Pigs Get Fat, Hogs Get Slaughtered: Property of the Estate and Exemption Issues in Consumer Cases

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A Tale about Jack and Diane

Jack owns a gallery which is located in the Crossroads District in downtown Kansas City, Missouri. He owns many of the pieces of art as well as holding artwork for several of the artists which he exhibits.

Diane is a successful cosmetic surgeon. She is originally from Missouri but has lived in Florida for roughly 10 years. In June 2010, Diane's parents passed away leaving their fishing cabin at the Lake of Ozarks to her. While she was visiting the cabin, she met Jack, who was there to take in a little trout fishing. It was love at first sight.

Upon much convincing by Jack and getting tired of a long distance relationship, Diane decided to move her medical practice to Overland Park, Kansas. She formed a limited liability company, Fresh Expressions, LLC, of which she is the sole member. The company entered into a long-term lease at a local medical park, which Diane was required to guarantee.

Upon completion of her Overland Park space, Diane sold her modest home in the Orlando area and moved in with Jack on August 1, 2011, who owned a loft in the River Market area of Kansas City, Missouri. Jack and Diane got married soon after. They did, however, enter into a prenuptial agreement agreeing to keep any property owned before the marriage separate, which includes the Lake Cabin.

Finding that the loft was a bit cramped, Jack and Diane decided to move to Mission Hills, Kansas. They sold Jack's loft and purchased a "mini mansion", which sits on approximately two acres of land and has a really nice pool. They were able to put a significant amount down from the proceeds from the loft sale, but in order to afford the Mission Hills home, they needed to take out a mortgage on the same. They officially moved into their new home on March 31, 2012.

As part of their long term estate planning, Jack and Diane decided to transfer all of their property to their individual revocable trusts, including the Mission Hills Home. The transfer took place on May 1, 2012. The Mission Hills Home lists the trusts as joint tenants.

Beginning September, 2012, things took a turn for the worst for Diane. A medical malpractice action was brought against her by a noted media personality. While the case was ultimately dismissed as frivolous, the bad publicity caused Fresh Expressions to go out of business. Unable to continue to make lease payments, Fresh Expressions was forced to break its lease and the landlord has a claim of $600,000 against Diane on her guarantee. Luckily, with the exception of the lease debt, Fresh Expressions was relatively debt free.

Diane's bad luck continues in that she also just found out her favorite uncle has approximately 18-24 months to live. Her uncle is very wealthy and has promised her many times that he would leave her his prized Fabergé egg, which was last appraised at $750,000.

Things have not fared well for Jack either. He was recently accused of art fraud in selling a forgery of "Dogs Playing Poker". While criminal charges are not being pursued and Jack proclaims his innocence, a civil action has been initiated against him by the buyer in Johnson County, Kansas for fraud.

Given the dour mood in the house, Jack thought he could spruce it up a little bit by transferring all of the artwork he owns at the gallery and placing it on the walls of the Mission Hills Home. Jack also sold one of the pieces of artwork, but decided to use the proceeds, approximately $20,000, to buy a new SUV that he uses exclusively for his fly fishing excursions. Jack also leases a car, which he uses on a regular basis for both gallery and personal purposes.

Additionally, knowing that money is tight given all the litigation costs and how much he loves the Lake House, Diane, as a surprise birthday gift, decides to re-title the Lake Cabin from her revocable trust into both of their names. The Lake Cabin is currently titled in both of their names as tenants by the entirety. The new deed was recorded on December 31, 2012.

Also, given the demise of Fresh Expressions, Diane has begun working for a local hospital on a new innovative program, where she visits patients recovering from cosmetic surgery at their homes. She is treated as an independent contractor and offices from her home, which is fine because this new program causes her to drive throughout the metro. It also allows her to focus on the multi-million dollar lawsuit that Fresh Expressions has initiated for malicious prosecution on account of the failed medical malpractice lawsuit.

Unfortunately, tragedy has struck Diane again, the stress caused by her uncle's declining health, was too much for Diane's aunt, who passed away in June, 2013. Knowing Diane's uncle was going to pass soon, Diane's aunt changed her estate plan bequeathing her IRA to Diane.

The stress of losing her aunt, and given the persistent collection attempts by her former landlord and the pending Johnson County Suit, Jack and Diane decide to consult J. M. Camp, a bankruptcy lawyer. J.M. has only been out of law school for a year, but has already made a reputation for himself as an aggressive (if not bordering reckless) bankruptcy attorney. After spending thirty minutes with Jack and Diane, J.M. decides on an aggressive strategy that requires Diane to file bankruptcy immediately.

J.M. files Diane's case in the District of Kansas on October 1, 2013. Diane's schedules, include the following information:

Description and Location of Property	H W J C	Current Value of Debtor's Interest In Property, Without Deducting Any Secured Claim or Exemption	Amount of Secured Claims
Mission Hills Home	J	$900,000	$500,000
Lake Cabin	J	$550,000	0
100% of Fresh Expressions, LLC	W	0	0
BMW	W	$20,000	$15,000

Diamond Ring	W	$900	0
RA (from her Aunt)	W	$300,000	0

Among other things, on Schedule C, Diane listed the following property as exempt:

Description of Property	Specify Law Providing Each Exemption	Value of Claimed Exemption	Current Value of Property Without Deducting Exemption
Mission Hills Home	KSA 60-2301	100%	$900,000
Lake Cabin	TBE – 11 U.S.C. 522(b)(3)(B)	100%	$550,000
BMW	KSA 60-2304(c)	100%	$20,000
Diamond Ring	KSA 60-2304(b)	$900	$900
IRA (from her Aunt)	11 U.S.C. 522(b)(3)(C)	100%	$300,000

Diane's debts include the $600,000 unsecured guarantee obligation, the joint secured debt of $500,000 on the Mission Hills Home, $15,000 on the car loan, and approximately $15,000 on two credit cards that are both in her and Jack's name. Diane has sought to reaffirm the secured loans and the mortgage. Additionally, she has sought to reaffirm the joint credit card debt, leaving the guaranty debt as the only debt to be discharged. Her former landlord is not happy about this and calls Diane's Chapter 7 trustee frequently to express his displeasure.

Diane tells J.M. about the Fresh Expressions lawsuit. J.M. tells Diane they don't need to list it because its Fresh Expressions' claim and they must observe corporate formalities. Liking J.M.'s style, Diane fires her counsel in the lawsuit and retains J.M. on a forty percent contingent fee to pursue the Fresh Expressions lawsuit.

Because the only other debt that Jack has is the mortgage on the Mission Hills Home and the joint credit card debt, J.M. decides that it is better to keep Jack out of bankruptcy given this new bankruptcy law he heard of, but that no one pronounces the same way. Rather that filing bankruptcy, J.M. decides that Jack should make a take it or leave it offer of $5,000 to the plaintiff in the civil complaint brought against him. After all, under Kansas law, Jack is essentially judgment proof. Jack told J.M. that if the plaintiff wants the gallery they can have it as he plans to become a professional fly fisherman based out of the Lake Cabin, where he spends most of his time at these days anyway.

PIGS GET FAT, HOGS GET SLAUGHTERED

PROPERTY OF THE ESTATE AND EXEMPTION ISSUES IN CONSUMER CASES

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A Tale about Jack and Diane

Is it proper for Diane to claim Kansas exemptions?

- **Most states have opted out Federal Exemptions under state law.**
- **522(b)(3) determines what exemptions apply**
  - First: Domicile for 730 days prior to filing
  - Second: Domicile for the better part of 180 days preceding the 730 days
  - Third: If no state exemption is applicable, then federal exemptions
    - *In re Bingham*, 2008 WL 186277 (Bankr. D. Kan. 2008)
    - *In re Nickerson*, 375 B.R. 869 (Bankr. W.D. Mo. 2007)

Is it proper for Diane to claim Kansas exemptions?

- **Whether exemptions are extraterritorial depends on state law.**
  - ***Compare*** *In re Woodruff*, 2005 WL 1139891 (Bankr. W.D. Mo. 2005) (Mo. homestead given extraterritorial effect)
  - ***With*** *In re Ginther,* 282 B.R. 16 (Bankr. D.Kan. 2002)(Kan. homestead exemption not given extraterritorial effect)
  - ***Compare*** *In re Townsend,* 2012 WL 112995 (Bankr. D. Kan. 2012) (concluding that the debtors are "entitled to claim the exemptions provided by § 522(d) because Oklahoma's opt-out statute does not apply to them") (majority position)
  - ***With*** *In re Garrett*, 435 B.R. 434 (Bankr. S.D.Tex. 2010)(finding that 522(b)(3) preempted provision of North Carolina law providing that its exemption laws would not have extraterritorial effect) (minority position)

Application to Hypothetical

- **Kansas Exemptions Do Not Apply.**
  - Only 549 days prior to petition.
  - Needs to be 730 days
- **Missouri Exemptions Do Not Apply.**
  - Only 792 days prior to petition.
  - Needs to be for 821 days (2 years, plus 91 days)
- **Florida Exemptions Do Not Apply.**
  - Florida exemptions found not to be extraterritorial.
  - *See In re Adams*, 375 B.R. 532 (Bankr. W.D. Mo. 2007)

Federal Exemptions will Apply
***See* 11 U.S.C. 522(d)**

Is the Inherited IRA Exempt?

- 522(b)(3)(C) and (d)12 exempt retirement funds that are exempt from taxation under IRC 408
- IRC 408 creates a tax exemption for an individual retirement accounts (IRA) by which a person provides for his or her own retirement.
- Inherited IRAs not treated the same. For example, non-spousal inherited IRAs must start taking distributions within a year of the original owner's death.
- Currently a Circuit Split
  - *In re Chilton*, 674 F.3d 486 (5th Cir. 2012) – Inherited IRAs exempt
    - *See also In re Nessa*, 426 B.R. 312, 314 (8th Cir. BAP 2010).
  - *In re Clark*, 714 F.3d 559 (7th Cir. 2013) – Inherited IRAs nonexempt

Is the Mission Hills Home Exempt?

- Listed Value: $900,000, Secured Debt: $500,000, Equity: $400,000
- Kansas does not recognize tenancy by the entirety
  - KSA 58-501
  - *Bouska v. Bouska*, 153 P.2d 923 (Kan. 1944)
- Federal Homestead Exemption – 522(d)(1): $22,975
- Exemption applies to equity
  - *In re Baldridge*, 2013 WL 1759365 (E.D.Mich. 2013)
  - *In re Urban*, 375 B.R. 882 (9th Cir. BAP 2007)

Because the Mission Hills Home is held in a revocable trust, is it entitled to claim the federal homestead exemption?

- ***Compare*** *In re Bowers*, 222 B.R. 191 (Bankr. D. Mass 1998) (real estate held in trust not subject to 522(d)(1) exemption)
- ***With*** *Redmond v. Kester*, 159 P.3d 1004, 1007 (Kan. 2007) (Kansas homestead exemption applies to property held in revocable trust)
- **If the federal homestead is not applicable, Diane may need to use federal wildcard exemption.**
  - 522(d)(5): $1,225 – base wildcard, $11,500 unused portion of federal homestead
  - Diane may be entitled to $12,725

Can the Trustee sell the Mission Hills Home even though it is subject to Diane's exemption and Jack's interest?

- **Partially exempt property can be sold.**
  - *In re Morgan-Busby*, 272 B.R. 257 (9th Cir. BAP 2002)
  - KSA 60-2302
- **Jointly owned property can be sold under certain conditions.**
  - *See* 363(g) and (h)
  - Jack gets a right of first refusal to purchase the property. *See* 363(i)

What should the trustee consider in contemplating a sale of the Mission Hills Home?

- **Costs and Expenses of Sale**. *See* 363(j), 506(c)
- **Payment of Mortgage**
  - Comes first out of non-exempt portion of sale proceeds
    - *See In re Downing*, 2005 WL 3299797 (Bankr. D. Kan. 2005)
  - But what is the exempt portion?
    - Diane's Exemption = Unlimited Size, Limited Amount ($21,625 or $12,725)
    - Jack's Exemption = Limited Size (1 acre), Unlimited Amount
- **Jack's Interest – 11 U.S.C. 363(j)**
  - ***Compare*** *In re Bryson*, 2007 WL 2219114 (Bankr. D. Kan. 2007) (Joint Tenancy creates rebuttable presumption of equal ownership)
  - ***With*** *In re Kasparek*, 426 B.R. 332 (10th Cir. BAP 2010) (Under Kansas law "[a]ll joint tenants acquire equal undivided interests as a matter of law unless otherwise stated in the deed.").

Is the BMW Exempt?

- **Listed Value: $20,000, Secured Debt: $15,000**
- **522(d)(2): Vehicle - $3,675**
- **522(d)(5): Wildcard - $1,225**
  - While not uniform, courts have found that the exemptions under 522(d)(2) and (5) can be aggregated
    - *In re McNutt*, 87 B.R. 84 (9th Cir. BAP 1988)
    - *Augustine v. U.S.*, 675 F.2d 582 (3rd Cir. 1982)
- **522(d)(6): Tools of the Trade - $2,300**
  - ***Compare*** *In re Branas*, 143 B.R. 64 (Bankr. W.D. Pa. 1992) (tractor could be exempted under both 522(d)(2) and (d)(6)); *McNutt*, 87 B.R. 84 (motor vehicle is tool of trade under (d)(6)); *In re LaFond*, 791 F.2d 623 (8th Cir. 1986) (tractor can be tool of trade)
  - ***With*** *In re Harrell*, 72 B.R. 107 (Bankr. N.D. Ala. 1987) (motor vehicles distinct from tools of the trade) and *In re Patterson*, 825 F.2d 1140 (7th Cir.1987) (tractor not tool of trade)
  - *See also In re Giles*, 340 B.R. 543 (Bankr. E.D.Pa. 2006) (discussing case law with respect to whether vehicles can constitute a tool of the trade)
  - **Inquiry: "Whether or not the vehicle is used by and is necessary to a debtor for his or her work, trade or occupation."** *See McNutt*, 87 B.R. at 87.

Is the Lake House Exempt?

- 522(b)(3)(B) – In addition to state law exemptions, debtor can also claim exempt entireties property.
- Entireties property only subject to joint debts
- Property owned by husband and wife presumed to be entireties property
- Must show Four Unities: Interest, Title, Time, and Possession
- Courts have found that a trustee cannot administer if joint debts are waived or reaffirmed.
  - *See, e.g., In re Rentfro*, 234 B.R. 97 (Bankr. W.D. Mo. 1999)
- Entireties Property not subject to 522(o) and (p) caps

Can the Trustee bring a fraudulent transfer action against Jack?

- Transfer took place two years before filing
- Was it an interest of the debtor in property since it came from a trust?
- ***Constructive Fraudulent Transfer*** –548(a)(1)(B)
  - Less than reasonable value was exchanged, is was gift.
  - Likely insolvent – *See* 101(32)
    - Transferred or exempt property not considered in analysis
    - Secured Debt is considered in analysis – Differs under UFTA
- ***Actual Fraudulent Transfer*** - 548(a)(1)(A)
  - Several Badges of Fraud
  - Transfer to insider, debtor remained in possession, insolvency, lawsuit threatened or pending, no consideration

J.M. amends Diane's schedules claiming federal exemptions, but except for changing the statutory reference, keeps most of the information the same.

The Trustee concludes the 341 hearing in Diane's bankruptcy. While she objects to several of the exemptions being claimed by Diane, she fails to object to the diamond ring exemption.

Approximately 45 days after the conclusion of the 341 hearing, the trustee discovers that the diamond ring actually has a value of $25,000.

Can the Trustee attempt to sell the Ring?

Objecting to Exemptions Basics

- Debtor must provide a description and value of the property, the amount of the claimed exemption, and the statutory basis for the claimed exemption. Bankr. Rule 4003(a)
- Entitlement to Exemption determined on petition date.
- Trustee and parties in interest have 30 days after the meeting of creditors has been ***concluded*** to object to exemptions. Bank. Rule 4003(b)
- Party asserting objection has burden of proof. Bankr. Rule 4003(c)
- The thirty day deadline may be extended for cause, but the request to extend must be filed before the objection deadline has passed. Bankr. Rule 4003(b)(1)
- Once this deadline has passed the bankruptcy court generally cannot extend this deadline on the basis of excusable neglect, even if the exemption was improper. Bankr. Rule 9006(b)(3)

Schwab v. Reilly, 130 S. Ct. 2652 (2010)

- Debtor claimed exemptions for business equipment listing the total value on her schedules as $10,718 under two specific statutory exemptions.
- Neither the trustee, nor any other interested party, objected to the claim.
- The trustee later determined that the approximate value of the equipment was $17,200 and moved the court to sell the equipment in order to provide the debtor with the $10,718 claimed as exemption and distribute the remaining $6,482 to creditors.
- Despite this 30 day limitation on exemptions, the Supreme Court held that a party is not required to object to a claimed exemption in order to recover value over the amount of the exemption listed by the debtor in the schedules.

Can the Trustee attempt to sell the Ring?

- 522(d)(4) - Jewelry Federal Exemption: $1,550
- Diane claimed an exemption of $900 in schedules
- Ring valued at $25,000
- Trustee entitled to sell the ring and provide Diane with the $900
- Diane may want to consider amending Schedule C to claim full exemption

The Trustee does initiate action against both Jack and Diane. The Trustee also seeks to extend the date to object to Diane's discharge.

On April 9, 2014, Diane's uncle dies and leaves her the Faberge Egg.

Jack and Diane immediately offer to split their "nest egg" to settle with the Trustee for $375,000.

Should the Trustee accept that offer?

Settlement Considerations

- **Rights to Inherited Property**
  - Property inherited 180 days after petition date is property of the estate – 541(a)(5)(A).
  - Egg would not be property of the estate because received 190 days after.
  - Is there a possibility of dismissing the case for bad faith?
- **Consideration of Other Property**
  - Inherited IRA
  - Mission Hills Home
  - BMW
  - Diamond Ring
  - Time and Sale Costs
- **Viability of Recovery on Fraudulent Transfer Action regarding the Lake Cabin**
  - Cost and Expense to pursue Fraudulent Transfer
  - Likelihood of Success
  - Cost of Sale if successful

Jack, Diane, and Trustee enter into a settlement agreement whereby in exchange for cash, the Trustee agrees to abandon all the listed assets back to Diane and drop any claims against Jack. Additionally, the Trustee agrees not seek any further extensions of the discharge deadline.

The Trustee files a motion to approve the settlement and abandon the property. In doing so, the Trustee identifies the main assets and indicates that based on the schedules, the other assets appear to have very little value.

The Court grants the motion and all of the listed assets are abandoned from the estate. Additionally, Diane obtains her discharge. The settlement proceeds are ultimately disbursed by the Trustee and the case is closed.

Fresh Expressions' malicious prosecution is at the dispositive motion stage. Defense counsel in that case just filed a motion for summary judgment seeking to have the case dismissed based on the doctrine of judicial estoppel.

What is the Judicial Estoppel Doctrine and when does it apply?

- The "purpose [of the doctrine] is to protect the integrity of the judicial process by prohibiting parties from deliberately changing positions according to the exigencies of the moment." *New Hampshire v. Maine*, 532 U.S. 742, 749-50 (2001).
- The Supreme Court recognized three factors in determining if the doctrine should be invoked:
  - "a party's subsequent position must be 'clearly inconsistent' with its former position."
  - "a court should inquire whether the suspect party succeeded in persuading a court to accept that party's former position, 'so that judicial acceptance of an inconsistent position in a later proceeding would create the perception that either the first or the second court was misled."
  - "the court should inquire whether the party seeking to assert an inconsistent position would gain an unfair advantage in the litigation if not estopped."

See Eastman v. Union Pacific Railroad Company, 493 F.3d 1151, 1156 (10th Cir. 2007) (citing, 532 U.S. 742, 749-50 (2001)). *See also Stallings v. Hussman Corp.,* 447 F.3d 1041 (8th Cir. 2006).

Does the defendant's claim of judicial estoppel have merit?

- **Clearly Inconsistent Position**
  - Diane is sole owner of Fresh Expressions
  - Diane listed the value of Fresh Expressions as $0 on her schedules
  - Fresh Expressions only asset is a claim for $7,000,000
  - Fresh Expressions only debt is $600,000
  - If successful, Fresh Expressions will net $4,200,000
- **Success in persuading a court to accept that party's former position**
  - Trustee's representations to Court were based, in part, on the schedules valuing the LLC interest as $0
  - Court approved settlement and abandonment of the asset
- **Unfair Advantage**
  - Diane received a discharge
  - Received a potential windfall on account of non-disclosure

See Vehicle Market Research, Inc. v. Mitchell Int'l, Inc., 2012 WL 5512340 (D. Kan. Nov. 12, 2012)(upholding application of judicial estoppel on similar facts)

Are there any defenses to the judicial estoppel doctrine?

- **Inadvertence or Mistake**
  - Must demonstrate the debtor either lacks knowledge of the claims or has no motive for their concealment
  - Difficult to prove
    - Knowledge: Diane told her bankruptcy counsel about the lawsuit
    - Motive: If successful, she, not the bankruptcy estate, would be the beneficiary of millions of dollars.
  - "Where a debtor has both knowledge of the claims and a motive to conceal them, courts routinely, albeit at times *sub silentio*, infer deliberate manipulation." *Eastman,* 493 F.3d at 1157.
- **No Harm, No Foul Defense**
  - Remainder of Landlord's claim likely could be satisfied out of litigation proceeds. Diane reaffirmed her other debt…so what is the harm?
  - Does not matter.
    - Purpose of doctrine is to promote judicial integrity
    - Creates incentive that a debtor should only consider disclosing assets if they get caught
    - *See Eastman*, 493 F.3d at 1160.

Should Jack's Creditor Take the $5,000 Settlement Offer?

Is Jack entitled to exempt the Mission Hills Home under the Kansas Homestead Law?

Size

- Mission Hills Home sits on 2 acres – only entitled to 1. KSA 60-2301
- Jack gets to designate which acre is exempt. KSA 60-2302
- Mortgagee can get paid out of non-exempt portion first.
  See In re Downing, 2005 WL 3299797 (Bankr. D. Kan. 2005)

Occupancy

- Does it matter that Jack intends to spend time at the cabin?
  - Party must intend to occupy property as homestead
  - Must actually occupy it as a homestead
  - Owner's intentions are critical

  See In re Hall, 395 B.R. 722 (Bankr. D. Kan. 2008)

One Homestead

- Diane and Jack must claim same acre
- *Compare In re Sauer*, 403 B.R. 722 (Bankr. D. Kan. 2009) (only one residence may be claimed as a homestead)
- *With Hall*, 395 B.R. at 722 (allowing married debtors to claim separate homesteads when they actually live apart on permanent basis and have established both properties as homesteads)

Is Jack's new SUV exempt?

KSA 60-2304(c)

- One means of conveyance *regularly* used for the transportation of the person or for transportation to and from the person's regular place of work
- $20,000 cap per person
- Issue: Jack has two cars, does the SUV fall into the regularly used category
  - Uses SUV for fly fishing
  - Uses leased car for gallery and personal business
  - *In re Carpenter*, 2003 WL 23765954 (Bankr. D. Kan. 2003)
    - Debtor had two vehicles - one for personal use and Peterbilt Truck
    - Court found that Peterbilt tractor truck did qualify for motor vehicle exemption

Conversion of Nonexempt Assets to Exempt Assets

- Issue: Sold non-exempt art and bought an exempt asset
- Generally, the mere conversion of non-exempt assets to exempt assets will not deprive a debtor the exemption unless a creditor has a peculiar equity in the non-exempt property. *See Metz v. Williams*, 149 Kan. 647 (1939)
- In bankruptcy, however, there may be ramifications for excessive exemption planning, including a reduction of the homestead exemption [522(o) and (p)], revocation of a discharge [727(a)(2)(A)], or initiation of a fraudulent transfer action [548(a)(1)(A)]. *See In re Agnew*, 355 B.R. 276 (Bankr. D. Kan. 2006)

Is the artwork that Jack moved from the gallery exempt?

KSA 60-2304(a) : Household Furnishings Exemption

- Must be in present possession
- Reasonably Necessary at the Principal Residence
  - Does not mean indispensable
  - Look at debtor's customary standard of living
  - *In re LeJuerrne*, 2004 WL 2192515 (Bankr. D.Kan. 2004)(displayed memorabilia found exempt under household furnishings exemption)
- For a period of one year
- No dollar limit

Are Jack's fly rods exempt as tools of the trade?

- **KSA 60-60-2304(e): $7,500**
- Debtor must be engaged in the trade on the date the petition was filed, mere intention of starting a business not sufficient.
- Must be primary occupation
- *See In re Cooper*, 324 B.R. 133 (Bankr. D. Kan. 2004)
  - Boat, motor, and trailer found not be exempt tools of trade
  - Intention of becoming a fishing guide not sufficient

With respect to the Lake House, can a Kansas resident use tenancy by the entireties if property is in Missouri?

- Kansas courts generally follow the First Restatement on Conflicts of Law.
  - *See ARY Jewelers, L.L.C. v. Krigel*, 277 Kan. 464, 85 P.3d 1151 (2004)
- Under First Restatement, "the nature of the interest in land created by a conveyance is determined by the law of the state where the land is."
  - Restatement (First) of Conflict of Laws § 221 (1934)
- Restatement (Second) of Conflicts of Law § 223 - same result
  - *See In re Holland*, 366 B.R. 825 (N.D.Ill. 2007)
    - Illinois resident allowed to claim Florida tenancy by the entirety on land located in Florida
    - Illinois follows Second Restatement
    - Discusses different choices in law, but found if Illinois choice of law rules applied, then the applicable law would be where the property was located

Should the tort creditor put Jack into an involuntary bankruptcy?

- **Can Jack's creditor put him into an involuntary bankruptcy?**
  - If tort creditor obtains a judgment and joins with credit card debt then could likely satisfy 303(b)(1): (i) 3 or more claimants; (ii) Not Contingent; (ii) Not subject to bona fide dispute; and (iii) at least $14,425 in unsecured debt exists.
  - If tort creditor obtains a judgment, may be able to go it alone under 303(b)(2): (i) fewer than 12 claim holders that meet the criteria of 303(b)(1); and (ii) it holds in excess of $14,425 in unsecured debt.
- **What would be the benefits?**
  - Jack could possibly be forced to take Missouri or Federal Exemptions.
    - *In re Woodruff*, 2005 WL 1139891 (Bankr. W.D. Mo. 2005) (Mo. homestead given extraterritorial effect)
  - Could argue that debt is excepted from discharge
- **What are the potential detriments?**
  - If petition dismissed: Jack's Costs and Attorney's Fees
  - If petition filed in bad faith: Actual and Punitive Damages

THANK YOU

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MATERIALS

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II. *Federal Bankruptcy Qualifications of State Homestead Exemption Laws* by Patrick B. Bauer

III. *Current Cases & Updates on Missouri Exemptions* by Jill D. Olsen

IV. *Brief Overview of Kansas Homestead Exemption Laws and Their Interrelationship with 11 U.S.C. § 522(m) and 11 U.S.C. § 522(p)* by Edward J. Nazar

V. *Recent 10th Circuit Cases* by Edward J. Nazar

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Property of the Estate and Exemption Overview

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I. PROPERTY OF THE ESTATE

Upon filing a bankruptcy, a new legal entity is created, the bankruptcy estate. *See* 11 U.S.C. § 541(a). Generally, the bankruptcy estate will be made up of various assets, which are referred to as "property of the estate." Whether or not a certain asset is considered "property of the estate" will affect its treatment in a bankruptcy, including whether the same can be liquidated by the trustee and the applicability of the automatic stay.

"Property of the estate" is broadly defined and encompasses a whole host of assets, including "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). However, if the debtor only holds bare legal title in property at the commencement of the case, but not an equitable interest, the property becomes property of the estate only as to legal title, but not to the extent of any such equitable interest not held by the debtor. 11 U.S.C. § 541(d). "For purposes of most bankruptcy proceedings, '[p]roperty interests are created and defined by state law.'" *Bailey v. Big Sky Motors, Ltd. (In re Ogden)*, 314 F.3d 1190, 1197 (10th Cir. 2002) (citing *Butner v. United States*, 440 U.S. 48, 55 (1979); T*aylor v. Rupp (In re Taylor*), 133 F.3d 1336, 1341 (10th Cir. 1998)).

Additionally, certain assets acquired by the debtor after the commencement of the case, will be considered property of the estate. For example, an inheritance received 180 days after the commencement of the case, may be property of the estate. *See* 11 U.S.C. § 541(a)(5). Additionally, in an individual Chapter 11 case, and in Chapter 12 and 13 cases, property acquired after the case is commenced, including earnings, but before the case is closed, dismissed, converted will be property of the estate to the extent it is the kind specified in Section 541. *See* 11 U.S.C. §§ 1115, 1207 and 1306.

II. EXEMPTION PRIMER

A. INTRODUCTION

In many instances, a bankruptcy case may be impacted by non-bankruptcy law, both state (*e.g.*, Uniform Commercial Code) and federal (*e.g.*, Tax Code). A primary example of non-bankruptcy law having a fundamental impact on the administration of a bankruptcy is with respect to exemptions. Section 522 of the Bankruptcy Code allows for individual debtors to exempt certain property out of the bankruptcy estate. *See* 11 U.S.C. § 522.

The ability to exempt property out of the estate is essential to the "fresh start" purpose of the Bankruptcy Code. *See* 12 COLLIER ON BANKRUPTCY (Alan N. Resnick & Henry J. Sommer eds. 16th Ed.) (hereinafter "COLLIER") Intro.02 at Intro-3. The result of exempting property of the estate is that it can no longer be liquidated by the trustee and distributed to the individual's creditors. *See id*. Also, in Chapters 11, 12 and 13 context, an individual generally has to pay the value of their nonexempt property through their plan. *See* 11 U.S.C. §§ 1129(7)(ii), 1225(a)(4) 1325(a)(4). Thus, what is considered exempt will have a significant impact on what the individual's plan will look like and the payments to be made under the same.

If an individual is claiming property exempt, then the individual must claim such exemptions in Schedule C of their bankruptcy schedules, which requires that the debtor provide a description and value of the property, the amount of the claimed exemption, and the statutory basis for the claimed exemption. Fed. R. Bankr. P. 4003(a). "A debtor's entitlement to claim an exemption of property is determined as of the bankruptcy petition date." *In re Thompson*, 311 B.R. 822, 825 (Bankr. D. Kan. 2004).

Further, the trustee and parties in interest have thirty days after the meeting of creditors has been concluded to object to exemptions. *See* Fed. R. Bankr. P. 4003(b). The objecting party has the burden of proof to show that the exemption is improper. *See* Fed. R. Bankr. P. 4003(c). The thirty day deadline may be extended for cause, but the request to extend must be filed before the objection deadline has passed. *See* Fed. R. Bankr. P. 4003(b). Once this deadline has passed the bankruptcy court generally cannot extend this deadline on the basis of excusable neglect, even if the exemption was improper. *See* Fed. R. Bankr. P. 9006(b)(3). *See Taylor v. Freeland & Kronz*, 503 U.S. 638, 643-45 (1992); *In re Kuhnel*, 495 F.3d 1177, 1180 (10th Cir. 2007); *In re Ladd*, 430 F.3d 751, 753 n.1 (8th Cir. 2006); *In re Smith*, 2004 WL 41401 at *2 (Bankr. W.D. Mo. 2004).

Despite this 30 day limitation on exemptions, the Supreme Court has held that a party is not required to object to a claimed exemption in order to recover value over the amount of the exemption listed by the debtor in the schedules. *Schwab v. Reilly*, 130 S. Ct. 2652, 2669 (2010). In *Schwab*, the debtor claimed exemptions for business equipment listing the total value on her schedules as $10,718 under two specific statutory exemptions. *Id*. at 2657-58. Neither the trustee, nor any other interested party, objected to the claim. *Id*. at 2658. The trustee later determined that the approximate value of the equipment was $17,200 and moved the court to sell

the equipment in order to provide the debtor with the $10,718 claimed as exemption and distribute the remaining $6,482 to creditors. *Id*. The Supreme Court held that the trustee was entitled to rely on the debtor's listed value and was not barred from recovering any value beyond that listed on the schedules. *Id*. at 2669. Thus, from a creditor's perspective, when reviewing the exemptions, special care should be taken to see how the debtor has listed their exemptions.

Prior to December 2010, there was an open issue as to whether the deadline recommences upon a conversion from a Chapter 13 to a Chapter 7. The Tenth Circuit BAP and the Eighth Circuit had adopted the minority position finding that the deadline recommences upon conversion. *In re Alexander*, 236 F.3d 431, 432 (8th Cir. 2001); *In re Campbell*, 313 B.R. 313, 319-20 (10th Cir. BAP 2004); *but see In re Beshirs*, 236 B.R. 42, 44 (Bankr. D. Kan. 1999) (adopting majority approach that conversion does not recommence the deadline). Effective December 1, 2010, the Bankruptcy Rules were amended to provide that a new 30 day deadline is set unless the conversion takes place more than a year after conversion or the case was previously a Chapter 7 and the time to object to exemptions had passed. Fed. R. Bankr. P. 1019(2)(B).

B. WHICH EXEMPTIONS APPLY

"The general rule under the Bankruptcy Code is that a debtor is permitted to choose between the scheme of federal exemptions prescribed in section 522(d) of the Code or the exemptions available under other federal law and the law of the state in which the debtor is domiciled." Collier at Intro-3. However, states can "opt out" of the Bankruptcy Code exemptions forcing a debtor to use the state exemptions and non-bankruptcy federal exemptions. *Id*.; 11 U.S.C. § 522(b)(2). Iowa, Kansas, Missouri and Nebraska have opted out of the federal bankruptcy exemptions. *See* Iowa Code Ann. § 627.10; K.S.A. § 60-2312(a); V.A.M.S. § 513.427; and Neb. Rev. Stat. § 25-15, 105.

While the Bankruptcy Code has been amended several times since 1978, sweeping changes were made to the same in April 2005 when the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA") was signed into law. Prior to BAPCPA where a party's domicile was for the 180 days immediately preceding the petition date would control which exemptions would apply. *See In re Bingham*, 2008 WL 186277 at *2 (Bankr. D. Kan. 2008) (explaining the domicile requirement pre-BAPCPA). For example, if a party was domiciled in Kansas for 91 days prior to Petition Date, Kansas exemptions would apply. If a

party was domiciled in Kansas for 45 days, but the balance of the time they were domiciled in Missouri, then the individual would not be entitled to Kansas exemptions.

In attempt to curb the perceived abuse of forum shopping of states with generous exemption laws (such as Kansas), section 522 was substantially amended by BAPCPA. Instead of looking at the 180 days prior to the petition date, the individual now needs to be domiciled in a single state for 730 days immediately preceding the petition date. *See* 11 U.S.C. § 522(b)(3). If that individual's domicile has not been in a single state for the preceding 730 days, then where the individual was domiciled in the 180 days preceding the 730 days will control. *Id*. Further, if on account of these requirements, a debtor is rendered ineligible for any exemption, the Debtor may then elect to use federal exemptions. *Id. See also Bingham*, 2008 WL 186277 at *5; *In re Nickerson*, 375 B.R. 869, 872 (Bankr. W.D. Mo. 2007).

The application of these amendments is best demonstrated by the following example, which is loosely based upon the *Bingham* case. The debtor currently lives in Kansas and has been domiciled in Kansas for the year preceding the filing of her bankruptcy. Prior to be being domiciled in Kansas, the debtor was domiciled in Missouri for a year and two months. Other than Kansas and Missouri, her only other domicile was in Texas. The debtor files for bankruptcy in Kansas and wishes to exempt her Kansas homestead.

In this example, the Kansas exemptions will not apply because she has not been domiciled in Kansas in the 730 days preceding her filing. Missouri exemptions also will not apply because she has not been domiciled in Missouri the better part of 180 days preceding the 730 days (she was only in Missouri approximately 60 days prior to the 730). Texas exemptions will not apply because under Texas law exemptions are not given extraterritorial effect. *See Bingham*, 2008 WL 186277 at *5. As a result, the federal exemptions will be the only exemptions available to the debtor.

C. THE HOMESTEAD EXEMPTION – THE BASICS

1. Kansas

The most generous of Kansas exemptions is the homestead exemption. "Both the Kansas Constitution and the Kansas Statutes provide for the reservation of a one acre homestead within an incorporated town or city, including a mobile or manufactured home to be "occupied as a residence by the owner or the family of the owner ... together with all the improvements on the same" from any forced sale." *In re Murphy*, 367 B.R. 711, 714 (Bankr. D. Kan. 2007). "Kansas

residents may exempt the full value of the qualified homestead regardless of its actual dollar value." *In re Stroble*, 2005 WL 3844208 at *2 (Bankr. D. Kan. 2005).

Homestead property is not exempt "from sale for taxes, or for the payment of obligations contracted for the purchase of such premises, or for the erection of improvements thereon." K.S.A. § 60-2301; KAN. CONST. ART. 15, § 9. Further, the homestead is subject to consensual liens and does not apply to any process of law obtained as a result of the same. However, if the property is held by both husband and wife, a creditor will need both parties consent for the lien to be valid. *Id*.

"The homestead exemption was established for the benefit of the family and society to protect the family from destitution, and society from the danger of her citizens becoming paupers." *Redmond v. Kester*, 159 P.3d 1004, 1007 (Kan. 2007) (internal quotations omitted). Accordingly, the exemption has been zealously guarded by the courts in Kansas and has been liberally construed. *Id.* As a result, the homestead protection has been extended to cover property over and above the mere land and dwelling. *See, e.g.*, *In re Thexton*, 39 B.R. 367, 372 (Bankr. D. Kan. 1984) (oil and gas royalty interests); *Ginther*, 282 B.R. at 16 (proceeds from the sale of a Kansas homestead (as long as debtor intends in good faith to reinvest proceeds in another homestead located in Kansas within a reasonable time)); *Stroble*, 2005 WL 3844208 (class action settlement proceeds); *Murphy*, 367 B.R. at 711 (certain causes of action under the Kansas Consumer Protection Act). Moreover, the fact that the property is held in a self-settled revocable trust will not defeat the homestead exemption. *Kester*, 159 P.3d at 1004.

2. Iowa

In general, Iowa has an extensive homestead statute and body of law. *See e.g.*, Iowa Code Ann. § 561.1 et seq.; *In re Sears*, 246 B.R. 881 (Bankr.S.D. Iowa 2000); *In re Wipperling*, 286 B.R. 106 (Bankr. N.D. Iowa 2002); *In re White*, 293 B.R. 1 (Bankr. N.D. Iowa 2003); *In re Hebert*, 301 B.R. 19 (Bankr. N.D. Iowa 2003); *In re McCabe*, 299 B.R. 564 (Bankr. N.D. Iowa 2003); *In re Allen*, 301 B.R. 55 (Bankr. S.D. Iowa 2003); *In re Stone*, 329 B.R. 860 (Bankr. N.D. 2005); *In re Sadler*, 327 B.R. 654 (Bankr. N.D. 2005); *In re Takes*, 334 B.R. 642 (N.D. Iowa 2005); *In re Heeren*, 324 B.R. 733 (Bankr. N.D. Iowa 2005); *In re Meyer*, 392 B.R. 416 (Bankr. N.D. Iowa 2008). The discussion herein is meant only to provide the very basics.

In Iowa, the homestead exemption covers one-half acre within city or town limits, and 40 acres outside city limits; provided, however, if the property is worth less than $500 the

homestead will be enlarged until it obtains that value. Iowa Code Ann. § 561.2. The "homestead" in Iowa is defined to include the debtor's house used as a home. If the debtor has two houses, then the debtor gets to select which one. The homestead may contain one or more contiguous lots or tracts of land, including buildings and appurtenances, as long as they are "habitually and in good faith" used as part of the same homestead. Iowa Code Ann. § 561.1. The homestead cannot have more than one dwelling house and or any other buildings, unless properly appurtenant thereto. A shop or building can be considered part of the homestead if used in the debtor's ordinary business, but it can't exceed $300 in value. Iowa Code Ann. § 561.3.

If persons reside together in a single household, there are entitled to claim only one homestead in the aggregate. Iowa Code Ann. § 561.16. If a new homestead is acquired with the proceeds of the hold, then the new homestead will be exempt from execution in the same manner as the former homestead would be. Iowa Code Ann. § 561.20.

While the Iowa homestead is to be liberally construed, it is not a complete bar from judicial sale. *See* Iowa Code 561.16; *Meyer,* 392 B.R. at 419; *Heeren*, at 324 B.R. at 737 (describing the exceptions). For example, there are several exceptions to the Iowa homestead exemption, including:

> 1. Those contracted prior to its acquisition, but then only to satisfy a deficiency remaining after exhausting the other property of the debtor, liable to execution.
>
> 2. Those created by written contract by persons having the power to convey, expressly stipulating that it shall be liable, but then only for a deficiency remaining after exhausting all other property pledged by the same contract for the payment of the debt.
>
> 3. Those incurred for work done or material furnished exclusively for the improvement of the homestead.
>
> 4. If there is no survivor or issue, for the payment of any debts to which it might at that time be subjected if it had never been held as a homestead.

Iowa Code Ann. § 561.21. In certain cases, the homestead can be waived. *In re Wagner*, 259 B.R. 694 (8th Cir. BAP 2001) (discussing waiver of homestead rights in agricultural land and construction of Iowa Code Ann. § 561.22).

3. Nebraska

Similar to Iowa, Nebraska has an extensive homestead statute and body of law, including how the homestead is to be selected. *See, e.g.,* Neb. Rev. Stat. § 40-101 *et seq.; In re Roberts*, 219 B.R. 235 (8th Cir. B.A.P. 1998); *In re Wegner*, 243 B.R. 731 (Bankr. D. Neb. 2000); *In re Uhrich*, 355 B.R. 783 (Bankr. D. Neb. 2006). The discussion herein is meant only to provide the very basics.

In Nebraska, the homestead shall not exceed $60,000 in value and covers "the dwelling house in which the claimant resides, its appurtenances, and the land on which the same is situated, not exceeding one hundred and sixty acres of land, to be selected by the owner, and not in any incorporated city or village, or, at the option of the claimant, a quantity of contiguous land not exceeding two lots within any incorporated city or village…." Neb. Rev. Stat. 40-101. Similar to other states, the exemption should be liberally construed. *See Uhrich*, 355 B.R. at 788. It is, however, not a complete bar. For example, the "homestead is subject to execution or forced sale in satisfaction of judgments obtained (1) on debts secured by mechanics', laborers', or vendors' liens upon the premises and (2) on debts secured by mortgages or trust deeds upon the premises executed and acknowledged by both husband and wife, or an unmarried claimant." Neb. Rev. Stat. 40-103. The sale proceeds of the homestead are exempt for six months. Neb. Rev. Stat. § 40-116.

4. Missouri

In Missouri, "[t]he homestead of every person, consisting of a dwelling house and appurtenances, and the land used in connection therewith, not exceeding the value of fifteen thousand dollars, which is or shall be used by such person as a homestead, shall, together with the rents, issues and products thereof, be exempt from attachment and execution." V.A.M.S. § 513.475. The Missouri homestead exemption "shall not be allowed for more than one owner of any homestead if one owner claims the entire amount" of the exemption. *Id*. If more than one owner, however, claims the homestead exemption with respect to the same piece of property, such exemptions cannot exceed $15,000 in the aggregate. *Id.*

D. EARNED INCOME CREDIT

Courts in the Eighth and Tenth Circuits have previously found that tax refunds are not exempt as wages. *See, e.g., In re Benn,* 491 F.3d 811 (8th Cir. 2007); *In re Rangel*, 317 B.R. 553

(Bankr. D. Kan. 2004).[2] Similarly prior to 2001, courts in Kansas and Missouri had found that the proceeds from the earned income credit ("EIC") were not exempt and subject to turnover. *See In re Earned Income Tax Credit Exemption Constitutional Challenge Cases*, 477 B.R. 791, 793 (Bankr. D. Kan. 2012) (C.J. Nugent); *In re Studstill*, 2011 WL 6208919 (Bankr. D. Kan. 2011) (J. Karlin); *In re Krahn*, 2009 WL 4907034 at *2-3 (Bankr. D. Kan. 2009)(J. Karlin); *In re Demars*, 279 B.R. 548, 551-52 (Bankr. W.D. Mo. 2002) (J. Federman).

However, the legislatures in Kansas and Missouri have taken recent steps to create an exemption for the EIC. In 2011, the Kansas legislature amended the exemption statutes to specifically exempt EIC as to bankrupt debtors. *See* KSA § 60-2315. Further, The Bankruptcy Courts have found that the exemption statute did not contravene either the Uniformity or Supremacy Clauses of the Constitution. *Earned Income Tax Credit Exemption Constitutional Challenge Cases*, 477 B.R. at 791; *In re Westby*, 473 B.R. 392 (Bankr. D. Kan. 2012)(J. Karlin) *affirmed by* 486 B.R. 509 (10th Cir. BAP 2013). Nebraska had enacted a similar law exempting EICs in 2004:

> In bankruptcy and in the collection of a money judgment, the full amount of any federal or state earned income tax credit refund shall be exempt from attachment, garnishment, or other legal or equitable process and from all claims of creditors.

Neb. Rev. Stat. § 25-1553.

In August, 2012, one of Missouri's primary exemption statutes, V.A.M.S. 513.430, was amended. One of the changes to the statute was that "local" was struck from the provision that provided an exemption for public assistance benefits. Previously, Judge Federman had refused to recognize an exemption for an EIC because of the "local" reference in the statute. *See Demars*, 279 B.R. at 551-52. Now that such language has been removed, it appears the impairment found *Demars* has been alleviated. *See In re Corbett*, 2013 WL 1344717 (Bankr. W.D. Mo. 2013). Similarly, at least one bankruptcy court in Iowa has found that "public assistance benefit" under Iowa Code Ann. § 627.6(8)(a) includes an EIC. *See In re Longstreet*, 246 B.R. 611 (Bankr. S.D. Iowa 2000).

[2] Iowa has a limited exemption for tax refunds. *See* Iowa Code Ann. § 627.6(10).

F. TENANCY BY THE ENTIRETY

Missouri also recognizes tenancy by the entirety.[3] "Tenancy by the entirety is a form of ownership in property created by marriage in which each spouse owns the entire property rather than a share or divisible part, and thus at the death of one spouse, the surviving spouse continues to hold title to the property." *In re Eads*, 307 B.R. 219, 222 (Bankr. W.D. Mo. 2004) (quoting *Rinehart v. Anderson*, 985 S.W.2d 363, 367 (Mo.Ct.App. 1998)). "Moreover, in Missouri there is a presumption that both personal property and real estate owned by a husband and wife are held as tenants by the entirety." *In re Brown*, 234 B.R. 907, 912 (Bankr. W.D. Mo. 1999).

"Four elements are necessary in creating a tenancy by the entirety: (1) the husband and wife take one and the same interest; (2) the husband and wife take the interest by the same conveyance; (3) the interests commence at the same time; (4) and the husband and wife hold by one and the same undivided possession." *See In re Popkin & Stern*, 292 B.R. 910 (8th Cir. B.A.P. 2003). "Moreover, in Missouri there is a presumption that both personal property and real estate owned by a husband and wife is held as tenants by the entirety." *In re Brown*, 234 B.R. 907, 912 (Bankr. W.D. Mo. 1999).

"The result of titling property as a tenancy by the entirety is that creditors find it difficult, if not impossible, to reach one spouse's interest in the property when the other spouse did not consent to the creation of the underlying debt." *Eads*, 307 B.R. at 222 (citing *Brown*, 234 B.R. at 912). "In other words, a creditor may only seek satisfaction from entireties property if the spouses have acted jointly to burden the property, and in the absence of joint action, the property is exempt from attachment and execution." *Eads*, 307 B.R. at 222 (citing *Otto F. Stifel's Union Brewing Co. v. Saxy*, 273 Mo. 159, 201 S.W. 67, 71 (1918); *Garner v. Strauss (In re Garner)*, 952 F.2d 232, 235 (8th Cir. 1991); *In re Smith*, 200 B.R. 213, 217 (Bankr. E.D. Mo. 1996)). "In bankruptcy, the effect of holding a joint obligation is important inasmuch as the creditor has the right to be paid from the proceeds of entireties property; the pool of available funds for individual creditors is generally much smaller." *Eads*, 307 B.R. at 222.

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[3] Kansas, Iowa, and Nebraska do not recognize tenancy by the entirety. *See* K.S.A. § 58-501; *Bouska v. Bouska*, 153 P.2d 923 (Kan. 1944); *Kerner v. McDonald*, 84 N.W. 92 (1900); *Sanderson v. Everson*, 141 N.W. 1025, 1026 (Neb. 1913); *Fay v. Smiley*, 207 N.W. 369, 371 (Iowa 1926). *But see* N. William Hines, *Joint Tenancies in Iowa Today*, 98 Iowa L. Rev. 1233, 1241-42 (Mar. 2013) (suggesting tenancy by entirety may be permissible under Iowa law).

In a bankruptcy context, a trustee can only generally administer joint assets for the benefit of joint creditors. In the case where only one spouse files for bankruptcy, the trustee sells the joint assets and then half of the proceeds are remitted to the non-filing spouse. Courts have also found that a trustee cannot administer a joint asset when either the joint debt is waived by the joint creditor or when such debt is reaffirmed by the debtor. *See In re Rentfro*, 234 B.R. 97, 100-01 (Bankr. W.D. Mo. 1999).

G. Converting Non-Exempt Assets to Exempt Assets

1. Pre-BAPCPA

"Prior to BAPCPA, it was well established that a debtor could engage in exemption planning, whereby assets which would be nonexempt could be converted to exempt assets prior to filing for bankruptcy protection." *In re Agnew*, 355 B.R. 276, 282 (Bankr. D. Kan. 2006). "An eleventh hour acquisition of exempt property will not require disallowance of an exemption." *Id*. at 282-83 (internal quotations omitted). "The Code's limitation on abusive prepetition planning was found primarily in § 727(a)(2)(A), which allows for the denial of discharge if a debtor, with intent to hinder, delay, or defraud a creditor, has diminished the estate within one year of filing." *Id.* at 283. "However, denial of discharge requires actual intent to defraud creditors, and in [the Tenth Circuit] the desire to convert assets into exempt property by itself does not constitute actual intent to defraud." *Id*. (citing *Marine Midland Business Loans, Inc. v. Carey (In re Carey)*, 938 F.2d 1073, 1077 (10th Cir. 1991)). *See also Addison v. Seaver (In re Addison)*, 540 F.3d 805, 816 (8th Cir. 2008) ("It is well settled that the mere conversion of non-exempt assets to exempt assets is not in itself fraudulent.") (citations omitted).

"Section 548(a)(1)(A), allowing the trustee to avoid a transfer made within one year of filing with "actual intent to hinder, delay, or defraud any entity" to which the debtor was indebted, likewise placed a limitation upon prepetition planning that was fraudulent rather than a simply taking advantage of the exemptions to which debtors are entitled." *Agnew*, 355 B.R. at 283.

The validity of such well-established law, however, has been questioned with the passage of BAPCPA at least with respect to the homestead. The additions of sections 522(o) and (p) were made in an attempt to correct the perceived abuse of the debtors converting nonexempt assets into their exempt homestead. Additionally, BAPCPA also enacted a "bad actor" limitation with respect to the homestead.

2. BAPCPA Amendments

a. 11 U.S.C. § 522(o)

"New § 522(o) reduces the value of [the homestead] exemption to the extent that such value can be (1) attributed to property disposed of in the ten years preceding filing; (2) with the intent to hinder, delay or defraud a creditor; (3) that the debtor could not otherwise exempt under § 522(b) on the petition date." *Parks v. Anderson (In re Anderson)*, 386 B.R. 315, 328 (Bankr. D. Kan. 2008), *aff'd in part, rev'd in part by* 406 B.R. 79 (D. Kan. 2009). The bankruptcy courts in Kansas that have addressed section 522(o) have found that the objecting party must show by a preponderance of the evidence actual intent to defraud creditors similar to section 727(a)(2)(A) and § 548(a)(1). *See Agnew*, 355 B.R. at 283-84; *In re Kleck*, 363 B.R. 193, 208 (Bankr. D. Kan. 2007); *Anderson*, 386 B.R. at 331-32; *In re Lakey*, 2010 WL 8985033 (Bankr. D. Kan. 2010), *aff'd by* 456 B.R. 687 (D. Kan. 2011). As Judge Somers found in *Agnew*:

> Substantial evidence of prebankruptcy planning to pay down a mortgage on a homestead using nonexempt assets is not sufficient [to] deny discharge, as actions to hinder, delay, or defraud creditors ***require something more***. In the Tenth Circuit that something can be evidenced by the following situations and actions as a basis to infer fraudulent intent: Debtor conceals prebankruptcy conversions; debtor converts assets immediately before filing; debtor continues to use the transferred property; the transfer is made to family members; debtor obtained credit in order to purchase exempt property; the conversion occurred after the entry of a large judgment against the debtor; debtor had engaged in a pattern of sharp dealing prior to bankruptcy; and the conversion rendered the debtor insolvent.

Agnew, 355 B.R. at 285 (emphasis added).

Applying a similar standard, Judge Karlin reduced a homestead by $15,972.79 on account of a debtor taking cash advances from credit cards to either improve his homestead or pay down a loan against the debtor's home. *Kleck*, 363 B.R. at 207-12. As Judge Karlin explained:

> This is not a case where a debtor simply converted non-exempt property he already owned to exempt property in anticipation of filing for bankruptcy, as part of legitimate bankruptcy estate planning clearly allowed in this Circuit. Instead, this Debtor purposely incurred substantial debt on his unsecured credit cards in order to obtain the non-exempt property, which he then converted to his homestead-in other words, this Debtor borrowed unsecured cash to "create" equity, not to preserve assets he already owned.

Id. at 209. In *Anderson*, Judge Nugent recognized that *Agnew* and *Kleck* represent the two extremes with respect to section 522(o). In *Anderson*, Judge Nugent was confronted with a case that fell in the middle of the two extremes. In overruling the section 522(o) objection, Judge Nugent recognized that the facts posed a close case, but that they lacked the "something more." *See Anderson*, 386 B.R. at 331-32 ("In short, the Court concludes that the debtor here did nothing more than take advantage of an exemption to which he is entitled. While his actions were intentional, the Court cannot find that they were done with the intent to hinder, delay or defraud.").

Like the Kansas bankruptcy courts, the Eighth Circuit believes that "something more" than merely converting non-exempt assets into exempt assets must exist to prove an actual intent to hinder, delay and defraud:

> [T]here has been no extrinsic evidence produced here that Addison had any indicia of fraud other than the suit or threat of suit resulting from personal liability on a defaulted loan: Addison did not borrow money to place into exempt assets; he had a preexisting homestead; he did not obtain goods on credit, sell them, then place the money into exempt property; and he did not attempt to conceal the transfers in his bankruptcy filings.
>
> The sort of indicia of fraud necessary to find fraudulent use on an exemption would be, *inter alia*, conduct intentionally designed to materially mislead or deceive creditors about the debtor's position or use of credit to buy exempt property. Additionally, converting a very great amount of property could also be an indication of fraud, as could the existence of conveyances for less than adequate consideration. In the present case, the record contains no extrinsic evidence of any of these indicia of fraud. The record only indicates that Addison's intent was to convert some of his nonexempt property to exempt property on the eve of bankruptcy, something that is "well established" in this circuit that he is allowed to do…. Accordingly, we conclude that it was clear error for the bankruptcy court to find that Addison had the requisite intent to hinder, delay, or defraud a creditor when he converted some nonexempt property into his homestead on the day he filed bankruptcy.

Addison, 540 F.3d at 816. *See also Clark v. Wilmoth (In re Wilmoth)*, 397 B.R. 915 (8th Cir. B.A.P. 2008).

b. 11 U.S.C. § 522(p)

Bankruptcy Code § 522(p) in relevant part provides that "a debtor may not exempt any amount of interest that was acquired by the debtor in the 1215 day period preceding the date of the filing of the petition that exceeds in aggregate $155,675 in value in … real or personal

property that the debtor or dependent of the debtor claims as the homestead." 11 U.S.C. § 522(p)(1)(D). Further, "any amount of such interest does not include any interest transferred from a debtor's previous principal residence (which was acquired prior to the beginning of such 1215-day period) into the debtor's current principal residence, if the debtor's previous and current residences are located in the same state." 11 U.S.C. § 522(p)(2). Recently Judge Nugent found that debtors can stack the cap amount to cover $292,900 in equity pursuant to 11 U.S.C. § 522(m). *See In re Rich*, 2013 WL 1628723 (Bankr. D. Kan. April 16, 2013).

The purpose of Section 522(p)(1) was to close the so-called "mansion loophole". *In re Anderson*, 374 B.R. 848, 852 (Bankr. D. Kan. 2007). In a very thorough opinion, Chief Judge Nugent found that section 522(p)(1) did not apply to a debtor who substantially ($240,000) paid down his mortgage on his homestead within the 1215 day period, but who purchased the homestead prior to such period. *Id.* at 861. On appeal, however, the District Court, in an equally thorough decision, reversed Judge Nugent's decision with respect to Section§ 522(p):

> Equity in a homestead purchased outside the 1,215 day period is an exempt asset under the bankruptcy code, and a homeowner selling that homestead and purchasing another does nothing more than transfer that already-existing exempt asset (equity in the old homestead) into another exempt asset (equity into the new homestead). The homeowner does not lose the exempt status of the equity by transferring the equity of a previous homestead into a new homestead. However, a homeowner's transfer of non-exempt funds during the 1,215-day period from, for example, a bank account, into the homestead as exempt equity above the $125,000[4] cap imposed under § 522(p)(1) is not a protected transfer under the statute. Permitting the transfer of a non-exempt asset into an exempt asset during the 1,215-day period above the $125,000 cap would run contrary to the plain reading of this section. Section 522(p) does permit a debtor to transfer funds from a non-exempt asset into homestead equity so long as it does not exceed $125,000 in the aggregate and is not done with fraudulent intent. Where there is fraudulent intent, § 522(o) may be invoked as a remedy.

Anderson, 406 B.R. at 95. The Tenth Circuit BAP in *Willcut* relying upon the District Court in *Anderson* concluded "that the phrase 'the value of an interest in ... real [ ] property ... shall be reduced" in 11 U.S.C. § 522(o) means that the equity in a debtor's home that was obtained through fraudulent transfer of non-exempt assets into exempt assets is to be reduced. If there is no equity, there is no value subject to reduction." *In re Willcut*, 472 B.R. 88, 98 (10th Cir. B.A.P. 2012). 11 U.S.C. § 522(q)

[4] The cap amount periodically adjusts.

c. 11 U.S.C. § 522(q)

Bankruptcy Code § 522(q) has been referred to as the "bad actor" provision. Section 522(q)(1) caps a debtor's homestead at $155,675 if:

> (A) the court determines, after notice and a hearing, that the debtor has been convicted of a felony (as defined in section 3156 of title 18), which under the circumstances, demonstrates that the filing of the case was an abuse of the provisions of this title; or
>
> (B) the debtor owes a debt arising from—
>
> > (i) any violation of the Federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934), any State securities laws, or any regulation or order issued under Federal securities laws or State securities laws;
> >
> > (ii) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 1934 or under section 6 of the Securities Act of 1933;
> >
> > (iii) any civil remedy under section 1964 of title 18; or
> >
> > (iv) any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years.

11 U.S.C. § 522(q)(1). Section 522(q) will not apply, however, to the extent the homestead is "reasonably necessary for the support of the debtor and any dependent of the debtor." 11 U.S.C. § 522(q)(2). It should be further noted that a debtor's discharge may be denied to the extent that Section 522(q)(1) is applicable. *See* 11 U.S.C. § 727(a)(12).

In sum, the law on these new provisions is continuing to develop and while there are several good bankruptcy cases interpreting the same, practitioners should be very careful when advising clients with respect to the permissible limits of exemption planning in light of the BAPCPA amendments.

III. JUDICIAL ESTOPPEL AND THE FAILURE TO DISCLOSE CAUSES OF ACTION

A. INTRODUCTION

Upon filing a bankruptcy case, a debtor is required to file schedules of its assets and liabilities and a statement of its financial affairs. *See* 11 U.S.C. § 521(a)(1). As discussed in

above, property of the estate is a broad concept, and would pick up various causes of action that a debtor has against a third party. In certain cases, the trustee will employ the debtor's prepetition counsel to continue to pursue the causes of action on behalf of the estate. However, in certain cases, such causes of action are not disclosed on the schedules or otherwise made known to the trustee, and the debtor continues to pursue the causes of action. In these circumstances, a frequent strategy employed by defense counsel is to raise the defense of judicial estoppel to the claim.

The doctrine of judicial estoppel[5] was recognized in detail by the Supreme Court in *New Hampshire v. Maine*. *See Eastman v. Union Pacific Railroad Company*, 493 F.3d 1151, 1156 (10th Cir. 2007) (citing *New Hampshire v. Maine*, 532 U.S. 742, 749-50 (2001)). The "purpose [of the doctrine] is to protect the integrity of the judicial process by prohibiting parties from deliberately changing positions according to the exigencies of the moment." *New Hampshire*, 532 U.S. at 749-50. The Supreme Court recognized three factors in determining if the doctrine should be invoked:

- "a party's subsequent position must be 'clearly inconsistent' with its form position."
- "a court should inquire whether the suspect party succeeded in persuading a court to accept that party's former position, 'so that judicial acceptance of an inconsistent position in a later proceeding would create the *perception* that either the first or the second court was misled."
- "the court should inquire whether the party seeking to assert an inconsistent position would gain an unfair advantage in the litigation if not estopped."

Eastman, 493 F.3d at 1156. Additionally, "[j]udicial estoppel is an equitable doctrine, and it is not equitable to employ it to injure creditors who are themselves victims of the debtor's deceit." *Cannon-Stokes v. Potter*, 453 F.3d 446, 448 (7th Cir. 2006). For this reason, if the debtor does not list the claims, but they are later discovered by a trustee who pursues them, courts may be less inclined to apply the judicial estoppel doctrine because the trustee was not a party to the deceit. *See Eastman*, 493 F.3d at 1155 n. 3.

[5] For a detailed discussion regarding the doctrine of judicial estoppel, *see* Eric Hilmo, Note, *Bankrupt Estoppel: The Case for a Uniform Doctrine of Judicial Estoppel as Applied Against Former Bankruptcy Debtors*, 81 Fordham L. Rev. 1353 (2012).

B. JUDICIAL ESTOPPEL CASE EXAMPLES

In *New Hampshire v. Maine*, 532 U.S. 742 (2001), the Supreme Court discussed in detail the doctrine of judicial estoppel. The case centered around a dispute between the states of New Hampshire and Maine and their inland river boundary with New Hampshire claiming that the entry Piscataqua River and all of Portsmouth Harbor belonged to it. The location of the boarder had been a subject of dispute on at least two prior occasions. In 1740, by decree of King George, the boarder was established to be the "middle of the river". *New Hampshire*, 532 U.S. at 745-749. In 1977, the states had entered into a consent decree establishing their lateral marine boundary and defining the "middle of the river" as "the middle of the main channel of navigation of the Piscataqua River." *Id*. at 747. In that decree, Maine and New Hampshire "expressly agreed … that the decree of 1740 fixed the boundary in the Piscataqua Harbor area." *Id*.

Applying the factors stated above, the Court invoked the doctrine of judicial estoppel. *Id*. at 749. It found that New Hampshire was taking a clearly inconsistent position with respect to its latest interpretation of the words "middle of the river", that it benefited from its previous interpretation, and that it led the Court to believe in 1977 that the agreement between the states was in each of their best interests. *Id*. at 749-755. While the Court found that it would not apply to the facts before it, the Court did leave open a possible exception if the party's previous position was a product of inadvertence or mistake. *Id*. at 752.

In *Stallings v. Hussman Corp.,* 447 F.3d 1041 (8th Cir. 2006), the debtor filed a lawsuit for wrongful termination against his employer. The debtor, however, was not terminated until after he had filed a Chapter 13 bankruptcy, which was ultimately dismissed without the debtor receiving a discharge. The defendant asserted, and the district court agreed, that the case should be dismissed, in part, on reliance of the judicial estoppel doctrine. The Eighth Circuit rejected the district court's judicial estoppel analysis and reversed. *Stallings,* 447 F.3d at 1043-45.

The Eighth Circuit, applying the *New Hampshire* factors, found that while the debtor took inconsistent positions, that the other factors did not support the application of the doctrine. First, there was no judicial acceptance of the debtor's prior inconsistent statement – his case was dismissed without receiving a discharge. Second, he did not obtain any advantage from the inconsistent positions. In this regard, the Eighth Circuit found that his claims did not arise until

after he had filed, so he would not have been able to list them on his initial schedules. Additionally, it was not clear whether the debtor even had a claim. *Id*. at 1045-49.

In discussing the judicial doctrine, the Eighth Circuit also provided the following analysis regarding the role of mistake or inadvertence in the application of the doctrine:

> Notably, judicial estoppel does not apply when a debtor's "prior position was taken because of a good-faith mistake rather than as part of a scheme to mislead the court." *Ryan Operations G.P. v. Santiam-Midwest Lumber Co.*, 81 F.3d 355, 362 (3d Cir.1996) (internal quotations and citation omitted). "Although it may generally be reasonable to assume that a debtor who fails to disclose a substantial asset in bankruptcy proceedings gains an advantage," the specific facts of a case may weigh against such an inference. *Id*. at 363. A rule that the "requisite intent for judicial estoppel can be inferred from the mere fact of nondisclosure in a bankruptcy proceeding [would] unduly expand the reach of judicial estoppel in post-bankruptcy proceedings and would inevitably result in the preclusion of viable claims on the basis of inadvertent or good-faith inconsistencies." *Id*. at 364. Careless or inadvertent disclosures are not the equivalent of deliberate manipulation. *Id*. Courts should only apply the doctrine as an extraordinary remedy when a party's inconsistent behavior will result in a miscarriage of justice. *Id*. at 365.

Id. at 1049.

In *Biesek v. Soo Line Railroad Co.*, 440 F.3d 410 (7th Cir. 2006), the debtor filed for bankruptcy in 2002. Prior to filing for bankruptcy, the debtor had a FELA claim pending against the railroad. Indeed, three months before filing bankruptcy, debtor received an offer from the railroad for $62,500. Neither the proposal or the claim were listed in the schedules. Had he accepted the offer, the debtor would have been solvent. The debtor had separate bankruptcy counsel, who upon finding out about the claim, promptly notified the trustee. *Biesek*, 440 F.3d at 411-12.

Debtor initiated a FELA action against the railroad seeking to enforce the $62,500 offer. The railroad sought dismissal based upon the doctrine of judicial estoppel. The district court agreed, and dismissed the case. While the case was pending appeal, the debtor entered into a stipulation with the trustee stating that the first $7,000 of any recovery would got to the Trustee's and the creditor's benefit. With stipulation in hand, the debtor sought to have the court reconsider its dismissal. The trustee did not intervene into the action. The motion to reconsider was denied. *Id*.

The Seventh Circuit affirmed the district court. In doing so, however, the Seventh Circuit did not give judicial estoppel a ringing endorsement in the bankruptcy context:

> Judges understandably favor rules that encourage full disclosure in bankruptcy. Yet pursuing that end by applying judicial estoppel to debtors' self-contradiction would have adverse effects on third parties: the creditors. [Debtor's] nondisclosure in bankruptcy harmed his creditors by hiding assets from them. Using this same nondisclosure to wipe out his FELA claim would complete the job by denying creditors even the right to seek some share of the recovery. Yet the creditors have not contradicted themselves in court. They were not aware of what [debtor] has been doing behind their backs. Creditors gypped by [debtor's] maneuver are hurt a second time by the district judge's decision. Judicial estoppel is an equitable doctrine, and using it to land another blow on the victims of bankruptcy fraud is not an equitable application. Instead of vaporizing assets that could be used for the creditors' benefit, district judges should discourage bankruptcy fraud by revoking the debtors' discharges and referring them to the United States Attorney for potential criminal prosecution.

Id. at 413.

The Seventh Circuit, however, questioned why the trustee was not more involved in the case. Essentially, the Seventh Circuit suggested several actions the trustee could have done that would have potentially altered the outcome, such as seeking remand so that the trustee could intervene. However, since no such actions were taken, it affirmed the district court's decision. *Id*. at 413-414.

In *Eastman v. Union Pacific Railroad Co.,* 493 F.3d 1151 (10th Cir. 2007), the debtor was injured in an auto accident while working for the railroad. He initiated a FELA action against the railroad. Subsequent to initiating his FELA claim, he filed for Chapter 7 bankruptcy. Debtor did not list the claims or disclose the lawsuit anywhere in his schedules or statement of financial affairs. When asked about any personal injury claims at his meeting of creditors, the trustee was misled in to believing the only claims that existed were exempt worker's compensation type claims. The trustee filed a no asset report and the case was closed. *Eastman*, 493 F.3d at 1152-54.

In doing a routine search, the debtor's personal injury counsel discovered the bankruptcy filing. The attorney promptly notified the trustee who sought to re-open the case, which was subsequently re-opened. The various defendants filed a motion for summary judgment seeking to dismiss claims on the basis of judicial estoppel doctrine. Prior to the Tenth Circuit's ruling, the trustee settled with two of the defendants and the debtor's creditors received payment in full, thus leaving only the debtor in the lawsuit as a plaintiff. The district court granted summary

judgment in favor of the defendants, and the debtor appealed. The Tenth Circuit affirmed. *Id*. at 1154-55.

Applying the *New Hampshire* factors, the Tenth Circuit took the debtor to task given the facts of this case. In doing so, the Tenth Circuit addressed some defenses that debtors claim when the doctrine is asserted against them. First, as to the mistake defense, the Tenth Circuit summarized the evolution of that defense in bankruptcy cases since *New Hampshire* decision was rendered:

> To be sure, in *New Hampshire*, 532 U.S. at 753, 121 S.Ct. 1808, the Supreme Court did "not question that it may be appropriate to resist application of judicial estoppel when a party's prior position was based on inadvertence or mistake." (emphasis added) (internal quotations omitted). Unfortunately for Gardner, our sister circuits, for what seem to us sound reasons, have not been overly receptive to debtors' attempts to recover on claims about which they "inadvertently or mistakenly" forgot to inform the bankruptcy court. Instead, courts addressing a debtor's failure to satisfy the legal duty of full disclosure to the bankruptcy court have deemed such failure inadvertent or mistaken "only when, in general, the debtor either lacks knowledge of the undisclosed claims or has no motive for their concealment." *In re Coastal Plains, Inc.,* 179 F.3d 197, 210 (5th Cir.1999); *accord Browning v. Levy*, 283 F.3d 761, 776 (6th Cir.2002); *Barger v. City of Cartersville*, 348 F.3d 1289, 1294 (11th Cir.2003). Where a debtor has both knowledge of the claims and a motive to conceal them, courts routinely, albeit at times sub silentio, infer deliberate manipulation. *See Burnes*, 291 F.3d at 1287 ("[S]everal circuits, in considering the particular issue of judicial estoppel and the omission of assets in a bankruptcy case, have concluded that deliberate or intentional manipulation can be inferred from the record.").

Id. at 1157. In *Eastman*, the Tenth Circuit found that the debtor both had the knowledge and motive.

Additionally, the Tenth Circuit addressed the fact that the creditors were paid in full, in other words "no harm, no foul" defense. In this regard, the Tenth Circuit found:

> That Gardner's bankruptcy was reopened and his creditors were made whole once his omission became known is inconsequential. A discharge in bankruptcy is sufficient to establish a basis for judicial estoppel, "even if the discharge is later vacated." *Hamilton*, 270 F.3d at 784. Allowing Gardner to "back up" and benefit from the reopening of his bankruptcy only after his omission had been exposed would "suggest[ ] that a debtor should consider disclosing potential assets only if he is caught concealing them. This so-called remedy would only diminish the necessary incentive to provide the bankruptcy court with a truthful disclosure of the debtor's assets." *Burnes*, 291 F.3d at 1288.

Id. at 1160.

In *Clemenston v. Countrywide Financial Corp.,* 464 Fed. Appx. 706 (10th Cir. 2012), the debtor, as a *pro se* plaintiff, initiated lawsuit against his mortgage company related to a refinancing of his mortgage in 2003. In 2007, to prevent foreclosure, the debtor filed for Chapter 7 bankruptcy. In 2009, the debtor sought a loan modification which was rejected by his mortgage company. The bankruptcy case was closed in 2009, and the debtor filed the action against the mortgage company in 2010. The magistrate judge recommended dismissal for most of the complaint, and the district court adopted the recommendation. The debtor appealed and the Tenth Circuit affirmed. *Clemenston,* 464 Fed. Appx. at 708-09.

The magistrate recommended dismissal because the debtor did not list the claims in his 2007 bankruptcy and did not have standing to pursue the same, as they were still property of his bankruptcy estate. Referencing its previous *Eastman* decision, the Tenth Circuit found that "a debtor's ignorance or mistake, even if insufficiently egregious to warrant application of judicial estoppel, does not excuse a debtor from listing all potential causes of action in a bankruptcy petition." *Id*. at 711.

In *Queen v. TA Operating, LLC*, -- F.3d --, 2013 WL 4419322 (10th Cir. Aug. 20, 2013), the debtors were a husband/wife semi-truck driving team. In February 2007, Mr. Queen injured himself in the parking lot of the defendant in Wyoming and the debtors initiated a negligence action for the same claiming several categories of defenses. While the district court action was pending, the debtors filed for Chapter 7 bankruptcy in California. In their schedules, they did not list the cause of action. The Chapter 7 trustee sent a pre-meeting of creditors questionnaire, which specifically asked if the debtors were suing anyone. In response, they stated: "Insurance company suing to get money refunded for my injury." No further questions were asked at the meeting of creditors and the trustee determined that there were no assets to distribute to creditors. *Queen*, 2013 WL 4419322 at *1-2.

The defendant became aware of the bankruptcy and notified the trustee of the Wyoming lawsuit. The trustee notified the debtors that he was not going to take any further action on the matter until the debtors amended their schedules and claimed any exemptions. The debtors filed amended schedules and placed a total value of the claims asserted in the lawsuit at $400,000 and sought to exempt the entire amount. Neither the Trustee, nor any creditors, objected to the exemptions, the trustee issued a no-asset determination, and the debtors were granted their discharge. *Id*. at *2-3.

After the debtors amended their schedules and were granted a discharge, the defendant filed a motion for summary judgment claiming judicial estoppel. The district court agreed and dismissed the lawsuit with prejudice. The debtors appealed and the district court was affirmed by the Tenth Circuit.

In affirming the district court, the Tenth Circuit applied the *New Hampshire* factors. First, the Tenth Circuit found that the debtors had taken clearly inconsistent positions. First, the debtors had failed to initially disclose the lawsuit. Second, in the amended schedules, they valued the lawsuit at a total of $400,000. In the actual lawsuit, they were seeking damages in excess of $1,500,000. Further, while they attempted to exempt the entire amount of the lawsuit, many of their claims were not covered by the exemption statutes. The court rejected the debtor's explanation that the amounts in the schedules were merely estimates. *Id*. at *4-7.

Second, the Tenth Circuit found that the debtors had succeeded in persuading the bankruptcy court to accept their inconsistent position. First, the Tenth Circuit agreed that when addressing this factor the relevant position is the one the debtor's took in the amended schedules. Second, the court emphasized that the concern is not whether the debtors had a nefarious plot mislead the court, but rather it was concerned with the perception that either first or second court was misled and that a risk of inconsistent court determinations would be introduced resulting in a threat to judicial integrity. Here, the court found that even just considering the amended schedules, the debtors took a materially inconsistent position, which ultimately led to their discharge. *Id*. at *8.

Finally, the Tenth Circuit found that the debtor would gain an unfair advantage if the doctrine was not applied. Specifically, given the improper disclosures as to value, the Tenth Circuit found that if the doctrine was not applied, the debtors would be able to receive an award that at least a portion could have gone to their creditors had they been truthful. *Id*. at *9. The Tenth Circuit also rejected the debtors' claims of mistake and inadvertence. The Tenth Circuit found that the debtors had both knowledge of the claims and motive to conceal the same. Further, the Tenth Circuit rejected the debtors attempt to blame their bankruptcy attorney finding that they were bound by the acts of the same. *Id*. at *10-11.

APPENDIX
Pigs Get Fat, Hogs Get Slaughtered:
Property of the Estate and
Exemption Issues in Consumer Cases
Common Exemption Quick Reference Guide

Nature of Exemption[1]	Bankruptcy Code	Kansas	Missouri	Iowa	Nebraska
Homestead	$22,975 § 522(d)(1)	Unlimited in Amount City: 1 acre Rural: 160 acres K.S.A. § 60-2301, KAN. CONST. ART. 15, § 9	$15,000 V.A.M.S. § 513.475	Unlimited in Amount City: ½ acre Rural: 40 acres I.C.A. § 561.1 *et seq*.	$60,000 City: 2 contiguous lots Rural: 160 acres N.R.S. § 40-101 et seq.
Household Goods & Furnishing, Wearing Apparel	$575 particular item $12,250 in aggregate § 522(d)(3)	Amount reasonably necessary for 1 year. K.S.A. § 60-2304(a)	$3,000 V.A.M.S. § 513.430(1)	$7,000 (household goods) I.C.A. § 627.6(5) $1,000 (Private libraries, family bibles, pictures, portraits, and paintings) I.C.A. § 627.6(3)	$1,500 (household goods) Unlimited (immediate personal possession and wearing apparel) N.R.S. § 25-1556
Jewelry	$1,550 § 522(d)(4)	$1,000 K.S.A. § 60-2304(b)	$500 (general) $1,500 (wedding ring) V.A.M.S. § 513.430(2)	$2000 (general) I.C.A. § 627.6(1)(b) Wedding/Engagement Rings –Unlimited, but subject to a $7,000, less general jewelry exemption, cap if purchased after marriage and within 2 years of claim the exemption I.C.A. § 627.6(1)(a)	NA

[1] This chart does not reflect all exemptions available to a debtor, e.g., exemptions regarding IRAs and pensions. Further, in many cases, exemptions are further limited or eliminated with respect to domestic support obligations, such as child support. This chart is generally reflecting exemptions for non-domestic support obligations. The reader is cautioned to confirm the information provided in this chart by independent research and analysis to ensure that it is accurate, complete, and current.

Automobile	$3,675 § 522(d)(2)	$20,000 K.S.A. §60-2304(c)	$3,000 V.A.M.S. § 513.430(5)	$7,000 I.C.A. § 627.6(9)	$2,400 (included in tools of trade exemption) N.R.S. § 25-1556 (4)
Burial Plot	NA	Unlimited K.S.A. - 60-2304(d)	1 acre or $100 value of recorded burial ground V.A.M.S. § 214.190	1 acre I.C.A. § 627.6(4)	Unlimited N.R.S. § 12-517, 520 and 506 and 605
Tools of the Trade	$2,300 § 522(d)(6)	$7,500 K.S.A. 60-2304(e)	$3,000 - V.A.M.S. § 513.430(4)	$10,000 (non-farming) I.C.A. § 627.6(11) $10,000 (farming, including livestock and feed) – but subject to certain restrictions I.C.A. § 627.6(12)	$2,400 N.R.S. § 25-1556 (4)
Insurance benefits	Any unmatured life ins. owned by debtor, other than a credit life ins. contract § 522(d)(7) $12,250 of debtor's interest in life ins. owned by the debtor where debtor or dependent is the insured § 522(d)(8)	Unlimited unless bankruptcy case commenced within 1 year of acquisition. K.S.A. §§ 40-414, 60-2313(7)	$150,000, but not protected if obtained one year before bankruptcy V.A.M.S. § 513.430(8)	Unlimited if beneficiary is spouse, child or dependent. If obtained or added to within two years of the exemption being claimed, then subject to $10,000 cap Proceeds are exempt from beneficiaries debts in the amount of $15,000 I.C.A. § 627.6(6)	$100,000, but not protected if obtained three years before bankruptcy. N.R.S. § 44-371
Alimony, Maintenance & Support	Unlimited to extent necessary to support debtor and dependent § 522(d)(10)(D).	Unlimited K.S.A. § 60-2308(e)	$750 V.A.M.S. § 513.430(10)(d)	Unlimited to extent necessary to support debtor and dependent I.C.A. § 627.6(8)(d)	NA *See* *In re Loftus*, BK97-82311 (suggesting that post-petition alimony accrues each month and not property of the estate); *but see* *In re Mehlhaff* 491 B.R. 898(8th Cir.

					B.A.P. 2013)(alimony is property of the estate)
Wages	NA	75% K.S.A. § 60-2310	75% or 90% (HOH) V.A.M.S. § 525.030	Further limitations than the 75% of federal law and sets certain maximums during a calendar year: Earnings = Max < 12k $250 12k-16k $400 16k-24k $800 24k-35k $1,500 35k-50k $2,000 >50K 10% I.C.A. § 642.21 In event of bankruptcy debtor's interest in accrued wages and federal and state tax refunds in the amount of $1,000 I.C.A. § 627.6(10)	75% or 85% (HOH) N.R.S. § 25-1558
Social Security	Unlimited § 522(d)(10)(A)	Unlimited 42 U.S.C. § 407	Unlimited V.A.M.S. § 513.430(10)(a) 42 U.S.C. § 407	Unlimited I.C.A. § 627.6(8)(a) 42 U.S.C. § 407	Unlimited 42 U.S.C. § 407
Workers' Compensation	Unlimited § 522(d)(10)(C)	Unlimited K.S.A. § 60-2313(3)	Unlimited V.A.M.S. § 287.260	Unlimited I.C.A. § 627.13	Unlimited N.R.S. § 48-149
Public Assistance	Unlimited § 522(d)(10)(A)	Unlimited K.S.A. § 60-2313(2)	Unlimited V.A.M.S. § 513.430(10)(a)	Unlimited I.C.A. § 627.6(8)(a)	Unlimited N.R.S. §§ 68, 148, 68-1013
Unemployment Compensation	Unlimited § 522(d)(10)(C)	Unlimited except for debtor's necessaries provided while debtor unemployed and certain	Unlimited except for debtor's necessaries provided while debtor unemployed and certain	Unlimited I.C.A. § 627.6(8)(a)	Unlimited except for debtor's necessaries provided while debtor unemployed and certain

		child support obligations K.S.A. § 60-2313(4)	child support obligations V.A.M.S.288.380; 513.430(10)(c)		child support obligations N.R.S. § 48-647
Wildcard	$1,225, plus up to $11,500 of unused homestead exemption. § 522(d)(5)	NA	$600 V.A.M.S. § 513.430(3)	$1,000 I.C.A. § 627.6(14)	$2,500 (except wages and in lieu of homestead) N.R.S. § 25-1552
Professionally prescribed health aids for debtor or dependent	Unlimited § 522(d)(9).	NA	NA	Unlimited I.C.A. § 627.6(7)	Unlimited N.R.S. § 25-1556(5)
Earned Income Credit	NA	Maximum credit allowed to the debtor for one tax year (bankruptcy debtors only) - KSA § 60-2315	Unlimited V.A.M.S.§ 513.430(10)(a)	Unlimited I.C.A. § 627.6(8)(a)	Unlimited N.R.S. § 25-1553
Shotgun, Rifle or Musket	NA	NA	NA	Unlimited	NA

FEDERAL BANKRUPTCY QUALIFICATIONS OF STATE HOMESTEAD EXEMPTION LAWS

33rd Annual Midwestern Bankruptcy Institute and Consumer Forum
Kansas City, Missouri - October 4, 2013

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Lynn M. LoPucki, A General Theory of the State Remedies/Bankruptcy System, 1982 Wis. L. Rev. 311

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Richard Hynes & Eric A. Posner, The Law and Economics of Consumer Finance, 4 American Law and Economics Review 168 (2002)

Lars Lefgren & Frank McIntyre, Explaining the Puzzle of Cross-State Differences in Bankruptcy Rates, 52 Journal of Law and Economics 367 (May 2009)

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CFCU Community Credit Union v. Hayward, 552 F3d 252 (2d Cir. 2009) (post-BAPCPA increase of New York homestead from $10,000 to $50,000 held retroactively applicable and not an unconstitutional contract impairment)

2. Federal Constraints (Bankruptcy and 5th Amendment Takings and Due Process Clauses)

U.S. v. Security Industrial Bank, 459 U.S. 70 (1982)

II. DEVELOPMENT AND DIMENSIONS OF STATE HOMESTEAD EXEMPTION LAWS

A. Rapid and Widespread Mid-Nineteenth Century Enactments

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B. Substantial Variations in Scope and Operation

State Homestead Exemption Laws, 46 Yale Law Journal 1023 (1937)

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C. The Homestead Laws of Iowa, Kansas, and Missouri

1. Iowa

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2. Kansas

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3. Missouri

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III. DEVELOPMENT AND DIMENSIONS OF BANKRUPTCY LAWS

A. Nineteenth Century Federal Bankruptcy Laws

1. The Bankruptcy Act of 1800 (repealed 1803) (federal exemptions)

2. The Bankruptcy Act of 1841 (repealed 1843) (federal exemptions)

3. The Bankruptcy Act of 1867 (repealed 1878) (federal exemptions + "static" state exemptions)

4. The Bankruptcy Act of 1898 (repealed 1979) (state exemptions)

Hanover National Bank v. Moyses,186 U.S. 181 (1902)

B. Nineteenth Century State Bankruptcy Laws

1. Constitutional Limitations on State Impairment of Contracts

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2. Territorial Limitations on Reach of State Legislative and Judicial Actions

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3. Significance in Intervals Between Nineteenth Century Federal Bankruptcy Laws and Displacement by 1898 Enactment of Permanent Federal Bankruptcy Law

International Shoe Co. v. Pinkus, 278 U.S. 261 (1929)

4. Continuing Availability of Non-Bankuptcy State Law Insolvency Procedures (Extensions/Compositions, Assignments for Benefit of Creditors, and Statutory/Equity Receiverships)

C. Late Twentieth Century Federal Bankruptcy Law

1. The Bankruptcy Reform Act of 1978

Commission on Bankruptcy Laws of the United States: Uniform federal exemptions

National Conference of Bankruptcy Judges: Federal exemptions or state exemptions

House of Representatives: Federal exemptions or state exemptions

Senate: State exemptions

Enactment: Federal exemptions or state exemptions, but subject to state opt-out

2. Extent and Dynamics of Opt-Out

Richard M. Hynes, Anup Malani, & Eric A. Posner, The Political Economy of Property Exemption Laws, 47 Journal of Law and Economics 19 (2004)

3. Occasional Subsequent Reversals of Initial Opt-Outs

D. Early Twenty-First Century Federal Bankruptcy Law

1. National Bankruptcy Review Commission Final Report (1997)(federal exemptions with homestead determined by incorporated state law subject to $20,000 floor and $100,000 ceiling)

2. Intermediate Congressional Positions

Susan Jensen, A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, 79 American Bankruptcy Law Journal 485 (2005)

105th Congress (1997-1998)
House of Representatives: One-year fraudulent conversion provision
Senate: $100,000 homestead limitation
Conference: Two-year residence and fraudulent conversion provision

106th Congress (1999-2000)
House of Representatives: $250,000 homestead limitation, but subject to contrary state constitutional provisions and to override by subsequent state legislation
Senate: $100,000 homestead limitation
Conference: Two-year residence requirement and $100,000 homestead limitation if acquired within two years

107th Congress (2001-2002)
House of Representatives: Two-year residence requirement and $100,000 homestead limitation if acquired within two years
Senate: $125,000 homestead limitation
Conference: Following Senate conferee's proposal of a five-year residence requirement and House conferee's proposal to reduce same to two and one-half years and to extend fraud conversion reach back period to ten years, conferees settled on residence period of forty months

108th Congress (2003-2004)
House of Representatives: Provisions reached by 2002 conference committee

3. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA)

109th Congress (2005)

IV. EARLIER INTERACTIONS AND DISCONTINUITIES BETWEEN STATE EXEMPTION LAWS AND THEIR OPERATION IN FEDERAL BANKRUPTCY PROCEEDINGS

A. Difficulties of Integrating State Exemption Laws into Federal Bankruptcy Proceedings

Appendix B: *Bauer, Challenges in Translating Iowa's "Bilateral" Preacquisition Debt Exception Into the "Multilateral" Circumstances of Bankruptcy Proceedings*

B. Other Overrides of State Exemption Law Not Subject to Opt-Out

1. Waivers (§ 522(e))

2. Lien Avoidance (§ 522(f))

C. Prior and Ongoing Debate Concerning the Appropriateness of Uniform Federal Bankruptcy Exemptions and the Importance of Giving Effect to State Exemption Laws

William H. Brown, Political and Ethical Considerations of Exemption Limitations: The Opt-Out as Child of the First and Parent of the Second, 71 American Bankruptcy Law Journal 149 (1997)

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Justin Pratt, The Inequitable Situation: A Look at the Bankruptcy Homestead Exemption After Five Years of Judicial Interpretation, 3 Estate Planning & Community Property Law Journal 97 (2010)

V. BAPCPA QUALIFICATIONS OF STATE HOMESTEAD EXEMPTION LAWS

A. CHOICE OF LAW

11 U.S.C. § 522(b) [*as amended by BAPCPA, P.L. 109-8, § 224(a)*]:

> (b)(1) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either paragraph (~~1~~2) or, in the alternative, paragraph (~~2~~3) of this subsection. ...
>
> (~~1~~2) Property listed in this paragraph is property that is specified under subsection (d) ~~of this section~~, unless the State law that is applicable to the debtor under paragraph (~~2~~3)(A) ~~of this section~~ specifically does not so authorize.
>
> (~~3~~2) Property listed in this paragraph is
>
> (A) subject to subsections (o) and (p), any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the ~~180~~ 730 days immediately preceding the date of the filing of the petition~~, or for a longer portion of such 180-day period than in any other place~~ or if the debtor's domicile has not been located at a single State for such 730-day period, the place in which the debtor's domicile was located for 180 days immediately preceding the 730-day period or for a longer portion of such 180-day period than in any other place; ~~and~~
>
> (B) any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law~~.~~ ;and
>
> (C) retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.
>
> If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt property that is specified under subsection (d).

The effects of the essentially territorial limitations of state legislative and judicial authority are clearly evident in the choice of law rules traditionally applied when exemption issues arise in state court proceedings. See generally Sheldon R. Shapiro, Choice of Law as to Exemption of Property from Execution, 100 A.L.R.3d 1235 (1980). In contrast, however, considerably different results sometimes followed from the combined effects of the choice of applicable state law specified

by the pre-BAPCPA version of § 522(b) and the generally national force of federal bankruptcy law.[1]

For example, shortly before BAPCPA's passage the Eighth Circuit determined that Minnesota's homestead statute could be applied to exempt a house that former Minnesota residents had acquired in Arizona shortly before filing a bankruptcy petition properly venued in Minnesota. In re Drenttel, 403 F.3d 611 (8th Cir. 2005), aff'g 302 B.R. 320 (8th Cir. BAP 2004). Later that same year, a debtor filing a Chapter 7 petition in Iowa because his failed business and resulting debts existed there was allowed to claim a homestead exemption under Wisconsin law for a residence located there where the debtor had resided in Wisconsin for the longest portion of the 180-day period that controlled both exemption choice of law and venue pre-BAPCPA. In re Stone, 329 B.R. 860 (Bankr. N.D. Iowa 2005) (Judge Kilburg).

In re Williams, 369 B.R. 470 (W.D. Ark. 2007) provides a rather striking example of the effects of the divergence between venue and exemption choice of law effected by BAPCPA. Debtors who had lived in Iowa from August 2000 until moving to Arkansas in March 2006 had secured proper venue for the Chapter 7 petition they filed in Arkansas on July 28, 2006. BAPCPA's exemption choice of law provision, however, required debtors to use Iowa exemptions and although the lack of any timely objection resulted in debtor's claimed personal property exemptions being allowed, the court clearly indicated that a contrary result otherwise would have followed from the combined effects of Iowa's opt-out provision and its restriction of personal property exemptions to

1. In a couple of pre-BAPCPA cases, Iowa bankruptcy courts applied Iowa law to determine the exempt nature of property located in another state, In re Lambert, No. 00-0255-DH (S.D. Iowa 2000) (Judge Hill) (abandonment of jointly owned house in Illinois occupied by ex-husband and children), or applied Nebraska law to a Nebraska homestead where the application of such law was required by the former version of § 522(b), In re Treadway, No. 95-50677XS (Bankr. N.D. Iowa 1995) (Judge Edmonds). Somewhat differently, several pre-BAPCPA cases reached differing conclusions about the effects of Iowa's incorporated homestead exemption in circumstances where debtors attempted to avoid the exception for pre-acquisition debts by invoking the carryover effects of a earlier homestead previously owned in another state. Compare In re Welch, No. A87-02433S (Bankr. N.D. Iowa 1988) (Judge Melloy) (carryover allowed) with In re Carlson, No. 98-0369S (Bankr. N.D. Iowa 1999) (Judge Melloy) (carryover not allowed) and In re Bausback, No. 02-0825-WH (Bankr. S.D. Iowa 2003) (Judge Hill) (same).

"a debtor who is a resident of this state." In contrast, over objection the debtor's homestead exemption claim under Iowa law was allowed based on the absence of any similar "resident of this state" limitation. (Although not squarely addressed by the decision, the facts of Williams illustrate the ambiguity of "any" in the "opt-out override" contained in § 522(b)(3)'s concluding sentence ("If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt property that is specified under subsection (d)." (emphasis added)). See also In re Camp, 631 F.3d 757 (5th Cir. 2011) (debtor currently residing in opt-out state (Texas) allowed to elect federal exemptions where opt-out provision of state of prior residence (Florida) encompassed only "residents").

Subsequent cases have involved sometimes bewildering intersections between the exemption laws of the state specified by BAPCPA's choice of law provision and determinations of either territorial or extraterritorial effect of those laws based on formulations seemingly framed in circumstances where anything other than territorial effect was essentially unthinkable. See Dale J. Gilsinger, Extraterritorial Application of State's Homestead Exemption Pursuant to Bankruptcy Code § 522, 47 A.L.R. Fed. 2d 335 (2010); Kay E. Oskvig, Look to the States: How the State-Specific Interpretation Clarifies BAPCPA's § 522 Ambiguity and Protects State Exemption Laws, 99 Iowa Law Review ____ (forthcoming 2014).

B. TIME-BASED VALUE LIMITATION

11 U.S.C. § 522(p) [*as amended by BAPCPA, P.L. 109-8, § 322(a)*]:

> (p)(1) Except as provided in paragraph (2) of this subsection and sections 544 and 548, as a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of interest that was acquired by the debtor during the 1215-day period preceding the date of the filing of the petition that exceeds in the aggregate [$155,675] in value in--
>
> (A) real or personal property that the debtor or a dependent of the debtor uses as a residence;
>
> (B) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;
>
> (C) a burial plot for the debtor or a dependent of the debtor; or
>
> (D) real or personal property that the debtor or dependent of the debtor claims as a homestead.
>
> (2) (A) The limitation under paragraph (1) shall not apply to an exemption claimed under subsection (b)(3)(A) by a family farmer for the principal residence of such farmer.
>
> (B) For purposes of paragraph (1), any amount of such interest does not include any interest transferred from a debtor's previous principal residence (which was acquired prior to the beginning of such 1215-day period) into the debtor's current principal residence, if the debtor's previous and current residences are located in the same State.

Early on cases divided over this provision's applicability in circumstances where applicable law denied debtors any choice between bankruptcy and nonbankruptcy exemptions. Compare In re McNabb, 326 B.R. 785 (Bankr. D. Ariz. 2005) (Judge Haines) (because it only encompasses homesteads a debtor has claimed as exempt "as a result of electing under subsection (b)(3)(A) to exempt property under State or local law," § 522(p) does not apply in states that do not allow debtors a choice between federal and state exemptions) with In re Kaplan, 331 B.R. 483 (Bankr. S.D. Fla. 2005) (Judge Mark) (construing § 522(p) to apply in opt-out states in light of intent clearly evident from examination of legislative history) and In re Wayrynen, 2005 WL 2756059 (Bankr. S.D. Fla.) (Judge Friedman) (§ 522(p) applicable in opt-out state because debtor "elects" law of such state by choosing to live there, but "carryover" value of homestead previously owned in same state

not limited to one owned immediately prior to present residence). The division subsided rather quickly in favor of § 522(p)'s applicability in opt-out states, a result arguably in line with the eight-justice approach of "text, context, and purpose" apparent in Justice Alito's opinion in Hamilton v. Lanning, 130 S.Ct. 2464 (2010) (adopting "forward-looking approach" to calculation of Chapter 13 debtors' "projected disposable income") and explicitly formulated as such in Justice Kagan's opinion in Ransom v. FIA Card Services, N.A., 131 S.Ct. 716 (2011) (disallowing car-ownership cost deductions by above-median Chapter 13 debtors owning unencumbered motor vehicles).

Circuit and bankruptcy appellate panel interpretations of § 522(p)(1) subsequently have considered the appropriateness of "title" versus "interest" approaches. Under the title approach, the section's value limitation is inapplicable to ownership interests acquired outside the 3 1/3 year period notwithstanding the occurrence of other legally relevant circumstances (e.g., occupation or declaration) within such period. In re Greene, 583 F.3d 614 (9th Cir. 2009) (initial occupation as a residence). See also In re Aroesty, 385 B.R. 1 (1st Cir. BAP 2008) (§ 522(p) encompasses transfer of title from trust within 1,215 day period even though beneficial ownership existed prior to such period); In re Khan, 375 B.R. 5 (1st. Cir. BAP 2007) (suggestion of same outcome where issue not reached because raised for first time on appeal).

In contrast, under the interest approach the value limitation applies where events occurring during the 3 1/3 year period either satisfy a non-ownership element of the exemption (e.g., occupation or declaration) or increase the value of the ownership interest through "active" efforts (e.g, construction of improvements or reduction of mortgage indebtedness). In re Fehmel, 372 Fed. Appx. 507 (5th Cir. 2010) (down payment, improvements, and mortgage payments). Even under the interest approach, however, the value limitation may not apply in situations where the homestead interest was "passively" acquired through inheritance or where the increase in its value was the

"passive" result of market appreciation. In re Rogers, 513 F.3d 212 (5th Cir. 2008).

In accordance with the provisions of § 522(m), the amount specified by § 522(p) may effectively be doubled in the circumstances of joint ownership by married debtors in a joint case. In re Nestlen, 441 B.R. 135 (10th Cir. BAP 2010). Also, § 522(p)'s limitation of the permissible amount of a homestead exemption does not allow post-petition attachment of a judgment lien to value in excess of that amount where such excess value previously had been protected against the attachment of any such lien by the effect of an unlimited state exemption. In re McCombs, 659 F.3d 503 (5th Cir. 2011).

See Gloria J. Liddell and Pearson Liddell, So He Huffed and He Puffed ... But Will the Home(stead) Fall Down?: The Applicability of Section 522(p)(1) of the United States Bankruptcy Code to Varying Interest Accumulations of the Debtor in Homestead Property, 57 Drake Law Review 729 (2009); David M. Holliday, Construction and Application of Bankruptcy Abuse and Consumer Protections Act's (BAPCPA) Limitation of Homestead Exemption, 11 U.S.C.A. § 522(p), 52 A.L.R. Fed. 2d 541 (2011); Timothy R. Tarvin, Bankruptcy, Relocation, and the Debtor's Dilemma: Preserving Your Homestead Exemption Versus Accepting the New Job out of State, 43 Loyola University Chicago Law Journal 141 (2011)

C. DOMESTIC SUPPORT OBLIGATIONS

11 U.S.C. § 522(c) [*as amended by BAPCPA, P.L. 109-8, § 216(1)*]:

> (c) Unless the case is dismissed, property exempted under this section is not liable during or after the case for any debt of the debtor that arose, or that is determined under section 502 of this title as if such debt had arisen, before the commencement of the case, except--
>
> ~~(1) a debt of a kind specified in section 523(a)(1) or 523(a)(5) of this title;~~
>
> (1) a debt of a kind specified in paragraph (1) or (5) of section 523(a) (in which case, notwithstanding any provision of applicable nonbankruptcy law to the contrary, such property shall be liable for a debt of a kind specified in section 523(a)(5));
>
> (2) a debt secured by a lien that is--
>
> (A) (i) not avoided under subsection (f) or (g) of this section or under section 544, 545, 547, 548, 549, or 724(a) of this title; and
>
> (ii) not void under section 506(d) of this title;
>
> (B) a tax lien, notice of which is properly filed; or
>
> (3) a debt of a kind specified in section 523(a)(4) or 523(a)(6) of this title owed by an institution-affiliated party of an insured depository institution to a Federal depository institutions regulatory agency acting in its capacity as conservator, receiver, or liquidating agent for such institution; or
>
> (4) a debt in connection with fraud in the obtaining or providing of any scholarship, grant, loan, tuition, discount, award, or other financial assistance for purposes of financing an education at an institution of higher education (as that term is defined in section 101 of the Higher Education Act of 1965 (20 U.S.C. 1001)).

This change seemingly was intended to reverse the effect of In re Davis, 170 F.3d 475 (5th Cir.) (en banc), cert. denied, 528 U.S. 822 (1999), and early on it was suggested that it might result in denials of claims of exemption and sales by trustees of otherwise exempt property with proceeds applied to the satisfaction of domestic support obligations. Dennis G. Bezanson & Gary B. Rudolph, The "Super-Priority of a "Domestic Support Obligation" ("DSO"): The Trustee as Liquidator of Exempt Property for the Benefit of DSO Claimants, and Other DSO Issues, 22 Journal of National Association of Bankruptcy Trustees 24 (2006). Bankruptcy courts, however, generally have

rejected both possibilities and limited the provision to a right persons owed domestic support obligations may pursue on their own by appropriate proceedings in either nonbankruptcy or bankruptcy courts. See In re Queszada, 368 B.R. 44 (Bankr. S.D. Fla. 2007). See also In re Vandeventer, 368 B.R. 50 (Bankr. C.D. Ill. 2007); In re Ruppell, 368 B.R. 42 (Bankr. D. Ore. 2007); In re Covington, 368 B.R. 38 (Bankr. E.D. Cal. 2006). Accord In re Westmeyer, No. 09-03590 (Bankr. N.D. Iowa 2010) (Judge Kilburg).

D. CLAIM-BASED VALUE LIMITATION

11 U.S.C. § 522(q) [*as amended by BAPCPA, P.L. 109-8, § 322(a)*]:

> (q)(1) As a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) which exceeds in the aggregate [$155,675] if–
>
> (A) the court determines, after notice and a hearing, that the debtor has been convicted of a felony (as defined in section 3156 of title 18), which under the circumstances, demonstrates that the filing of the case was an abuse of the provisions of this title; or
>
> (B) the debtor owes a debt arising from--
>
> (i) any violation of the Federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934), any State securities laws, or any regulation or order issued under Federal securities laws or State securities laws;
>
> (ii) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 1934 or under section 6 of the Securities Act of 1933;
>
> (iii) any civil remedy under section 1964 of title 18; or
>
> (iv) any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years.
>
> (2) Paragraph (1) shall not apply to the extent the amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) is reasonably necessary for the support of the debtor and any dependent of the debtor.

Although this section has been construed to encompass nonwillful instances of criminal negligence, In re Larson, 513 F.3d 325 (1st Cir. 2008), the generally applicable carry-through "immunization" effect of § 522(c) ("property exempted under this section is not liable during or after the case for any debt of the debtor that arose, or that is determined under section 502 of this title as if such debt had arisen, before the commencement of the case ... ") is sufficient to prevent the enforcement of a nondischargeable pre-petition debt against the proceeds of a sale of a residence previously allowed as exempt homestead in an earlier bankruptcy proceeding. In re Cunningham, 513 F.3d 318 (1st Cir. 2008). In rather similar circumstances where the bankruptcy court had

deferred initial consideration of the issue to the district court, however, the same circuit affirmed a determination that the proceeds of a sale of residence exempted as a homestead in a prior bankruptcy proceeding were reachable by the United States through a garnishment issued to enforce a restitution order of more than $300,000 for mail fraud imposed upon the debtor pursuant to the Mandatory Victims Restitution Act (18 U.S.C. § 3613). U.S. v. Hyde, 497 F.3d 103 (1st Cir. 2007).

In some instances, post-petition homestead sales have provided a basis for successful objections to claimed exemptions in sale proceeds where a debtor has not reinvested them in new homestead within a specific period of time prescribed by state law. Compare In re Jacobson, 676 F.3d 1193 (9th Cir. 2012) (exemption lost because of debtor's failure to reinvest proceeds of post-petition judicial sale of homestead into new homestead within specific time period required by state law) with In re Morgan, 481 Fed Appx. 183 (5th Cir. 2012) (same where exemption not claimed until after post-petition consensual sale of homestead and thus only in the proceeds thereof). But see Braunger v. Karrer, 563 N.W.2d 1 (Iowa 1997) (§ 522(c)(1) protects proceeds of homestead from execution upon nondischargeable pre-acquisition debt so long as same held with requisite intent to use in purchase of new homestead).

E. FRAUDULENT TRANSFORMATIONS

11 U.S.C. § 522(o) [*as amended by BAPCPA, P.L. 109-8, § 308*]:

> (o) For purposes of subsection (b)(3)(A), and notwithstanding subsection (a), the value of an interest in--
>
> (1) real or personal property that the debtor or a dependent of the debtor uses as a residence;
>
> (2) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;
>
> (3) a burial plot for the debtor or a dependent of the debtor; or
>
> (4) real or personal property that the debtor or a dependent of the debtor claims as a homestead;
>
> shall be reduced to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10-year period ending on the date of the filing of the petition with the intent to hinder, delay, or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the debtor had held the property so disposed of.

The "title" versus "interest" issue a number of courts have addressed in § 522(p) cases generally has not arisen in § 522(o) cases because the phrasing of the section more clearly encompasses increases in the value of a debtor's interest in a homestead within the specified ten-year period notwithstanding an acquisition of title before then. In re Willcut, 472 B.R. 88 (10th Cir. BAP 2012).

Pre-BAPCPA, the Eighth Circuit significantly limited the ability to rest the denial of a discharge on simple conversions of non-exempt assets into an exempt homestead. In re Johnson, 880 F.2d 78 (8th Cir. 1989). See Appendix B § E. Although such reasoning left open the possibility of avoiding such transfers under state law, In re Sholdan, 217 F.3d 1006 (8th Cir. 2000) (Minnesota law), it also had been viewed as perhaps separately qualifying a creditor's ability to raise objections to homesteads claimed as exempt by debtors in bankruptcy proceedings, In re Rizzuti, No. 97-05572-CH (Bankr. S.D. Iowa 1999) (Judge Hill) (use of proceeds of non-exempt property to reduce encumbrances on existing homesteads).

In In re Addison, 540 F.3d 805 (8th Cir. 2008), a panel of three circuit judges (Smith, Bye, and Colloton) unanimously reversed as clearly erroneous factual findings of fraudulent intent by Bankruptcy Judge Kressel previously affirmed by a unanimous decision of the Eighth Circuit Bankruptcy Appellate Panel (see In re Addison, 368 B.R. 791 (8th Cir. BAP 2007) (Judges Federman, Schermer, and Venters)). Before turning to a comprehensive review of prior cases, the circuit panel dismissed the trustee's assertion that § 522(o) involved any change in relevant substantive standards:

> We reject the Trustee's position that § 522(o) provides a new standard for determining what type of evidence establishes a debtor's "intent to hinder, delay, or defraud" a creditor when the debtor converts nonexempt assets into his homestead. Rather, in our view, § 522(o) merely establishes a 10-year look-back period, from the date of the bankruptcy filing, from which such evidence may be considered.

540 F.3d 805, 812 n.7. In overturning both state and federal grounds advanced in support of an objection to the exemption and an accompanying issue-preclusion based discharge denial resting upon an $11,500 payment in reduction of homestead mortgage, the circuit panel emphasized the exacting nature of both the necessary elements and requisite proof required by circuit case law:

> In the instant case, the bankruptcy court found sufficient evidence to establish that Addison acted with the intent to hinder, delay, and defraud a creditor. However, Addison took less aggressive actions than those present in Sholdan--wherein we concluded that the facts did not support a finding of intent to hinder or delay. Applying our precedent, we conclude that the record here does not support the reduction of Addison's homestead exemption based on an intent to hinder or delay. Id.
>
> ....
>
> The bankruptcy court's underlying factual findings are themselves not clearly erroneous; however, they do not identify any "extrinsic evidence of fraud." In the absence of extrinsic evidence of fraud, we find clear error in the bankruptcy court's ultimate determination of intent to defraud.
>
> ....
>
> Here, only the fact that Addison had been sued or threatened with suit prior to making the mortgage payment was extrinsic to the fact of conversion--all of the other facts cited relate to a debtor's simple conversion of nonexempt property to

> exempt property on the eve of bankruptcy, which we have long held to be permissible. If these facts alone constitute extrinsic evidence of intent to defraud Hanson and Johnson would have reached that same result. See Hanson, 848 F.2d at 867-68 (rejecting argument that extrinsic evidence established debtor's intent to defraud where debtors, after defaulting on bank loans and talking to bankruptcy counsel, converted approximately $20,000 into life insurance policies a couple of weeks prior to filing and prepaid an additional $11,033 on their homestead mortgage two days before filing); Johnson, 880 F.2d at 79 ("agree[ing] that there is no fraud as to [debtor's] homestead exemption," where debtor, in contemplation of filing bankruptcy, talked to bankruptcy attorney and paid off $175,000 in debts against his home after creditors obtained judgments against him). Moreover, the bankruptcy court's finding that Addison converted his nonexempt property to exempt property with the intent "to keep value away from creditors" does not provide extrinsic evidence of fraud as such an intent is not automatically impermissible. Hanson, 848 F.2d at 868; Tveten, 848 F.2d at 873-74.
>
> ....
>
> ... [W]e conclude that the bankruptcy court clearly erred in finding that Addison converted nonexempt property into his homestead with the intent to hinder, delay, or defraud a creditor. On the record before us, there is no extrinsic evidence of intent to hinder, delay, or defraud a creditor sufficient to uphold that finding. The evidence only suggests that Addison was converting nonexempt assets to exempt assets to place some (but not all or substantially all) of those assets beyond the reach of creditors--something our precedent permits.

540 F.3d 805, 813-816 (emphasis in original). The Eighth Circuit Bankruptcy Appellate Panel subsequently followed Addison in affirming a bankruptcy court's rejection of an objection exemption based on $140,000 payment in reduction of homestead mortgage by Arkansas debtors. In re Wilmoth, 397 B.R. 915 (8th Cir. BAP 2008). See also In re Cippola, 476 Fed. Appx. 301 (5th Cir. 2012) (requiring redetermination of § 522(o) limitation of homestead exemption where bankruptcy court's finding of fraud based on inappropriate assumption that attorney debtor was aware of the significant difference between the homestead exemptions of Missouri and Texas).

On a related front, the ability to avoid gratuitous transfers of exempt property not subject to avoidance under state law was expanded by a separate change to lengthen the pre-petition period during which such transfers can be challenged under § 548 from one year to two years. 11 U.S.C. § 548(a)(1), P.L. 109-8, § 1402(1). The efficacy of such transfers still can be separately challenged

under state law, In re Bargfrede, 117 F.3d 1078 (8th Cir. 1997) (per curiam) (gratuitous transfer of proceeds of exempt homestead), and under § 522(g), any consensual transfers avoided as either fraudulent or preferential cannot subsequently be claimed as exempt by the debtor, In re Arzt, 252 B.R. 138 (8th Cir. BAP 2000). But see In re Hill, 562 F.3d 29 (1st Cir. 2009) (§ 522(g) does not countermand debtor's homestead exemption where fraudulently transferred residential property was voluntarily reconveyed to the debtor prior to the petition in response to a creditor's efforts).

See David M. Holliday, Reduction, Under § 522(o) of Bankruptcy Code, 11 U.S.C.A. § 522(o), of Value of Interest in Property Claimed by Debtor as Homestead, 48 A.L.R. Fed. 569 (2010).

Appendix A*

BASIC STATE LAW DIMENSIONS OF IOWA'S "UNLIMITED" HOMESTEAD EXEMPTION

I. INTRODUCTION

A. General Purpose

Iowa's homestead exemption protects a debtor's interest in his or her home by preventing certain debts from being enforced against it. "Homestead exemption is allowed, not for the financial profit, or merely as a margin of financial safety to the debtor. The exemption is for the benefit of the family, to provide wife (or husband), children, and dependents with a home. The exemption is granted, not merely out of grace to the debtor, but as a matter of public policy. ... The law allowing the exemption is to be liberally construed, and is not to be pared away by construction, so as to defeat its beneficent, sociological, and economic purpose." American Savings Bank v. Willenbrock, 209 Iowa 250, 253, 228 N.W. 295, 297 (1929).

B. Historical Background

Iowa first enacted a homestead exemption in 1849. See "An Act to exempt a homestead from forced sale," Ch. 124, 1849 Iowa Acts 152 (up to forty acres used for agricultural purposes, or up to one-fourth of an acre located within a recorded town plat, but value thereof not to exceed $500). Two years later, the 1849 enactment was displaced by the homestead exemption provisions contained in the Code of 1851. See Iowa Code §§ 1245-1266 (1851). While some adjustments have been made over the course of the intervening 162 years, most of the fundamental features of Iowa's homestead exemption have not changed appreciably since 1851. Compare id. with Iowa Code Ch. 561 (2013).

II. THE HOMESTEAD'S BASIC DIMENSIONS

A. Statutory Definition

The basic dimensions of the homestead are defined in Iowa Code §§ 561.1-.3 (2013):

(i) "The homestead must embrace the house used as a home by the owner," § 561.1;

(ii) The homestead "must not embrace more than one dwelling house, or any other buildings except such as are properly appurtenant thereto ... ," § 561.3;

(iii) The homestead "may contain one or more contiguous lots or tracts of land, with the building and other appurtenances thereon, habitually and in good faith used as part of the same homestead," § 561.1; and

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* Based upon Patrick B. Bauer, "Iowa's Homestead Exemption" (Nineteenth Annual Advanced Bankruptcy Procedures Seminar, Cedar Rapids, Iowa 1989).

(iv) "If [it is] within a city plat, [the homestead] must not exceed one-half acre in extent, otherwise it must not contain in the aggregate more than forty acres ... ," § 561.2.

B. Use of a House as a Home

A homestead does not exist until an owner has occupied a house as his or her home, see, e.g., Christy v. Dyer, 14 Iowa 438, 440 (1863) ("[T]he homestead character does not attach to property until it is actually occupied and used ... as a home. ... A mere intention to occupy, though subsequently carried out, does not make the premises the hom[e]stead until there is actual residence."), and it subsequently will cease to exist upon the owner's removal from the house with no intention of returning, see, e.g., Crail v. Jones, 206 Iowa 761, 764, 221 N.W. 467, 469 (1928) ("[T]he actual removal from a homestead with no intention to return to it as a home is an equivalent to a surrender of all claim of homestead to the premises ... ."). A homestead will continue to exist following an owner's cessation of actual residence in the house, however, if the owner retains an intention to return at some later date. See, e.g., In re Estate of McClain, 220 Iowa 638, 644, 262 N.W. 666, 669 (1935) ("[O]nce the homestead character has attached, the owner may remove therefrom and the homestead character is preserved as long as he has an intention to return. ... [I]ntention to occupy in the future, while insufficient to establish a homestead originally, is sufficient to continue a homestead previously established.")

C. One Dwelling House and Other Buildings Properly Appurtenant Thereto

In some early cases where the owner's home occupied only part of a building, remaining parts of the building were deemed not to be within the homestead exemption. See, e.g., Rhodes, Pegram & Co. v. McCormack, 4 Iowa 368 (1857). Such segmentation of a single structure, however, entailed various difficulties, and Olsen v. Lohman, 234 Iowa 580, 13 N.W.2d 332 (1944) suggests that the use of part of a building for other purposes normally will not place that part beyond the homestead exemption. Cf. In re Marriage of McMorrow, 342 N.W.2d 73, 75 n. 2 (Iowa 1983) (quoting law review article statement that "[t]he ingenuity of the court ... should be equal to the challenge of a debtor who seeks to dwell in the marble halls of an office building ... .").

In addition to one dwelling house, the homestead may include both (i) "other buildings ... properly appurtenant thereto" and (ii) "a shop or other building ... actually used and occupied by the owner in the prosecution of the owner's ordinary business, and not exceeding three hundred dollars in value," Iowa Code § 561.3 (2013). While a separate duplex was not deemed appurtenant to the cottage used as a home by the owner in Kurz v. Brusch, 13 Iowa 371 (1862), a barn, a corncrib and machine shed, a feed house, and three farrowing houses were deemed appurtenant to a home on a rural forty acre homestead in In re Estate of Sueppel, 255 Iowa 974, 124 N.W.2d 154 (1963).

D. Land on Which the Home is Located

The interests in land which can be claimed as a homestead are not confined to fee simple estates. See, e.g., Stinson v. Richardson, 44 Iowa 373 (1876) (interest of vendee under contract for deed); Livasy v. State Bank of Redfield, 185 Iowa 442, 170 N.W. 756 (1919) (tenant in common); Lutz v. Ristine & Ruml, 136 Iowa 684, 112 N.W. 818 (1907) (life estate); Pelan v. DeBevard, 13

Iowa 53 (1862) (leasehold). See generally Rutledge v. Wright, 186 Iowa 777, 783, 171 N.W. 28, 30 (1919):

> It is not essential to the acquisition of a homestead ... that the claimant have a perfect or complete legal title. It is essential that he have a sufficient title to justify his occupancy. Occupancy under such a title will justify a claim of homestead right ... .

E. Platting and Value

So long as it includes a house used as a home, an urban homestead of up to one-half acre or a rural homestead of up to forty acres may be platted out of any part of a larger tract of land owned by the debtor. See, e.g., Berner v. Dellinger, 206 Iowa 1382, 1383, 222 N.W. 370, 371 (1928) ("Until [the homestead] is actually platted, the right to the selection [of any part of a larger tract] as ... the homestead inheres in every square foot of the larger area."). The existence of a homestead, however, is not dependent upon a platting thereof. See, e.g., Mitchell v. West, 93 N.W.2d 380 (Iowa 1903) (unplatted homestead not subject to judgment lien); Green v. Farrar, 53 Iowa 426, 428, 5 N.W. 557, 558-59 (1880) (unplatted homestead not subject to execution).

III. THE EXEMPTION AND THE EXCEPTION FOR PRE-ACQUITION DEBTS

A The Basic Exemption

Iowa Code § 561.16 (2013) provides as follows:

> The homestead of every person is exempt from judicial sale where there is no special declaration of statute to the contrary. Persons who reside together as a single household unit are entitled to claim in the aggregate only one homestead to be exempt from judicial sale. A single person may claim only one homestead to be exempt from judicial sale. For purposes of this section, "*household unit*" means all persons of whatever ages, whether or not related, who habitually reside together in the same household as a group.

Until1981, the exemption was limited to the homestead "of every family" (emphasis added). That year an enactment which precluded recourse to the federal bankruptcy exemptions established by 11 U.S.C. § 522(d) and modified the personal property exemptions contained in Iowa Code Ch. 627 also changed § 561.16 to provide that "[t]he homestead of every person is exempt from judicial sale, where there is no special declaration of statute to the contrary ... ." (emphasis added). See Ch. 182, § 1, 1981 Iowa Acts 582, 582-83.

A judgment entered on a debt which is not enforceable against a judgment debtor's homestead does not create any lien upon such homestead, and it thus can be conveyed to another free and clear of such judgments. See, e.g., Lamb v. Shays, 14 Iowa 567 (1863). Furthermore, "a conveyance of a homestead is not a fraud upon creditors as it is not subject to their claims," James v. James, 252 Iowa 326, 334, 105 N.W.2d 498, 502-03 (1960). The proceeds of a voluntary sale of a homestead, however, are subject to execution unless they are held with an intent to reinvest them in a new homestead. See Huskins, Bryson & Co. v. Hanlon, 72 Iowa 37, 33 N.W. 352 (1887).

B. Existence and Operation of the Exception for Pre-Acquisition Debts

"The homestead may be sold to satisfy debts ... contracted prior to its acquisition, but then only to satisfy a deficiency remaining after exhausting the other property of the debtor, liable to execution." Iowa Code § 561.21(1) (2013). A debtor who does not direct the sheriff to such other property, however, cannot later object to a sale of the homestead on the ground that such other property was not exhausted. Foley v. Cooper, 43 Iowa 376 (1876). Similarly, where a judgment upon a pre-acquisition debt could not have been satisfied by a sale of the nonhomestead portion of a tract of land, a sheriff's deed was sustained despite the debtor's contention that the nonhomestead portion had not been sold before the sale of the homestead. Smith v. De Kock, 81 Iowa 535, 46 N.W. 1056 (1890).

An ordinary debt is "contracted" when it is incurred, and a judgment upon a debt incurred before a debtor's acquisition of a homestead is enforceable against such homestead even though such judgment is not obtained until after the homestead was acquired. See, e.g., Bills v. Mason, 42 Iowa 329 (1876). In Sloan v. Waugh, 18 Iowa 224 (1865), a debt barred by the statute of limitations before the debtor acquired a homestead was held enforceable against the homestead when such debt had been revived after the homestead's acquisition by a new promise to pay.

Because a homestead does not exist until an owner has occupied a house as his or her home, see supra § II.B., debts incurred after an owner purchases land but before the owner actually occupies such land as his or her home are "debts contracted prior to [the homestead's] acquisition." See, e.g., Elston v. Robinson, 23 Iowa 208 (1867); Hale v. Heaslip, 16 Iowa 451 (1864). Similarly, a debt incurred during the debtor's occupancy of land can be enforced against an interest in the land which the debtor did not obtain until after such debt was incurred. See, e.g., Wertz v. Merritt, 74 Iowa 683, 39 N.W. 103 (1888) (land inherited from father subject to debts of son incurred during son's prior occupancy of land as father's tenant).

By virtue of either or both of the foregoing principles, a debtor's homestead is subject to debts incurred for its purchase. See, e.g., Christy v. Dyer, 14 Iowa 438, 441 (1862) ("Plaintiff was the vendor and defendant the vendee of the premises. ... Under such circumstances, it is, in our opinion, contrary to the policy of the statute, to say that this debt was so contracted after the purchase of the homestead as to render the property exempt." (emphasis in original)). But cf. In re Krantz, 97 B.R. 514, 531 (Bky. N.D. Iowa 1989) (right to invoke pre-acquisition debt exception waived by mortgagee's prior release of homestead from mortgage incurred to purchase farm and construct residence). The fact that the proceeds of a debt incurred after the acquisition of a homestead are applied towards payment of either the homestead's purchase price or some other pre-acquisition obligation, however, may be insufficient to permit such debt to be enforced against the homestead. See, e.g., Johnson County Savings Bank v. Carroll, 109 Iowa 564, 80 N.W. 683 (1899) (purchase price); Brauch v. Freking, 219 Iowa 556, 258 N.W. 892 (1935) (pre-acquisition obligation).

Pre-acquisition contractual undertakings involving contingencies not materializing until after a homestead is acquired may not constitute pre-acquisition debts. See Hunt, Hill & Betts v. Moore, 219 Iowa 451, 258 N.W. 114 (1935) (lawyer's contingent fee under 1916 contract not enforceable against homestead acquired in 1920 where claim not recovered until 1924 nor satisfied until 1928);

Anderson v. Kyle, 126 Iowa 666, 102 N.W. 527 (1905) (initial grantee's claim against grantor for breach of warranty of title made in 1890 not enforceable against homestead acquired by grantor in 1895 where initial grantee not held liable to subsequent grantee for title defect until 1896). But see In re Galvin's Estate, 238 Iowa 894, 29 N.W.2d 230 (1947) (widow's claim under 1918 antenuptial agreement allowing her $10,000 if she were to survive her husband enforceable against homestead acquired in 1919); Smith v. Andrew, 209 Iowa 99, 222 N.W. 587 (1929) (receiver of insolvent bank appointed on December 25, 1927 allowed to enforce claim for double liability against stockholder's homestead where bank stock received on March 17, 1926 and homestead occupied on June 20, 1927); Merchants National Bank v. Eyre, 107 Iowa 13, 77 N.W. 498 (1898) (daughter's liability as surety upon note of father not due until after his death held a debt contracted prior to daughter's inheritance of homestead from father).

Where a defendant committed a fraud before he acquired a homestead, a post-acquisition tort judgment against him for resulting damages was deemed entered upon a pre-acquisition "debt" because the plaintiff could have waived the tort and sued in assumpsit. See Warner v. Cammack, 37 Iowa 642, 644 (1873):

> Wherever a party has derived a pecuniary advantage from a wrong done by him, and it is competent for the person suing thereon to waive the tort and maintain his action upon the promise implied by the law, there the obligation to pay is a debt, and this, regardless of the form of the action in which that obligation is sought to be enforced.

In other circumstances, however, torts may not constitute "debts" until such time as the tortfeasor's liability therefore has been reduced to judgment. See id.:

> The converse of the proposition just stated must also be true, that wherever a wrong is done resulting in no pecuniary advantage to the wrong-doer, and where the action must be in tort, and sound only in damages, there the obligation to pay is not a debt until ascertained by judgment.

Because a parent's obligation to support a child is considered to have arisen upon the child's birth, a child support judgment can be enforced against a homestead acquired between the birth of the child and the entry of such judgment. In re Marriage of Armetta, 417 N.W.2d 223 (Iowa Ct. App. 1987).

Where a debtor's interest in the homestead is encumbered, the debtor can satisfy part or all of the encumbrance without subjecting the homestead to debts incurred between the debtor's acquisition of such encumbered interest and the debtor's satisfaction of such encumbrance. See, e.g., American Savings Bank of Marengo v. Willenbrock, 209 Iowa 250, 259, 228 N.W. 295, 300 (1929):

> [T]he homesteader, after his right of exemption accrues, may pay for the property, may pay off liens upon it; and the fact that he does so does not bring forward the date from which his right of exemption to the tract as an entirety accrues, nor would such fact confer on the creditor the right to impose upon the homestead liability to the amount of such expenditures made after the incurring of the debt to him.

Moreover, where debts have been incurred after a homestead has been acquired, improvements to the homestead subsequently made by the debtor cannot be subject to the payment of such debts. See, e.g., Ebersole v. Moot, 112 Iowa 596, 84 N.W. 696 (1900).

Where the debtor owns one tract of land which is the debtor's homestead and a second tract of land which is not the debtor's homestead, the debtor may change his homestead from the first tract to the second and the second tract will be exempt (i) as against debts to which the first tract was exempt (ii) to the extent of the value of the first tract. See Iowa Code § 561.20 (2013); Berner v. Dellinger, 206 Iowa 1382, 222 N.W. 370 (1928). Such a change, however, "shall not prejudice ... liens ... created previously thereto," Iowa Code § 561.7 (2013). See Elston & Green v. Robinson, 21 Iowa 531 (1866); see also Chariton Feed and Grain, Inc. v. Kinser, 794 F.2d 1329 (8th Cir. 1986). Moreover, if the first tract was mortgaged before the change, any deficiency which subsequently might ensue upon a foreclosure of the mortgage will be enforceable against the second tract.

The debtor also can sell his present homestead and acquire a new homestead with the resulting proceeds, and the new homestead will be exempt (i) as against debts to which the old homestead was exempt (ii) to the extent of the value of the old homestead. See Iowa Code § 561.20 (2013). The purchaser of the old homestead takes it free of any judgments against the debtor upon debts which were not enforceable against the old homestead, see supra § III.A., and so long as the debtor holds the proceeds with an intention to reinvest them in a new homestead, the proceeds of the sale of the old homestead are exempt for a reasonable period of time thereafter, see, e.g., Richards v. Orr, 118 Iowa 724, 92 N.W. 655 (1902).

Any surplus of proceeds from the sale of an old homestead remaining after the purchase of a new homestead, however, will be subject to the claims of the owner's creditors. See Webster, Button & Call v. Saunders, 8 Iowa 579 (1858); cf. Millsap v. Faulkes, 236 Iowa 848, 20 N.W.2d 40 (1945).

For purposes of determining the extent to which the new homestead is exempt, the value of the old homestead is ascertained without regard to the existence of any encumbrances thereon. See American Savings Bank of Marengo v. Willenbrock, 209 Iowa 250, 228 N.W. 295 (1929). If the value of the new homestead exceeds the value of the old homestead, the new homestead is to that extent subject to debts incurred between the dates the old and new homesteads were acquired. Id. Interim creditors, however, may be prevented from proceeding against the new homestead if the excess value is fully encumbered by senior liens. Id.; cf., e.g., Laidley v. Aikin, 80 Iowa 112, 45 N.W. 384 (1890) (purchase money mortgages entitled to priority over liens of earlier judgments).

Appendix B*

CHALLENGES IN TRANSLATING IOWA'S "BILATERAL" PRE-ACQUISTION DEBT EXCEPTION INTO THE "MULTILATERAL" CIRCUMSTANCES OF BANKRUPTCY PROCEEDINGS

A. Introduction

The use of state exemption law in bankruptcy proceedings is complicated by the fact that state exemptions generally have been formulated and applied in settings which in some important respects are quite different from the circumstances normally present in bankruptcy. Outside of bankruptcy, exemptions usually are invoked in an essentially bilateral context where the issue is whether a specific creditor can reach a particular asset, and where any unsatisfied portion of the creditor's claim will remain enforceable against other assets the debtor subsequently might acquire. In contrast, the essentially multilateral nature of bankruptcy normally involves a focus on the collective interests of groups of creditors, and the bankruptcy discharge usually insulates not only subsequently acquired assets but also the proceeds of any later disposition of a presently owned asset that pre-petition creditors currently cannot reach in its present form. See Countryman, For a New Exemption Policy in Bankruptcy, 14 Rutgers L. Rev. 678, 681 (1960); Comment, Bankruptcy Exemptions: Critique and Suggestions, 68 Yale L.J. 1459, 1508 (1959).

These differences have led some to embrace the conclusion that bankruptcy might function best with a nationally uniform "pure value" exemption (e.g., assets of any kind having a total value of no more than a specified dollar amount). See Countryman, supra, at 746-47; Comment, supra, at 1507-09. Others, however, have argued that state exemption laws represent deliberate balancings of the conflicting needs of credit promotion and debtor protection, and that such policy determinations should be respected by bankruptcy law. See Kennedy, Limitation of Exemptions in Bankruptcy, 45 Iowa L. Rev. 445, 449-51 (1960). A further argument for bankruptcy's incorporation of state exemption law is the need to avoid the incentives for voluntary debtor petitions or involuntary creditor petitions which might result from material disparities between the exemptions available within and outside of bankruptcy. Id. at 452.

The push and pull between these concerns can be seen in the statutory development of bankruptcy exemptions. The Bankruptcy Acts of 1800 and 1841 relied exclusively on a set of uniform federal exemptions, and the Bankruptcy Act of 1867 used a combination of uniform federal and incorporated state exemptions. See ch. 19, § 5, 2 Stat. 19, 23 (1800); ch. 9, § 3, 5 Stat. 440, 442 (1841); ch. 176, § 14, 14 Stat. 517, 522-23 (1867). The Bankruptcy Act of 1898, however, did not include any uniform federal exemptions and deferred fully to the exemptions established by state law. See ch. 541, § 6, 30 Stat. 544, 548 (1898). Most recently, the evolution of the current Bankruptcy Code included, in chronological order, (i) an initial bankruptcy commission proposal involving exclusive federal exemptions, (ii) a House bill affording debtors a choice between federal and state exemptions, (iii) a Senate bill restricting debtors to state exemptions, and (iv) the finally

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* Based upon Patrick B. Bauer, "Iowa's Homestead Exemption: Three Decades of Bankruptcy Court Application and Development" (Fortieth Annual Barbara A. Everly Advanced Procedures Bankruptcy Seminar, Cedar Rapids, Iowa 2010).

enacted compromise effort allowing debtors to choose between federal and state exemptions unless and until the choice has been eliminated by state legislative action. See H.R. Doc. No. 93-137, 93rd Cong., 1st Sess., pt. 2 (1973) (§ 4-503); H.R. 8200, 95th Cong., 1st Sess. (1977) (§ 522(b)); S. 2266, 95th Cong., 2d Sess. (1978) (§ 522(b)); 11 U.S.C. § 522(b). The fact that the vast majority of states have exercised the "opt-out" option is suggestive of the powerful nature of the pressures in favor of bankruptcy's utilization of state law exemptions.

B. Shifting Effects of the Exception for Pre-Acquisition Debts

Although Iowa seemingly adheres to "the general rule that the conversion of nonexempt property into exempt property does not, of itself, invest the creditor with any right to follow the exempt property," American Savings Bank v. Willenbrock, 209 Iowa 250, 259, 228 N.W. 295, 299-300 (1929), outside of bankruptcy the consequences for homesteads are quite limited because pre-acquisition debts are enforceable against the homestead after the exhaustion of other nonexempt property, see supra Outline § III.B. The implementation of the pre-acquisition debt exception in bankruptcy, however, has proven over the years to be a matter of continuing substantive and procedural difficulty.

The initial incorporation of state exemption laws in the Bankruptcy Act of 1867 presented problems when it became apparent that it included the relatively absolute prohibition of retroactive effectiveness which state exemption laws then were held to under the Contract Clause. Accordingly, in 1873 Congress amended the Act to provide that exemptions were to "be valid against debts contracted before the adoption and passage of [state exemption laws], as well as those contracted after the same, and against liens by judgment or decree of any state court." When this amendment subsequently was invoked in a bankruptcy proceeding involving an Iowa homestead, it was held to insulate the homestead from the claims of creditors holding pre-acquisition debts. See Darling v. Berry, 13 F. 659 (C.C.D. Iowa 1882).

Shortly after the enactment of the Bankruptcy Act of 1898, the United States Supreme Court set forth a procedure for honoring the rights of creditors holding claims which were enforceable under state law against otherwise exempt property. Because "generally" exempt property did not pass into the bankruptcy estate, the Court held that bankruptcy courts lacked jurisdiction to apply exempt property towards the claim of a creditor holding a waiver of exemptions which was valid and enforceable under state law. In recognition of the "equity" of the creditor who had obtained the waiver, however, the Supreme Court indicated that the discharge of the creditor's debt should be withheld temporarily to allow the creditor an opportunity to reach the otherwise exempt property in a state court proceeding. See Lockwood v. Exchange Bank, 190 U.S. 294 (1903).

The Lockwood approach was utilized in a number of Iowa bankruptcy proceedings involving homesteads and pre-acquisition debts. See, e.g., Ingram v. Wilson, 125 F. 913 (8th Cir. 1903); Duffy v. Tegeler, 19 F.2d 305 (8th Cir. 1927). If a pre-acquisition debt had been reduced to judgment before bankruptcy, the resulting judgment lien could be enforced against a homestead even after a discharge had been granted. Cf. Schwanz v. Farmers' Co-op. Co., 204 Iowa 1273, 214 N.W. 491 (1927). Once a discharge had been granted, however, a pre-acquisition debt which had not been reduced to judgment would no longer be enforceable against the homestead. See Drees v. Armstong, 180 Iowa 29, 161 N.W. 40 (1917).

In 1932, however, the Iowa Supreme Court ruled that a pre-acquisition creditor could not obtain a lien upon a debtor's homestead through equitable proceedings prosecuted during a stay of the debtor's discharge because the creditor's claim against the homestead was deemed to be inconsistent with the bankruptcy court's determination that the property was exempt. See Bracewell v. Hughes, 214 Iowa 241, 242 N.W. 66 (1932). Although the breadth of Bracewell's holding was somewhat unclear, it subsequently was determined to have freed Iowa homesteads from the claims of pre-acquisition creditors where bankruptcy proceedings had been commenced before such claims had been reduced to judgment. See Harris v. Hoffman, 379 F.2d 413 (8th Cir. 1967).

The enactment of the Bankruptcy Code presented a new set of procedural and substantive issues about the integration of Iowa's homestead exemption in bankruptcy proceedings. By including exempt property in the estate, § 541(a)(1) eliminated the jurisdictional limitation which had barred bankruptcy courts from directly adjudicating exceptions to exemptions and had channeled the determination of all such issues into the state courts. The incorporation of state exemption law in § 522(b)(2)(A) obviously left open the possibility that exceptions to state exemptions might have to be recognized and reflected in bankruptcy proceedings, but the waivers which seemingly provided the bulk of the exceptions handled under the Lockwood procedure were expressly invalidated by § 522(e). The possibility of further qualifications of exceptions to state exemptions were presented by § 522(c)'s specification of the post-bankruptcy status of property exempted from the estate and by both the judicial lien and security interest avoidance provisions of § 522(f). The import of the various provisions of § 522, however, is complicated by the fact that subsections (c), (e), and (f) remained largely the same as the content of subsection (b) shifted from exclusively federal exemptions through a choice between federal and state exemptions and a scheme of exclusively state exemptions to the enacted version involving a choice between federal and state exemptions which can be eliminated by state legislation restricting debtors to the exemptions established by state law.

Initially, the bankruptcy judges in both Iowa districts concluded that the freedom from unsecured pre-acquisition debts produced by Harris v. Hoffman could be augmented by using § 522(f)(1) to avoid the liens of any judgments obtained upon pre-acquisition debts prior to the commencement of the bankruptcy proceeding. See In re Mosher, No. 86-491-C (Bky. S.D. Iowa 1986) (Judge Stageman), remanded for determination of existence and extent of other nonexempt assets, 79 B.R. 840 (S.D. Iowa 1987), settled by parties before further proceedings (see 84 B.R. 576 n.2); In re Ziesman, No. 83-03017 (Bky. N.D. Iowa 1985) (Judge Thinnes). Subsequently, however, the case law in both districts swung back to a position in which the effect of the homestead as against pre-acquisition debts is significantlly less than that available under Harris v. Hoffman.

The shift occurred first in the Northern District, with District Judge David R. Hansen's rulings that a homestead could not be claimed as exempt as against a pre-acquisition debt in In re Wooten, 82 B.R. 84 (N.D. Iowa 1986) and In re Ellingson, 82 B.R. 88 (N.D. Iowa 1986). Although the cases involved pre-acquisition debts which had not yet become liens on the homestead, Judge Hansen expressly indicated that § 522(f)(1) could not be used to avoid any lien which might attach to a homestead upon the entry of a judgment upon pre-acquisition debt either before or after the filing of bankruptcy.

In the Southern District of Iowa, Bankruptcy Judge Lee M. Jackwig initially also used a case

involving a pre-acquisition debt which was not yet a lien upon the homestead to hold that a homestead could not be claimed as exempt as against such a debt and that any lien which might attach to a homestead upon the entry of a judgment upon a pre-acquisition debt either before or after the filing of bankruptcy could not be avoided under § 522(f)(1). See In re Nehring, 84 B.R. 571 (Bky. S.D. Iowa 1988). In that same case, however, Judge Jackwig went on to indicate that "[a]s a general rule and absent blatant abuse of the statutory framework, this court will not grant relief from the stay to an antecedent claimholder for the purpose of reducing the debt to judgment." Id., at 578.

Subsequently, in In re Schuldt, 91 B.R. 501 (Bky. S.D. Iowa 1988), Judge Jackwig sustained a trustee's objection to a homestead exemption on behalf of all holders of pre-acquisition debts, and stated that the homestead would be "subject to liquidation and distribution in accordance with sections 704(1) and 726 ... to the extent the antecedent debts are not satisfied after the other property of the debtors subject to execution is exhausted," id., at 503. Presumably, the suggested procedure consists of a two-step liquidation process in which nonexempt property other than the homestead first is applied towards satisfaction of both post-acquisition and pre-acquisition debts, followed by an application of the homestead towards satisfaction of the remaining balance of all pre-acquisition debts. But see England v. Sanderson, 236 F.2d 641 (9th Cir. 1956) (through an apparent combination of Constance v. Harvey and Moore v. Bay, trustee allowed (i) to obtain portion of homestead not exempt as to creditors holding claims pre-dating non-retroactive increase in dollar limitation seemingly without regard to the amount of the claims actually held by such creditors, and (ii) to distribute such portion among all creditors without regard to whether their claims arose before or after the date of the exemption increase).

Objections to homestead exemptions are limited in amount to the pre-acquisition debts remaining after the exhaustion of all other property of the debt subject to execution. In re Thompson, No. 95-32455XF (Bankr. N.D. Iowa 1996) (Judge Edmonds). This functional deference to state law's prescription of the exception's extent, however, does not carry over to distributions of resulting recoveries which are made in accordance with generally applicable provisions which do not include any distinctions based on whether particular debts were contracted before or after the debtor's acquisition of a homestead. In re Nehl, No. 97-60192-W (Bankr. N.D. Iowa 1997) (Judge Kilburg); In re Wulff, No. 95-41790XM (Bankr. N.D. Iowa 1998) (Judge Edmonds).

A renewed challenge to the effects in bankruptcy proceedings of the pre-acquisition debt exception was initiated shortly after the First Circuit's decision in In re Weinstein, 164 F.3d 677 (1st Cir. 1999) (Massachusetts exception for pre-acquisition debts preempted by contrary implications of federal bankruptcy law). The rejection of this challenge in In re Norkus, 256 B.R. 298 (Bankr. S.D. Iowa 2000) (Judge Jackwig), however, left in place the case law consensus which generally has prevailed since Wooten and Ellingson were decided by Judge Hansen in 1986.

Issues about the operation of the pre-acquisition debt exception have been presented both in cases involving the existence of liens of debts reduced to judgment (a circumstance which could readily arise in the absence of a bankruptcy proceeding) and in cases involving the ability of such debts to eventually become liens where they have not yet been reduced to judgment (which in the absence of a bankruptcy proceeding conceivably might only arise in the context of a fraudulent conveyance). Issues addressed included such things as the time when a homestead is deemed to

have been first occupied, In re Brown, No. 97-01623S (Bankr. N.D. Iowa 1997) (Judge Edmonds); In re O'Brien, No. L88-01436W (N.D. Iowa 1989) (Judge Melloy), the effect of subsequent increases in the quantity or quality of an existing interest, In re Burmester, No. 85-02282M (Bankr. N.D. Iowa 1988) (Judge Edmonds), In re Takes, No. 04-04020 (Bankr. N.D. Iowa 2005) (Judge Kilburg), rev'd 334 B.R. 642 (N.D. Iowa 2005) (Judge Reade), aff'd 478 F.3d 902 (8th Cir. 2007), the fact and timing of alleged abandonments, In re Estes, No. 87-02006W (Bankr. N.D. Iowa 1988) (Judge Edmonds); In re Conley, No. 87-02006W (Bankr. N.D. Iowa 1996) (Judge Kilburg); In re Goodvin, No. 87-02006W (Bankr. N.D. Iowa 2000) (Judge Edmonds), In re Devine, 2005 WL 1926038 (Bankr. N.D. Iowa 2005) (Judge Edmonds); In re Westmeyer, No. 09-03590 (Bankr. N.D. Iowa 2010) (Judge Kilburg), and the effects of transfers to and from or ownership by "personal" corporations, In re Henss, No. 93-2401-CH (Bankr. S.D. Iowa 1995) (Judge Hill), aff'd (S.D. Iowa 1996) (Judge Wolle), aff'd 1997 WL 249958 (8th Cir. 1997) (per curiam); In re Jennings, No. 98-2902-WH (Bankr. S.D. Iowa 1999) (Judge Hill).

C. Pre-acquisition Debts in Circumstances Involving "Carryover" Exemptions

The operation of the pre-acquisition debt exception is complicated by the provision which limits its application in situations the debts were contracted subsequent to the acquisition of an earlier homestead unless (and then only to the extent that) the later homestead is of greater value:

> Where there has been a change in the limits of the homestead, or a new homestead has been acquired with the proceeds of the old, the new homestead, to the extent in value of the old, is exempt from execution in all cases where the old or former one would have been.

Iowa Code § 561.20 (2013).

A carryover exemption has been recognized in circumstances where the debtor moved between two previously owned properties. In re Hogrefe, No. 92-41695XM (Bankr. N.D. Iowa 1993) (Judge Edmonds). Such a shift may not be allowed, however, where it would adversely affect an existing lien. Chariton Feed & Grain, Inc. v. Kinser, 794 F.2d 1329 (8th Cir. 1986); In re Springer, No. 92-1239-C H (Bankr. S.D. Iowa 1993) (Judge Hill).

Carryover exemptions have been rejected in cases where the properties were separate from each other and not merely components of a larger single parcel, In re Allen, 301 B.R. 55 (Bankr. S.D. Iowa 2003) (Judge Jackwig), or where the debtor established an interim residence at property owned by someone else, In re O'Brien, No. L88-01436W (Bankr. N.D. Iowa 1989) (Judge Melloy); In re Conley, No. 87-02006W (Bankr. N.D. Iowa 1996) (Judge Kilburg); In re Tibbe, No. 99-02072S (Bankr. N.D. Iowa 2000) (Judge Edmonds). Courts have reached differing conclusions about whether a carryover exemption can be obtained in circumstances where the prior homestead was located in another state. Compare In re Welch, No. A87-02433S (Bankr. N.D. Iowa 1988) (Judge Melloy) (yes) with In re Carlson, No. 98-0369S (Bankr. N.D. Iowa 1999) (Judge Melloy) (no) and In re Bausback, No. 02-0825-WH (Bankr. S.D. Iowa 2003) (Judge Hill) (same).

The exemption's extension to a later homestead necessarily includes an essentially derivative protection of the proceeds of a sale of the earlier homestead, In re Tigges, No. L88-00894D (Bankr.

N.D. Iowa 1988) (Judge Melloy); In re Scheer, No. 96-50422XS (Bankr. N.D. Iowa 1996) (Judge Edmonds), but this protection is lost if there has been an abandonment of the earlier homestead prior to its sale, In re Husted, No. 87-01413-S (Bankr. N.D. Iowa 1988) (Judge Edmonds), or in the absence or upon cessation of an intent to apply the proceeds towards the acquisition of a new homestead, In re Ersepke, 1993 WL 767975 (Bankr. N.D. Iowa 1993) (Judge Edmonds).

One series of three cases involves the distinction between the continuation of an existing homestead and the acquisition of a new one received successive attention in a series of three opinions. In re Takes, No. 04-04020 (Bankr. N.D. Iowa 2005) (Judge Kilburg), rev'd 334 B.R. 642 (N.D. Iowa 2005) (Judge Reade), aff'd 478 F.3d 902 (8th Cir. 2007). Debtors' 1994 entry into a life-long lease for a unit in a complex of "independent living" town homes involved a substantial "entrance fee" of $110,000 seemingly paid in kind through personal endorsement of a mortgage and various services in conjunction with the development of the project. Five years later the debtors personally guaranteed another note and five years after that purchased the town home for an amount that included both the entrance fee's accumulated value ($125,773) and an additional amount ($51,527) derived from other sources. The circumstances of a life-long lease, the "equity" equivalence of the sizable entrance fee (refundable upon releasing to the extent of the entrance fee payable by a successor tenant), and the "maturation" effect entailed in the conversion of a life-long lease into a fee interest led Judge Kilburg to view the circumstances as a continuation of a single homestead that had been enhanced in value through satisfaction of the remaining portion of the purchase price with funds obtained elsewhere. In contrast, Judges Reade and Loken viewed the debtors' shift over to a fee ownership interest as constituting the acquisition of a new homestead, but then recognized a carryover exemption in the new fee homestead based on the value (in the form of the appreciated amount of the entrance fee) of the debtor's prior homestead interest in the leasehold.

A substantial line of cases holds that the value of the old homestead may be carried over to a new homestead even though the acquisition of the new homestead has not involved the use of any proceeds of the old homestead. In re Husted, No. 87-01413-S (Bankr. N.D. Iowa 1988) (Judge Edmonds); In re Estes, (Bankr. N.D. Iowa 1988) (Judge Edmonds); In re Whyle, (Bankr. N.D. Iowa 1996) (Judge Edmonds); In re Litwiller, 2002 WL 1446780 (Bankr. N.D. Iowa 2002) (Judge Edmonds); In re White, 293 B.R. 1 (Bankr. N.D. Iowa 2003) (Judge Kilburg); In re Meyer, 392 B.R. 416 (Bankr. N.D. Iowa 2007) (Judge Kilburg). In a case involving other complicating circumstances, however, debtors' carryover exemption was limited to the amount of proceeds actually realized from their disposition of the prior homestead, In re Hayes, 1996 WL 1038496 (Bankr. N.D. Iowa 1996) (Judge Kilburg), and the principle has since been applied in a later case in which similarly complicating circumstances were not apparent, In re Russow, 357 B.R. 133 (Bankr. N.D. Iowa 2007) (Judge Kilburg).

Whether the new homestead will be subject to a debt that could have been enforced against the old homestead may depend on the particular exception that would have permitted such enforcement. Thus, a new homestead may be liable for debts contracted prior to the acquisition of the old homestead, In re Versluis, No. 94-61420KW (Bankr. N.D. Iowa 1995) (Judge Kilburg), or those incurred for improvements to the old homestead, In re Streeper, 158 B.R. 7832 (Bankr. N.D. Iowa 1993) (Judge Edmonds). Opposing results have been reached, however, concerning the new homestead's liability for the unpaid balance of a debt enforceable against the old homestead only

because of the existence of a mortgage. Compare In re Erickson, No. X87-02428S (Bankr. N.D. Iowa 1988) (Judge Edmonds) (liable) with In re White, 293 B.R. 1 (Bankr. N.D. Iowa 2003) (Judge Kilburg) (not liable).

D. The Effects of Homestead "Indivisibility"

The effects of pre-acquisition debts and carryover exemptions in bankruptcy proceedings involved interactions between longstanding state law elements and changed elements of bankruptcy law caused by differences between the 1898 Act and the 1979 Code. The different resulting effects of pre-acquisition debts, however, were in turn significantly qualified by the advent of new state law principles about the "indivisible" nature of the homestead exemption in circumstances involving property owned jointly or commonly by married persons.

The Iowa Supreme Court first recognized the concept in a case involving a waiver, Merchants Mutual Bonding Co. v. Underberg, 291 N.W.2d 19 (Iowa 1980), but shortly thereafter noted its implications in the circumstances of a mechanics lien, Francksen v. Miller, 297 N.W.2d 375 (Iowa 1980). The concept subsequently was applied in a situation involving a mortgage, Decorah State Bank v. Zidlicky, 426 N.W.2d 388 (Iowa 1988) and thereafter with significantly widened effect in a case involving a pre-existing family support obligation, Baratta v. Polk County Health Services, 588 N.W.2d 107 (Iowa 1999).

After initial application in a joint case involving a jointly owned home and pre-acquisition debts owed only by one spouse, In re Butler, No. 86-2252-C (Bankr. S.D. Iowa 1987) (Judge Jackwig),[1] the concept was extended to circumstances where the home was jointly owned but a filing by only one spouse involved no evidence of any debts owed by the other spouse, In re Tyree, 116 B.R. 682 (Bankr. S.D. Iowa 1990) (Judge Hill). Later cases involved debts incurred for homestead improvements, In re Streeper, 158 B.R. 7832 (Bankr. N.D. Iowa 1993) (Judge Edmonds), and circumstances where each spouse individually owed pre-acquisition debts without any of such debts being owed jointly, In re Breiner, No. 96-50355XS (Bankr. N.D. Iowa 1996) (Judge Edmonds).

Some of the outer boundaries of the principle of indivisibility have been explored in a case where the homestead was owned solely by one spouse and a lien had (or had not) attached to it because a judgment upon the pre-acquisition debts had (or had not) been entered against such spouse before the date of the marriage. In re Knode, No. 97-01814-C (Bankr. N.D. Iowa 1997) (Judge Kilburg) (stated date of judgment before date of marriage), aff'd Appeal No. 98-0012 (N.D. Iowa 1998) (Judge Melloy) (stated date of judgment after date of marriage). The principle has been recognized in another case, however, where joint ownership of the homestead involved a gift of a half interest from one spouse to the other and a marriage which did not occur until after the homestead had been acquired. In re Opel, No. 98-01862-C, (Bankr. N.D. Iowa 1998) (Judge Kilburg). Although the latter case included a suggestion that it might have come out differently if the owners of the homestead had not subsequently married, indivisibility has been applied to prevent the attachment of a judgment as a lien to the husband's interest where his own individual exemption

1. Accord In re McGrath, No. X91-01410F (Bankr. N.D. Iowa 1993) (Judge Edmonds); In re Bausback, No. 02-0825-WH (Bankr. S.D. Iowa 2003) (Judge Hill).

had been terminated by his removal from the house upon separation because the wife's continued occupancy of the house resulted in an ongoing continuation of her individual exemption, In re Powers, 286 B.R. 726 (Bankr. N.D. Iowa 2002) (Judge Kilburg).[2]

E. Lien Avoidance

Efforts to avoid judicial liens on homesteads have necessarily always presented issues about the existence and effects of exceptions to the exemption. An initial pair of cases essentially made lien avoidance pretty much a null set by determining that there was nothing to avoid where the underlying debt was not within any exception because a judgment upon such a debt did not result in the attachment of any lien, In re Keane, 7 B.R. 844 (Bankr. N.D. Iowa 1980) (Judge Thinnes),[3] and conversely, that where the exception for dissolution decrees was sufficient to allow a lien to attach to the homestead, the lien could not be avoided because it caused no impairment of the exemption, In re Adams, 29 B.R. 452 (Bankr. N.D. Iowa 1982) (Judge Thinnes).[4]

Lien avoidance was available during a brief period when homestead exemptions were deemed to be impaired by the liens of judgments entered upon pre-acquisition debts, see supra § B., but generally ended with the turn to the view that the exemption was subject to objection to the extent of such debts, id. Efforts to avoid liens within exceptions to the exemption were renewed following the U.S. Supreme Court's decision in Owen v. Owen, 500 U.S. 291 (1991), but such efforts were unsuccessful. In re Reinders, 138 B.R. 937 (Bankr. N.D. Iowa 1992) (Judge Edmonds); In re Meseraull, No. 94-11048KC (Bankr. N.D. Iowa 1994) (Judge Kilburg), aff'd, (N.D. Iowa 1995) (Judge McManus), aff'd 1996 WL 185736 (8th Cir. 1996) (per curiam).[5]

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2. See also In re Attrill, No. X88-01008 (N.D. Iowa 1989) (Judge Edmonds) (judgments did not attach as liens upon debtor's abandonment of jointly owned house because of homestead exemption of ex-wife who remained in possession of the house); cf. In re Rizzuti, No. 97-05572-CH (Bankr. S.D. Iowa 1999) (Judge Hill) (debtor's ability to claim carryover exemption not defeated by interim transfer of ownership of former homestead to non-spouse co-owner required by lender as condition of favorable refinancing); In re Reyerson, 2006 WL 1452805 (Bankr. N.D. Iowa 2006) (Judge Edmonds) (indivisibility separate ground for non-attachment of any of a judgment against husband entered after entry of divorce decree transferring husband's interest to wife notwithstanding husband's failure to execute independently required quitclaim deed).

3. Accord In re Winkowitsch, No. 93-607121LW (Bankr. N.D. Iowa 1993) (Judge Kilburg); In re McCammant, No. 91-3633-C H (Bankr. S.D. Iowa 1994) (Judge Hill); In re Shanahan, No. 94-11127KC (Bankr. S.D. Iowa 1995) (Judge Hill).

4. Accord In re Parman, No. 94-10592KC (Bankr. N.D. Iowa 1994) (Judge Kilburg); In re Mease, No. 97-10048-C (Bankr. N.D. Iowa 1999) (Judge Kilburg). But see In re Steigerwald, No. 02-00061-H (Bankr. S.D. Iowa 2003) (Judge Hill) (although they "do not attach to exempt homestead property[,] ... judgment liens do provide a cloud on the title of real property ... and create headaches for title examiners and parties attempting to sell their homes. Accordingly, the court will grant [the debtor's] motion to avoid [the creditor's] lien."). Northern District Local Rule 4003-2 helpfully addresses this circumstance with the suggestion that "[a] debtor moving to avoid a judicial lien against his or her homestead may join with the motion an alternative request for a determination that the creditor's lien has not attached to the homestead."

5. But cf. In re Macke, 136 B.R. 209 (Bankr. S.D. Iowa 1992) (Judge Hill) (accepting Owen contention about impairment, but denying lien avoidance based on Farrey analysis that lien did not fix upon an interest of the debtor).

Numerous possible permutations of debts, judgments, and varying real estate interests can create difficulties of clear or clouded title that may not always be fully resolved by the cumulative effects of 11 U.S.C. § 524(a)(1) ("A discharge in a case under this title ...voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged under section 727, 944, 1141, 1228, or 1328 of this title ... .") and Iowa Code § 624.23(3) ("Judgment liens ... shall not attach to subsequently acquired real estate owned by the defendant if the personal liability of the defendant on the judgment has been discharged under the bankruptcy laws of the United States."). As a possible alternative to some appropriate bankruptcy court proceeding, consideration should be given to the possible sufficiency of the procedure available under the provisions of Iowa Code § 624.23(2)(b) (2013):

> A claim of lien against real estate claimed as a homestead is barred unless execution is levied within thirty days of the time the defendant, the defendant's agent, or a person with an interest in the real estate has served written demand on the owner of the judgment. The demand shall state that the lien and all benefits derived from the lien as to the real estate alleged to be or to have been a homestead shall be forfeited unless the owner of the judgment levies execution against that real estate within thirty days from the date of service of the demand. The demand shall contain an affidavit setting forth facts indicating why the judgment is not believed to be a lien against the real estate. A warranty of title by a former occupying homeowner in a conveyance for value constitutes a claim of exemption against all judgments against the current homeowner or the current homeowner's spouse not specifically exempted in the conveyance. Written demand shall be served in any manner authorized for service of original notice under the Iowa rules of civil procedure... . A copy of the written demand and proof of service of the written demand shall be filed in the court file of the case in which the judgment giving rise to the alleged lien was entered.

F. The Effects of Satisfying Encumbrances or Improving the Homestead

The current treatment of the pre-acquisition debt exception in bankruptcy proceedings involving Iowa homesteads arguably does not directly implicate the issues raised in situations where a debtor devotes otherwise nonexempt funds to the satisfaction of encumbrances or the construction of physical improvements to the homestead. See supra § B. Prior to the enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, however, such conduct might be challenged (i) as a fraudulent conveyance which can be avoided under 11 U.S.C. § 548, (ii) as a basis for the denial of a discharge under 11 U.S.C. § 727, or (iii) as grounds for qualifying or denying the exemption itself pursuant to (a) incorporated state law or (b) limiting principles derived from the general structure and content of the Bankruptcy Code.

A noteworthy aspect of the judicial treatment of cases involving challenges to the conversion of nonexempt assets into exempt assets is the frustrating absence of meaningful theoretical principles which might demark some bright line between permissible and impermissible conduct. This circumstance certainly is not new, compare, e.g., Forsberg v. Security State Bank, 15 F. 499 (8th Cir.) (reversing denial of discharge based on farmer's trading of nonexempt cattle for exempt hogs) with Kangas v. Robie, 264 F.2d 92 (8th Cir. 1920) (affirming denial of exemption where merchant channeled $13,000 into homestead), and has changed little with the passage of time, compare, e.g.,

Hanson v. First National Bank in Brookings, 848 F.2d 866 (8th Cir. 1988) (overruling objection to exemptions under South Dakota law where debtor had used proceeds of sales of nonexempt property to purchase $19,955 in exempt life insurance policies and to prepay $11,033 on homestead mortgage) with Norwest Bank Nebraska, N.A. v. Tveten, 848 F.2d 871 (8th Cir. 1988) (affirming denial of Chapter 7 discharge to debtor physician who sold almost all nonexempt property in seventeen separate transactions and used proceeds to purchase approximately $700,000 in exempt life insurance policies and annuities) [but cf. In re Tveten, 97 B.R. 541 (Bky. D. Minn. 1989) (same debtor entitled to Chapter 11 discharge)], In re Trost, No. L88-00703W (Bky. N.D. Iowa 1989) (Judge Melloy) (allowing exemption for $25,000 of life insurance purchased by widow while indebted to bank for $38,000 in real estate investment loans incurred by deceased husband), and In re Smeby, No. X88-00159M (Bky. N.D. Iowa 1989) (Judge Edmonds) (allowing exemption for almost $130,000 of life insurance where debtors retained unencumbered nonexempt property worth approximately $125,000) with In re Krantz, 97 B.R. 514 (Bky. N.D. Iowa 1989) (denying exemption for more than $525,000 of life insurance purchased by farmer while indebted to federal land bank for $1.5 million farm purchase loan).

The distinctions being drawn in these cases perhaps have been explained most colorfully in In re Zouhar, 10 B.R. 154, 157 (Bky. D.N.M. 1981) (while indebted to wife under property settlement, debtor anesthesiologist pledged stock in professional corporation as security for loan used to purchase exempt annuity which eventually would repay loan in full):

> The difference, which seems initially to be one merely of degree, at some point as yet unspecified becomes a difference in kind which requires a different result. This same principle was succinctly stated by Judge Logan in Dolese v. United States of America, 605 F.2d 1146, 1154 (10th Cir. 1979), "There is a principle of too much; phrased colloquially, when a pig becomes a hog, it gets slaughtered." That principle fully applies here. While a bankrupt is entitled to adjust his affairs so that some planning of one's exemptions under bankruptcy is permitted, a wholesale sheltering of assets which would otherwise go to creditors is not permissible.

A somewhat more jurisprudential observation about the comparable uncertainties existing in the cases involving the priority of future advances in mortgage settings suggests that greater clarity may not be possible or desirable:

> [T]he conceptually nonsensical distinction between "obligatory" and "voluntary" has had the result (which is not in the least nonsensical) of preserving (or creating) a wide area of judicial discretion. There are few, if any, future advance clauses which an astute judge cannot, at will, classify on one side or the other of the line between obligatory and voluntary. When he has picked his label, he has also picked his priority rule. The distinction amounts to an absence of rule; the judges are invited to pick and choose, case by case, ad hoc or ad hominem. This is a recurrent phenomenon in a common law system when the arguments for or against a given position balance each other exactly. There is much to be said for giving the mortgagee an absolute priority. There is much to be said for allowing other creditors a chance at the assets (or the debtor's equity in the assets). There is much to be said for allowing the mortgagor freedom to choose new sources of financing and for

> allowing new lenders to come in with secure liens. Only a very wise or a very foolish man would be willing to state, categorically, where truth lies and to propose a rule for application in all possible situations. There is, then, much to be said for having no rule at all, or only a make-believe rule, and for letting the judges decide: judges are not necessarily wiser than other people, but they are paid to decide things.

Grant Gilmore, Security Interests in Personal Property § 35.4 (1965).

In such circumstances, it hardly is possible to offer any certainties about the likely outcome of cases in which nonexempt funds have been used to satisfying encumbrances upon or to make improvements to an Iowa homestead. One important circumstance, of course, is the absence or presence of culpable conduct separate and apart from the enhancement of the homestead. See, e.g., McCormick v. Security State Bank, 822 F.2d 806 (8th Cir. 1987) (discharge denied where debtor who was both airline pilot and lawyer lied to creditor about inability to pay debt while engaged in transfer of approximately $60,000 into exempt homestead); In re Rodemeyer, 99 B.R. 416 (Bky. N.D. Iowa 1989) (denying life insurance exemption to extent policy purchased with funds derived from debtor's conversion of creditor's collateral). Another presumably is the amount of funds involved in the enhancement. See, e.g., In re Ellingson, 63 B.R. 271 (Bky. N.D. Iowa 1986) (Judge Melloy) (use of $51,899.13 to pay down balance owing on contract for deed for debtors' homestead not a fraudulent conveyance under 11 U.S.C. § 727(a)(2)). In many cases, the debtor's acquisition of an interest in the homestead before incurring the debts subject to the exemption may provide some meaningful assurance that the homestead was acquired at least in part because of its functional usefulness as a dwelling, and not solely as a means for sheltering assets from creditors. Cf., e.g., In re Eden, 96 B.R. 895 (Bky. N.D. Iowa 1988) (wearing apparel exemption encompasses jewelry actually worn and used by debtor, but not jewelry held primarily for investment or resale purposes).

In the Eighth Circuit, however, a discharge cannot properly be denied based solely on the debtor's channelling of nonexempt assets into an exempt homestead where such conduct is permitted by state law. See In re Johnson, 880 F.2d 78, 82-84 (8th Cir. 1989):

> We read Tveten and Hanson to reaffirm the rule that conduct sufficient to defeat discharge requires indicia of fraud beyond mere use of the exemptions. Under Tveten, Hanson, and the cases they discuss, extrinsic evidence can be composed of: further conduct intentionally designed to materially mislead or deceive creditors about the debtor's position; conveyances for less than fair value; or, the continued retention, benefit or use of property allegedly conveyed together with evidence that the conveyance was for inadequate consideration. In addition, Tveten establishes that where an exemption, other than a homestead exemption, is not limited in amount, the amount of property converted into exempt forms and the form taken may be considered in determining whether fraudulent intent exists.
>
> ... Each state's selection and structuring of their exemptions reflects judgments about particular state interests. Variations in the law are sanctioned by Congress' choice to allow the states to fix their own exemptions. In deciding whether to invade a prerogative bestowed on the states by Congress, we must first consider the importance of the claimed exemption in furthering state objectives.

> ....
>
> ... We have recognized that no exemption is more central to the legitimate aims of state lawmakers than a homestead exemption. ...
>
> ....
>
> We hold that Tveten does not apply to homestead exemptions absent traditional extrinsic evidence of fraud unrelated to the amount of money involved. In addition, we remind the lower courts that there is nothing fraudulent per se about making even significant use of other legal exemptions. Ultimately, fixed dollar limits on the use of exemptions must be set by legislatures. Tveten and Hanson sanction an exceptional use of judicial discretion. In light of the dangers that judges will inadvertently fix inconsistent or arbitrary limits on the statutory exemptions, we must err in favor of the debtor. The power sanctioned in Tveten should be reserved for exceptional cases and had no application to homestead exemptions.

(Emphasis added.)

CURRENT CASES & UPDATES ON MISSOURI EXEMPTIONS

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- ***Earned Income Tax Credit is now exempt (a change in law)*** – In re Corbett, 2013 WL 1344717 (Bankr. W.D.Mo. April 2, 2013)

- ***Personal Injury Claims*** – In re Abdul-Rahim, 477 B.R. 747 (8th Cir. BAP 2012) (follows Benn)

- ***Inherited IRAs – the Circuits are split***
  - In re Clark, __ F.3d __, 2013 WL 1729600 (7th Cir. April 23, 2013) – not exempt
  - In re Chilton, 674 F.3d 486 (5th Cir. 2012) – exempt
  - In re Nessa, 426 B.R. 312 (8th Cir. BAP 2010) – exempt

- ***Possible Missouri Statutory Amendments***
  - Personal Injury Claims (to make them exempt)
  - Homestead (to increase the amount from $15,000)

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Slip Copy, 2013 WL 1344717 (Bkrtcy.W.D.Mo.), 2013-1 USTC P 50,265
(Cite as: 2013 WL 1344717 (Bkrtcy.W.D.Mo.))

United States Bankruptcy Court,
W.D. Missouri.
In re Paula R. CORBETT, Debtor.

No. 13–60042.
April 2, 2013.

ORDER OVERRULING TRUSTEE'S OBJECTION TO EXEMPTIONS

ARTHUR B. FEDERMAN, Chief Bankruptcy Judge.

***1** The Chapter 7 Trustee objects to Debtor Paula R. Corbett's claimed exemption in the earned income tax credit portion of her 2012 income tax refund pursuant to § 513.430.1(10)(a) of the Missouri Statutes.[FN1] For the reasons that follow, the Objection is OVERRULED.

FN1. The Debtor initially claimed the earned income tax credit fully exempt in an "unknown" amount under § 513.430.1(10)(a), (b), and (c). Debtor's counsel clarified at hearing that she is only claiming the exemption under paragraph (a)—paragraphs (b) and (c) are not applicable. The Debtor also clarified in a post-hearing brief that the amount of the credit is now known: she is claiming only the amount of her federal tax refund that is traceable to the earned income tax credit, which is $622.

In the Eighth Circuit, income tax refunds are property of a debtor's estate when a bankruptcy case is filed.[FN2] In addition, the bankruptcy courts in this district have consistently held that the portion of a tax refund attributable to the earned income tax credit (EITC) is also property of the estate.[FN3] The question presented here is whether debtors in Missouri may claim an exemption in the EITC portion of a tax refund, particularly in light of a recent amendment to Missouri's exemption statute relating to public assistance benefits.[FN4]

FN2. 11 U.S.C. § 541(a); *In re Benn,* 491 F.3d 811, 813 (8th Cir.2007) ("A debtor's anticipated refund, to the extent it is attributable to events occurring prior to the filing of the petition for bankruptcy, is part of the estate.").

FN3. *See In re Goertz,* 202 B.R. 614, 616 (Bankr.W.D.Mo.1996) (holding that EITC payments are property of the estate); *In re Demars,* 279 B.R. 548, 550 (Bankr.W.D.Mo.2002) (same).

FN4. Mo.Rev.Stat. § 513.430.1(10)(a).

Missouri has opted out of the federal exemption scheme in 11 U.S.C. § 522,[FN5] "thereby restricting Missouri residents to the exemptions available under Missouri law and under federal statutes other than 11 U.S.C. § 522(d)."[FN6] The Eighth Circuit has long held that income tax refunds are not exempt as "earnings" under Missouri's garnishment statutes,[FN7] and in *In re Benn,* the Eighth Circuit held that, even though income tax refunds are "not subject to attachment or execution" in the hands of the government, that alone does not make them exempt property.[FN8] Rather, the only way a Missouri debtor in bankruptcy can claim an exemption in income tax refunds is to fit it within a specifically enumerated exemption statute, such as the wildcard[FN9] or head of family exemption.[FN10]

FN5. Mo.Rev.Stat. § 513.427.

FN6. *In re Benn,* 491 F.3d at 813 (*quoting Wallerstedt v. Sosne (In re Wallerstedt),* 930 F.2d 630, 631 n. 1 (8th Cir.1991); *see also Garner v. Strauss (In re Garner),* 952 F.2d 232, 234 (8th Cir.1991)).

FN7. *In re Wallerstedt,* 930 F.2d 630 (8th Cir.1991).

FN8. *In re Benn,* 491 F.3d at 814–16.

FN9. Mo.Rev.Stat. § 513.430.1(3) (exempting "[a]ny other property of any kind, not to exceed in value six hundred dollars in the aggregate).

FN10. Mo.Rev.Stat. § 513.440 ("Each head of a family may select and hold, exempt from execution, any other property, real, personal or mixed, or debts and wages, not exceeding in value the amount of one thousand two hundred fifty dollars plus three hundred fifty dollars for each of such person's unmarried dependent children under the age of twenty-one years....").

As it relates to the EITC portion of a refund, in *In re Goertz*[FN11] and *In re Demars,*[FN12] the bankruptcy courts in this district held that EITC payments were not exempt under § 513.430.1(10)(a) of the Missouri Statutes, which, at the time those decisions were issued, permitted debtors to exempt payments received in the form of a "local public assistance benefit." Under the language of the statute as it existed then, the courts in this district held that the EITC portion of a federal income tax refund is not a form of *local* public assistance, inasmuch as the EITC was not a creation of state or local government. Therefore, they could not be claimed exempt in a bankruptcy case under the local public assistance benefit exemption.

FN11. *In re Goertz,* 202 B.R. at 617.

FN12. *In re Demars,* 279 B.R. at 551.

Two events have occurred since the decisions in *Goertz* and *Demars* were handed down. Most recently, the Missouri legislature amended § 513.430.1(10)(a), effective August 28, 2012, to remove the word "local": The statute now allows debtors to claim an exemption in such person's right to receive "a public assistance benefit." Since *Goertz* and *Demars* held that the exemption as previously worded did not include federal EITC payments because the exemption was restricted to "local" benefits, the Debtor here asserts that the Missouri legislature intended, when it removed the "local" restriction, to have federal and other non-local public assistance benefits included within the exemption.

***2** The other event which occurred after *Goertz* and *Demars* was that the Eighth Circuit issued the *Benn* decision, where it held that " '[e]xemption' is a term of art in bankruptcy, and ... while exemption may mean different things in different contexts, in the context of 11 U.S.C. § 522, it refers to laws enacted by the legislative branch which explicitly identify property that judgment-debtors can keep away from creditors for reason of public policy."[FN13] The Trustee asserts here that, the amendment to § 513.430.1(10)(a) notwithstanding, that statute still does not specifically refer to EITCs. And, he says, nothing in the Internal Revenue Code refers to EITCs as "public assistance benefits." Therefore, following *Benn,* the Trustee asserts that EITCs are not, in and of themselves, exempt under any Missouri statute.

FN13. 491 F.3d 811, 814 (8th Cir.2007) (citation and internal modifications omitted).

I do not read *Benn* to mean that every conceivable item of particular property, or variation thereof, must be specifically identified by name in order to fit within one of the exemption statutes. Naturally, several of the exemptions refer to broad categories of items because it would be impractical, if not impossible, to list everything that could conceivably fit into the category. By way of example, the statute generally exempts "tools of the trade,"[FN14] without providing a list, or even a definition of that phrase. Courts have therefore had to employ tests to determine what items of specific property might constitute an exempt tool of the trade.[FN15] The same is true for "household goods," "motor vehicles," "veterans' benefits," and "disability, illness or unemployment benefits," as additional examples.

FN14. Mo.Rev.Stat. § 513.430.1(4).

FN15. *See, e.g., In re Gray,* 303 B.R. 632 (Bankr.W.D.Mo.2003) (holding that horses used to give riding lessons were tools of the trade because they were reasonably necessary to the debtor's business); *In re Baker,* 139 B.R. 468 (Bankr.W.D.Mo.1992) (holding that a van used by the debtors in the business of transporting passengers was a tool of the trade as being reasonably necessary for the business); *In re Eakes,* 69 B.R. 497 (Bankr.W.D .Mo.1987) (holding that cattle were not tools of the trade because the statute separately enumerated "animals" and "tools of the trade" and because "tool" commonly refers to inanimate objects).

As with those categories of property, the Missouri legislature could not have reasonably been expected to list every conceivable form of public assistance benefit that might be exempt. Indeed, as the Debtor points out, such an interpretation would require the Missouri legislature to amend the statute every time a new benefit were enacted by a governmental body. Such an interpretation is unrealistic. Rather, I read *Benn* to hold that, unless a Missouri statute expressly declares property as "exempt," a term of art in bankruptcy, debtors in bankruptcy cases are not permitted to claim exemptions in that property, even if such property might be immune from attachment or execution outside of bankruptcy. It does not require that a particular item be specifically listed, so long as it reasonably fits within a listed category of "exempt" items.

The question, therefore, is whether EITCs can reasonably be held to fit within the general category of "public assistance benefits." The EITC was enacted as a mechanism for providing relief to low income families hurt by rising food and energy prices and to provide an incentive to work instead of relying on other forms of government assistance.[FN16] As the court in *Goertz* said, "[a]n earned income credit, created by 26 U.S.C. § 32 (1994), is a refundable tax credit provided for low income workers who have dependent children and who maintain a household."[FN17] "Courts have characterized the earned income credit as 'an item of social welfare legislation' effectuated through income tax laws."[FN18] *Goertz* and *Demars* made pretty clear that EITCs would qualify as exempt public assistance benefits under the prior version of § 513.430.1(10)(a), but for the "local" restriction, and several other courts from across the country have found the EITC to be a public assistance benefit.[FN19] I agree.

FN16. *Sorenson v. Secretary of Treasury,* 475 U.S. 851, 106 S.Ct. 1600, 89 L.Ed.2d 855 (1986); *see also In re Demars,* 279 B.R. at 550–51 ("Congress made [the EITC] program available to low income earners for the following three reasons: (1) to reduce the disincentive to work caused by the imposition of Social Security taxes on earned income; (2) to stimulate the economy by placing funds in the hands of consumers who would spend them immediately; and (3) to provide relief for families impacted by rising food and energy prices.") (citation omitted).

FN17. 202 B.R. at 616 (citation omitted).

FN18. *Id.* (citations omitted).

FN19. *See, e.g., In re James,* 406 F.3d 1340 (11th Cir.2005) (holding that because the EITC was enacted "to provide relief for low-income families," it fit within the "ordinary meaning" and dictionary term of "public assistance" as "government aid to needy persons"); *Flanery v. Mathison,* 289 B.R. 624, 628–29 (W.D .Ky.2003) (EITC payments exempt under Kentucky statute exempting public-assistance benefits); *In re Tomczyk,* 295 B.R. 894, 897 (Bankr.D.Minn.2003) (same, under Minnesota exemption); *In re Longstreet,* 246 B.R. 611, 617 (Bankr.S.D.Iowa 2000)

(same, under Iowa exemption); *In re Brockhouse,* 220 B.R. 623, 625 (Bankr.C.D.Ill.1998) (same, under Illinois exemption); *In re Fish,* 224 B.R. 82 (Bankr.S.D.Ill.1998) (same); *In re Jones,* 107 B.R. 751(Bankr.D.Idaho 1989) (same, under Idaho exemption).

***3** Based on the foregoing, the restriction to local benefits having been removed, public assistance benefits coming from the federal government, including EITC payments, are now included in § 513.430.1(10)(a). As a result, the Debtor properly claimed her EITC exempt under § 513.430.1(10)(a).[FN20]

FN20. Prior to the 2012 amendment to § 513.430.1(10)(a) making EITCs exempt, I previously held, in an unpublished decision, that, as property of the estate, EITCs should be prorated as of the date of the bankruptcy petition, in the same way garden-variety income tax refunds are prorated in this district. *In re Noel Keith Harris and DeeDee Kye Harris,* Case No. 10–61610, *Order Granting Trustee's Motion to Compel Turnover* (Doc. # 52) (Bankr.W.D. Mo. June 2, 2011). Because I hold that they are now fully exempt, I need not decide whether they should be prorated.

ACCORDINGLY, the Trustee's Objection to Exemptions is OVERRULED. The Debtor will be permitted to claim the portion of her federal income tax refund which is traceable to the earned income tax credit as fully exempt under § 513.430.1(10)(a).

IT IS SO ORDERED.

Bkrtcy.W.D.Mo.,2013.
In re Corbett
Slip Copy, 2013 WL 1344717 (Bkrtcy.W.D.Mo.), 2013-1 USTC P 50,265

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2012, order denying the debtor's motion for new trial are both affirmed.

In re Abdullah I. ABDUL–RAHIM, formerly known as Larry Hickson, and Stephanie A. Abdul–Rahim, Debtors.

Abdullah I. Abdul–Rahim and Stephanie A. Abdul–Rahim, Debtors–Appellants,

v.

John V. LaBarge, Jr., Trustee–Appellee.

BAP No. 12–6037.

United States Bankruptcy Appellate Panel of the Eighth Circuit.

Submitted: Sept. 12, 2012.

Decided: Sept. 21, 2012.

Background: Order was entered by the United States Bankruptcy Court for the Eastern District of Missouri, 472 B.R. 904, denying debtors an exemption for their interest in unliquidated personal injury claim. Debtors appealed.

Holdings: The Bankruptcy Appellate Panel, Kressel, Chief Judge, held that:

(1) Missouri's opt-out statute, which bars debtors who file for bankruptcy in Missouri from claiming federal bankruptcy exemptions, but allows them to exempt, from bankruptcy estate, property exempt from attachment and execution under other Missouri statutes, did not create any new exemptions under Missouri law, and

(2) debtors could not rely on Missouri common law to exempt their interest in unliquidated personal injury claim.

Affirmed.

1. Bankruptcy ⚿2764

Missouri's opt-out statute, which bars debtors who file for bankruptcy in Missouri from claiming federal bankruptcy exemptions, but allows them to exempt, from bankruptcy estate, property exempt from attachment and execution under other Missouri statutes, did not create any new exemptions under Missouri law, and could not be relied upon by Chapter 13 debtors as basis to exempt their unliquidated personal injury claim. V.A.M.S. § 513.427.

2. Bankruptcy ⚿2764

Missouri's opt-out statute, in permitting debtors who file for bankruptcy in Missouri to exempt, as alternative to exemptions provided by Congress in the Bankruptcy Code, property exempt from attachment and execution under other Missouri statutes, permitted debtors to exempt only property identified as exempt from attachment and execution in some other legislation enacted by Missouri legislature, and not under Missouri common law, such that creditors' inability to attach inchoate asset like debtors' unliquidated personal injury claim under Missouri common law did not provide basis for debtors to successfully claim their interest in this personal injury cause of action as exempt from administration by trustee. V.A.M.S. § 513.427.

Andrew Ryan Magdy, St. Louis, MO, for Appellant.

Joseph Michael Wilson, St. Louis, MO, for Appellee.

Before KRESSEL, Chief Judge, FEDERMAN and NAIL, Bankruptcy Judges.

KRESSEL, Chief Judge.

The bankruptcy court [1] denied the debt-

1. The Honorable Kathy A. Surratt–States, United States Bankruptcy Judge for the East-

ors a claimed exemption in an unliquidated personal injury claim. On appeal, the debtors argue that the Eighth Circuit precedent relied upon by the bankruptcy court is erroneous and we should disregard it and reverse. We decline the debtors' invitation and affirm the bankruptcy court.

BACKGROUND

The background of this case is simple. The debtors filed a chapter 13 petition on August 3, 2011, and in an amended schedule C, claimed a personal injury claim as exempt under Mo.Rev.Stat. § 513.427 and Missouri common law. The trustee objected to the exemption and the bankruptcy court, relying on the Eighth Circuit's opinion in *Benn v. Cole (In re Benn),* 491 F.3d 811 (8th Cir.2007), disallowed the exemption.

DISCUSSION

[1] The disposition of this appeal is equally simple. The debtors rely first on Mo. Stat. § 513.427. However, the Eighth Circuit explicitly held that that section was not an exemption statute. *Benn, supra.* It said "section 513.427 opts out of the federal exemptions listed in 11 U.S.C. § 522(d), but announces no new exemptions under Missouri law. The statute simply provides that where another Missouri *statute* specifies that certain property is exempt from attachment and execution, then a debtor may exempt that property from the bankruptcy estate." *Benn,* 491 F.3d at 814.

[2] The debtors alternatively argue that they can exempt their personal injury claim under Missouri "common law." However, the Eighth Circuit in *Benn* also held that "in the context of 11 U.S.C. § 522, [exemption] refers to laws enacted by the legislative branch which explicitly identify property that judgment debtors can keep away from creditors for reasons of public policy." *Benn,* 491 F.3d at 814 (citations omitted). By definition, common law does not meet the Eighth Circuit's requirement that an exemption be created by the legislative branch. At bottom, the debtors are confusing the concept of a bankruptcy exemption with a creditor's inability to attach certain assets because of their inchoate nature.[2]

The debtors lastly have a litany of arguments based on Supreme Court opinions from *Erie Railroad Co. v. Tompkins,* 304 U.S. 64, 58 S.Ct. 817, 82 L.Ed. 1188 (1938) through *Butner v. United States,* 440 U.S. 48, 99 S.Ct. 914, 59 L.Ed.2d 136 (1979) and the Constitution's bankruptcy clause's uniformity requirement. However, what the debtors fail to appreciate is that in *Benn,* the Eighth Circuit was interpreting federal law, specifically what Congress meant when it used the word "exemption" throughout § 522.

CONCLUSION

Because the debtors' arguments raise issues already decided by the Eighth Circuit, we are compelled by principles of *stare decisis* to affirm the bankruptcy court's disallowance of the debtors' exemption.

ern District of Missouri.

2. In fact, while the debtors refer us to Missouri cases that they argue make personal injury claims exempt, they do not use the word exempt, but only hold that such claims are not attachable because of their contingent or unliquidated nature.

Westlaw.

--- F.3d ----, 2013 WL 1729600 (C.A.7 (Wis.))
(Cite as: 2013 WL 1729600 (C.A.7 (Wis.)))

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Only the Westlaw citation is currently available.

United States Court of Appeals,
Seventh Circuit.
In the Matter of Brandon C. CLARK and Heidi Heffron–Clark, Debtors–Appellees.
Appeal of William J. Rameker, Trustee.

Nos. 12–1241, 12–1255.
Argued Sept. 6, 2012.
Decided April 23, 2013.

Background: Chapter 7 trustee and judgment creditor objected to exemption claimed by debtors in debtor-wife's inherited individual retirement account (IRA). The United States Bankruptcy Court for the Western District of Wisconsin, 450 B.R. 858, upheld objection. The United States District Court for the Western District of Wisconsin, Barbara B. Crabb, J., 466 B.R. 135, reversed, and trustee and judgment creditor appealed.

Holding: The Court of Appeals, Easterbrook, Chief Judge, held that funds in non-spousal inherited individual retirement account (IRA) were not "retirement funds" within meaning of Bankruptcy Code provision setting forth exemptions for tax-exempt retirement funds.

Reversed.

West Headnotes

Bankruptcy 51 ⚿0

51 Bankruptcy

Funds in non-spousal inherited individual retirement account (IRA) were not "retirement funds" exempt from creditors' claims in bankruptcy. 11 U.S.C.A. § 522(b)(3)(C), (d)(12).

Appeals from the United States District Court for the Western District of Wisconsin. No. 11–cv–482–bbc—Barbara B. Crabb, Judge.Denis P. Bartell, Attorney, Sean Michael Murphy, Attorney, DeWitt, Ross & Stevens, S.C., Madison, WI, for Debtors–Appellees.

Stephen L. Morgan, Attorney, Murphy & Desmond, S.C., Madison, WI, for Trustee.

Before EASTERBROOK, Chief Judge, and FLAUM and WILLIAMS, Circuit Judges.

EASTERBROOK, Chief Judge.

***1** Congress has decided that funds set aside for retirement need not be used to pay pre-retirement debts. This policy is implemented through 11 U.S.C. § 522(b)(3)(C) and (d)(12), which exempt retirement funds from creditors' claims in bankruptcy. This appeal presents the question whether a non-spousal inherited individual retirement account ("inherited IRA" for short) is exempt.

Section 522(b)(3)(C) and (d)(12) are identical. Each exempts from creditors' claims any "retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under sections 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986." An individual retirement account by which a person provides for his or her own retirement meets this requirement. If a married holder of an IRA dies, the decedent's spouse inherits the account and can keep it separate or roll it over into his or her own IRA. Either way, the money remains "retirement funds" in the same sense as before the original owner's death: the surviving spouse cannot withdraw any of the money before age 59 1/2 without paying a penalty tax and must start withdrawals no later than the year in which the survivor reaches 70 1/2 . Because the money entered the IRA without being subject to the income tax, all withdrawals are taxed at ordinary rates.

Different rules govern inherited IRAs. We il-

--- F.3d ----, 2013 WL 1729600 (C.A.7 (Wis.))
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lustrate using the facts of this case. At her death, Ruth Heffron owned an IRA worth approximately $300,000. Ruth's daughter Heidi Heffron–Clark was the designated beneficiary. Ruth's account passed to Heidi. It remains sheltered from taxation until the money is withdrawn, but many of the account's other attributes changed. For example, no new contributions can be made, and the balance cannot be rolled over or merged with any other account. 26 U.S.C. § 408(d)(3)(C). And instead of being dedicated to Heidi's retirement years, the inherited IRA must begin distributing its assets within a year of the original owner's death. 26 U.S.C. § 402(c)(11)(A), incorporating 26 U.S.C. § 401(a)(9)(B). Payout must be completed in as little as five years (though the time can be longer for some accounts). In other words, an inherited IRA is a time-limited tax-deferral vehicle, but not a place to hold wealth for use after the new owner's retirement. This statutory treatment allows the beneficiary to avoid paying income tax immediately after the original owner's death (recall that money in a normal IRA is pre-tax dollars; unlike assets that pass with a decedent's estate, the contents of an inherited IRA are taxable) while limiting the duration of tax deferral. If recipients of inherited IRAs could hold the wealth until their own retirement, tax deferral might become tax exemption, as capital held in IRAs could pass down through the generations without ever being subject to income tax.

In the bankruptcy proceeding initiated by Heidi Heffron–Clark and her husband Brandon Clark ("the Clarks"), Bankruptcy Judge Martin held that an inherited IRA does not represent "retirement funds" in the hands of the current owner and so is not exempt under § 522(b)(3)(C) and (d)(12). 450 B.R. 858 (Bankr.W.D.Wis.2011). The bankruptcy judge concluded that money counts as "retirement funds" (a term that the Bankruptcy Code does not define) only when held for the owner's retirement, while an inherited IRA must be distributed earlier. A district judge reversed, 466 B.R. 135 (W.D.Wis.2012), adopting the view, first articulated in *In re Nessa,* 426 B.R. 312 (BAP 8th Cir.2010), that any money representing "retirement funds" in the decedent's hands must be treated the same way in successors' hands. The fifth circuit has since agreed with that approach, *In re Chilton,* 674 F.3d 486 (5th Cir.2012), observing that § 522(b)(3)(C) and (d)(12) refer to "retirement funds" without providing that they must be the debtor's. It is enough, *Chilton* concludes, if they were ever anyone's retirement funds.

***2** Sometimes assets are exempt in bankruptcy because of how they function in someone else's hands. Suppose Heidi Heffron–Clark were the trustee of a retirement account for the benefit of her sister. Trustees are legal owners of the assets they administer, but the Clarks' creditors could not reach retirement assets that Heidi was holding as trustee. So we follow *Chilton* in observing that exemptions in bankruptcy do not (necessarily) depend on whether an asset is a retirement fund (or an agricultural tool, or one of the other categories of exemption) as the debtor uses it. But by the time the Clarks filed for bankruptcy, the money in the inherited IRA did not represent *anyone's* retirement funds. They had been Ruth's, but when she died they became no one's retirement funds. The account remains a tax-deferral vehicle until the mandatory distribution is completed, but distribution precedes the owner's retirement. To treat this account as exempt under § 522(b)(3)(C) and (d)(12) would be to shelter from creditors a pot of money that can be freely used for current consumption.

To see this, suppose Ruth had withdrawn the entire $300,000 from her IRA, paying the penalty tax if necessary, waited a month, then given the money to Heidi. The money would have been "retirement funds" while in Ruth's IRA, but not thereafter; in Heidi's bank account the money would be no different from any other assets she could save or spend at will. And that would have been true during the month Ruth banked the funds before sending them to Heidi. Ruth's creditors could have reached the money, notwithstanding the fact that it formerly was part of her retirement ac-

count. Why should it make a difference whether the money passed to Heidi on Ruth's death or a little earlier? Either way, the money used to be "retirement funds" but isn't now. We doubt that *Chilton* would think that money expressly withdrawn from an IRA retains its character as "retirement funds." Section 522(b)(3)(C) and (d)(12) provides that the exemption depends on the *conjunction* of tax deferral and assets' status as "retirement funds"; that an inherited IRA provides tax benefits is not enough.

Chilton and *Nessa* give weight to the phrase "inherited individual retirement account." It includes the word "retirement," after all. True enough, but the "IRA" part of "inherited IRA" (as the Internal Revenue Code uses the phrase) designates the funds' *source*, not the assets' current status. As we have observed, an inherited IRA does not have the economic attributes of a retirement vehicle, because the money cannot be held in the account until the current owner's retirement.

Chilton and *Nessa* also give weight to the fact that many of the other exemptions in § 522 refer to "the debtor's" interests, while § 522(b)(3)(C) and (d)(12) does not. For example, § 522(b)(3)(B) exempts "any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest ... is exempt from process under applicable nonbankruptcy law". This sort of language has a temporal effect: what is exempt is the debtor's tenancy when the bankruptcy begins. A debtor who on the date of filing has $100,000 in cash and no real property cannot later invest the $100,000 in a joint tenancy and then claim the property as exempt. Similarly a farmer cannot buy new farm implements after filing for bankruptcy and claim the acquisition as exempt. Section 522(b)(3)(C) and (d)(12) gives debtors a break by omitting a temporal restriction: new value added to a retirement fund during bankruptcy (an employer may continue to make retirement contributions) is outside creditors' reach, even though new real property and new farm tools are not. But temporal differences in the way exemptions work does not suggest that a pot of assets that is not "retirement funds" *any time* during the bankruptcy is exempt just because the debtor's predecessor in interest had saved for retirement.

***3** Consider a parallel situation. The Bankruptcy Code provides a homestead exemption (subject to caps under state law). So if Ruth had been living at home and had filed for bankruptcy, some or all of the house's value would have been exempt from creditors' claims. Section 522(b)(3)(A) implements this by exempting a "domicile" in which the debtor lived for at least 730 days before filing for bankruptcy. Suppose Heidi had inherited her mother's house and rented it out. She could not claim the property as exempt just because it used to be her mother's home; it would be exempt only if it had been Heidi's home for the two years before the Clarks' filing. Exemption would depend on how Heidi used the property, not how her mother used it. Just so with retirement funds.

At oral argument, the Clarks' lawyer told us that reading the Bankruptcy Code to exempt assets that formerly were someone's retirement funds, but have never been the debtors' retirement funds, would encourage people to save in order to make larger bequests to their children. If parents know that anything in their IRAs could be passed to their relatives free of creditors' claims, they would save more and draw less from IRAs during retirement. That's true enough, but it does not imply an a temporal meaning of "retirement funds." One could equally say that it would promote savings to hold that *any* asset acquired from one's relatives by will, insurance, annuity, or survivorship designation is exempt from creditors' claims. That is not remotely what § 522 provides, however. It is always possible to get more of whatever objective may have prompted a given clause, but "no legislation pursues its purposes at all costs. Deciding what competing values will or will not be sacrificed to the achievement

of a particular objective is the very essence of legislative choice—and it frustrates rather than effectuates legislative intent simplistically to assume that *whatever* furthers the statute's primary objective must be the law." *Rodriguez v. United States,* 480 U.S. 522, 525–26, 107 S.Ct. 1391, 94 L.Ed.2d 533 (1987) (emphasis in original). Section 522(b)(3)(C) and (d)(12) does not throw creditors' claims to the wolves in order to enhance the savings and bequest motives. It provides a specific exemption for retirement funds—and inherited IRAs do not qualify, because they are not savings reserved for use after their owners stop working.

The district judge thought the question close and believed that close questions should be decided in debtors' favor. We do not think the question close; inherited IRAs represent an opportunity for current consumption, not a fund of retirement savings. It is therefore unnecessary to decide whether there is or should be an interpretive principle favoring either side in a dispute about the scope of an exemption, or whether any such principle would depend on a combination of federal law (for federal exemptions) plus state law (for state exemptions), as in *In re Barker,* 768 F.2d 191, 196 (7th Cir.1985) .

***4** The bankruptcy judge got this right. We disagree with the fifth circuit's decision in *Chilton*. Because our conclusion creates a conflict among the circuits, we circulated the opinion before release to all judges in active service. None of the judges requested a hearing *en banc*.

REVERSED.

C.A.7 (Wis.),2013.
In re Clark
--- F.3d ----, 2013 WL 1729600 (C.A.7 (Wis.))

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conditions would also have made it very difficult if not impossible for any counsel that Appellees might have reached to provide meaningful assistance. We do not suggest (or deny) that there is a blanket emergency exception to the Sixth Amendment right to counsel. Rather, we hold only that in light of the security risks and unique emergency conditions he faced, Hunter did not act in an objectively unreasonable manner under clearly established law. The district court therefore erred by not granting Hunter qualified immunity as a matter of law.

V. Conclusion

There is no doubt that Appellees suffered terribly while held in custody after Hurricane Katrina struck New Orleans. It is equally clear, however, that (1) Gusman's failure to release Appellees falls within the emergency exception to the rule that a probable cause determination must be made within 48 hours, and (2) Hunter's failure to allow Appellees to use cell phones was not objectively unreasonable in light of any clearly established law. We therefore reverse and vacate the judgment of the district court, and remand with instructions to enter judgment in favor of Gusman and Hunter on all claims asserted by Appellees.

REVERSED, VACATED, and REMANDED WITH INSTRUCTIONS.

In the matter of Janice Elaine CHILTON; Robert Gregg Chilton, Debtors.

Robert Gregg Chilton and Janice Elaine Chilton, Appellees,

v.

Christopher Moser, Appellant.

No. 11–40377.

United States Court of Appeals, Fifth Circuit.

March 12, 2012.

Background: Bankruptcy trustee in Chapter 13 case objected to debtors' claim that individual retirement account (IRA) inherited pre-petition by debtor-wife was exempt from bankruptcy estate. The Bankruptcy Court, Brenda T. Rhoades, J., 426 B.R. 612, sustained the objection, and debtors appealed. The United States District Court for the Eastern District of Texas, Ron Clark, J., 444 B.R. 548, reversed, and appeal was taken.

Holdings: The Court of Appeals, Carl E. Stewart, Circuit Judge, held that:

(1) as a matter of first impression, funds in inherited IRA constituted "retirement funds" within meaning of statute providing for the exemption of retirement funds from bankruptcy estates, and

(2) funds were in a fund or account that was exempt from taxation under the enumerated provisions of the Internal Revenue Code.

Affirmed.

1. Bankruptcy ⚿3782

Court of Appeals reviews questions of law such as the interpretation of the Bankruptcy Code de novo.

2. Bankruptcy ⚿2779

An exemption claimed under statute providing for the exemption of retirement funds from bankruptcy estates must satisfy two requirements: (1) the amount the

debtor seeks to exempt must be retirement funds, and (2) those retirement funds must be in an account that is exempt from taxation under sections 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code. 11 U.S.C.A. § 522(d)(12); 26 U.S.C.A. §§ 401, 403, 408, 408A, 414, 457, 501(a).

3. Statutes ⚿188

To interpret statutory language, Court of Appeals begins with its plain meaning.

4. Bankruptcy ⚿2779

Funds in individual retirement account (IRA) inherited prepetition by debtor-wife constituted "retirement funds" within meaning of statute providing for the exemption of retirement funds from bankruptcy estates; funds were "set apart" for retirement at time they were deposited in the IRA. 11 U.S.C.A. § 522(d)(12).

See publication Words and Phrases for other judicial constructions and definitions.

5. Bankruptcy ⚿2779

Funds in individual retirement account (IRA) inherited prepetition by debtor-wife were in a fund or account that was exempt from taxation under enumerated provisions of the Internal Revenue Code, as required for them to be exempt from bankruptcy estate pursuant to statute providing for the exemption of retirement funds from bankruptcy estates. 11 U.S.C.A. § 522(d)(12); 26 U.S.C.A. § 408.

Robert M. Nicoud, Jr. (argued), Olson, Nicoud & Gueck, L.L.P., Dallas, TX, for Appellees.

Timothy Andrew York (argued), Quilling, Selander, Lownds, Winslett & Moser, P.C., Dallas, TX, for Appellant.

Tara Ann Twomey, San Jose, CA, for Amicus Curiae.

Appeal from the United States District Court for the Eastern District of Texas.

Before BENAVIDES, STEWART and GRAVES, Circuit Judges.

CARL E. STEWART, Circuit Judge:

The debtors Robert Gregg Chilton and Janice Elaine Chilton inherited an IRA worth $170,000 from Janice Elaine Chilton's mother, Shirley Jean Heil. When they filed for bankruptcy, the debtors sought to exempt the inherited IRA from the bankruptcy estate pursuant to 11 U.S.C. § 522(d)(12), which permits debtors to exempt certain "retirement funds to the extent that those funds are in a fund or account that is exempt from taxation" under specified provisions of the Internal Revenue Code. Christopher Moser, the Chapter 7 Trustee for the debtor's bankruptcy proceeding, objected to the exemption, arguing that inherited IRAs do not qualify for exemption under section 522(d)(12). After the bankruptcy court ruled for the trustee, the district court reversed the bankruptcy court. Because we hold that inherited IRAs are exempt from the bankruptcy estate pursuant to 11 U.S.C. § 522(d)(12), we AFFIRM the district court's judgment.

I.

The facts are not disputed. For several years, Heil held an individual retirement account ("IRA") with RBC Dain Rauscher. After Heil died on November 28, 2007, Heil's account passed directly to Chilton, the account's designated beneficiary and Heil's daughter, without passing through probate proceedings. Chilton established an IRA with RBC Dain Rauscher to receive distributions from Heil's IRA. Chil-

ton's IRA was established as an inherited IRA under the Internal Revenue Code (the "inherited IRA").

The debtors filed for bankruptcy under Chapter 7 of the Bankruptcy Code on December 18, 2008. They listed the inherited IRA as an asset in their bankruptcy petition and sought to exempt $170,000 contained in the inherited IRA pursuant to 11 U.S.C. § 522(d)(12). The trustee objected to the claimed exemption on the grounds that the funds in the inherited IRA are not "retirement funds" within the meaning of 11 U.S.C. § 522(d)(12) and are not contained in the type of tax-exempt accounts specified in 11 U.S.C. § 522(d)(12). In response to the trustee's objection, the debtors converted their filing to a bankruptcy under Chapter 13 of the Bankruptcy Code.

The trustee again objected to the debtors' claimed exemption. After a hearing on October 28, 2009, the bankruptcy court sustained the trustee's objection by order dated March 5, 2010. The district court then reversed the ruling of the bankruptcy court, citing a number of cases decided subsequent to the bankruptcy court's ruling that arrived at the opposite result. This appeal followed.

II.

A.

[1] This court reviews questions of law such as the interpretation of the Bankruptcy Code de novo. *See, e.g., In re England (Pritchard v. Trustee),* 153 F.3d 232, 234 (5th Cir.1998).

B.

The Bankruptcy Code permits debtors to exempt certain property from the bankruptcy estate.

> As a general matter, upon the filing of a petition for bankruptcy, all legal or equitable interests of the debtor in property become the property of the bankruptcy estate and will be distributed to the debtor's creditors. To help the debtor obtain a fresh start, the Bankruptcy Code permits him to withdraw from the estate certain interests in property, such as his car or home, up to certain values.

Rousey v. Jacoway, 544 U.S. 320, 325, 125 S.Ct. 1561, 161 L.Ed.2d 563 (2005) (quotation marks and internal citations omitted). A claim of exemptions is presumably valid, and the objecting party has the burden of proving that exemptions are not properly claimed. 11 U.S.C. § 522(*l*); Fed. R. Bank. P. 4003(c).

[2] At issue in this appeal is the exemption in the Bankruptcy Code for "[r]etirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986." 11 U.S.C. § 522(d)(12). Put another way, an exemption claimed under section 522(d)(12) must satisfy two requirements: (1) the amount the debtor seeks to exempt must be retirement funds, and (2) those retirement funds must be in an account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code. *In re Nessa,* 426 B.R. 312, 314 (8th Cir. BAP 2010).

We must decide whether inherited IRAs satisfy the two requirements of section 522(d)(12), a question of first impression for this court and our sister circuits.

C.

[3] We begin with whether the funds in an inherited IRA are "retirement funds" as that phrase is used in section 522(d)(12). The phrase "retirement funds" is not defined in the Bankruptcy Code. To inter-

pret statutory language, we begin with its plain meaning. *See, e.g., Conn. Nat'l Bank v. Germain,* 503 U.S. 249, 253–54, 112 S.Ct. 1146, 117 L.Ed.2d 391 (1992). "[R]etirement" is defined as "withdrawal from office, active service, or business"; "fund" is defined as "a sum of money or other resources the principal or interest of which is set apart for a specific objective or activity." *Webster's Third New Int'l Dictionary* 921, 1939 (1993). The trustee argues that these definitions do not describe inherited IRAs because beneficiaries of inherited IRAs do not suffer penalties for withdrawing funds from inherited IRAs before retirement age.

Most of the courts that have analyzed this issue have concluded that inherited IRAs are "retirement funds" as that phrase is used in section 522(d)(12).[1] *Nessa,* 426 B.R. at 314; *In re Kuchta,* 434 B.R. 837, 843–44 (Bankr.N.D.Ohio 2010); *In re Tabor,* 433 B.R. 469, 476 (Bankr. M.D.Pa.2010); *In re Thiem,* 443 B.R. 832, 843–44 (Bankr.D.Ariz.2011); *In re Weilhammer,* No. 09–15148–LT7, 2010 WL 3431465, at *4–*6 (Bankr.S.D.Cal. Aug. 30, 2010); *In re Stephenson,* 2011 WL 6152960, at *2–*3, 2011 U.S. Dist. LEXIS 142360, at *7–*8. These courts have noted that the statute does not explicitly limit "retirement funds" to retirement funds that belong to the debtor. *See, e.g., Nessa,* 426 B.R. at 314. Accordingly, they have reasoned that "retirement funds" can include the funds that others had originally set aside for their retirement, as with inherited IRAs. *Id.*

[4] We find the reasoning in these decisions persuasive. The plain meaning of the statutory language refers to money that was "set apart" for retirement. Thus, the defining characteristic of "retirement funds" is the purpose they are "set apart" for, not what happens after they are "set apart." Here, there is no question that the funds contained in the debtors' inherited IRA were "set apart" for retirement at the time Heil deposited them into an IRA. This reasoning finds further support from 11 U.S.C. § 522(b)(4)(C), which provides that "a direct transfer of retirement funds from 1 fund or account that is exempt from taxation under section ... 408 ... of the Internal Revenue Code of 1986, ... shall not cease to qualify for exemption under ... subsection (d)(12) by reason of such direct transfer." In other words, the direct transfer of "retirement funds" does not alter their status as "retirement funds." As we see no reason to interpret the statutory language differently from its plain meaning, we hold that the $170,000 contained in the inherited IRA constitute "retirement funds" as that phrase is used in section 522(d)(12).

D.

We next consider whether the funds in the inherited IRA are "in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986." 11 U.S.C. § 522(d)(12). While the parties agree that the debtors' inherited IRA is tax exempt, they disagree over which section of the Internal Revenue

1. We are aware of three bankruptcy court decisions that arrived at the opposite conclusion, each of which was reversed on appeal. *In re Chilton,* 426 B.R. 612, 616 (Bankr. E.D.Tex.2010), *rev'd,* 444 B.R. 548 (E.D.Tex. 2011); *In re Clark,* 450 B.R. 858 (Bankr. W.D.Wis.2011), *rev'd,* No. 11–cv–482, 2012 WL 233990 (W.D.Wis. Jan. 5, 2012) (interpreting analogous provision 11 U.S.C. § 522(b)(3)(C)); *In re Stephenson,* No. 11–cv–10848, 2011 WL 6152960, 2011 U.S. Dist. LEXIS 142360 (E.D.Mich. Dec. 12, 2010) (reversing oral pronouncement of bankruptcy judge that inherited IRA was not exempt from bankruptcy estate).

Code renders it exempt. The trustee contends that inherited IRAs are tax exempt pursuant to 26 U.S.C. § 402(c)(11)(A). The trustee argues that this provision explains why IRAs are not taxed when they are converted to inherited IRAs. *Id.* The debtors respond by arguing that the inherited IRA is tax exempt pursuant to 26 U.S.C. § 408(e).

We assume without deciding that, at the time an IRA becomes an inherited IRA, the transfer itself is tax exempt pursuant to 26 U.S.C. § 402(c)(11)(A). Since the transfer of Heil's IRA had already occurred at the time the debtors filed for bankruptcy, however, the issue we must decide is which provision renders the inherited IRA exempt from taxation subsequent to the transfer.

We agree with the other courts to have considered this question that, post-transfer, inherited IRAs are exempt from taxation by reason of 26 U.S.C. § 408(e).[2] The statute's expansive language, which provides that "*[a]ny* individual retirement account is exempt from taxation under this subsection . . . .", indicates that section 408 is the exempting section for all individual retirement accounts. *See Estate of Kahn v. Comm'r,* 125 T.C. 227, 231, 2005 WL 3081656 (T.C.2005) ("[E]arnings from assets held in an IRA are not subject to taxation in the IRA when earned, but rather, are subject to taxation when distributions are made. This fact does not change when the IRA is inherited from the decedent. *See* sec. 408(e)(1)."); *Nessa,* 426 B.R. at 314; *In re Kuchta,* 434 B.R. at 843–44; *In re Tabor,* 433 B.R. at 476; *In re Thiem,* 443 B.R. at 844–45; *In re Weilhammer,* 2010 WL 3431465, at *6; *In re Stephenson,* 2011 WL 6152960, at *3, 2011 U.S. Dist. LEXIS 142360, at *8–*9. While inherited IRAs operate differently from traditional IRAs, the definition of "individual retirement accounts" in the Internal Revenue Code encompasses inherited IRAs. *See* 26 U.S.C. § 408(d)(3)(C)(2) ("An individual retirement account or individual retirement annuity shall be treated as inherited if—(I) the individual for whose benefit the account or annuity is maintained acquired such account by reason of the death of another individual, and (II) such individual was not the surviving spouse of such other individual."). Accordingly, after an inherited IRA is established, it stands to reason that distributions from the inherited IRA are subject to the same provision as all other IRAs—that is, section 408—for the purpose of determining whether they are exempt from taxation.

[5] For these reasons, section 408 of the Internal Revenue Code rendered the inherited IRA exempt from taxation following its transfer from Heil to the debtors. Because section 408 is one of the sections named in 11 U.S.C. § 522(d)(12), inherited IRAs are contained in an "account" that is "exempt from taxation" as that phrase is used in section 522(d)(12).

III.

Accordingly, we AFFIRM the district court's judgment.

2. As with the "retirement funds" issue, we are aware of three bankruptcy court decisions that arrived at the opposite conclusion with respect to this issue, each of which was reversed on appeal. *In re Chilton,* 426 B.R. at 616, *rev'd,* 444 B.R. 548; *In re Clark,* 450 B.R. 858, *rev'd,* 2012 WL 233990; *In re Stephenson,* 2011 U.S. Dist. LEXIS 142360.

ruptcy Procedure 7052. A separate Order will be entered.

ORDER

For the reasons stated in an Opinion entered this day, IT IS HEREBY ORDERED as follows:

1. The motion filed by the Debtor, Scot R. Furlong, to reconsider the Court's prior order denying his motion to extend the automatic stay is GRANTED.

2. The order denying the Debtor's motion to extend the automatic stay is VACATED.

3. The motion filed by the Debtor to extend the automatic stay is GRANTED.

4. The automatic stay becomes effective as to all of the Debtor's creditors upon entry of this Order.

5. The Clerk is directed to schedule and notice a hearing to consider confirmation of the Chapter 13 plan.

In re Nancy A. NESSA, Debtor.

Gene W. Doeling, Trustee–Appellant,

v.

Nancy A. Nessa, Debtor–Appellee.

No. 10–6009.

United States Bankruptcy Appellate Panel of the Eighth Circuit.

Submitted: March 11, 2010.

Filed: April 9, 2010.

Background: Chapter 7 trustee objected to debtor's claim of an exemption in an individual retirement account (IRA) that she inherited from her father prepetition. The United States Bankruptcy Court for the District of Minnesota, Dennis D. O'Brien, J., 2010 WL 128313, overruled the objection, and trustee appealed.

Holding: The Bankruptcy Appellate Panel (BAP), Schermer, J., held that debtor's inherited IRA qualified as exempt under the Bankruptcy Code's exemption for retirement funds.

Affirmed.

1. Internal Revenue ⚿3594

Under the Internal Revenue Code, the beneficiary of an inherited individual retirement account (IRA) may not treat the account as his or her own by making contributions to it or rolling over the account into another retirement plan. 26 U.S.C.A. § 408(d)(3)(C).

2. Bankruptcy ⚿3782

Bankruptcy Appellate Panel (BAP) reviews the bankruptcy court's conclusions of law de novo.

3. Bankruptcy ⚿2532, 2533

Debtor's bankruptcy estate is defined broadly to include all legal and equitable interests of the debtor in property, as well as other specific interests of the debtor. 11 U.S.C.A. § 541.

4. Bankruptcy ⚿2779

Bankruptcy Code imposes two requirements before a debtor may claim an exemption in retirement funds: (1) the amount the debtor seeks to exempt must be retirement funds, and (2) the retirement funds must be in an account that is exempt from taxation under one of the provisions of the Internal Revenue Code set forth therein. 11 U.S.C.A. § 522(d)(12).

5. Bankruptcy ⚿2779

Individual retirement account (IRA) that Chapter 7 debtor inherited from her father prepetition qualified as exempt under the Bankruptcy Code's exemption for retirement funds; it was undisputed that the amounts in the father's IRA were his retirement funds prior to his death, the contents of the father's account remained, in form and substance, "retirement funds" following their direct "trustee-to-trustee" transfer to the inherited account, even though they were not debtor's own retirement funds, and debtor's inherited account was exempt from taxation under the section of the Internal Revenue Code governing individual retirement accounts. 11 U.S.C.A. § 522(d)(12); 26 U.S.C.A. §§ 408, 408(e).

6. Bankruptcy ⚿2779

Although the Bankruptcy Code's exemption for retirement funds requires that account be comprised of retirement funds, it does not specify that they must be the debtor's retirement funds. 11 U.S.C.A. § 522(d)(12).

Gene W. Doeling, Fargo, ND, for appellant.

Jean P. Hannig, Fargo, ND, for appellee.

Before SCHERMER, VENTERS and SALADINO, Bankruptcy Judges.

SCHERMER, Bankruptcy Judge.

Gene W. Doeling, Chapter 7 trustee (the "Trustee") for the bankruptcy estate of Nancy A. Nessa (the "Debtor") appeals from an Order Overruling Objection to Exemption. The bankruptcy court [1] overruled the Trustee's objection to the Debtor's claim of an exemption of her inherited IRA account under section 522(d)(12) of the Title 11 of the United States Code (the "Bankruptcy Code"). We have jurisdiction over this appeal from the final order of the bankruptcy court. *See* 28 U.S.C. § 158(b). For the reasons set forth below, we affirm.

ISSUE

The issue on appeal is whether the Debtor's inherited IRA qualifies as exempt pursuant to section 522(d)(12) of the Bankruptcy Code. We conclude that it does.

BACKGROUND

[1] The Debtor filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code in January 2009. Prior to that filing, the Debtor's father, Robert Borrett, had established an individual retirement account ("IRA") pursuant to Section 408 of Title 26 of the United States Code (the "Internal Revenue Code"). The Debtor was named the beneficiary of that IRA. After her father died in August 2008, and before filing her bankruptcy petition, the Debtor made a trustee-to-trustee transfer of the IRA to her own account at Wells Fargo; she did not "roll over" the account to her own IRA nor did she take any distributions from her father's IRA.[2] The Debtor has not contributed any of her own funds to the inherited account, and any withdrawals will be taxable to her.

The Debtor claimed the inherited account as exempt in her Schedule E, pursuant to section 522(d)(12) of the Bankruptcy

1. The Honorable Dennis D. O'Brien, United States Bankruptcy Court for the District of Minnesota.

2. In fact, the beneficiary of an inherited account may not treat the account as his or her own by making contributions to it or rolling over the account into another retirement plan. *See* 26 U.S.C. § 408(d)(3)(C).

Code. The Trustee objected to the Debtor's claim of an exemption for the inherited account.

The bankruptcy court overruled the Trustee's objection to the Debtor's claimed exemption. It explained that the transfer of the contents of the Debtor's father's account to the inherited account was a trustee-to-trustee transfer as described in the Internal Revenue Service's Publication 590. *Individual Retirement Arrangements, (IRAs),* Department of the Treasury, Internal Revenue Service, Publication 590, at 20. The bankruptcy court then concluded that the transfer from the Debtor's father's account retained their character as retirement funds. Accordingly, it concluded that the funds in the account qualified for an exemption under Bankruptcy Code section 522(d)(12).

STANDARD OF REVIEW

[2] We review the bankruptcy court's conclusions of law *de novo. Alexander v. Jensen–Carter (In re Alexander),* 239 B.R. 911, 913 (8th Cir. BAP 1999), *aff'd* 236 F.3d 431 (8th Cir.2001). The facts are not in dispute.

DISCUSSION

[3, 4] A debtor's bankruptcy estate is defined broadly to include all legal and equitable interests of the debtor in property, as well as other specific interests of the debtor. 11 U.S.C. § 541. Bankruptcy Code section 522 allows the debtor to exempt certain property from his estate. 11 U.S.C. § 522. Pursuant to section 522(d)(12), the debtor may take an exemption for:

> [r]etirement funds to the extent those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.

11 U.S.C. § 522(d)(12). Accordingly, section 522(d)(12) imposes two requirements before a debtor may claim an exemption under that section: (1) the amount the debtor seeks to exempt must be retirement funds; and (2) the retirement funds must be in an account that is exempt from taxation under one of the provisions of the Internal Revenue Code set forth therein.

The Debtor's father's account was an "individual retirement account", as that term is defined under section 408(a). 26 U.S.C. § 408(a). It is now classified as an "inherited individual retirement account" because the Debtor acquired the account by reason of her father's death. 26 U.S.C. § 408(d)(3)(C).

Retirement Funds

[5, 6] The bankruptcy court correctly determined that the amounts in the inherited account were "retirement funds". The Trustee does not dispute the bankruptcy court's determination that, the amounts in the Debtor's father's IRA were his retirement funds prior to his death. He suggests, however, that to retain their status as retirement funds under section 522(d)(12) in the Debtor's inherited account, the contents of the inherited account would have to have been contributed by the Debtor or be part of the Debtor's retirement plan. Bankruptcy Code section 522(d)(12) makes no such distinction. Section 522(d)(12) requires that the account be comprised of retirement funds, but it does not specify that they must be the *debtor's* retirement funds. The Trustee's definition of retirement funds would impermissibly limit the statute beyond its plain language. *U.S. v. Ron Pair Enterprises,* 489 U.S. 235, 241, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989)("where, as here, the statute's language is plain, 'the sole function of the courts is to enforce it according to its terms' ") (citation omitted). In accordance with the terms of Bankruptcy Code section

522(d)(12), even though the contents of the Debtor's inherited account were the Debtor's father's retirement funds, not the Debtor's own retirement funds, they remain in form and substance, "retirement funds." [3]

Exempt from Taxation

The Debtor's inherited account is exempt from taxation under Internal Revenue Code section 408. The Trustee acknowledged that the Debtor's inherited account is not taxed until the Debtor makes a withdrawal. However, he suggested that the inherited account does not meet the requirements of Bankruptcy Code section 522(d)(12), reasoning that the "rules are different . . . regarding the use, distribution, and taxation of funds in an IRA versus an Inherited IRA." It is irrelevant whether a traditional IRA and an inherited IRA have different rules regarding minimum required distributions. Section 408(e) of the Internal Revenue Code provides, in pertinent part, that "*[a]ny* individual retirement account is exempt from taxation." 26 U.S.C. § 408(e)(1)(emphasis added). It does not distinguish between an inherited IRA and traditional types of IRAs.

Bankruptcy Code Section 522(b)(4)(C)

Bankruptcy Code section 522(b)(4)(C) reinforces our conclusion that the funds in the Debtor's inherited account are exempt under Bankruptcy Code section 522(d)(12). Section 522(b)(4)(C) provides that direct transfers from an account under Internal Revenue Code section 408(a) are exempt under Bankruptcy Code section 522(d)(12). It states, in pertinent part, that:

> [a] direct transfer of retirement funds from 1 fund or account that is exempt from taxation under section . . . 408 . . . of the Internal Revenue Code of 1986, . . ., shall not cease to qualify for exemption under . . . subsection (d)(12) by reason of such direct transfer.

11 U.S.C. § 522(b)(4)(C). The parties did not dispute that the retirement account held by the Debtor's father before his death was an individual retirement account under Internal Revenue Code section 408 or that the transfer from the father's account to the Debtor's inherited account was a direct trustee-to-trustee transfer. Accordingly, the direct transfer of funds from the father's account to the Debtor's inherited account did not destroy the Debtor's ability to claim the funds exempt under Bankruptcy Code section 522(d)(12) by virtue of Bankruptcy Code section 522(b)(4)(C).

CONCLUSION

For the foregoing reasons, we affirm the decision of the bankruptcy court.

3. *But see In re Chilton,* 426 B.R. 612, 2010 WL 817331 (Bankr.E.D.Tex. Mar.5, 2010), holding that the words ''retirement funds'' as used in section 522(d)(12), when read in context, ''cannot reasonably be understood to authorize an exemption of an inherited IRA.'' *Chilton* at *4–7, 426 B.R. at 618–22. Our research has not disclosed any other cases dealing with the exemption of an inherited IRA under section 522(d)(12) since the amendment of section 522 of the Bankruptcy Code in 2005, nor have the parties suggested any. We believe that the *Chilton* court's conclusion is erroneous because *inter alia,* it fails to take into account section 522(b)(4)(C) of the Bankruptcy Code, discussed *infra,* and in fact it would make that section totally meaningless.

1. EXEMPTIONS IN BANKRUPTCY

a. A debtor may exempt (1) property listed in §522(d) of the Bankruptcy Code or (2) property that is exempt under applicable state law and federal law other than §522(d). *See* 11 U.S.C. § 522(b) (1). Additionally, a state may "opt out" of the federal bankruptcy exemptions.

b. Missouri has opted out pursuant to Mo. Rev. Stat. 513.427. *Stanton v. Bryan* (In re Bryan), 466 B.R. 460, (8th Cir. B.A.P. 2012).

c. To create an exemption in Missouri, the statute may explicitly state that the property is "exempt" and not merely state that the property is "not subject to" attachment or execution. *In re Benn*, 491 F.3d 811, 814 (8th Cir. 2007) (holding that state and federal tax refunds are not exempt under Mo. Rev. Stat. 513.427, which is Missouri's opt-out statute and not an exemption statute). *See, also, In re Bryan*, 2011 WL 3882281 (Bankr. W.D. Mo. Sep. 2, 2011), *aff'd on other grounds*, *Stanton v. Bryan* (In re Bryan), 466 B.R. 460, (8th Cir. B.A.P. 2012) (the language of "liable to" does not have the same legal significance as "exempt" thus Mo. Rev. Stat. 377.330 is not an exemption statute).

d. Exemption laws are enacted to provide relief to the debtor and are to be liberally construed. *In re Schissler*, 250 B.R. 697, 700 (Bankr. W.D. Mo. 2000). However, a bankruptcy court must be careful not to depart substantially from the express language of the exemption, or to extend the legislative grant as expressed by Congress. *In re Collett*, 253 B.R. 452, 454 (Bankr. W.D. Mo. 2000).

e. A debtor's exemptions are determined as of the time of the filing of the petition. *Armstrong v. Peterson* (In re Peterson), 897 F.2d 935 (8th Cir. 1990).

2. PROCEDURES

a. Claim of exemptions. A debtor shall list the property claimed as exempt on the schedule of assets required to be filed by Fed. R. Bankr. P. 1007. Debtor's dependent my file the schedule of exemptions, if debtor failed to do so. Fed. R. Bankr. P. 4003(a).

b. Amendments. A debtor has the right to amend schedules at any time before the case is closed. Fed. R. Bankr. P. 1009(a); *In re Ladd*, 319 B.R. 599, 603 (8th Cir. B.A.P. 2005); *In re James*, 332 B.R. 397, 399 (Bankr. W.D. Mo. 2005).

   i. The right to freely amend a claimed exemption is subject to two exceptions: bad faith by the debtor or prejudice to creditors. *Ladd v. Ries* (In re Ladd), 450 F.3d 751, 755 (8th Cir. 2006); *Kaelin v. Bassett* (In re Kaelin), 308 F.3d 885, 889 (8th Cir. 2002).

   ii. Illustrative of bad faith is the case of *Bauer v. Iannacone* (In re Bauer), 298 B.R. 353 (B.A.P. 8th Cir. 2003) in which debtors' amended homestead exemption was denied for their bad faith in knowingly undervaluing the property. Minnesota debtors valued their homestead at $80,000 in their chapter 7 case. After the case was closed, the homestead was destroyed by fire. Debtor reopened the case to claim a homestead exemption of $200,000, the limit of the Minnesota homestead exemption. The trustee objected arguing that debtors had previously valued their property at only $80,000 when the home had an assessed value of $203,000 and had been insured for $276,000. The bankruptcy court sustained the trustee's objection, and the BAP affirmed, finding that debtors acted in bad faith by intentionally undervaluing their homestead. Their bad faith precluded them from amending their exemption schedules to claim the actual value of the home.

   iii. A debtor's bad faith is determined by examining the totality of the circumstances. *In re Evinger*, 354 B.R. 850, 854 (Bankr. W.D. Ark. 2006) (trustee's objection to amended exemptions sustained because debtors demonstrated bad faith by viewing bankruptcy as a matter not requiring their full attention, candor, and integrity).

c. Time to file Objection. A party in interest may file an objection to the list of property claimed as exempt only within 30 days after the meeting of creditors is concluded or within 30 days after any amendment to the list or

supplemental schedules is filed, whichever is later. The court may, for cause, extend the time for filing objections if, before the time to object expires, a party in interest files a request for an extension. Fed. R. Bankr. P. 4003.

d. The 30-day deadline of Rule 4003(b) (1) is strictly applied. *Taylor v. Freeland & Kronz*, 503 U.S. 638, 112 S.Ct. 1644, 118 L.Ed.2d 280 (1992). (Trustee's objection was untimely when he filed objection after the 30-day deadline expired to a Schedule C listing an injury claim with a value of "unknown," even though the debtor had no statutory basis to assert an exemption in the injury claim).

e. *Compare, Schwab v. Reilly*, 130 S.Ct. 2652 (2010). Trustee was not required to object to debtor's claimed exemption to business equipment and tools of the trade when debtor claimed the full statutory allowance of the exemption. Under these circumstances, the Trustee was permitted to sell the equipment and tools and retain for the estate the excess value after payment to the debtor of the statutory exemption amounts.

f. Rule 3004(b)(2) makes an exception to the 30-day deadline for debtor's fraudulent conduct. It allows a trustee to file an objection to a claim of exemption at any time prior to one year after the closing of the case if the debtor fraudulently asserted the claim of exemption.

g. Burden of proof. The party objecting to an exemption has the burden of proof to show that the exemption should not be allowed. Fed. R. Bank. P. 4003(c).

3. EXEMPTION PLANNING

a. As a general rule, a debtor may convert non-exempt assets to exempt assets before filing bankruptcy, unless the debtor has engaged in some additional conduct that amounts to "extrinsic" evidence of fraudulent intent. *In re Addison*, 540 F.3d 805 (8th Cir. 2008).

b. In *Addison*, debtors used nonexempt assets to contribute $4,000 to Roth IRAs in the months before filing bankruptcy and, on the day of filing, used non-exempt assets to pay down the principal on their home mortgage by

$11,500. The Court stated that "[i]t is well established that . . . a debtor's conversion of non-exempt property to exempt property on the eve of bankruptcy for the express purpose of placing that property beyond the reach of creditors, without more, will not deprive the debtor of the exemption to which he otherwise would be entitled." *Id*. at 814. In order to deny a debtor an exemption due to pre-bankruptcy exemption planning, there must be "extrinsic evidence" of intent to defraud other than the conversion of non-exempt assets to exempt assets, even if the debtor expressly admits that the purpose for doing so was to place the assets beyond the reach of creditors. *Id*. at 814-15. The Eighth Circuit suggested four indicia of "extrinsic" evidence of fraud: (1) conduct intentionally designed to materially mislead or deceive creditors about the conversion of assets; (2) use of credit to buy exempt property; (3) converting a "very great amount" of nonexempt property to exempt property; and (4) conveyances by the debtor for less than adequate consideration. *Id*. at 816.

c. Judge Federman applied the *Addison* analysis to the term "fraudulent" under Mo. Rev. Stat. 513.430.1(10)(f) and allowed debtors' claimed exemptions in IRAs acquired within two months of filing bankruptcy. *In re Montanaro*, 398 B.R. 688 (Bankr. W.D. Mo. 2008). Mo. Rev. Stat. 513.430.1(10)(f) exempts a debtor's right to receive money from a qualified retirement plan unless the deposit was "fraudulent," which term had been defined by a Missouri probate statute to mean that the deposit was made within three years of the bankruptcy filing and with a intent to hinder, delay, or prevent a creditor from collecting a lawful debt, or was insolvent, or not paying debts as they came due, or when a creditor lawsuit was pending. In a prior decision, Judge Federman had concluded, after reviewing the applicable Missouri statutes, that ". . . contributions to retirement accounts made in contemplation of bankruptcy are not exempt." *In re Orgeron*, 2006 WL 335438, *2 (Bankr. W.D. Mo. Feb. 2, 2006. He reconsidered that conclusion in light of the subsequent *Addison* decision;

and, in *Montanaro*, after a factual analysis applying the *Addison* indicia of extrinsic fraud, held that debtors were entitled to an exemption in their IRAs.

d. Other examples of allowed exemption planning are:

i. *In re Wilmoth*, 397 B.R. 915 (8th Cir. B.A.P. 2008) (paying down mortgage by $140,000 was acceptable exemption planning under *Addison*).

ii. *In re Johnson*, 880 F.2d 78, 79 (8th Cir. 1989) (paying off $175,000 in debts against a home was acceptable exemption planning).

iii. *Hanson v. First Nat'l Bank in Brookings*, 848 F.2d 866, 867-68 (8th Cir. 1988) (converting approximately $20,000 into life insurance policies and prepaying an additional $11,033 on a homestead mortgage was acceptable exemption planning).

4. MISSOURI EXEMPTIONS

a. Annuities

i. *Stanton v. Bryan* (In re Bryan), 466 B.R. 460 (8th Cir. B.A.P. 2012) (Debtor's interest in a non-qualified deferred variable annuity is not exempt under the life insurance provisions of Missouri statutes).

1. In 1993, Debtor purchased from an insurance company a non-qualified deferred variable annuity for $30,000. Payments under the annuity contract were to begin in 2033. Debtor filed a Chapter 13 case in 2010, which was converted to Chapter 7. Debtor claimed the annuity contract as exempt under §§ 513.430.1(7), 377.330 and 377.090. The trustee objected. Bankruptcy court sustained the objection, and Debtor appealed. The B.A.P. affirmed on the grounds of *res judicata* and, additionally, because the court properly disallowed the claimed exemption.

2. Debtor had filed several amendments claiming the annuity as exempt, citing various statutes at different times,

including §513.430.1(10)(e) (annuity exempt because it was reasonably necessary for support), 513.430.1(7) (life insurance exemption), §§ 377.330, 376.530, 376.550, and 376.560 (specialized insurance regulatory statutes). The court held hearings in April 2011 and in September 2011. The court entered an order in April sustaining the trustee's objection to claimed exemptions under various statutes. Debtor then claimed the annuity exempt under just Mo. Rev. Stat. 413.520.1(7) and 377.330 and 377.990. The court issued an opinion in September 2011, noting that at the April 2011 hearing it had already stated that the life insurance exemption did not apply to an annuity. The court had also previously denied the exemption under §§ 377.330 and 377.990, as debtor had cited these statutes in the Schedule C then under consideration by the court. In affirming denial of the claimed exemptions under *res judicata*, the court found that the same parties were involved in the hearings, the debtor could have, and should have, litigated the issues related to her claim of exemptions under all the Missouri statutes at the first hearing, and the various claims of exemptions shared a common nucleus of operative facts in that they involved interpretation of the annuity and debtor's rights in it.

3. Sections 377.330 and 377.990 apply to Assessment Plan and Stipulated Premium Plan life insurance. These are specialized forms of life insurance. The two statutes restrict from attachment money or benefits paid by corporations authorized to do business under chapter 377 to any beneficiary under the policy. The appeals court affirmed the bankruptcy court's ruling that these statutes did not apply to debtor's annuity. In particular, debtor

failed to demonstrate that the insurance company that was paying debtor's annuity was a corporation "authorized to do business" as a stipulated premium insurance company or as an assessment plan insurance company. In light of this ruling, the appeals court declined to consider whether §§377.330 and 377.990 were even exemption statutes as defined under the *Benn* decision.

4. In addition, the appeals court affirmed the bankruptcy court's holding that §§ 513.430.1(7), 377.330, and 377.990 apply only to insurance policies and not annuities, and debtor's annuity was not insurance.

ii. The bankruptcy court has also held that the final $10,000 payment from a structured settlement agreement was not exempt under § 513.430(10)(e) as an annuity on account of a disability. *In re Kuhrts*, 405 B.R. 333 (Bankr. W.D. Mo. May 20, 2009). Mo. Rev. Stat. 513.430(10)(e) makes exempt from attachment ". . . an annuity or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of such person and any dependent of such person. . . ." Courts define "disability" as meaning a "loss of earnings capacity" and not a "loss of bodily function." Citing *In re Bonuchi,* 322 B.R. 868 (Bankr. W.D. Mo. 2005), the Court explained that Missouri's disability exemption applied to a debtor who received monthly payments as a result of an injury at work. Debtor was injured in a non-work related motorcycle accident and had never been certified a disabled and had never received disability payments. Missouri's exemption statute covers annuities awarded for work-related injuries that cover lost earnings.

iii. In a pre-*Benn* decision, Judge Dow held that annuity payments as part of a settlement for job-related injury are not exempt under Missouri statute that allows exemption for workers' compensation

award payable to debtor. *In re Bonuchi*, 322 B.R. 868 (Bankr. W.D. Mo. 2005)

1. Debtor was injured on the job and filed a workers' compensation claim. Debtor also asserted tort claims against his employer. A settlement was reached and approved by the Missouri Department of Labor and Industrial Relations. Under the settlement, Debtor received an initial lump sum payment of $200,000, eight $10,000 payments in 2005 and 2006, and a $2,144.93 monthly annuity for life. The employer's insurance carrier purchased an annuity with debtor as payee. Debtor filed Chapter 7 and claimed the annuity and settlement amounts as exempt.
2. Workers' compensation portion of the annuity payments is not exempt under Mo. Rev. Stat. 287.260. This statute provides that "[t]he compensation payable under this chapter, whether or not it has been awarded or is due, shall not be assignable, shall be exempt from attachment, garnishment, and execution, . . ." Citing *SSM Health Care System v. Bartel*, 914 S.W. 2d 8 (Mo.Ct.Appl 1995), as case on point, the bankruptcy court held that Missouri's workers' compensation exemption statute protects only awards that are unliquidated and payable. In this case, "[o]nce the lump sum compensation was placed in the annuity it was liquidated and no longer 'payable' to Debtor, and Debtor was free to assign or transfer his interest in the payments. Thus, the amount placed in the annuity was no longer exempt pursuant to § 287.260." *Id.* at 872.
3. Accepting as true Debtor's assertion that settlement was a structured settlement, the annuity payments are not exempt under 513.427 and 407.1062. Debtor argued that 407.1062,

Missouri's structured Settlement statute, restricts the assignability of such settlements. Debtor then argued that property that is not assignable is not subject to attachment or execution pursuant to Missouri common law. Continuing with the argument, Debtor contended that the annuity was exempt under §513.427, which (under the then prevailing law) exempted property that is not subject to attachment or execution. The Court disagreed with Debtor's interpretation that Missouri's Structured Settlement Statute prohibited the assignment of such settlements. It noted that subject to court approval and other criteria, structured settlements are "clearly assignable under Mo.Rev.Stat. 407.1062. The Court thus denied Debtor's claimed exemption under Missouri's Structured Settlement Statute.

4. Still, the annuity payments could be exempt under § 513.430(10)(e) to the extent reasonably necessary for the support of the debtor and debtor's dependents. The court reserved that question for a future evidentiary hearing.
5. The trustee ultimately recovered the annuity payments except for $60,000 allotted to the Debtor.
6. Please note that *Bonuchi* was decided before *Benn*. After *Benn* the discussion regarding the Structured Settlement non-assignability issue would be unnecessary because *Benn* held that § 513.427 is not an exemption statute.

iv. *In re Cox*, 2009 WL 3754101 (Bankr. E.D. Mo. Nov. 4, 2009) (debtor established that monthly annuity payments were exempt under Mo. Rev. Stat. 513.430.1(10)(e) as payments on account of a work-related injury and death that were reasonably necessary for debtor's support).

1. Debtor received monthly annuity payments from a life insurance company based on a settlement with deceased

spouse's former employer. Debtor's spouse had passed away due to injuries suffered in a work-related accident. Debtor was the spouse's only dependent and his annual income was under $18,000. Debtor claimed the annuity payments as exempt under Mo.Rev.Stat. 513.430.1(10)(e), which provides that any payment under a death benefit plan or right to a participant account in any deferred compensation program, or annuity on account of illness, disability, death, to the extent necessary for the support of such person and any dependent of such person. The purpose of 513.430.1(10)(e) is to replace lost future earnings of a debtor, or a person on whom a debtor is dependent, related to employment. *See In re Stover*, 332 B.R. 400, 403 (Bankr. W.D. Mo. 2005). An annuity payment may be exempt to the extent reasonably necessary for the support of a debtor. Court allowed the exemption finding that the annuity was created to compensate debtor's deceased spouse (and her dependents) who had been injured on the job for lost future earnings and the annuity was reasonably necessary for Debtor's support.

v. *In re Stover,* 332 B.R. 400 (Bankr. W.D. Mo. 2005) (sustained chapter 13 trustee's objection to annuity purchased with proceeds of wrongful death settlement). Debtor received annuity through inheritance from his mother, who had taken out annuity after the death of her husband, Debtor's father. Debtor's claimed exemption was denied (1) because debtor failed to produce any evidence that debtor was dependent on father at time of his death when debtor was 31 years old; and (2) and the annuity was unrelated to employment, a precondition for applicability of the exemption under § 513.430.1(10).

vi. *In re Collett*, 253 B.R. 452 (Bankr. W.D. Mo. 2000) (inheritance received in form of an annuity is not exempt).

vii. *In re Hughes*, 318 B.R. 704 (Bankr. W.D. Mo. 2004) (remaining payments due under annuity issued by Metropolitan Life Insurance Company held to be not exempt) (J. Federman).

b. <u>Head of Household</u>

i. Mo. Rev. Stat. 513.440 allows each head of a family to exempt the amount of $1,250 plus $350.00 for each dependent under 21 years of age.

ii. Missouri decisions interpreting the phrase "head of household" adopt a broad view of the concept of "family." *In re Swigart*, 339 B.R. 724, 728 (Bankr. W.D. Mo. 2006).

iii. But the "head" of the family must in fact be supporting the household. *Murray v. Zuke*, 408 F.2d 483, 485-86 (8th Cir. 1969).

iv. Missouri precedents hold that relatives other than parents can assume the obligation of support and qualify has head of a family. *In re Arnold*, 193 B.R. 897, 901 (Bankr. W.D. Mo. 1996) (granting motion to quash administrative freeze placed on debtor's account by unsecured creditor and allowing head of household exemption in the amount of $1,850).

v. Missouri cases also demonstrate that one need not be a biological father of those in the household to qualify as head of household. *In re Arnold*, 193 B.R. at 902 (holding that debtor whose household consisted of himself, a new spouse and her three children – debtor's step-children – qualified for the head of household exemption.).

vi. Debtor's claim of head of household exemption was denied in *In re Swigart*, 339 B.R. 724 (Bankr. W.D. Mo. 2006) based on lack of evidence of Debtor's support of family. Debtor claimed to have supported his mother and unemployed 20-year old brother before and at the time of filing bankruptcy. The evidence showed that,

although the three had lived together, Debtor had never claimed his mother or brother as dependents on his tax return and did not assert head of household status on the return. Further, the three had ceased living together immediately after Debtor filed bankruptcy and they were no longer on speaking terms. The court concluded that the fact that the household disintegrated so quickly after the date of filing undermines the credibility of the contention that it was a stable family of the kind that should qualify the debtor for the head of family exemption.

vii. Debtor not entitled to claim head of household exemption for noncustodial child for whom he was not meeting his child support obligations on the date of filing bankruptcy. *In re Arnold*, 193 B.R. 897, 901 (Bankr. W.D. Mo. 1996)

viii. The head of household exemption may only be claimed by one person in each family. *In re Soper*, 258 B.R. 748 (Bankr. W.D. Mo. 2001). Court denied head of household exemption claimed by both husband and wife. Debtors had one minor child and both claimed the head of household exemption of $850 in an attempt to exempt their equity in a Jet Ski and outboard motor.

ix. *In re Thorpe*, 251 B.R. 723 (Bankr. W.D. Mo. 2000) (denying head of household exemption for debtor who had no children and had separated from his wife three months before filing bankruptcy).

c. <u>Homestead</u>

i. In Missouri, a debtor may exempt a homestead, which consists of a dwelling house and appurtenances, and the land used in connection therewith, up to the value of $15,000. Mo. Rev. Stat. 513.475(1)(2008).

ii. In order to claim the homestead exemption, the debtor must

1. occupy the qualified exemption property or
2. exhibit both an intent to occupy such property, and

3. have the ability to control or strongly influence the time of occupation.

iii. Intent to occupy the premises must be exhibited by both a declaration of such intent and overt acts in support of such intention.

iv. To show control over the time of occupation, the debtor must prove that such occupation is either imminent or reasonably close in time and is neither indefinite nor incapable of measurement. *In re Schissler*, 250 B.R. 697, 700 (Bankr. E.D. Mo. 2000); *In re Dennison*, 129 B.R. 609, 610 (Bankr. E.D.Mo. 1991); *In re Campbell*, 2009 WL 2762716 (Bankr. W.D. Mo. Aug. 25. 2009).

1. In *Campbell*, the court sustained the trustee's objection to a claimed homestead exemption in property in Pawhuska, Oklahoma, finding that debtors' planned to move to Oklahoma after son graduates from high school in two years is "far too tenuous" to qualify as an intent to occupy and not reasonably close in time to support a determination that debtors have sufficient control or influence over the timing of their occupation of the property.

v. Under Missouri law, the homestead exemption is to be liberally and broadly construed in favor of the debtor. *In re Robinson*, 75 B.R. 985 (Bankr. W.D. Mo. 1987) (avoiding judgment liens on approximately one-block area in Gravois Mills, Missouri, claimed as homestead on which is situated an operating bar, and closed motel and restaurant, where debtor makes his home in a storage room and kitchen. The court declined to avoid the judgment lien on a portion of the area that situated a post office, which produced monthly rental income to the debtor of $135.)

vi. Debtors unable to claim "dual" exemption of $1,000 for mobile home and $8,000 for homestead. *In re Thornton*, 269 B.R. 682 (Bankr. W.D. Mo. Nov. 19, 2001) (J. Federman). But court

allowed $8,000 exemption because the mobile home was sufficiently affixed to real estate for debtors to be allowed larger homestead exemption. *Compare, In re White*, 287 B.R. 232 (Bankr. E.D. 2002). Debtor could not claim Missouri homestead exemption in mobile home that had never been affixed to the real estate owned by debtor.

vii. Married couple living together cannot claim a homestead exemption in more than one home. *In re Soper,* 258 B.R. 748 (Bankr. W.D. Mo. 2001). Court sustained trustee's objection to Debtors who claimed homestead exemption in Sugar Creek, Missouri residence and their vacation cabin in Rocky Mont, Missouri. Debtors claimed the combined equity in both homes was less than the allowed homestead exemption and they spend a considerable amount of time at both homes. Their claimed exemption was denied because the Missouri homestead exemption statute speaks of the homestead in the singular and several Missouri court decisions support that interpretation.

viii. Allowance of the homestead exemption is typically fact-driven focusing on debtor's intent. *In re Mueller*, 2006 WL 4449685 (Bankr. W.D. Mo. Feb. 24, 2006). Court overruled trustee's objection to debtor's claim of homestead exemption in house in Fair Play, Missouri, finding that debtor occupied the house on the date of filing, intended to continue to occupy the home, and intended to improve the premises so his children could live there. Court's decision was fact-driven largely based on debtor's stated intent, as he had only periodically lived in the house before filing bankruptcy and the house was in such poor condition it was unsuitable for children to live there.

ix. Court allowed debtor to claim $15,000 homestead exemption in property located in Mississippi, even though debtor had moved from the property in 1996. *In re Woodruft*, 2005 WL 1139891

(Bankr. W.D. Mo. Apr. 28, 2005). Debtor testified that the property had always been in the family, he considered it his only home, his mother had recently lived in the home, and he had been unable to return to the home due to his missionary assignments as an evangelist minister and his one-year convalescence from a back injury.

x. In *Woodruft*, the Court also considered whether the Missouri homestead exemption has extraterritorial effect. The Court concluded that Missouri statutes and case law are silent on the issue as to whether the Missouri homestead could be claimed on real estate located outside the state. In view of this silence, the Court applied the policy of liberally construing exemptions in favor of the debtor, and allowed $15,000 Missouri exemption on real estate located in Mississippi.

xi. *Compare, In re Adams* 375 B.R. 532 (Bankr. W.D. Mo. 2007) (denying debtor's claim of Florida exemption in real and personal property located in Missouri because Florida's exemptions are not applicable to property located outside of Florida); *In re Nickerson*, 375 B.R. 869 (Bankr. W.D. Mo. 2007) (denying claim of Kansas homestead exemption by debtor currently residing in Missouri because Kansas exemption law, as previously determined by the Kansas Supreme Court, has no effect in other states.)

d. <u>Earned Income Tax Credit</u>

i. On April 2, 2013, Judge Federman held in *In re Corbett*, Case No. 13-60042, that the earned income tax credit portion of debtor's 2012 income tax refund was exempt under § 513.4301(10)(a) of Missouri Revised Statutes. This is a change in law based on a 2012 amendment to § 513.430.1(10)(a). Previously, section 513.430.1(10)(a) permitted debtors to exempt payments received in the form of a "local public assistance benefit." Based on the restriction that the benefit had to be "local" for it to be exempt, the

court in *In re Goertz*, 202 B.R. 614 (Bankr. W.D. Mo. 1996) held that the portion of a federal tax refund attributable to the earned income tax credit was not exempt because it was a federal and not local public assistance benefit. In 2012, the Missouri statute was amended to remove the word "local." The statute now allows debtors to claim an exemption in such person's right to receive "a public assistance benefit." With removal of the "local" restriction from the statute, public assistance benefits paid by the federal government, including the earned income tax credit, are now included in § 513.430.1(10)(a) and may be claimed as exempt. *Id.* at 7.

ii. Judge Federman also rejected the trustee's argument in *Corbett* that an exemption was unavailable because neither the Missouri statute nor the Internal Revenue Code expressly refer to earned income tax credits as public assistance benefits. The Trustee argued that *Benn* requires an express designation of property as exempt. The Court did not read *Benn* to mean that every conceivable item of particular property must be specifically identified by name for it to fit within the exemption statutes. The Court held that if was sufficient for the statute to refer to a category of items as exempt. *Benn* does not "require that a particular item be specifically listed, so long as it reasonably fits within a listed category of 'exempt' items." *Id.* at 5-6.

e. <u>Missouri Public School Retirement System</u>

i. *In re Smith*, Case No. 10-60388 (Bankr. W.D. Mo. 2010). Court denied debtor's claimed exemption in his interest in a pension plan with the Missouri Public School Retirement System, which the debtor acquired as a result of his mother's death. Debtor claimed the pension interest exempt under Mo.Rev.Stat. 169.090, which provides that "[n]either the funds belonging to the retirement system nor any benefit accrued or accruing to any person under the

provisions of section 169.010 to 169.130 shall be subject to execution, garnishment, attachment or any other process whatsoever, nor shall they be assignable, . . .” Following *Benn*, the court held that the words not “subject to execution, garnishment, attachment” do not create an exemption. In order for property to be exempt in a bankruptcy case in Missouri, the Missouri legislature must have expressly declared such property to be exempt.

f. Motor Vehicles

i. Mo.Rev.Stat. 513.430.1 (5) allows a debtor to exempt from attachment and execution his interest in “any motor vehicles, not to exceed three thousand dollars in value in the aggregate.” This statute was amended in 2012 to clarify that a debtor could claim an exemption in more than one vehicle. The comments to the Senate provided that: “Currently any motor vehicle less than $3,000 in value is exempt from execution or attachment. The act requires that all motor vehicles owned by a debtor be considered together and only their aggregate value less than $3,000 shall be exempt.”

ii. Although the statute was also amended in 2003 in an attempt to address the issue whether more than one vehicle could be claimed as exempt, there remained litigation and confusion over the issue.

iii. The clarification codified by the 2012 amendment reflects the decisional law in the Western District of Missouri. In 2005, after reviewing the history of § 513.430.1(5), Judge Federman allowed a debtor to claim an exemption in more than one vehicle by his decision. *In re Bell,* 333 B.R. 839 (Bankr. W.D. Mo. 2005). The prior statute had been interpreted by courts to limit debtor’s exemption to only one motor vehicle. *See In re Hinckley*, 2005 WL 2371968 (Bankr. W.D. Mo. Sep. 7, 2005); *In re Struckhoff*, 231 B.R. 69 (Bankr. E.D. Mo. 1999). After the 2003 amendment, the Bankruptcy Court in the Eastern District reassessed the statute and

held that it could be applied to more than one vehicle. *In re Scott*, 332 B.R. 377 (Bankr. E.D. Mo. 2005). The court in *Scott* also relied on an interpretative provision of Missouri statutes that defined the "singular' in a statute to include the "plural." Thus, *Scott* held that § 513.430.1(5) is deemed to refer to "any motor vehicles" as well as "any motor vehicle." *In re Bell*, 333 B.R. at 841. While noting that "[i]t is not at all clear what the legislature intended in the 2003 amendment," Judge Federman in *Bell* followed the reasoning of *Scott* and overruled the trustee's objection to Debtor's exemption to more than one motor vehicle.

iv. Judge Federman held similarly in the case of *In re Urie*, 2006 WL 533514 (Bankr. W.D. Mo. Jan. 31, 2006) and allowed the Debtor's claimed exemption in two motor vehicles. But the court also allowed the trustee to liquidate one of the vehicles because there was still equity for the estate after allowance of the $3,000 exemption in the motor vehicles.

v. A motorcycle, but not a motorized bicycle, may be a motor vehicle under the exemption statute. *In re Lund*, No. 05-62219 (Bankr. W.D. Mo. Dec. 9, 2005). Court overruled trustee's objection to debtor's exemption of a 1979 Swiss Army Condor motorcycle as a "motor vehicle" under § 513.430(5). Trustee contended that the Condor was a "motorized bicycle," which would not be considered a vehicle under the exemption statute. The Court held that the Condor was capable of speeds exceeding 30 mph on level ground, which placed it within the statutory definition of a motor vehicle and not a motorized bicycle.

vi. Debtor must have an ownership interest in the motor vehicle to assert an exemption in the vehicle. *In re Thorpe*, 251 B.R. 723 (Bankr. W.D. Mo. 2000) (holding that estranged wife did not have an ownership interest in Harley Davidson Softtail motorcycle to

allow her to assert motor vehicle exemption when parties stipulated that husband was sole owner and wife's "marital property" rights under Mo. Rev. Stat. 452.330 for property acquired during the marriage was insufficient to create an interest cognizable in bankruptcy for purposes of determining the validity of a claimed exemption.)

vii. *In re Hicks*, 342 B.R. 596 (Bankr. W. D. Mo. 2006) (disallowed debtors' claimed exemption in value of equity in vehicle that trustee recovered through an avoidance action).

g. <u>Personal Injury Claims</u>

i. Relying on the Eighth Circuit Court of Appeals decision in *Benn*, Judge Federman has ruled that unliquidated personal injury claims are not exempt under Missouri law. *In re Mahony*, 374 B.R. 717 (Bankr. W.D. Mo. 2007). There is no specific Missouri or federal exemption statute for unliquidated personal injury claims. In light of *Benn*, the Debtor's cannot use § 513.427 or prior case law to claim an exemption in their unliquidated personal injury claims. The *Benn* decision is "very clear that, unless there is a specific Missouri statute, or a federal statute other than 522, providing an exemption in property, a Missouri debtor cannot claim an exemption in it."

ii. The *Mahony* decision was followed by the District Court in *Dylewski v. Amco Ins. Co.,* 2010 WL 1727870 (E.D. Mo. Apr. 29, 2010). The District Court for the Eastern District of Missouri dismissed plaintiff's personal injury claim against insurance company for lack of standing. Plaintiff had filed a chapter 7 bankruptcy and asserted that the personal injury claim was exempt under Mo. Rev. Stat. 513.427. The insurance company challenged the plaintiff-debtor's standing to assert the claim. Following *Benn*, and citing *Mahony*, the court held that plaintiff-debtor's personal

injury claim was not exempt and was property of the bankruptcy estate.

iii. The *Mahony* decision abrogates certain prior decisions, including: *In re Williams*, 293 B.R. 769 (Bankr. W.D. Mo. 2003) (Pending or potential causes of action arising out of personal injury tort are exempt in their entirety); *In re Wilkie* (Bankr. W.D. Mo. Jan. 22, 2004) (holding that legal malpractice claim is exempt under Missouri law because it is not assignable and therefore not subject to attachment or execution under 513.427); *compare, In re Searcy*, 193 B.R. 895, 986-97 (Bankr. W.D. Mo. 1996) (holding that proceeds of a personal injury settlement are not exempt under Missouri law).

iv. The bankruptcy court's holding in *Mahony* was questioned by the Missouri Court of Appeals in *Russell v. Healthmont of Missouri, LLC*, 348 B.R. 784 (Mo.App. W.D. 2011). In *Russell*, the appeals court reversed the circuit court's dismissal of plaintiff-debtor's declaratory judgment action seeking a declaration that he could exempt in bankruptcy an unliquidated personal injury claim. The circuit court dismissed the action citing *Benn* and *Mahony*. The appeals court held that the trial court "erred in relying upon federal cases interpreting a Missouri statute in a manner contrary to that of established Missouri case law. . . ." *Id*., at 788.

v. The *Russell* decision was commented upon by the Eighth Circuit Bankruptcy Appellate Panel in *Stanton v. Bryan*. While the Bryant court declined to consider whether certain Missouri statutes were exemption statutes, it noted that "the precedential effect of *Benn* on this Court was not affected by the *Russell* decision." *Id*., at *10.

vi. On September 21, 2012, in the case of *In re Abdul-Rahim*, 477 B.R. 747 (8th Cir. B.A.P. 2012) the Bankruptcy Appellate Panel for the Eight Circuit Court of appeals affirmed a holding that neither

Missouri's common law nor Mo. Rev. Stat. 513.237 created an exemption for an unliquidated personal injury claim. *See In re Abdul-Rahim*, 472 B.R. 904 (Bankr. E.D. Mo. 2012). The bankruptcy court in *Abdul-Rahim* expressly declined to follow the ruling in *Russell*; the BAP decision affirming the bankruptcy court did not mention *Russell* but cited *Benn* as binding precedent on the issue that a personal injury claim is not exempt in Missouri.

vii. The *Abdul-Rahim* decision was appealed and is now under submission with the Eighth Circuit Court of Appeals.

h. Retirement Plans

i. Civil Service Retirement Account. *In re Anderson*, 410 B.R. 289 (Bankr. W.D. Mo. 2009) (Debtors' proceeds from their civil service retirement retained their exempt status after they were paid to debtors and placed in their bank account).

ii. Inherited IRAs. The Eighth Circuit Bankruptcy Appellate Panel has held that funds received by a debtor from an IRA by inheritance are exempt retirement funds under 11 U.S.C. § 522(d)(12). *In re Nessa*, 426 B.R. 312 (8th Cir. B.A.P. 2010). Section 522(d)(12) exempts from creditor's claims any "retirement funds to the extent that those funds are in a fund or account that is exempt from taxation" under the Income Tax Code. The Fifth Circuit Court of Appeals agreed with *Nessa* and held that inherited IRA funds are exempt under § 522(d)(12). *In re Chilton*, 674 F.3d 486 (5th Cir. 2012). On April 23, 2013, the Seventh Circuit held that an inherited IRA is not exempt, thus creating a split in the circuits. *In the Matter of Clark*, __F.3d __, 2013 WL 1729600 (7th Cir. April 23, 2013). The court concluded that once the funds from the IRA are distributed to the beneficiary via inheritance they are no longer retirement funds. "To treat this account as exempt . . . would be to shelter from creditors a pot of money that can be freely used for current consumption." *Id.* at *2.

i. Tenancy by the Entireties

i. Tenancy by the entireties is a form of property ownership created by marriage in which each spouse owns the entire property rather than a share or divisible part and thus at the death of one spouse, the surviving spouse continues to hold title to the property. *In re Eads*, 307 B.R. 219 (Bankr. W.D. Mo. 2004).

ii. The result in titling property as a tenancy by the entirety is that creditors find it difficult, if not impossible, to reach one spouse's interest in the property when the other spouse did not consent to the creation of the underlying debt. Stated differently, a creditor may only seek satisfaction from entireties property if the spouses have acted jointly to burden the property, and in the absence of joint action, the property is exempt from attachment from execution. In bankruptcy, the effect of holding a joint obligation is important because that creditor has the right to be paid from the proceeds of entireties property; the pool of available funds for individual creditors is generally much smaller. *Id.*

iii. In Missouri, all property acquired by a married couple during the marriage is presumed to be entireties property, unless the transaction specifies otherwise.

iv. Under the Bankruptcy Act before 1979, bankruptcy courts used their equitable powers to afford relief to creditors adversely effected by the entireties tenancy. This first occurred in the situation where only one spouse filed bankruptcy in an effort to defeat creditors with claims against both spouses. If one spouse's obligation under a joint debt was discharged in bankruptcy, the creditor would thereafter be unable to execute upon entireties property even if the creditor was successful in obtaining judgment against the non-filing spouse. With this tactic, the married couple would in effect gain protection of their entireties property from joint creditors for the price of one bankruptcy. This result was

considered inequitable because, under the Bankruptcy Act, the debtor's interest in entireties property was not included in the bankruptcy estate when only one spouse filed. *See In re Wetteroff*, 453 F.2d 544, 546 (8th Cir. 1972), *reh'g and reh'g enbanc denied*, Feb. 2, 1972). Thus, there was no way for the trustee to administer the debtor's interest in the entireties asset even for the benefit of joint creditors that would be entitled to execute upon entireties property in state court.

v. To prevent this anomalous result, which one court described as "legal fraud," bankruptcy courts invoked their equitable powers. In *Rensenhouse Electric Supply Co. v. Magee* (In re Magee), 415 F. Supp. 521 (W.D. Mo. 1976), the district court affirmed the bankruptcy court's order delaying the debtor's discharge and granting the creditor relief from the automatic stay so the creditor could pursue to judgment its joint claims against both the debtor and his non-filing spouse. The Court relied on a line of cases that fashioned this equitable remedy "to permit creditors to satisfy their debts out of their debtors' property properly subject to the payment of such debtor but not subject to bankruptcy liquidation and administration by reason of the peculiarities of state's property and exemptions laws." 415 F. Supp. at 527.

vi. Even after enactment of the Bankruptcy Code, which expressly authorizes inclusion in the bankruptcy estate of a debtor's interest in entireties property, courts exercised their equitable powers under the precedent of *Rensenhouse Electric* and similar decisions to delay a debtor's discharge and order relief from the stay to permit a joint creditor to proceed in state court to obtain judgment against both spouses to preserve its ability to reach the entireties property to satisfy the joint debt. *See Matter of Anderson*, 12 B.R. 483 (Bankr. W.D. Mo. 1981).

vii. Likewise, in *In re Johnson*, 132 B.R. 408 (Bankr. E.D. Mo. 1991), the bankruptcy court granted such relief to a bank creditor so it could seek judgment against the debtor and his non-filing spouse in state court on guarantees of a corporate debt. Noting that there was no "specific directive" in the Bankruptcy Code addressing the issue, the court held that the "appropriate remedy in these circumstances" was to allow the bank to satisfy its entirety claim "outside of the bankruptcy." "A debtor cannot be permitted to destroy a creditor's bargained for right to satisfy its claims based on entirety obligations, from entirety property, by subjecting only his or her individual interests" to the protections of the Bankruptcy Code.

viii. Even though the Bankruptcy Code provided that tenancy by the entireties property was part of the bankruptcy estate, some courts concluded that the unity principle – the legal fiction that the married couple is one entity -- precluded the trustee from administering entireties property when only one spouse filed because the property was owned by the marriage and each spouse had no individual interest that could be included in the estate. Each spouse's "indivisible interest" simply could not be dissected for purposes of bankruptcy distribution, even if joint creditors might suffer from this result.

ix. Judge Koger challenged the unity principle in *In re Townsend*, 72 B.R. 960 (Bankr. W.D. Mo. 1987) when he held that a debtor's entireties interest was available to the trustee for administration, even when the other spouse elected not to file bankruptcy, to the extent that there were joint debts which the trustee could satisfy by liquidation of the entireties property.

x. This issue was finally settled by the Eighth Circuit Court of Appeals in *Garner v. Strauss,* 952 F.2d 323 (8th Cir. 1991). The Circuit Court held that a debtor's interest in entireties property is

included in the bankruptcy estate when the debtor's spouse does not join in the bankruptcy petition. The district court had concluded that the unity principle precluded inclusion of entireties property in the bankruptcy estate when only one tenant filed. "The inevitable conclusion is that the bankrupt-debtor, without his wife, has no legal or equitable interest in property by the entirety, and thus the property cannot be included in the bankruptcy estate." *Garner v. Strauss*, 121 B.R. 356, 360 (W.D. Mo. 1990).

xi. In reversing, the Circuit Court relied upon the broad language of § 541 of the Bankruptcy Code, which provides that "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). Citing the section's plain meaning, Congressional intent that the bankruptcy estate be all encompassing, and the decisions of a majority of courts, the Circuit Court held that debtor's interest in certificates of stock owned with his non-filing spouse as tenants by the entirety were included in the bankruptcy estate.

xii. With its reversal, the court of appeals directed that one-half of the proceeds from the sale of the stock be paid to the non-filing spouse. The court noted that the stock had already been sold and converted to cash and therefore partition of the entireties property was not possible under § 363(j). It concluded that one-half the proceeds should be returned to Mrs. Garner without deduction for transactional costs as it was not equitable to penalize her because partition had not been attempted before the shares were liquidated.

xiii. The *Garner* decision's precedent of dividing entireties property has led to litigation on exactly how to do that. Courts have struggled with reconciling the legal fiction that two parties can own property indivisibility and the practical reality that some allocation of their ownership interest is necessary for the administration of one tenant's bankruptcy estate.

xiv. The Eighth Circuit amplified upon the *Garner* decision in the 1999 case of *Van Der Heide v. LaBarge* (In re Van Der Heide), 164 F.3d 1183 (8th Cir. 1999). Mr. Van Der Heide filed a voluntary Chapter 13 petition and filed a plan proposing total payment s to unsecured creditors of $2,858. Mrs. Van Der Heide, with whom the debtor owned a house as tenants by the entirety, did not file bankruptcy. 11 U.S.C. §1325(a)(4) required debtor to show that the proposed plan was in the best interests of creditors, or that creditors would receive at least as much as they would receive in a hypothetical chapter 7 liquidation. The debtor argued this requirement was satisfied by his agreement in the plan to pay in installments an amount equal to the value of his non-exempt equity in the residence. At trial on confirmation of the plan, it was agreed the entireties property would produce $24,495 in a hypothetical liquidation. The debtor urged that after deduction for his non-filing spouse's half and available homestead and other exemptions, only $2,347.50 remained for creditors. His proposed plan payments totaling $2,858 exceeded this amount and therefore satisfied the best interest's test. The trustee objected to the plan and argued that the entire $24,495, less allowed exemptions, be included in calculating the hypothetical liquidation. The bankruptcy court agreed with the trustee, denied confirmation of debtor's plan, and ultimately dismissed the case when debtor failed to file an amended plan.

xv. The Bankruptcy Appellate Panel affirmed the bankruptcy court concluding that the debtor owned an indivisible interest in the residence and because it was subject to the bankruptcy estate, all of the sale proceeds be included in the hypothetical best-interests calculation.

xvi. The Eighth Circuit reversed holding that one-half of the hypothetical sale proceeds, less allowed exemptions, are subject to

the bankruptcy estate. The court explained it was applying, as it did in *Garner*, "an equitable rule that preserves the balance of the breadth of federal bankruptcy and state property law." 1185. The court, however, was disturbed by the result if the *Garner* analysis was applied blindly. Garner created a shield to "protect the nonfiling spouse's interest in entireties property from joint creditors." 164 F.3d at 1186. Mr. Van Der Heide, however, was using *Garner* as a sword by attempting to discharge his share of the $23,180 joint debt by paying only $2,858. Moreover, the estate's only asset was the equity in the residence, thus upon discharge, joint creditors could no longer seek recovery from the entireties property by pursing Mrs. Van Der Heide. For the price of one discharge and the payment of a faction of the joint debt, debtor -- and his non-filing spouse -- would have freed the entireties property, which contained substantial equity, from the reach of joint creditors.

xvii. Noting that "there can be no doubt as to the federal interest in preventing debtors from exploiting this tension between bankruptcy and state property law," the court held that the debtor would be entitled to claim only one-half of the $8,000 homestead exemption, increasing the amount available to creditors by $4,000, if he invoked *Garner* for confirmation of his plan. *Id.*

xviii. In the case of *In re Brown*, 234 B.R. 907 (Bankr. W.D. Mo. 1999), Judge Federman provided guidance on the issue of who gets paid from liquidation of entireties property. The court considered which creditors could share in the proceeds of the trustee's sale of farm land owned by the debtors as tenants by the entirety. Debtors originally filed a chapter 11 case, which was converted to chapter 7 after they were unable to obtain confirmation of a plan. In the chapter 7 proceeding, the trustee sold debtors' farm land for $300,000. Debtors asked the court to direct the trustee to pay only

their joint debts of $72,228.28 from the sale proceeds and to return the balance to them, asserting that the monies were exempt as the proceeds of entireties property.

xix. The trustee and a creditor of Mr. Brown objected arguing that debtors had waived their entireties exemption when they delayed seven months after the sale to claim the exemption, consented to severance of their entireties tenancy by filing a joint bankruptcy petition, consented to payment of all debts when they had proposed in their unsuccessful plan to sell the farm property and use the proceeds to pay all creditors without regard to whether the debts were owed jointly or by only one of the debtors, and had failed to correctly list the joint debt on their schedules. Both the trustee and creditor argued that it was inequitable for the debtors to a part of the sale proceeds while discharging the debts of the individual creditors.

xx. Explaining that a person's liability on a debt is a matter of law and cannot be altered by how the debt is listed on the bankruptcy schedules, the court allowed debtors to file an amended exemption schedule to claim the entireties property, and found no intentional relinquishment of their right to claim an exemption either by misclassifying the debts on their schedules or by the filing of the joint voluntary bankruptcy petition. Since their plan was not been confirmed, the court concluded they were not bound by its terms that required payment of all creditors. The court ordered the proceeds from the sale of the entireties property first paid to joint creditors with the balance paid to the debtors. 234 B.R. at 914.

xxi. Likewise, in the case of *In re Eads*, 271 B.R. 371 (Bankr. W.D. Mo. 2002), Judge Venters decided how to distribute the proceeds from the trustee's sale of the former residence of the debtor and his non-filing spouse, who were getting divorced. Citing *Van Der Heide*, the court ruled each spouse was entitled to one-half of the

proceeds less mortgage encumbrances and ordinary costs of sale. The debtor's portion then came into the estate for the limited purpose of paying allowed joint claims. Any balance left after payment of the joint debt and costs of administration would be returned to the debtor.

xxii. The court allowed the trustee to sell the property under §363 (h), which permits a trustee's sale of both the debtor's interest and a co-owner's interest in property provided certain conditions are met, including a finding that the partition of the property is not practicable. In such sales, §363(j) provides the framework for the distribution of the proceeds to the non-filing co-owner. The sale proceeds must be distributed "according to the interests of the spouse or co-owner, and of the estate," less the costs and expenses of the sale, not including the trustee's compensation. Determination of the respective interests of the non-filing spouse and the debtor are controlled by the decisions of *Garner* and *Van Der Heide*.

xxiii. The rule that only creditors of both tenants can share in distribution from entireties property can invite manipulation of claims. Judge Koger tried to discourage such actions in the case of *In re Renfro*, 234 B.R. 97 (Bankr. W.D. Mo. 1999). In *Renfro*, debtor elected to reaffirm his one joint unsecured debt to avoid the trustee's liquidation of entireties assets. Debtor claimed as exempt over $67,000 of equity in a homestead and $4,000 of equity in several vehicles, all of which he owned with his non-filing spouse. The trustee filed an objection to the claimed exemption, asserting that he was entitled to administer debtor's interest in the entireties assets to recover sufficient money to pay debtor's scheduled joint debt. Besides an $18,545 mortgage debt, Debtor had scheduled a $5,754 credit card debt as a joint liability. In response to the trustee's objection, the debtor proposed to reaffirm the credit card

debt, thus leaving no joint debts for the trustee to pay with entireties property. The trustee countered that the debtor could later rescind the reaffirmation agreement under §524(c) when the trustee would no longer be able to recover assets to pay the debt. The court denied the trustee's objection and held the case open until the 60 day period for rescission of the reaffirmation had expired to ensure that the debtor finalized his commitment to repay the joint debt outside of bankruptcy. At the end of the day, debtor was able to discharge $35,000 of his individual unsecured debt and retain assets with equity valued at over $71,000 in exchange for reaffirmation of a $5,754 debt. Without the reaffirmation, the trustee arguably could have forced the sale of the homestead and/or vehicles to pay in full with interest the one unsecured joint debt.

xxiv. In the context of federal tax law, the United States Supreme identified a situation where the entireties estate was divisible. The Court held that each entireties tenant possessed sufficient individual rights in the entireties estate to constitute "property" or rights to property" under 26 U.S.C. 6321 for attachment of a federal tax lien for unpaid taxes of only one tenant. *U.S. v. Craft*, 122 S.Ct. 1414 (2002).

j. <u>Tools of the Trade</u>

i. Missouri statutes allow a debtor to exempt from attachment and execution a person's interest in "any implements or professional books or tools of the trade of such person or the trade of a dependent of such person not to exceed three thousand dollars in value in the aggregate;" Mo.Rev.Stat. 513.430.1(4) (August 28, 2011)

ii. Test is whether the item claimed exempt as a tool of the trade is reasonably necessary to the debtor's trade or business. *Production*

Credit Association of St. Cloud v. LaFond (In re LaFond), 791 F.2d 623 (8th Cir. 1986).

iii. Large items of farm equipment may be considered tools of the trade and exempt to bankruptcy debtors who are farmers. *Id.* Affirming judgment that farmer debtor's tractor, plow, wagon and silage box, and other farm implements were exempt as tools of the trade as being reasonably necessary for the debtor to continue with his farming operation.

iv. Animals may be considered "tools of the trade." *In re Gray*, No. 03-62330 (Bankr. W.D. Mo. Dec. 16, 2003) (J. Federman). Four horses and four heifers were held to be tools of the trade. Debtor used the horses and heifers to give riding lessons and teach roping and penning to rodeo participants.

v. Vehicles may be considered "tools of the trade." *In re Baker*, 139 B.R. 468-471 (Bankr. W.D. Mo. 1992) (van used by debtors in the business of transporting passengers was a tool of the trade for lien avoidance purposes).

k. <u>Wages</u>

i. Before *Benn*, Mo. Rev. Stat. 525.030 was considered an exemption statute. Section 525.030 exempts from garnishment 90 percent (for a head of household; 25 percent for others) of a debtor's "earnings." Earnings are defined in the statute as "compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus, or otherwise. . . ." Applying 525.030 as an exemption statute, money in a bank account at the time of filing bankruptcy was declared exempt because it was traceable to wages paid as severance. *See In re Garst*, No. 09-30655 (Bankr. W.D. Mo. Dec. 22, 2009); *In re Arnold III*, 193 B.R. 897 (Bankr. W. D. Mo. 1996).

ii. Citing *Benn*, Judge Surratt-States held that § 525.030 is not an exemption statute. *In re Parsons*, 437 B.R. 854 (Bankr. E.D. Mo.

2010). The court sustained the trustee's objection to a claim of exemption under § 525.030(2) to 90 percent of $1,300.04 held in debtor's checking account. The Court explained that §525.030 does not explicitly identify property that judgment debtors can keep away from creditors for reasons of public policy. Instead, the purpose of §525.030 is to regulate enforcement of garnishment orders. "While true, the Missouri Garnishment Statute was used as an exemption statute in times past, in light of the holding in *In re Benn*, this can no longer be the case." *Id*. at 858.

iii. *Compare, In re Hidy*, 364 B.R. 679 (Bankr. W.D. Mo. 2007) (unused sick and vacation benefits paid after debtor was terminated from employment were "earnings" and therefore exempt under 525.030(2)). In *Hidy*, the Court did not consider, as the Court did in *Parsons*, whether §525.030(2) should be considered an "exemption" statute in light of *Benn*.

iv. *Compare, In re James,* 332 B.R. 397 (Bankr. W.D. Mo. 2005) (In pre-*Benn* decision, the court held that life insurance renewals were in the nature of compensation for personal services, which debtor could exempt under Missouri "earnings" exemption).

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BRIEF OVERVIEW OF KANSAS HOMESTEAD EXEMPTION LAWS AND THEIR INTERRELATIONSHIP WITH 11 U.S.C. §522(m) AND 11 U.S.C. §522(p)

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I. Kansas Opt Out Federal Bankruptcy Exemption Scheme

In Re Hodes 402 F.3d 1005 (10th Cir. 2005) (""Kansas has opted out of the federal exemption scheme thus limiting the debtor to exemptions available under Kansas law.") Citing 11 U.S.C. §522(b)(1)

Therefore, look to applicable Kansas State Law on exemptions first, then consider federal exemptions:

In Re Lampe, 331 F.3d 750, 754 (10th Cir. 2003) ("Upon filing a bankruptcy petition, the debtor's property becomes property of the bankruptcy estate subject to exemptions listed in 11 U.S.C. §522. See 11 U.S.C. §§522 & 541. Section 522(b) specifies the debtor can take the exemptions enumerated in §522(d) unless applicable state laws specifically provides otherwise. Kansas has opted out of the federal plan, and has enacted in its own set of exemptions.")

II. Broad Standard Qualifications for Exemptions Under Kansas Law

In *Nohinek v. Logsdon*, 6 Kan. App. 2d 342, 624 P.2d 257 (1986) the trial court initially granted a ruling finding all household furnishings exempt regardless of their value or necessity. On appeal, the Court held that under K.S.A. 60-2304(1) the exempt goods were only those household furnishings that were "reasonably necessary to a debtor's custom or standard of living."

> "An exemption is granted by law to a debtor to retain a portion of his property free from judicial seizure and sale by his creditors. It is a privilege granted by the state to secure to an unfortunate debtor and his family the means to avoid destitution. This right to hold one's property, or any part of it, free and clear from the claims of creditors

> is not a common law right, but a creation of constitutions and statutes. Therefore, a state has the power, within constitutional limits, to declare what property shall be exempt from the claims of creditors."

See also Ortiz v. Rajala, 436 B.R. 133 (D. Kan. 2010) (the debtor attempted to claim as exempt under 11 U.S.C. §522(d)(10)(E) an annuity for wrongful death settlement. The district court, on appeal, concluded that 11 U.S.C. §522(d)(10) only applies to a pension, profit sharing, or similar plan intended to replace wages lost upon retirement disability or the death of a wager, not a wrongful death settlement annuity. Exemption denied.);

In *In Re Dittmar*, 2011 Bankr. LEXIS 1210 (Bankr. Kan. March 30, 2011) the tortured history of the Boeing/Spirit bonuses or stock appreciation rights was exempt under K.S.A. 60-2310. The Court liberally construed K.S.A. 60-2310 finding earnings was a broader definition that wages in K.S.A. 44-313(c). The history of this issue was that the stock appreciation rights were previously determined by a Bankruptcy Court to be "not sufficiently rooted in the pre-bankruptcy past to be property of the debtor's bankruptcy estate." *In Re Lowe, et al.*, 380 B.R. 251 (Bankr. D. Kan. 2007).

Upon an adverse ruling in the bankruptcy court, the trustee appealed to the Bankruptcy Appellate Panel, which affirmed the trustee. *In Re Dittmar,* 410 B.R. 71 (10th Cir. BAP 2009).

Upon further appeal, the 10th Circuit reversed the BAP without remanding. See *Parks v. Dittmar,* 618 F.3d 1199 (10th Cir. 2010).

Thus, the Circuit's decisions effectively operated as an order granting the trustee's prior turnover motion of the stock appreciation rights. In response to that mandate, Dittmar amended his schedules B and C to claim the stock appreciation as property of the estate and to exempt them as exempt compensation under K.S.A. 60-2310. The Bankruptcy Court's decision in *In Re Dittmar,* 211 B.R. 11210, determined that they were, in fact, compensation. There is no subsequent appellate history on the issue.

III. Evidentiary Burden For Challenge to Exemption

The objecting party has the burden of proof upon objection to a claimed exemption by a preponderance of evidence that the exemption was improper. *In Re Hodes*, 403 F.3d 1005, 1010 (10th Cir. 2000). *See also In Re Dittmar*, 2011 Bankr. LEXIS 1210 (Bankr. Kan. March 20, 2011).

Once a standard is satisfied, the burden shifts back to the debtors to come forward with evidence to demonstrate that the claimed exemption is proper. *In Re Hall*, 352 B.R. 722 (Bankr. Kan. 2008). *See also In Re Robinson* (10th Cir. BAP 2003) (Oklahoma Case).

IV. Survey of Historical Example of Kansas Homestead Issues

Under K.S.A. 60-2301, the following requirements are necessary:

1. One acre within the city;
2. One hundred sixty acres of farming ground – interpreted as capable of being farmed.

Historical examples:

Hoffman v. Hill, 47 Kan. 611, 28 P. 623 (1892) exemption allowed for two adjoining lots where a building was erected on one lot with a porch extending over to the second lot. The building was used as both a residence for the debtor's family and a hotel and boarding house. The debtor also maintained a separate building on the second lot that was used in connection with the family hotel and boarding house, along with other out buildings that were located on both lots.

Layson v. Grange, 47 Kan. 440, 29 P. 585 (1892) three lots together that were less than one acre and also contained a separate carpenter shop that had been converted to rooms that were rented out – entire tract of land exempt.

Iola Wholesale Grocery Co. v. Johnson, 114 Kan. 89, 216 P. 828 (1923) two lots that total less than one acre qualified as a homestead on the entire tract even though the owner resided in a separate home and also operated a grocery store in a separate building on the property.

Barten v. Martin, 133 Kan. 329, 299 P. 614 (1931) tract of ground included home and a separate building that was rented out to a dentist – entire tract exempt. The renting and use of a building as a dental office, together with the ground beneath it, did not show an intention by the debtor to abandon the property as a homestead and the use to which it was in connection with the rest of the premises was not inconsistent with the homestead character of the property.

More recently, *In Re McBratney*, 2007 Bankr. LEXIS 3048 (Bankr. D. Kan. 2007) debtor resides in one side of duplex while leasing out the other half – entitled to claim as exempt entire structure (both sides). *See also In Re McCambry*, 327 B.R. 469 (D. Kan. 2005) (same result).

See In Re Springmann, 328 B.R. 251 (Bankr. D.C. 2005) analyzing exemption claims for debtor's homestead where there are income producing attributes from tenants or businesses conducted within the homestead.

In Re Sawyer, 403 B.R. 722, 730 (Bankr. D. Kan. 2009) married debtors who separated shortly before filing bankruptcy could not each claim as exempt one acre residences in separate Kansas cities.

Commerce Bank of Kansas City v. O'Dell, 16 Kan. App. 2d, 704, 827 P.2d 1205 (1992) joint debtors could claim exempt their entire interest in only one homestead exemption of 160 acres. Thus, joint tenants in a 240 acre tract could not each claim one-half of the tract exempt, only each co-tenant's interest in the 160 acres could be claimed as exempt.

See also *Nelson v. Stocking*, 154 Kan. 676, 121 P.2d 1215 (1942) the debtor with one fourth interest in 281 acres may only claim as exempt 160 acres.

But see *In Re Hall*, 395 B.R. 722 (Bankr. D. Kan. 2008) married debtors jointly owned 1.33 acre tract of ground within the city limits. Two structures were located on the tract, a house occupied by the wife and children and a mobile home occupied by the husband. The husband had lived apart from his wife for two years prior to the filing of the bankruptcy. He lived in the mobile home because of the finding of child abuse that prohibited him from residing with the family. Evidence established that the debtors had intended to live in these two separate residences on a permanent basis. Special facts limited to the case.

Historical precedent*, Atchison Savings Bank v. Wheeler's Administrator*, 20 Kan. 625, 878 – the law does not recognize two homesteads for one family.

V. Extra Territorial Effect of Kansas Exemption

The Kansas Supreme Court has historically ruled that Kansas exemptions have no extra territorial enforcement right. *See B. & M.R. Railroad Co. v. Thompson*, 31 Kan. 180, 1 P. 622 (1884); *C.F. Kansas City S.J. & C.B.R. Co. v. Gough*, 35 Kan. 1, 10 P. 89 (1886). *See State v. Holcomb*, 85 Kan. 178, 181, 116 P. 215 (1911) ("a state is sovereign only within its boundaries, and its laws have no extraterritorial force.")

More recently, in *In Re Ginther*, 282 B.R. 16 (Bankr. Kan. 2002) Judge Nugent determined that Chapter 7 debtors who filed a bankruptcy in Kansas after receiving the proceeds of sale of their Kansas homestead intending to use the proceeds to purchase a home in Colorado were not able to avail themselves with the Kansas homestead law, as the Kansas homestead law had no extraterritorial effect. In *Ginther*, the debtors sold their home in Atwood, Kansas, held the proceeds at the time of the filing of the bankruptcy, claimed the proceeds as exempt claiming they sought to use the proceeds to purchase a Colorado homestead.

Ginther cites historical precedence of *First National Bank v. Dempsey*, 135 Kan. 608, 609; 11 P.2d 735, 736 (1932) that the proceeds of a Kansas homestead intended for reinvestment in another homestead within the state of Kansas are exempt from execution or garnishment. *See also In Re Daniel*, 65 B.R. 703 (Bankr. D. Kan. 1986) (proceeds from an involuntary sale of the homestead are exempt if the debtor intended to purchase another homestead with the proceeds).

But see In Re Sipka, 149 B.R. 181 (D. Kan. 1992) refusing to exempt under Kansas law the proceeds of an involuntary sale of a Michigan residence by Kansas residents.

See also In Re Peters, 91 B.R. 401 (Bankr. W.D. Tex. 1988) holding that Texas homestead exemption, which is limited by statutes to homesteads in the state, was not available to out of state residents.

But see In Re Tanzi, 287 B.R. 557 (Bankr. W.D. Wash. 2002) holding that neither Washington nor California exemptions apply to the debtor's Florida residence and *In Re Stratton*, 269 B.R. 716 (Bankr. Oregon 2001) upholding the debtor's claim of Oregon homestead exemption for property located in California.

See In Re Drenttel, 403 F.3d 611 (8th Cir. 2005) finding that the debtors' claim pursuant to Minnesota's homestead exemption laws, an exemption for an Arizona residence would be allowed the exemption. Shortly before they filed their bankruptcy petition, the debtors sold their Minnesota home and purchased an Arizona residence. The trustee objected when they claimed that residence pursuant to Minnesota's homestead exemption laws. It noted that 11 U.S.C. §522(b)(2)(A) permitted the debtors' to exempt homestead property under the laws in the state where they filed their petition. It rejected the trustee's suggestions that choice of law applies holding that 11 U.S.C. §522(b)(2)(A) clearly designates which state laws were applicable.

VI. The Intersection with 11 U.S.C. §522

Two Relevant Sections:

11 U.S.C. §522(m)(1):

> "(m) Subject to the limitations in subsection (b), this section shall apply separately with respect to each debtor in a joint case.
>
> (p)(1) Except as provided in paragraph (2) of this subsection in sections 544 and 548, as a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of interest that was acquired by the debtor during the 1215-day period preceding the date of the filing of the petition that exceeds in the aggregate $146,450[1] in value in –
>
> (A) real or personal property that the debtor or dependent of the debtor uses as a residence;…
>
> (D) real or personal property that the debtor or dependent of the debtor claims as a homestead.
>
> (2)(B) For purposes of paragraph (1), any amount of such interest does not include any interest transferred from a debtor's previous residence (which was acquired prior to the beginning of such 1215-day period) into the debtor's current principal residence, if the debtor's previous and current residences are located in the same State."

The Relationship of 522(m) with 522(p).

See In Re Rich, 2013 Bankr. LEXIS 1603 (Bankr. Kan. April 16, 2013). In *Rich*, the debtors acquired their homestead within 1215 days before filing a joint bankruptcy. To do so they used sale proceeds from their previous homestead

[1] Effective April 1, 2013, the dollar amount increased to $155,675 by the Judicial Conference of the United States for 2013.

along with funds from the husband's IRA savings and the proceeds of construction loans. As of the petition date the house was considered worth $509,500 encumbered by a $205,868 mortgage, leaving "equity" of $303,632. The trustee objected because the equity exceeded the $146,450 cap or maximum.

The Court ruled each party was entitled to apply separately the provisions of 11 U.S.C. §522(m) meeting the total exemption for the joint debtors.

See *In Re Nestlen*, 441 B.R. 135 (10th Cir. BAP 2010) allowing "stacking" of 522(p) exemption cap in an Oklahoma bankruptcy case. In *Nestlen*, the debtor failed to pay for landscaping. A state court judgment was taken and on the date of filing bankruptcy, $26,772.54 remained unpaid. Within 1215 days prior to the bankruptcy the debtors paid $180,886.18 balance on their loan and spent an additional $80,000.00 to $100,000.00 to repair and add improvements to the homestead. In *Nestlen*, the Court interpreted the phrase "interest that was acquired" which is subject to two interpretations:

1. the "equity view" – improvement of the equity or monetary interest, or
2. the "title view" - acquiring a title or ownership interest.

As noted by the Bankruptcy Appellate Panel in *Nestlen*:

> "The §522 cap is purely a federal concept. Moreover because Oklahoma protects every dollar of the value of the debtor's homestead, there is no reason why an Oklahoma legislature or court would ever address whether married couples could 'stack' or double the value of their homestead exemptions. Two times infinity is still

> infinity. Moreover, we cannot conceive any reason why joint debtors in different states should be subject to different federal caps, *i.e.* why Florida joint debtors possessing an otherwise unlimited homestead exemption should be entitled to exempt $273,750 of the value of their homestead in bankruptcy. Oklahoma joint debtors also possessing an otherwise unlimited exemption would be entitled to exempt and retain only $136,875 of the value of their home.
>
> For these reasons we conclude that state law does not govern whether this §522(p) cap is doubled by virtue of §522(m). As a potential diminution of an Oklahoma debtor's unlimited homestead exemption for bankruptcy purposes is imposed by federal law and not by Oklahoma law, whether §522(p) should be doubled for joint debtors is a question of federal law." 441 B.R. at 143

See also *Parks v. Anderson*, 406 B.R. 79 (D. Kan. 2009) determining that the phrase "any amount of interest that was acquired by the debtor during the 1215-day period preceding the date of filing" refers to an equity interest and not a title interest and reversed the Bankruptcy Court.

Hn. 6:

> "In the context of 11 U.S.C. §522(p), a debtor may acquire equity in one of three ways. The debtor may acquire equity by making a down payment, paying down a mortgage, or through appreciation due to market conditions. The first two require active conduct by a debtor, but the latter does not. The phrase 'by the debtor' is a restrictive clause modifying the term 'acquired,' which implies that more than a passive acquisition of equity was required to trigger the

> provision, such as the affirmative act of a mortgage pay down. The phrase 'aggregate of $125,000 in value,' implies that successive acquisitions of equity by the debtor are to be aggregated, further supporting the reasoning that 'interest' applies to equity and not to fee ownership."

In *In Re Long*, 470 B.R. 186 (Bankr. D. Kan. 2012) the Court construed the provisions of 11 U.S.C. §522(d)(3). The debtors, in *Long*, had not resided in Kansas for the 730 days preceding the petition date. Thus, under 11 U.S.C. §522(d)(3) the debtor was required to claim the exemptions allowed by the state she inhabited for the greater part of the 180 days preceding the 730 days before she filed the petition – in this case Nebraska.

The trustee argued that the Bankruptcy Code preempted Nebraska law that allowed only Nebraska residents to employ Nebraska exemptions. The Court found that the debtor could claim the exemptions under 11 U.S.C. §522(d) because her domicile state for exemption purposes had enacted an opt-out provision that only applied to persons filing bankruptcy in Nebraska, the debtor was prohibited from doing so by the venue provisions, the Bankruptcy Code, or the debtor could claim the federal exemptions as Nebraska law limited state exemptions to Nebraska residents, something she was not.[2] ("Congress did not intend to preempt state exemption laws when it enacted a statute that expressly provides for a state law to apply when the debtor chooses, and, indeed, to apply exclusively when the state opts out of the federal exemption scheme. This antithesis of preemption period nor is there a conflict with state law when §522(d) accommodates state law…. Determining what exemptions apply is almost

[2] Neb. Rev. Stat. §25-1552 allows "each natural person residing in this state" to exempt personal property valued at $2,500.00 other than wages.

entirely driven by state law, as are most other property ownership issues under the Bankruptcy Code.")

See also In re Townsend, 212 Bankr. LEXIS 149, 2012 W.L. 112995 (Bankr. D. Kan. Jan. 12, 2012) (Somers, J.) (Oklahoma opt out statute only restricts "natural person(s)" residing in this state from electing the section 522(d) scheme).

VII. Value of an Interest as Defined in 11 U.S.C. §522(o)(4)

In *In Re Willcut*, 472 B.R. 88, 212 Bankr. LEXIS 2341 (BAP 10th Cir. 2012) the Bankruptcy Appellate Court was called upon to construe §522(o)(4) which reads:

> "(4) [T]the value of an interest in… real or personal property that the debtor… claims as a homestead… shall be reduced to the extent that such value is attributable to any portion of any property the debtor disposed of in the 10-year period ending on the date of the filing of the petition with the intent to hinder, delay, or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the debtor had held the property so disposed of."

The Bankruptcy Appellate Panel determines that the phrase "value of an interest" is an economic interest, as opposed to a title interest.

The trustee filed an objection to the debtors' claim of exemption arguing that §522(o)(4) requires that approximately $100,000 that the debtors had applied from the auction of nonexempt property towards the purchase of the home was an attempt to defraud creditor and, thus, a conversion of nonexempt assets.

The Appellate Court overruled the trustee's objection to exemption finding that the home had a fair market value of $425,000 with a $415,000 mortgage against it, that there was no realizable equity interest in the property and that, therefore, the objection to exemption was effectively moot.

Willcut presents an interesting analysis of sister court decisions defining the phrase "interest in property" under 11 U.S.C. §522. Those courts holding a title definition in §522(p) include:

In Re Green, 583 F.3d 614, 624, 625 (9th Cir. 2009) filing a homestead claim for an underlying property interest does not fall within §522(p) because a homestead claim is not an ownership interest;

In Re Aroesty, 385 B.R. 1, 7 (1st Cir. BAP 2008) holding the debtor had previously held a beneficial interest in real property held in trust "an interest" under §522(p) when record title was received to the trust;

In Re Sinler, in §522(p) means title interest because of the phrase "interest that was acquired" implies actively acquiring title to property;

In Re Blair, 334 B.R. 374, 376-377 (Bankr. N.D. Tex 2005) concluding that the plain meaning of "interest" in real property under §522(p) is the title to a home because "one does not actually 'acquire' equity in a home."

The Courts holding an equity definition when interpreting §522(o) and §522(p) include:

In Re Presto, 376 B.R. 544, 572 (Bankr. S.D. Tex 2007):

> "The [objecting party] bears the burden of establishing current market value in excess of the $521,800 purchase price in order to show by what amount the improvements made by the debtor actually increased the value of the Royal Rose property."

In Re Reinhard, 377 B.R. 315, 320 (Bankr. N.D. Fla. 2007) (deciding that "interest" refers to equity and not ownership under §522(p);

In Re Rasmussen, 349 B.R. 747, 756 (Bankr. N.D. Fla. 2006) (interpreting "interest" to mean acquisition of entity under §522(p)).

Kansas cases utilizing §522(o) include:

In Re Keck, 363 B.R. 193 (Bankr. D. Kan. 2007) the trustee contended that the value of cash advances from credit cards used to pay off a line of credit securing the debtor's home, along with cash advances totaling approximately $11,000 used to pay for a new driveway and patio, should be deducted from the amount of claimed exemption. The Court noted the elements necessary to succeed under 11 U.S.C. §522(o)(4):

1. That the debtor dispose of property within ten years preceding the filing of the bankruptcy petition;
2. That the proceeds from such disposition were used to increase the value of the debtor's homestead;
3. That the property disposed of was not self-exempt; and
4. In doing so, the debtor acted with actual intent to hinder, delay or defraud a creditor.

See also *In Re Agnew*, 355 B.R. 276 (Bankr. D. Kan. 2006), In *Agnew*, the Ford Motor Credit Company obtained a judgment on February 10, 2005. Other creditors took judgment around that same time. In September, 2005, the debtor met with his bankruptcy counsel. On October 5, 2005, the debtor acquired his homestead property in exchange for his undivided interest in a 720 acre tract of agricultural land and all of his farm equipment. The debtor's Statement of Financial Affairs disclosed the exchange. The debtor denied that the acquisition was motivated by his bankruptcy filing, which occurred five days later stating that family issues motivated the exchange. The Court found that the time of the exchange must have been influenced by the contemplated bankruptcy, but accepted the debtor's uncontradicted testimony as to the motivation for the exchange.

As noted by the Court:

> "[T]here is nothing in the… legislative history of BAPCPA to suggest that Congress intended to change the longtime standing policy of permitting intentional, but nonfraudulent conversion of nonexempt property to exempt property on the eve of filing. It expressly made the limitation in 522(o) applicable only to the extent of value attributable to actions intended to hinder, delay or defraud leading commentators state 'section 522 continues to adopt the position favorably viewed by the court that the mere conversion of nonexempt property into exempt property, without fraudulent intent, does not deprive the debtor of exemption rights in the converted property'." 355 B.R. at 283

See also In Re Carey, 938 F. Supp. 1073 (10th Cir. 1991):

> "The liquidation of… assets used to pay down the home mortgage occurred over a two year period and was in the open; the activity and payment appears to be consistent was what had been approved by Congress to take advantage of exemptions. [Debtor] fully disclosed all payments and transfers in her bankruptcy schedules and at the meeting of creditors. [Debtor] retained no beneficial interest in any converted property. She did not obtain credit to purchase exempt property. Under these circumstances we cannot find that the district court and bankruptcy court heard in finding that she did not intend to 'hinder, delay or defraud' her creditors or acted improperly in relation to her homestead." 938 F.2d at 1078 (Oklahoma)

Compare *In Re Agnew*, 355 B.R. 276 (Bankr. D. Kan. 2006) substantial evidence of pre-bankruptcy planning to pay down a mortgage on a homestead using nonexempt assets is not sufficient to deny discharge, as actions to hinder, delay or defraud creditors requires something more. In the 10th Circuit that something can be evidence by the following situations and actions as a basis to infer fraudulent intent:

1. Debtor conceals pre-bankruptcy conversion;
2. Debtor converts assets immediately before filing;
3. Debtor continues to use the transferred property;
4. The transfer is made to family members;
5. Debtor obtained credit in order to purchase exempt property;
6. The conversion occurred after the entry of a large judgment against the debtor;

7. Debtor has engaged in a pattern of sharp dealing prior to bankruptcy;
8. The conversion rendered the debtor insolvent.

The holding of *Keck* was criticized in *In Re Presto*, 376 B.R. 554 (Bankr. S.D. Tex 2007). In *Presto*, the debtor, after a judgment was entered against him in the amount of $2 million, sold his prior home and received net proceeds of over $675,000. The debtor used those proceeds to purchase his new home for $521,800. After purchasing the property, Presto spent over $119,000 on improvements to the property. His trustee challenged the exemption claim under 11 U.S.C. §522(o). The exemption claim was to the money spent for the value of the improvements. The Court in *Presto* held that unlike the decision in *Keck*, only the value "attributable" to the transfer was exempt, not the actual amount. Since the home value increased only $28,200 by the $119,000 payments made, the objection to exemption was for the between the difference between current market value and the original purchase price.

In *In Re Lakey*, 2010 Bankr. LEXIS 6270 (Bankr. D. Kan. October 4, 2010) *aff'd* 456 B.R. 687 (D. Kan. 2011), the Court denied an objection to exemption under 11 U.S.C. §522(o).

> "§522(o) imposes a new restriction on the homestead exemption. Congress meant to minimize abuse by debtors who padded their homestead exemptions instead of repaying creditors in the maximum amounts they could afford. Section 522(o) strikes a balance between debtors and creditors in states with unlimited homestead exemptions. Abusive pre-bankruptcy planning is still determined under the familiar 'intent to hinder, delay or defraud a creditor' standard and now there is a ten year look back period."

In *Lakey*, the Court found that the timing of the debtors' homestead acquisition did not show that the debtors padded their homestead value with hinder, delay or defraud of the creditor. The Court found that the debtors were already planning to move to Kansas in May, 2001, before the creditors signed their construction contract with the debtors' company or had undertaken substantial activity to move to Kansas at the time the dispute with the creditors arose. No evidence that the debtors mislead or deceive a creditor about the conversion of his assets. His bank was aware of the debtor's holdings pursuant to regularly updated credit memos. Although the debtor had converted "a very great amount of nonexempt property to exempt property" by liquidating certificates of deposit and selling two commercial properties, the debtor also maintained over $1 million of liquidity for years after his Kansas homestead acquisition. Two years after the dispute with his creditor and approximate five years before the filing of the bankruptcy, the debtor averaged $1.3 million in the bank, even after the purchase of the home. The acquisition of the Kansas homestead did not "subsume" more than half the debtor's net worth at the time.

RECENT 10TH CIRCUIT CASES

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I. Abandonment Under 11 U.S.C. §554 and Federal Rule of Bankruptcy Procedure 6007(a)

In Re Cook, 2013 U.S. App. LEXIS 6566 (10th Cir. April 2, 2013)

The trustee's notice of abandonment and report of no distribution did not satisfy 11 U.S.C. §554(a) or F.R.B.P. 6007(a) because notice and request for a hearing was not provided. The trustee did not abandon any claims or causes of action. Affirming the decision of the Bankruptcy Appellate Panel in *In Re Cook*, 2012 Bankr. LEXIS 1764 (B.A.P. 10th Cir. April 19, 2012).

> "Abandonment is possible only after notice and hearing. 11 U.S.C. §554(a) The purpose of the notice is to provide an opportunity for any potential opponent to the abandonment of such property to file objections and be heard by the court."

II. Exception for Discharge Under 11 U.S.C. §523(a)(4) Fraud or Defalcation While Acting in a Fiduciary Capacity

In Re Bratt, 489 B.R. 414 (Bankr. D. Kan. 2013) (Bratt #1)

Although a member of a limited liability company has general fiduciary duties under state law in favor of their fellow members, whether the individual is a fiduciary for the standard §523(a)(4) is a matter of federal law. Citing *Fowler Brothers v. Young*, 91 F.3d 1367, 1371 (10th Cir. 1996). The Court noted in *Bratt*:

> "[T]o find that a fiduciary relationship existed under §523(a)(4), the court must find that the money or property on which the debt at issue was based was entrusted to the debtor…. Thus, an express or technical trust must be present for a fiduciary

> relationship to exist under §523(a)(4)…. Neither a general fiduciary duty of confidence, trust, loyalty, and good faith…, nor an inequality between the parties' knowledge or bargaining power…, is sufficient to establish a fiduciary relationship for purposes of dischargeability…. Any trust relationship must be imposed by the law rather than implied from it. The Kansas Revised Limited Liability Company Act does not expressly create a trust relationship sufficient to impose liability under §523(a)(4)." 489 B.R. at 425-426

Compare *In Re Karr*, 442 B.R. 785 (Bankr. D. Kan. 2011) (relationship of a corporate officer to a corporation "commonly imposes a fiduciary relationship"). *See also In Re Cowley*, 35 B.R. 526 (Bankr. D. Kan. 1983) ("with respect to the first element [express or technical trust], it has long been settled that a corporate officer is a 'fiduciary' of the corporation in the meaning of section 523(a)(4)").

In Re Bratt, 491 B.R. 572 (Bankr. D. Kan. 2013) (Bratt #2)

In Bratt #2, the Court ruled on a motion for order amending judgment pursuant Federal Rule Civil Procedure 59(e) whether "conversion" constituted embezzlement as that term is defined in 11 U.S.C. §523(a)(4).

The Court found that the proof of conversion might support a nondischargeability claim if a "willful and malicious" injury existed pursuant to a finding under 11 U.S.C. §523(a)(6). There was no authority supporting plaintiff's claim that proof of conversion was tantamount to proof of embezzlement in the context of 11 U.S.C. §523(a)(4), nor were the elements of the tort of conversion under Kansas law the same as the elements of embezzlement under 11 U.S.C. §523(a)(4) because the tort of conversion did not require fraudulent content while embezzlement did.

Conversion under Kansas law is the unauthorized assumption and exercise of the right of ownership of personal property belonging to another to the exclusion of the other's property. The plaintiff must have a general property right in the converted property and a right to immediate possession of it. No fraudulent content on the part of converter is required, the intent required is simply to use or dispose the property.

Embezzlement as used in 11 U.S.C. §523(a)(4) as defined by federal law requires a showing that the debtor fraudulently appropriated money or property in which the debtor was entrusted or that lawfully found its way into the debtor's hands. Under Tenth Circuit precedent proof of embezzlement requires a fraud in fact or moral turpitude and intentional wrong.

III. Section 524 Post Discharge Issues

In Re Timmons, 2012 Bankr. LEXIS 4396 (Bankr. D. Kan. Sept. 24, 2012)

The Chapter 7 debtor filed a motion asking the Court to hold a creditor in contempt for violating the automatic stay or the discharge injunction when it allegedly accelerated her student loan debt based solely on her bankruptcy filing. The debtor also contended the creditor violated Kansas Statute 16a-5-109.

The Court ruled that the discharge injunction under 11 U.S.C. §524 did not apply to any debt that fell within 11 U.S.C. §523(a)(8). The Court's ruled its power under 11 U.S.C. §105(a) is not broad enough to authorize the Court to protect the debtor from creditor's post-discharge post-case collection action. The creditor allegedly accelerated the indebtedness solely because of the debtor's bankruptcy filing.

> "Nondischargeable debt are those types of debt such as taxes or child support payments, that Congress thought important

> enough to be paid in full, even if doing to impeded the debtor's ability to make a fresh start." Citing *United States v. White*, 466 F.3d 1241, 1247 (11th Cir. 2006) and *In Re DePaolo*, 45 F.3d 373 (10th Cir. 1995)

See also In Re Houlik, 481 B.R. 661; 2012 Bankr. LEXIS 5091 (10th Cir. BAP 2012) reversing *In Re Houlik*, 2011 Bankr. LEXIS 3632 (Bankr. D. Kan., Sept. 25, 2011).

In *Houlik*, the Bankruptcy Court had awarded minimal actual damages and punitive damages of $25,000 in favor of individual Chapter 11 debtors and against the vehicle finance company as a sanction for the wrongful repossession of a vehicle. The finance company had mistakenly believed the debtors had missed two monthly payments and repossessed the vehicle approximately one year after the confirmed Chapter 11 Plan revesting the vehicle in the debtors subject to the creditor's rights in the collateral.

Upon appeal, the Bankruptcy Appellate Panel ruled otherwise. The BAP ruled the debtors were not entitled to any alleged violation of the stay under 11 U.S.C. §362, as that right terminated upon confirmation of the Chapter 11 Plan. Further, because the debtors had sought an administrative closing of the case prior to discharge (presumably to avoid payment of the ongoing United States Trustee fees during the five year period post-confirmation), it was not entitled to utilize 11 U.S.C. §524(a)(2), the discharge injunction, since the case was closed without a discharge. 11 U.S.C. §524(i) was also not available to the debtors for the creditor's failure to properly credit the debtors' payment made under the Plan since the discharge injunction under 11 U.S.C. §524(a)(2) was not granted.

The Bankruptcy Appellate Panel also opined upon continuing Bankruptcy Court jurisdiction post-confirmation noting:

> "[I]t is generally accepted that a bankruptcy court's jurisdiction narrows to some extent after plan confirmation with respect to noncore proceedings and 'related to' jurisdiction." 481 B.R. at 675

The Appellate Court concluded that the Bankruptcy Court did not have post-confirmation 'related to' jurisdiction over the wrongful repossession action. Even though the action was brought by the debtors, the action affects neither an integral aspect of the bankruptcy process, nor the interpretation, implementation, consummation, execution or administration of the confirmed Plan. The Appellate Court concluded that although there was not a bankruptcy remedy, there was a state court remedy.

Pursuant to 11 U.S.C. §1141(a), after confirmation of a Plan, the debtors and creditors are bound by the provisions thereof. The Bankruptcy Court's jurisdiction is not derived from provisions of the Bankruptcy Code, and is instead confined solely to proceedings described in Title 28 of the United States Code. In other words, §§105, 1141, and 1142 of the Bankruptcy Code do not provide an independent basis for jurisdiction.

IV. Reaffirmation Issues

In Re Rowe, 342 B.R. 341 (Bankr. D. Kan. 2006)

When a consumer debtor is current on payments the Kansas court may find default under the Kansas Uniform Consumer Credit Code, K.S.A. 16a-1-101 *et seq.*, only when the circumstances evidence "significant impairment." Therefore, although BAPCPA eliminated the "ride through" option under 11 U.S.C. §521 and 11 U.S.C. §362, now there are consequences for failing to obtain a right of continued possession through redemption reaffirmation as applied to consumer transactions. In Kansas, the creditor's remedy upon termination of the stay under 11 U.S.C. §362 may be illusory because the

conditions to declare a default and obtain possession of the collateral will not be present under Kansas law when the debtor remains current on the obligation and there is no other basis for significant impairment.

But see Paul v. Ford Motor Credit Company, LLC, 292 Kan. 176, 254 P.3d 526 (2011) (a significant impairment under K.S.A. 16a-5-109(2) may be created by the debtor's actions and inactions which endanger the prospect of a continuing relationship with the creditor, even though the debtor may be current on the note payments).

In *Paul*, the debtor filed a Chapter 7 bankruptcy, but the debtor failed to reaffirm its debt to Ford Motor Credit Company. After discharge, the debtor continued to make the required monthly payments. Despite the continued payments, which were current, and the fact that the debtor maintained the required insurance and kept the truck in good condition, Ford attempted to repossess the truck. The debtor filed a petition alleging violations of the Kansas Consumer Protection Act and violations of the Kansas Uniform Consumer Credit Code, K.S.A. 16a-5-109. The trial court made the specific findings that significant impairment existed, including:

1. Plaintiff's filing a Chapter 7 petition for bankruptcy;
2. The discharge in bankruptcy of plaintiff's debt and other duties and obligations owed to the defendant under its finance contract with Ford;
3. The debtor's refusal to reaffirm its personal obligations under the contract, which would have cured the prospective default occurring as a result of the bankruptcy discharge; and
4. The fair market value of the vehicle being less than the debt it secures.

For historic case law substantiating factual instances of significant impairment existence *see also:*

Johnson County Auto Credit, Inc. v. Green, 277 Kan. 148, 83 P.3d 152 (2004) (by entering an extension agreement for a default in payment, the creditor modified its original contract and waived the debtor's obligation to maintain insurance, so the debtor's failure to have insurance was no longer a contractual default);

Prairie State Bank v. Hoefgen, 245 Kan. 236, 777 P.2d 811 (1989) (repossession of floral business allowed. The court cited 13 factors that effected the substantial impairment of the collateral. The creditor was significantly under collateralized);

Medling v. Wecoe Credit Union, 234 Kan. 852, 678 P.2d 115 (1984) (repossession of a secured vehicle upon which payments were current was based principally upon the debtor's false or inconsistent statements to the creditor and debtor's failure to meet with the creditor after doing so).

See also Narro v. Ford Motor Credit, 2012 Bankr. LEXIS 4276 (Bankr. D. N.M. Sept. 12, 2012) (debtor, but not creditor, signed and filed a reaffirmation with the court).

The debtor receives discharge and post-discharge, despite being current on the payments and having insurance on the vehicle, the creditor repossessed the vehicle. The debtor's counsel failed to make the "no undue hardship" certification. As a result, the court found that the reaffirmation agreement was

not enforceable and the debtor's claim against Ford was not a case under Title 11. The claim does not "arise under" Title 11, and the claim was not created or governed by any provision in Title 11. The contract claim also does not "arise in" a case under Title 11. The claim for wrongful repossession could exist whether the bankruptcy case was filed or not. Only federal jurisdiction exists if the claim is "related to a case under Title 11."

This claim was not related to the debtor's bankruptcy case, as the claim is not estate property and any proceeds of the claim would benefit the debtors only, not their creditors. Therefore, the Bankruptcy Court lacks jurisdiction to hear or determine the debtor's post-petition contract claim against Ford.

V. Jurisdiction Issues

UMB Bank, N.A. v. KANZA Bank, 213 U.S. Dist. LEXIS 80030 (D. Kan. June 17, 2013) (an opinion by Magistrate Judge David Waxse construes "related to" Bankruptcy Court jurisdiction).

The Court in *UMB Bank* cites the "conceivable effect" test for determining whether a civil proceeding "relates to a bankruptcy case."

> "[T]he test for determining whether a civil proceeding is related in bankruptcy is whether the outcome of that proceeding could have any effect on the estate being administered in bankruptcy…. Although the proceeding need not be against the debtor or his property, the proceeding is related to the bankruptcy if the outcome could alter the debtor's rights, liabilities, options or freedom of action in any way thereby impacting on the handling and administration of the

> bankruptcy estate." Citing *In Re Gardner*, 913 F.2d 515, 518 (10th Cir. 1990)

The Court finds that the removed action was related to the debtor's bankruptcy case under the "conceivable effect" test.

> "A 'conceivable effect' is one that 'could alter' the debtor's rights, liabilities, options or freedom of action (either positively or negatively) in which in *any way* impacts upon the handling of the administration of the bankruptcy estate."

In Re Angel Fire Corporation v. Angel Fire Resorts Operation, LLC, 2013 U.S. Dist. LEXIS 69413 (D. N.M. May 2, 2013) (this case involves post-confirmation "related to" jurisdictional issues).

A declaratory action was filed seeking an interpretation of negative easement clauses on development lots and a determination that the negative easement does not apply to the properties in question. The negative easement was included as part of the debtor's Plan. The plaintiff brought the action in the United States Bankruptcy Court.

The issue was succinctly whether the Bankruptcy Court had jurisdiction to construing provisions of negative easements placed upon the land as a result of the debtor's Plan of Reorganization. The Bankruptcy Court ruled in the negative.

In Re Angel Fire Corp., 2012 Bankr. LEXIS 5444 (Bankr. NM, Nov. 20, 2012)

In Re Angel Fire Corp. suggests the following test for "related to" jurisdiction in the post-confirmation context:

1. Post-confirmation "related to" jurisdiction is not simply limited to the actual implementation or execution of a confirmed plan.
2. Such jurisdiction is none the less narrower than that applied in the pre-confirmation context.
3. The appropriate standard is no broader than the close nexus test.
4. Whatever standard is used, a post-confirmation action that "sufficiently affects the creditors' recoveries under a plan of reorganization," and a debtor's fraud action that involves bankruptcy trusts, each trigger Bankruptcy Court jurisdiction. *34

The "close nexus test" is:

> "[A] close nexus to the underlying bankruptcy case requires a demonstrable impact on that case or its confirmed plan…. More importantly, this understanding is consistent with a narrow jurisdiction established by Congress and recognized by the Supreme Court…"

Upon appeal, the findings and recommendations of the Magistrate concluded that such jurisdiction did not exist.

> "The trend in recent decades has been towards a restrictive understanding of the bankruptcy court jurisdiction…. [The Supreme Court] continues to recognize the limited nature of

bankruptcy court jurisdiction, particularly with respect to disputes that may adjudicate in other venues." *21

VI. Withdrawal of Reference

Ballway v. Persels & Associates, *LLC*, 2012 Bankr. LEXIS 3812 (July 19, 2012)

In this action a Chapter 7 trustee alleged that the defendants, a Maryland legal corporation and a Kansas attorney committed legal malpractice, breached fiduciary duties to the debtor, violated Kansas statutes and charged an unreasonable fee for a bankruptcy. The defendants sought a withdrawal of reference of the adversary proceeding and transferred to the district court under 28 U.S.C. §157(d).

28 U.S.C. §157(d) permits a District Court to withdraw reference in whole or in part of any case or proceeding referred to the Bankruptcy Court on timely motion. Cause is not defined. However, demand for a jury trial has been defined as cause.

Citing *Manley Truckline, Inc. v. Mercantile Bank of Kansas City*, 106 B.R. 696 (D. Kan. 1989), the Court in *Ballway* found jury trial is available:

1. For trustee's avoidance claim under 11 U.S.C. §548;
2. For the claims to recover preferential transfers under 11 U.S.C. §547;
3. For funds transferred to the debtor within 90 days of the filing of the bankruptcy petition;
4. For certain aspects of the trustee's claims under the Kansas Consumer Protection Act for engaging in deceptive and unconscionable acts and practices prohibited upon the act.

5. For the trustee's claim for legal malpractice and breach of fiduciary duty; and
6. For the claim for actual and punitive damages under the Kansas Services Organization Act.

VII. Bankruptcy Jurisdiction Question Issues

In Re Rock Structures Excavating, Inc., 2013 U.S. Dist. LEXIS 44940 (D. Utah, March 27, 2013) (motion for withdrawal of reference of fraudulent conveyance conversion relating claims was denied because the motion was untimely).

Construing *Stern v. Marshall*, the District Court found that although the Bankruptcy Court can no longer enter a final judgment on a state law counterclaim brought under 28 U.S.C. §157(b)(2)(C), *Stern* "does not preclude the bankruptcy court from entering final judgment in a fraudulent conveyance action." The defendants asserted that the entire adversary proceeding brought involving both a fraudulent action under 11 U.S.C. §548 and state law claims put the entire adversary proceeding beyond the jurisdiction of the Bankruptcy Court.

The trustee acknowledged the majority of its claims were noncore, however, all was unwarranted because "the bankruptcy court may still hear the case and enter proposed findings, facts and conclusions of law."

Holding that despite the Supreme Court's position in *Granfinanciera S.A. v. Nordberg*, 492 U.S. 33, 105 Sp. Ct. 2782, 106 L.Ed.2d 26 (1989), (which provides a right of trial by jury on a fraudulent conveyance action).

In the absence of a request for jury trial, a final judgment in a fraudulent conveyance action can be heard by the Bankruptcy Court.

Concluding that the claims brought by the bankruptcy trustee did not evoke any counterclaims based upon state law issues, the Bankruptcy Court holds jurisdiction and reference was denied as to all core matters and that as to any noncore matters propose findings of fact and conclusions of law would be offered.

See also Thompson v. Titus Transportation, LP, 2012 U.S. Dist. LEXIS 168730 (D. Kan. Nov. 27, 2012).

In *Thompson*, an action was filed in state court and removed to federal district court, followed by a subsequent Chapter 11 proceeding. The Court needed to construe whether, under 28 U.S.C. §157 and 28 U.S.C. §1334, the cause of action either "arose under" or was "related to" the bankruptcy action.

Noting that because the case involved state law causes of action, it is not a core proceeding directing arising under the Bankruptcy Court. The Bankruptcy Court may exercise jurisdiction if it "relates to" the bankruptcy. The Court found that the confirmation of the *Titus* bankruptcy case revested all property of the estate with the reorganized debtor. Because no assets remained in the bankruptcy estate following confirmation, the Texas Bankruptcy Court lacked "related to" jurisdiction and the action could proceed in Federal District Court in Kansas.

VIII. Monetary Judgments in Dischargeability Actions

The Tenth Circuit Court of Appeals held Bankruptcy Courts possess jurisdiction to enter monetary judgments against debtors and adjudicating creditors' nondischargeability claims. *See In Re Riebesell*, 586 F. 3d 782 (10th Cir. 2009)

In *In Re Brown*, 213 Bankr. LEXIS 2701 (N.D. OK, July 3, 2013)

The Bankruptcy Court was confronted by the assertion that *Stern v. Marshall* barred the Bankruptcy Court from entering monetary judgments in nondischargeability actions. The Bankruptcy Court ruled that *Stern v. Marshall* addressed jurisdiction over a debtor's common law action against a creditor that was unrelated to the creditor's claim and did not overtly or covertly overrule *Riebesell*. Thus, the Court held that is has jurisdiction to determine to enter judgment on all issues relating to 11 U.S.C. §523(a)(2) and 11 U.S.C. §523(a)(4), including validity and the amount of the debt, as well as dischargeability. Thus, it may enter monetary judgments in the exception to discharge action.

But see Executive Benefits Insurance Agency v. Arkison (*In Re Bellingham Insurance Agency, Inc.*, 2012 W.L. 6013836 (9th Cir. Dec. 4, 2012) c*ert. granted* (12-1200, June 24, 2013).

While federal law authorizes bankruptcy judges to hear and determine all cases under Title 11 and all core proceedings arising under Title 11, the Constitution prohibits bankruptcy judges from entering a final judgment in core proceedings when the cause of action is against a third party who is not a creditor of the estate.

Contra. Waldman v. Stone, 698 F.3d 910, 921 (6th Cir. 2012) (finding *in dicta* that Bankruptcy Courts may "entertain" orders in judgments in core proceedings, not proposed finding of fact and conclusions of law).

See also Law v. Siegel, 435 Fed. Appx. 697 (9th Cir. 2011), *cert. granted* (12-5196 June 17, 2013).

The Chapter 7 debtor appealed pro se to the Ninth Circuit from the BAP's order affirming the Bankruptcy Court's surcharging of the debtor's homestead and imposing discovery sanctions. The Circuit found that the BAP properly affirmed the Bankruptcy Court's order granting the trustee's surcharge motion because the surcharge was calculated to compensate the estate for the actual monetary cost imposed by the debtor's misconduct and was warranted to protect the integrity of the bankruptcy process. The BAP properly affirmed the Bankruptcy Court's order imposing discovery sanctions in light of the debtor's refusal to comply with the trustee's permissible discovery requests in a contested matter.

Case on appeal determines the appropriate boundaries of the Bankruptcy Court's authority under 11 U.S.C. §105.

IX. Judicial Estoppel

Clementson v. Countrywide Financial Corporation, et al., 464 Fed. Appx. 706; 2012 U.S. App. LEXIS 2296 (10th Cir. Feb. 7, 2012) (the failure for the debtor to list a cause of action in his bankruptcy petition devested him with standing to pursue them in litigation).

The debtor filed a Chapter 7 bankruptcy action of March 14, 2007. On November 20, 2009, the debtor's bankruptcy action was closed. In July, 2010, the debtor filed a Colorado state court action against the lender. The action was removed to Federal District Court. The Tenth Circuit upheld the District Court determination of the debtor's claims for property of the bankruptcy estate, because the claims accrued before the debtor filed bankruptcy and since the claims were not listed in the bankruptcy estate, remains property of the bankruptcy estate. Although the bankruptcy action was closed, the claims

belong to the bankruptcy estate and the debtor lacks standing to bring an action post-closing and post-discharge.

X. Appellate Standing in Involuntary Bankruptcies

In Re C.W. Mining Company, 636 F.3d 1257 (10th Cir. 2011).

An involuntary bankruptcy was taken against a limited liability company. Upon adjudication as a debtor, a trustee was appointed. The debtor's former managers, purporting to act on the debtor's behalf, appealed the involuntary bankruptcy stating that a putative debtor must have standing to bring a Bankruptcy Court's involuntary order for relief before an Appellate Court. The Bankruptcy Appellate heard the appeal. However, the case turned upon the fact that it was the manager's authority to bring the appeal, not the debtor's standing. Only the debtor had standing to appeal and, by appointment of the trustee, the trustee was the only person authorized to bring an appeal, because the managers were "completely ousted when the debtor's bankruptcy was converted to Chapter 7 and a trustee was appointed."

> "Appellate review of a bankruptcy court order is limited to 'persons aggrieved' by the order. To qualify as a 'person aggrieved' a person's rights or interests must be directly and adversely affected, pecuniarily by the decree or order of the bankruptcy court. Accordingly, unless the estate is solvent and excess will eventually go to the debtor or the debtor's equity holders, or unless the matters involve rights unique to the debtor, the debtor is not a party aggrieved by orders effecting the administration of the bankruptcy estate. A hopelessly insolvent debtor does not have standing to appeal orders affecting the size of the estate since such an order

> would not diminish the debtor's property, increase advertence or detrimentally affect his rights."

XI. Limited Liability Company's Interest as an Asset of the Bankruptcy Estate

In Re Willcut, 2012 Bankr. LEXIS 3104 (Bankr. D. OK 2012) (the Chapter 7 trustee moved for the turnover and accounting and return of all monies received by a debtor's wife from a limited liability company in which she owned an interest. The debtors argue that because the terms of the limited liability company's Operating Agreement prohibited the transfer of the wife's interest in the limited liability company without the consent of other members, no interest in the limited liability company became part of the bankruptcy estate and that the trustee could not claim any interest in the funds received by the wife from the limited liability company. The Court noted that there was no legal authority for this position).

Under 11 U.S.C. §541(c)(1), the wife's interest in the limited liability company was property of the debtor's bankruptcy estate. The trustee was entitled to administer those interests. Federal bankruptcy law trumped the terms of the Operating Agreement. The Operating Agreement sought to make differences between permitted transfers and impermissible transfers, holding that impermissible transferees held no interest in the limited liability company under the following language:

> "9.3 Consequences of Impermissible Transfer. In the event any Unit or Units are transfer other than as permitted… then so long as such transfer has not been approved by a Majority Vote of the Members owning Voting Units as provided for… neither the transferor or Member nor the Impermissible Transferee shall be considered to be a member for any purposes whatsoever, and all Profits shall be allocated and all

> distributions shall be made exclusively to the other Members…."

Relying upon 11 U.S.C. §541(c)(1), the Court finds that the language of the Operating Agreement amounts to enforceable restriction on the bankruptcy estate's interest.

XII. Impari Delicto

> *"Impari delicto potior est conditio defendentis"* or "in the case of equal or mutual fault… the position of the [defending] party… is the better one." *Mosier v. Callister*, *Nebeker & McCullough, P.C.*, 546 F.3d 1271, 1275 (10th Cir. 2008)

In Re Vaughan Company Realtors, 213 Bankr. LEXIS (Bankr. D. NM March 11, 2013) (the Chapter 7 Trustee brought an adversary complaint against a transferee asserting that the debtor had operated a Ponzi scheme and the trustee sought to avoid certain transfers made).

The theories brought by the trustee included avoidance of transfers under the actual fraud and construction fraud provisions of 11 U.S.C. §548 and applicable state law. The defendant transferee argued that the trustee's claims were subject to the affirmative defense of *impari delicto.* The Bankruptcy Court found that actions brought under 11 U.S.C. §544 and 11 U.S.C. §548 were not subject to the defense because they had not existed prior to the commencement of the bankruptcy case and, thus, did not arise independently of the bankruptcy case. Therefore, they were not subject to the affirmative defense of *impari delicto*. However, the Court found that state law claims were subject to the *impari delicto* defense.

The ruling also held that a trustee may not use the turnover provisions of 11 U.S.C. §542 to recover a fraudulent transfer because the fraudulently

transferred property does not become property of the bankruptcy estate until the transfer is avoided. The trustee cannot use 11 U.S.C. §542 in lieu of a fraudulent transfer action.

The doctrine of *impari delicto* can be used to prohibit the trustee from pursuing certain claims or causes of action belonging to the debtor when it commenced its bankruptcy case. If the trustee must rely on 11 U.S.C. §541 for standing in the case, he or she will not be insulated from the wrong doing of the debtor.

XIII. 11 U.S.C. §550 – Liability of Transferee of Avoided Transfer

Brooke v. Logan Wildlife Corp., 443 B.R. 847, 2010 Bankr. LEXIS 3567 (Bankr. D. Kan., Oct. 6, 2010) and *Brooke v. NCMIC Finance Corporation*, 488 B.R. 459, 2013 Bankr. LEXIS 922 (Bankr. D. Kan., March 13, 2013).

Both these cases concern whether in an action under 11 U.S.C. §548 it is necessary to name the initial transferee, as well as the transferee of such initial transferee.

Citing the *Slack-Horner* decision, 971 F.2d 577 (10th Cir. 1992), the Court found on both *Brooke* cases that the initial transferee is a necessary party to any action against any downstream transferee. *Slack-Horner* has been consistently construed to require that the avoidability of the initial transfer be determined in litigation brought against the initial transferee. Thus, the plaintiff must bring a successful suit against the initial transferee before recovery can be obtained from any subsequent transferee.