation by DataQuick against Steele; to Steele's assertion of its rights under the License Agreement to have those issues determined by the arbitrator; and thence to the arbitration award, judgment and eventual payment from the appeal bond. The arbitration did not itself represent a conveyance or obligation: it merely delimited the consequences of the obligation undertaken by Steele in the License Agreement.

The plaintiff seeks to avoid the general rule that a final judgment, unless void, is not susceptible to collateral attack. *E.g.* Fisher v. De Mar, Md. App., 174 A.2d 345, 347-48 (1961). The plaintiff's argument, if accepted, would expose every arbitration award and every judicial decision unfavorable to an insolvent debtor to collateral attack by the creditor. Under the plaintiff's scheme, any arbitration award or judgment adverse to the debtor would be without "fair consideration," and thus any creditor would be entitled to a trial *de novo* of his insolvent debtor's liability to a third party. The potential adverse consequences to the finality of awards and judgments that would result from such a

reading of the Act are obvious, and are no doubt responsible for the fact that no court has ever read Section 15-204 to compel such a result.

The plaintiff relies on BFP, 511 U.S. 531, to support his position by analogy. In that case, applying the Federal Bankruptcy Code, the United States Supreme Court held that a creditor may not collaterally attack a transfer of title via a foreclosure sale of his insolvent debtor's property, to the extent that the conveyance was "properly done" under state law, regardless of the value (or lack thereof) received by the debtor. The plaintiff argues that the arbitration here was not "properly done," thus he is free to collaterally attack the arbitration under the rationale in BFP.

First, BFP involved an actual transaction—a non-judicial foreclosure sale—that diluted the potential potency of a creditor's claim. *See* Md. Code Ann., Com. Law, § 15-210.1 (providing that foreclosure sales and the like are not fraudulent for purposes of the Act if done in accordance with applicable law). As I have explained above, this case involves an arbitration and award, arising from a ten-year-old transaction that is not itself claimed by the plaintiff to be fraudulent. Moreover, even if BFP were factually on point it should give the plaintiff no comfort here. BFP limited attacks on the transaction in question to those situations where a foreclosure sale failed to comply with applicable law. Here, both the trial and appellate federal courts have affirmed the arbitration award, despite vigorous attempts by Steele to have the award set aside.

The other case relied on by the plaintiff is Dowell v. Dennis, Okla. Civ. App., 998 P.2d 206 (1999). The plaintiff there, Dowell, was a judgment creditor of the defendant husband. Subsequent to judgment in favor of Dowell, the debtor husband and his wife entered into a divorce settlement agreement, which was accepted by the divorce court, resulting in a decree of divorce. Dowell sought to attack the settlement agreement and decree. He alleged that the husband had entered into the settlement agreement, which transferred virtually all of his property to his wife, to frustrate Dowell's ability to execute his judgment against the husband, and that the divorce court had merely accepted the divorce agreement without equitable review. The trial court dismissed Dowell's attack on the agreement and decree as an impermissible collateral attack on a judgment. The appellate court reversed, finding that Dowell's allegation was that fraud existed in the formation of the settlement agreement *extrinsic* to the decree, and that the plaintiff-creditor could therefore pursue his claim under the rationale that the effect of a divorce decree may be avoided by a creditor where procured by his debtor's fraud.

Without opining on whether, under Maryland law, a decree of divorce could be attacked under facts similar to those in Dowell, I note that the Dowell rationale is simply not applicable here. The property settlement agreement in Dowell was allegedly a transfer without value that left the husband insolvent, and was thus constructively fraudulent. The transaction in this case analogous to the settlement agreement in Dowell is the License Agreement. The plaintiff has failed to allege that the Agreement was

fraudulent in any way. Thus the Dowell rationale provides no basis for the plaintiff to attack the arbitration award and judgment here.[7]

Conclusion

The complaint fails to allege any "conveyance" or "obligation" incurred without "fair consideration" that could trigger application of the Act to void a transaction as fraudulent. The obligation at issue arose under the License Agreement. Through the litigation process, an arbitrator found that Steele was obligated to DataQuick under the License Agreement for over $6 million. The plaintiff, as a creditor of now-insolvent Steele, wishes to re-litigate Steele's obligation to DataQuick under the License Agreement, hoping for an outcome more favorable than that received at the hands of the arbitrator. Because the only grounds on which the plaintiff asserts standing to make such a collateral attack is that the arbitration award and subsequent judgment may be set aside as fraudulent under Sections 15-204 and 15-205 of the Act, and because I have found that those statutes are inapplicable here, the complaint must be dismissed.

/s/ *Sam Glasscock, III*
Master in Chancery

[7]In Dowell, the alleged fraud extrinsic to the judgment involved actions of the *debtor* intended to obtain a judgment to the detriment of his creditor. Here, the acts complained of are acts by the arbitrator intrinsic to the arbitration award. Far from colluding to obtain the arbitration award, Steele, the debtor here, fought vigorously (if unsuccessfully) in the district and appellate courts to overturn the arbitration award.