AMERICAN BANKRUPTCY INSTITUTE

Consumer Practice Extravaganza

Bankruptcy Crossover

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2024

ABI's 2024-2025 Consumer Practice Extravaganza

Bankruptcy Crossover Issues

Tuesday, November 12, 2024

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Note: The following outline provides an overview of some of the many issues that overlap in bankruptcy and divorce cases. It is not intended as a complete and exhaustive outline of bankruptcy law, family law and/or the issues which may arise in connection with cases involving bankruptcy and divorce issues. The reference to cases is not exhaustive and in many cases, provides a starting point for further research. The outline is intended for general information purposes only and should not be relied upon for any purpose without independent verification and analysis with respect to the specific facts and circumstances of each case.

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PART ONE

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DIVORCE AND BANKRUPTCY: CURRENT ISSUES

I. Introduction

Divorce and bankruptcy are two hardships which most people would prefer to avoid. Unfortunately, a high percentage of marriages end in divorce. Often, financial problems precipitate conflict leading to divorce. Costs associated with divorce, particularly the expense of maintaining separate households, often create newfound financial problems. Divorced spouses may seek relief from obligations owed pursuant to a divorce settlement and from other financial obligations under the protection afforded by the Bankruptcy Code (the "Code"). Both divorce and bankruptcy are alike in that each attempts to afford an individual a "fresh start." However, the objectives of divorce are not consistent with the goals of a bankruptcy filing. Divorce attempts to divide assets, apportion debt, and provide support for the disadvantaged spouse and minor children. Bankruptcy attempts to discharge debt and distribute non-exempt assets among creditors. An analysis of the impact of bankruptcy upon a divorce settlement and the obligations thereunder must begin with a review of the applicable Code provisions, and, as with any bankruptcy case, an analysis of the particular property of the estate issues in the divorce context.

A. The Bankruptcy Petition

All Chapter 7, 11 and 13 cases are commenced by the filing of a bankruptcy petition.

See 11 U.S.C. §§ 301 and 302.

B. The Automatic Stay

The filing of a bankruptcy petition gives rise *automatically* to an "automatic stay" of most actions to enforce pre-petition debts. See 11 U.S.C. § 362(a).

Exceptions:

Among other exceptions, the automatic stay does not stay:

> (1) the commencement or continuation of an action to establish paternity, to establish or modify an order for domestic support obligations, concerning child custody or visitation, regarding domestic violence and/or for the dissolution of marriage, except to the extent that such proceeding seeks to determine the division of property that is *property of the bankruptcy estate*;
>
> (2) the collection of a domestic support obligation from property that is not *property of the bankruptcy estate;*
>
> (3) with respect to the withholding of income that is property of the estate or property of the debtor for payment of a domestic support obligation under a judicial or administrative order or a statute.
> See 11 U.S.C. § 362(b)(2).

C. Definition of Domestic Support Obligation ("DSO")

A debt that accrues before, on or after the entry of the order for relief (usually the filing of the bankruptcy case), including interest that accrues on the debt as provided under applicable nonbankruptcy law, that is:

> (1) recoverable by a spouse, former spouse, or child of the debtor or such child's parent, legal guardian, or responsible relative; or, a governmental unit;
>
> (2) in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit) of such spouse, former spouse or child of the debtor or such child's parent, without regard to whether such debt is expressly so designated;
>
> (3) established or subject to establishment before, on, or after the date of the order for relief in a bankruptcy case, pursuant to a separation agreement, divorce decree, or property settlement agreement, an order of a court of record, or a determination made in accordance with applicable non-bankruptcy law by a governmental unit, and not assigned to a governmental unless assigned voluntarily by the recipient for the purpose of collecting the debt.
>
> See 11 U.S.C. § 101(14A).

D. Property of the Bankruptcy Estate

The filing of a bankruptcy petition also creates a bankruptcy estate. The estate is comprised of all of the debtor's legal or equitable interests in property at the time the petition is filed plus certain property that the debtor acquires (or becomes entitled to acquire) within 180 days after the petition is filed: e.g., through a spousal property settlement or divorce decree. See 11 U.S.C. §§ 541(a)(1) and (a)(5)(B).

Note - Community Property:

With very limited exceptions, the bankruptcy estate also includes all interests of the debtor *and of the debtor's spouse* in community property on the petition date even if the debtor's spouse has not joined in the bankruptcy petition. See 11 U.S.C. § 541(a)(2).

Note - Post-petition Wages:

Chapter 7: The debtor's post-petition wages are not *property of the estate*.

Chapter 11: The debtor's post-petition wages are *property of the estate*. See 11 U.S.C. § 1115(a)(2).

Chapter 13: The debtor's post-petition wages are *property of the estate*. See 11 U.S.C. § 1306.

E. Bankruptcy Schedules and Statement of Financial Affairs

In Chapter 7, Chapter 11 and Chapter 13 cases, the debtor is required to file schedules of assets and liabilities and a statement of financial affairs, either with the petition or within 15 days of the petition date. See Fed.R.Bankr.Proc. 1007(c).

Chapter 11 Plan:

In a Chapter 11 case, the debtor may also file a plan of reorganization for repayment of creditors, and has the exclusive right to so do within 120 days after the order for relief is entered. 11 U.S.C. § 1121(b).

Chapter 13 Plan:

In a Chapter 13 case, the debtor is required to file a plan for repayment of creditors, either with the petition or within 15 days of the petition date. See Fed.R.Bankr.Proc. 3015(b).

F. Meeting of Creditors

Shortly after the petition is filed, the debtor is required to appear at a meeting of creditors, which is held at the Office of the United States Trustee, to answer under oath questions posed by the Chapter 7 or Chapter 13 trustee and/or United States Trustee and by creditors. See 11 U.S.C. § 341; Fed.R.Bankr.Proc. 2003(a).

Chapters 7 and 11: In a Chapter 7 or Chapter 11 case, the meeting of creditors must be held within 20 to 40 days after the petition is filed.

Chapter 13: In a Chapter 13 case, the meeting of creditors must be held within 20 to 50 days after the petition is filed.

G. Notice of Meeting of Creditors and Miscellaneous Deadlines

A notice of the time and place of the meeting of creditors is sent to all of the creditors listed by the debtor on its bankruptcy schedules. The notice contains important information, including the deadline for filing proofs of claim and for filing complaints objecting to the discharge of the debtor or to the dischargeability of a particular claim against the debtor.

NOTE KEY DEADLINES

Filing Claims

Chapters 7 and 13: The deadline for filing proofs of claim is 90 days after the *first date set* for the meeting of creditors. See Fed.R.Bankr.Proc. 3002(c). Typically, in Chapter 7 cases, no proof of claim is required unless the Trustee determines that assets are available, at which time a new notice will be sent to creditors by the court.

Chapter 11: A deadline will be set by the court and a notice sent to creditors. However, creditors need not file claims if listed in the schedule of liabilities, unless they are listed as disputed, contingent or unliquidated. See Fed.R.Bankr.Proc. 3003(b) and (c).

Filing Complaints Objecting to Discharge and/or Dischargeability

Chapter 7, 11 and 13: The deadline for filing an adversary proceeding for nondischargeability of a debt under 11 U.S.C. § 523(c) or an objection to the debtor's discharge under 11 U.S.C. § 727(a) in a Chapter 7 case is 60 days after the *first date set* for the meeting of creditors. The deadlines for objections to discharge and to the dischargeability of a particular debt are rigidly applied, so be careful not to miss them. See Fed.R.Bankr.Proc. 4004(a), 4007(c).

Objections to Exemptions: The deadline for filing objections to a debtor's claim of exempt property is 30 days after the *conclusion of* the *meeting of creditors*. See Fed.R.Bankr.Proc. 4003(b).

Chapter 13 Objections to Confirmation

Objections to confirmation of a Chapter 13 plan must be filed by the date of the meeting of creditors although the trustee may consider an oral objection. If there is no objection, the Chapter 13 trustee may recommend confirmation, and the plan will probably be confirmed without judicial review.

H. Proof of Claim

All creditors wishing to receive payment in a Chapter 7 or 13 case must file a proof of claim within the prescribed deadline.

See Note under Notice of Meeting of Creditors and Miscellaneous Deadlines above.

I. Chapter 7

Purpose: A primary purpose of a Chapter 7 case is to liquidate the debtor's nonexempt assets and distribute the proceeds to creditors. Secured claims are generally paid first from proceeds of such parties' collateral, then priority claims are paid, and then general unsecured claims. Most individual debtors have few, if any, nonexempt assets, and most Chapter 7 cases are closed very quickly with little or no payment to creditors. Most liens survive the Chapter 7 bankruptcy unless they are "set aside" through the bankruptcy court process. Debtors must qualify to file Chapter 7 either because they pass the "means test" or the majority of their debts are classified as business debts as opposed to consumer debts.

Trustee: There is a panel of Chapter 7 trustees who are assigned at random to these cases. If a creditor suspects that the debtor has not listed his or her assets or has undervalued them, these suspicions should be communicated to the trustee (not to the judge).

Objections to Discharge: In a Chapter 7 case, the debtor normally receives a discharge (i.e. relief from personal liability) of most types of debts. However, if the debtor has behaved dishonestly in connection with the bankruptcy case, either before or during the case, the debtor may be denied a discharge. An objection to the debtor receiving a discharge must be filed as an adversary proceeding (i.e., a complaint, not just a motion) by the deadline, which is 60 days following the first date set for the meeting of creditors. See 11 U.S.C. § 727; Fed.R.Bankr.Proc. 4004(a). **Note:** If no one files a timely action objecting to the granting of the debtor's discharge, the discharge is granted.

Nondischargeability Actions: Even if the debtor receives a discharge, certain types of debt will not be discharged and are nondischargeable by their nature, e.g., certain tax debts, student loans, DSOs and divorce-related debts to a spouse, former spouse or child of the debtor. There is no deadline for filing an action to determine whether such types of debts exist (i.e. they are automatically non-dischargeable); however, an action may be brought either in state court or bankruptcy court for certainty. However, other types of debts are nondischargeable only if a timely action seeking a determination of their nondischargeability is filed in the bankruptcy court: e.g., debts incurred through fraud, breach of fiduciary duty, or willful and malicious injury. See 11 U.S.C. § 523.

J. Chapter 13

Eligibility: A debtor must have less than $1,081,400 in secured debt and $360,425 in unsecured debt to be eligible to file a Chapter 13 case. See 11 U.S.C. § 109(e).

Purpose: The purpose of a Chapter 13 case is for the debtor to propose a plan to repay creditors. See 11 U.S.C. § 1321. Generally, whether the plan must be for 36 months or 60 months is determined based upon a debtors' gross receipts for the 6-month period prior to the filing of the bankruptcy case ("current monthly income"). The monthly payment amount is generally determined based upon the debtor's monthly net disposable income after deducting certain allowable expenses from the current monthly income plus other factors. See 11 U.S.C. §§ 1322 and 1325. Unsecured creditors must receive at least as much as they would receive in a Chapter 7 case. See 11 U.S.C. § 1325(a)(4).

Note: Priority claims must be paid in full through the plan. DSOs are priority claims. See 11 U.S.C. §§ 1322(a)(2), 507(a)(1). However, priority support obligations assigned to a governmental agency for collection do not have to be paid in full through the plan. See 11 U.S.C. §§ 1322(a)(4), 507(a)(1)(B).

Note: Most Chapter 13 cases are filed to permit the debtor to catch up with the arrears on their mortgage. The arrears are paid through the plan. Post-petition mortgage payments must be kept current and are normally paid by the debtor directly to the secured creditor.

Trustee: There are generally one or two Chapter 13 trustees assigned to a geographical area who supervise all Chapter 13 cases. The trustee reviews the debtor's plan, collects and disburses payments, and usually files a motion to dismiss the case if plan payments are delinquent.

Discharge: In most cases, a Chapter 13 debtor does not receive a discharge until he or she completes making the payments required by the Chapter 13 plan. The Chapter 13 discharge is only slightly broader in scope than a Chapter 7 discharge. This is a significant change from prior law. A spousal obligation arising out of a dissolution agreement that is not a DSO (See § 523(a)(15)) is discharged under Chapter 13, but only upon the completion of a Chapter 13 plan. See 11 U.S.C. §§ 523(a)(15), 1328(a)(2). For example, property settlements can still be discharged in a Chapter 13 upon completion of the Chapter 13 plan even if the debtor pays less than 100% of the debt.

Domestic Support Obligations: A Chapter 13 debtor must certify that he/she is current with respect the payment of post-petition DSOs in order to receive his/her discharge. 11 U.S.C. § 1328(a). Failure to keep post-petition DSO payments current also a basis for dismissal of a Chapter 13 case. 11 U.S.C. § 1307(c)(11).

K. Chapter 11

A primary purpose of Chapter 11 is to permit debtors to propose repayment plans which can be based on future income, asset liquidation, recapitalization, refinance or otherwise. Since the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), it could be argued that there is a new sub-chapter of Chapter 11 which applies to individuals, in large part, because post-petition income of an individual is property of the estate. There is initially no court-appointed trustee when a case is filed, although one may be appointed later.

Chapter 11 Plans: Chapter 11 plans are not limited by length of term of repayment, and there is no limitation on eligibility for Chapter 11 based on the amount of debt. Chapter 11 is very flexible and requires substantial attention and effort to satisfy governmental regulatory requirements. It is

therefore a very expensive process. Creditors vote on proposed plans, although the Court has the ability to override the vote in some cases. A quarterly fee is payable to the United States Trustee.

Discharge and Priorities: Dischargeability issues and the priority distribution rules are generally the same as in Chapter 7 cases. 11 U.S.C. § 1141. Except as otherwise provided in the Chapter 11 plan or order confirming the plan, confirmation of a Chapter 11 plan in most cases discharges the debtor from its debts (other than debts otherwise not dischargeable under 11 U.S.C. § 523). See 11 U.S.C. § 1141.

L. Relevant Bankruptcy Code Sections

11 U.S.C. § 101 Definitions (selected portions)

11 U.S.C. § 109 Who may be a debtor - eligibility

11 U.S.C. § 362 Automatic stay

11 U.S.C. § 507 Priorities

11 U.S.C. § 522 Exemptions

11 U.S.C. § 523 Exceptions to discharge

11 U.S.C. § 524 Effect of discharge

11 U.S.C. § 541 Property of the estate - See also 11 U.S.C. § 1115 re: Chapter 11 and 11 U.S.C. § 1306 re: Chapter 13 property of the estate issues

11 U.S.C. § 544 Trustee as lien creditor and as successor to certain creditors and purchasers

11 U.S.C. § 727 Discharge - See also 11 U.S.C. § 1141 re: Chapter 11 discharge provisions and 11 U.S.C. § 1328 re: Chapter 13 discharge issues

11 U.S.C. § 1129 Confirmation of a Chapter 11 plan

11 U.S.C. § 1325 Confirmation of a Chapter 13 plan - See also 11 U.S.C. § 1322

PART TWO

FAMILY LAW BASICS

I. Characterization of Marital Property

Community Property: Generally, all property, real or personal, wherever situated, acquired by a married person during marriage while domiciled in California is community property. See California Family Code § 760 [hereinafter Family Code or "F.C."]. Unless the trust instrument expressly provides otherwise, community property that is transferred to a revocable trust remains community property during the marriage, regardless of the identity of the trustee; however, the power to revoke as to community property may be exercised by either spouse acting alone. See F.C. § 761. Except as otherwise provided, the respective interests of husband and wife in community property during continuance of the marriage relation are present, existing and equal interests. See F.C. § 751.

Separate Property: Separate property of a married person includes all property owned before marriage, all property acquired after marriage by gift, bequest, devise or descent, and the rents, issues and profits of such property. See F.C. § 770. Earnings and accumulations while the spouses are living separate from each other are the separate property of each spouse, as are the earnings and accumulations acquired after entry of a judgment of legal separation. See F.C. §§ 771 and 772.

Methods of Holding Property: A husband and wife may hold property as joint tenants or tenants in common, or as community property, or as community property with a right of survivorship. F.C. § 750.

Community Property Presumption: For the purpose of property on dissolution of marriage or legal separation of the parties, property acquired by the parties during marriage in joint form, including property held in tenancy in common, joint tenancy, tenancy by the entirety, or as community property, is presumed to be community property. The presumption is a presumption affecting the burden of proof and may be rebutted by a clear statement in the deed or other documentary evidence of title by which the property is acquired that the property is separate and not community or by proof that the parties made a written agreement that the property is separate property. See F.C. § 2581.

II. Community Property Interest in Separate Property

In re Marriage of Moore, 28 Cal.3d 366, 168 Cal.Rptr. 662 (1980) and In re Marriage of Marsden, 130 Cal.App.3d 426, 181 Cal.Rptr. 910 (1982). When community property is contributed to the separate property of a spouse during marriage, the community acquires an interest in the property. This principle is known as the "Moore/Marsden rule" and addresses the apportionment of the appreciation in value to a spouse's separate property due to funds expended by the community.

In re Marriage of Zaentz, 218 Cal.App.3d 154, 267 Cal.Rptr. 31 (1990). In this case, the Court affirmed the finding that the community was entitled to $600,000 as compensation for the husband's contributions to the movie "Amadeus" which was owned by SZC, a corporation which had been formed by the husband prior to the parties' marriage. The case discusses the two models generally used in apportioning increased value in separate property. The *Pereira* approach is to allocate a return on the separate property investment as separate income and to allocate any excess to the community property as arising from the husband's efforts. Pereira v. Pereira, 156 Cal. 1, 7-8, 103 P. 488, 491-492 (1909). The *Van Camp* approach is to determine the reasonable value of the

husband's services and to allocate that amount as community property, and treat the balance as separate property attributable to the normal earnings of the separate estate. Van Camp v. Van Camp, 53 Cal.App. 17, 199 Pac.Rptr. 885 (1921).

III. Transmutation of Property

Married couples may, by agreement or transfer, with or without consideration, and subject to the provisions of F.C. §§ 851 to 853, transmute community property to the separate property of either spouse, transmute separate property of either spouse to community property and/or transmute the separate property of one spouse to the separate property of the other spouse. F.C. § 851 provides, however, that transmutations are subject to the laws governing fraudulent transfers which are set forth in California Civil Code §§ 3439 et seq. See also In re Marriage of Barneson, 69 Cal.App.4th 583, 81 Cal.Rptr.2d 726 (1999); and Estate of MacDonald, 51 Cal.3d 262, 794 P.2d 911, 272 Cal.Rptr. 153 (1990).

IV. Liability of Marital Property

Generally, the community estate is liable for a debt incurred by either spouse before or during marriage, regardless of which spouse has the management and control of the property and regardless of whether one or both spouses are parties to the debt or to a judgment for the debt. "During marriage" does not include the period during which the spouses are living separate and apart before a judgment of dissolution or legal separation of the parties. See F.C. § 910.

Quasi-community property is liable to the same extent as community property. See F.C. § 912.

The earnings of a married person during marriage, which are community property, are not liable for a debt incurred by the person's spouse before marriage. After earnings of the married person are paid, they remain not liable so long as they are held in a deposit account in which the person's spouse has no right of withdrawal and are uncommingled with other property in the community estate, except property insignificant in amount. See F.C. § 911.

A support obligation of a married person that does not arise out of the marriage shall be treated as a debt incurred before marriage. See F.C. § 915.

The separate property of a married person is liable for a debt incurred by the person before or during marriage. The separate property of a married person is not liable for a debt incurred by the person's spouse before or during marriage, notwithstanding that the married person may have joined or consented to encumbering community property to secure payment of a debt incurred by the person's spouse. See F.C. § 913. However, the separate property may be liable for necessaries of life incurred by the person's spouse pursuant to F.C. § 914.

After the division of community and quasi-community property, F.C. § 916 provides for the following:

(1) The separate property owned by a married person at the time of the division and the property received by the person in the division is liable for a debt incurred by that person before or during marriage, and the person is personally liable for the debt, whether or not the debt was assigned for payment by the person's spouse in the division.

(2) The separate property owned by a married person at the time of the division and the property received by the person in the division is not liable for a debt incurred by the person's spouse before

or during marriage, and the person is not personally liable for the debt, unless the debt was assigned for payment by the person in the division of property, subject to any liability of property for the satisfaction of a lien on the property.

(3) The separate property owned by a married person at the time of the division and the property received by the person in the division is liable for a debt incurred by that person's spouse before or during marriage, and the person is personally liable for the debt, if the debt was assigned for payment by the person in the division of property. If a money judgment for the debt is entered after the division, the property is not subject to enforcement of the judgment unless the person is made a party to the judgment.

V. Reimbursement Claims and Credits

Generally: The right of reimbursement arises regardless of which spouse applies the property to satisfaction of the debt, whether the property is applied to the satisfaction of the debt voluntarily or involuntarily, regardless of whether the debt to which it is applied is satisfied in whole or in part. The right is subject to an express written waiver of the right by the spouse in whose favor the right arises. The right of reimbursement is measured by the value of the property or interest in property at the time the right arises. See F.C. § 920.

Epstein Credits: All rights of reimbursement to which a party may be entitled as a result of payment of community obligations since the date of separation with separate property. See In re Marriage of Epstein, 24 Cal.3d 76, 154 Cal.Rptr. 413 (1979).

Watts Credits: All rights of reimbursement to which a party or the community may be entitled as a result of one party's use of community assets since the date of separation, e.g. use of the family home. See In re Marriage of Watts, 171 Cal.App.3d 366, 217 Cal.Rptr. 301 (1985).

Frick Credits: All rights of reimbursement to which a party or the community may be entitled due to one party's use of community assets for the improvement of separate property during marriage. See In re Marriage of Frick, 181 Cal.App.3d 997, 226 Cal.Rptr. 766 (1986).

F.C. § 915(b): All rights of reimbursement due the community for payment by the community of a child or spousal support obligation of either party arising from a prior marriage or relationship.

F.C. § 916(b): All rights of reimbursement for application of the property owned by a married person at the time of the division of property and received in the division of property, to satisfaction of a money judgment for a debt incurred by the person that is assigned for payment by the person's spouse.

F.C. § 2626: The court has jurisdiction to order reimbursement as it deems appropriate for debts paid after separation but before trial.

F.C. § 2640: All rights of reimbursement for separate property contributed to the acquisition, maintenance or improvement of community property.

F.C. § 2641: All rights of reimbursement due the community or a party for contributions made by the community to either of the parties for the education or training of a party that substantially enhances the earning capacity of the party.

VI. Fiduciary Duties Between Spouses

F.C. § 721: In transactions between themselves, a husband and wife are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other. This confidential relationship imposes a duty of the highest good faith and fair dealings on each spouse. This confidential relationship is a fiduciary relationship subject to the same rights and duties of nonmarital business partners, as provided in Sections 16403, 16404, and 16503 of the California Corporations Code.

F.C. § 1100: Imposes fiduciary duties on the parties and provides that spouses may not make gifts of, or dispose of, community personal property for less than fair and reasonable value without the written consent of the other spouse, nor can spouses sell, convey or encumber community personal property without written consent of the other spouse. In the case where a spouse is operating a business, the spouse shall obtain the written consent of the other spouse to take various actions regarding the sale of the business and/or assets. See also F.C. § 1101 which provides remedies for breach of the fiduciary duty between spouses.

F.C. § 2102: Provides that from the date of separate through the date of distribution of the community asset or liability in question, each party is subject to the standard provided in F.C. § 721, as to all activities that affect the assets and liability of the other party.

VII. Registered Domestic Partnerships

Domestic Partner Rights and Responsibilities Act ("DPRRA"), F.C. § 297, was passed in 1999. F.C. § 297.5, added in 2003, became effective January 1, 2005. The amendment extended to registered domestic partners ("RDPs") most of the rights and obligations of married persons, including rights with regard to community property assets and liabilities. Therefore, commencing with the date of their registration, RDPs acquire community property like spouses, and their creditors have recourse to both RDPs' interests in such property to the same extent as creditors of married persons.

On June 26, 2013, the United States Supreme Court struck down portions of the Defense of Marriage Act (DOMA). Section 3 of DOMA defined "spouse," for purposes of federal law, to refer *only* to a person of the opposite sex who is a husband or wife, and marriage is limited to opposite-sex couples. 1 U.S.C. § 7. See also 28 U.S.C. § 1738C. Thus, legally married same-sex couples are now entitled to the same federal benefits as married opposite-sex couples.

Prior to striking down DOMA, there were numerous unresolved issues raised by the interplay of DPRRA and DOMA. For a thoughtful treatment of these issues, see Robert F. Kidd & Frederick C. Hertz, *Partnered in Debt: The Impacts of California's New Registered Domestic Partner Law on Creditors' Remedies and Debtors' Rights, under California Law and under Federal Bankruptcy Law*, 28 Cal. Bankr. J. 148 (2006). While many issues may no longer be applicable following the Supreme Court's decision, others may continue and new issues may arise, particularly in states such as California where the constitutionality of same-sex marriage remains hotly contested. See Part 6 below for further discussion.

VIII. Miscellaneous Provisions

Marital Settlement Agreement/MSA: Codified in statute and defined in case law and practice as an agreement involving the division of property/debts/custody/spousal and child support. Generally incorporated and merged into the judgment of dissolution

Automatic Temporary Restraining Order/ATRO: Immediately effective restraining orders upon proof of service of divorce summons -- restrains both parties from: removing child from state, cashing, borrowing against, cancelling, transferring, disposing of, or changing the beneficiaries of any insurance or other coverage including life, health, automobile, and disability for other spouse or children or transferring, encumbering, hypothecating, concealing or in any way disposing of any property, real or personal, whether community, quasi-community, or separate without the written consent of the other party or order of the court, except in the usual course of business or for necessities of life.

F.C. § 2033 : Family law attorney's real property liens.

F.C. § 2550 : Property presumptions - The Court shall divide the community estate equally.

F.C. § 3592 : Discharge in bankruptcy; power of Court to make new orders re support.

Note: Applicable if the obligation discharged was pursuant to a written agreement for settlement of property. See also In re Marriage of Lynn, 101 Cal.App.4th 120, 123 Cal.Rptr.2d 611 (2002). F.C. § 4320 factors to modify support must be considered.

Evid. C. § 662 : Owner of legal title to property is presumed to be the owner of beneficial title. The presumption may be rebutted by clear and convincing proof.

BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT 2005

PROVISIONS AFFECTING FAMILY LAW

I. Effective Date of "BAPCPA"

BAPCPA was enacted on April 20, 2005. However, with a few exceptions, most of its amendments became effective October 17, 2005 and applicable to cases filed on or after that date.

II. Are You a Debt Relief Agency?

11 U.S.C. § 101(12A) defines "debt relief agency" to mean, "any person who provides bankruptcy assistance to an assisted person in return for the payment of money or other valuable consideration. Section 101(3) defines "assisted person" to mean, 'any person whose debts consist primarily of consumer debts and the value of whose nonexempt property is less than $175,750 (**Note** - applicable amount as of April 1, 2010). Section 101(4A) defines "bankruptcy assistance" to mean, "any goods or services sold or otherwise provided to an assisted person with the express or implied purpose of providing information, advice, counsel, document preparation, or filing, or attendant at a creditors meeting or appearing in a case or proceeding on behalf of another or providing legal representation with respect to a case or proceeding under this title."

Milavetz, Gallop & Milavetz, P.A. v. U.S., 130 S.Ct. 1324 (2010). Attorneys who provide bankruptcy assistance to "assisted persons" are "debt relief agencies" within the meaning of BAPCPA. Thus, pursuant to 11 U.S.C. § 526(a)(4), attorneys who are "debt relief agencies" are precluded from advising a debtor to incur more debt because the debtor is filing for bankruptcy, rather than a valid purpose.

III. Domestic Support Obligations

11 U.S.C. § 101(14A) defines a "domestic support obligation" ("DSO") generally, as a debt, whenever it accrues, and including interest on that debt under nonbankruptcy law, that is owed or recoverable by a spouse, former spouse, or child of the debtor or such child's parent, legal guardian, or responsible relative or a governmental unit, in each case in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit), and is generally considered to be somewhat more expansive than debts "in the nature of support" as defined by prior 11 U.S.C. § 523(a)(5).

A DSO includes both prepetition and postpetition obligations, as well as interest that accrues on the debt under applicable nonbankruptcy law, and obligations established or subject to establishment before, on, or after the date of the order for relief.

Priority of a DSO: All DSOs are "first priority" under § 507(a)(1). However, within the category of DSOs, those assigned to a governmental unit (other than for collection) or owed directly to the governmental unit under nonbankruptcy law are second in priority to those owed to a spouse, former spouse, child of the debtor, or child's parent, legal guardian or responsible relative, or recoverable by a governmental unit on their behalf. See 11 U.S.C. §§ 507(a)(1)(A) and (a)(1)(B). The administrative expenses of the trustee to administer assets for these claims is given higher priority than the DSOs. 11 U.S.C. § 507(a)(1)(C).

Preferences: 11 U.S.C. § 547(c)(7) was amended to provide that bona fide DSO payments cannot be avoided by a trustee, including those assigned to government units.

Chapter 11 and Chapter 13 Plan Confirmation: One of the requirements for plan confirmation in both Chapter 11 and Chapter 13 cases is that all DSO obligations incurred post-petition through the date of confirmation have been paid.
See 11 U.S.C. § 1325(a)(8) and 11 U.S.C. § 1129(a)(14).

Chapter 13 cases and the DSO

If a DSO is not paid in full, with interest, through a Chapter 13 plan, the interest that accrued throughout the pendency of the plan survives and is not discharged.
Note: The same is true in Chapter 11 cases.

In order to obtain a Chapter 13 discharge, a debtor must certify that all post-petition DSO payments that became due subsequent to the bankruptcy filing and DSO payments provided by the plan have been paid. 11 U.S.C. § 1328(a).

Failure to keep post-petition DSOs current is a basis for dismissal of a Chapter 13 case. 11 U.S.C. § 1307(c)(11).

Although DSOs assigned to a governmental agency (other than for collection) are priority obligations, they do not have to be paid in full through a Chapter 13 plan under certain conditions. 11 U.S.C. § 1322(a)(4).

NOTE: It is important to review a debtor's petition to determine whether a debt has been characterized as a DSO or a property debt, as well as whether the debt was listed as priority, secured or general unsecured. Since the nature and character of the debt affects the creditor's right to payment and other rights of the creditor in Chapter 7 asset cases and in cases under Chapters 11, 12 and 13, it is important to file claims asserting the nature and character of the debt, and take whatever other actions are necessary, to assure the creditor receives proper treatment.

IV. 11 U.S.C. § 362(b)(2) - The Automatic Stay

In addition to the pre-BAPCPA exceptions to the automatic stay regarding the commencement or continuation of an action or proceeding to establish paternity, to establish or modify an order for support and to collect support from property that is not property of the bankruptcy estate, BAPCPA expanded the automatic stay exceptions to allow actions or proceedings (1) to dissolve the marriage, (2) concerning child custody or visitation, (3) proceedings regarding domestic violence, (4) the withholding of income to pay a "domestic support obligation" (even from property of the estate in certain circumstances), (5) the intercepting of tax refunds for DSOs, (6) the withholding of or restructuring of licenses (e.g. a driver's or professional's license) or restricting licenses for failure to pay support, (7) the reporting of overdue support owing by a parent to consumer reporting agencies, and (8) the enforcement of certain medical support obligations. Basically, the only remaining limitation (i.e. matter subject to the automatic stay) is that related to the stay of actions with respect to the division of marital property specifically related to property of the bankruptcy estate.

V. Dischargeability Issues - 11 U.S.C. § 523(a)(5) and § 523(a)(15)

All DSOs are excepted from discharge under the Bankruptcy Code. In addition, all other marital debts, such as property settlement debts, which are incurred in the course of a divorce or separation are now excepted from discharge in Chapter 7, Chapter 11 and Chapter 12 cases. The only exception is that § 523(a)(15) debts are dischargeable in Chapter 13 cases, but only upon completion of the plan.

Note: Divorce-related debts may be non-dischargeable in Chapter 13 cases on other grounds such as fraud or misrepresentation under 11 U.S.C. § 523(a)(2) and/or breach of fiduciary duty under 11 U.S.C. § 523(a)(4).

VI. Miscellaneous Provisions

Exemptions

11 U.S.C. § 522(c) was amended by BAPCPA to allow DSO creditors to proceed against exempt property.

11 U.S.C. § 522(f) was amended to prevent avoidance of judicial liens for DSOs.

Requirement to Provide Tax Records upon Request of Creditor

11 U.S.C. § 521(e)(2)(A), (B) and (C). A debtor must provide to the trustee a copy of the Federal income tax return (or transcript of such return) for the most recent year ending immediately before the commencement of the bankruptcy case and for which a Federal income tax return was filed, and at the same time the debtor must provide a copy thereof to any creditor that timely requests such copy. Failure to produce such information is grounds for dismissal of the case.

PART FOUR

SELECTED BANKRUPTCY ISSUES AND CASES INVOLVING

BOTH BANKRUPTCY AND DIVORCE

I. Property of the Bankruptcy Estate

Upon filing of a bankruptcy petition, all legal and equitable rights of the debtor in property become property of the bankruptcy estate. 11 U.S.C. 541(a)(1). Property of the estate includes "all interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is under the sole, equal or joint management and control of the debtor; or that is liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable. 11 U.S.C. § 541(a)(2). [See also 11 U.S.C. § 101(7) which defines "community claim" as a pre-petition claim for which community property is liable. See also F.C. §§ 900-916 re: Liability of Marital Property.]

Whether property becomes property of the estate is a question of federal law; however, state law is used to determine whether the debtor has an interest in the property in question. In determining what is § 541(a)(2) property, issues are raised regarding whether property is characterized as separate or community (this may be affected by whether title is held as community property, joint tenancy or joint tenants), and whether the community property has been divided.

Property of the estate includes the community's interest in the separate property of a spouse, which interest is acquired during marriage based upon the contribution of community property to the spouse's separate property during marriage. With regard to the community's interest in real property the principle is known as the "Moore/Marsden rule." With regard to the community's interest in the value of and/or the earnings from a separate property business, the alternative approaches referred to below have been developed. [See Community Property Interest in Separate Property, above and section on "Property Rights" below.] Property of the estate also includes all rights of reimbursement to which the debtor or the community is entitled. [See Reimbursement Claims, above.]

In re Nassar, No. 2:15-bk-11540-ER (Bankr.C.D.Cal. 2015). In a cautionary tale for spouses whose soon-to-be-ex-spouses may be considering bankruptcy, husband and wife listened in the family court at the end of their divorce trial as the judge made the necessary findings and declared the marriage to be ended effective upon the date of entry judgment, and then directed the spouses' counsel to prepare proposed statements of decision in lieu of closing arguments, indicating a decision would follow. That decision awarded the family residence to wife and the business to husband, and directed wife's counsel to prepare, serve and lodge a judgment in accordance with the decision. Before that was done, husband filed a Chapter 7 case, believing he was divorced, and did not claim the residence as exempt, instead believing it had been awarded to wife, and instead claimed the wild card exemption under CCP 703.140(b)(5). The time to object to the exemptions lapsed and the trustee successfully moved to sell the family residence. Note: The Nassar case served as the basis for "Non-Filing Spouses, Homestead Exemptions, and Voidable Transfers", by Michael G. D'Alba, Cal. Bankr. J., Vol. 34, No. 2 (2017).

II. Characterization Cases

Matter of Paderewski, 564 F.2d 1353 (9th Cir. 1977). If property has been divided by a final order of the divorce, the bankruptcy estate is bound by the terms of that order, subject to any rights which the creditors may retain. See Fraudulent Transfers below.

In re McCoy, 111 B.R. 276 (9th Cir. BAP 1990). Applicable state law determines the characterization of property as separate or community as of the date of one spouse's bankruptcy filing, so as to be included or excluded from property of the estate. The non-debtor spouse's interest in proceeds from the sale of the community property residence is not liable for the debts incurred by the debtor after separation but prior to dissolution or prior to the division of community property. (Applying old California Civil Code § 5120.110) **Note:** A non-debtor spouse's share of the community property may not be available to pay creditors in the bankruptcy estate if there are no community claims.

In re Reed, 940 F.2d 1317 (9th Cir. 1991). Non-debtor's joint tenancy interests are separate property and not property of debtor's estate. State law determines existence and scope of debtor's interest in property. Creditor may argue otherwise based on presumptions and treatment of property under California law.

In re Keller, 185 B.R. 796 (9th Cir. BAP 1995). Proceeds from sale of Chapter 7 debtor's house, which was ordered to be sold by state divorce court pursuant to January 1990 dissolution judgment, were not estate property where state divorce court retained jurisdiction to approve disbursement of proceeds as between debtor and his ex-wife, so proceeds were beyond reach of the debtor or alienation by his creditors.

In re Summers, 332 F.3d 1240 (9th Cir. 2003). Property acquired by spouses through deed as joint tenants was held to be joint tenancy property, not community property. Case appeared to infer that F.C. § 760 presumption that property acquired during marriage was community property could apply (even though no divorce pending); the court stated the presumption could be overcome by evidence that the parties agreed to hold the property as joint tenants, and indicated that the declaration in the deed that parties took the property as joint tenants raised a presumption that the couple intended to take title as joint tenants.

In re Fadel, 2013 WL 2369998 (9th Cir. BAP 2013). Rebuttable presumption that property acquired during marriage is community property is trumped by form of title presumption, coupled with spousal consent, to reflect actual ownership as the sole and separate property of the spouse taking legal title.

In re Mantle, 153 F.3d 1082 (9th Cir. 1998). Sales proceeds from community property residence were property of estate notwithstanding the non-debtor, separated wife's right to reimbursement of her separate property interest.

In re Marriage of Drapeau, 93 Cal.App.4th 1086, 114 Cal.Rptr.2d 6 (2001). Early retirement benefit earned with marital labor during marriage and before separation was community property.

In re Marriage of Iredale, Cates, 121 Cal.App.4th 321, 16 Cal.Rptr.3d 505 (Cal. Ct. App. 2004). Community property interest in spouse's law partnership was limited to value of spouse's partnership capital account.

A. Select Property of the Estate Issues

1. Quasi-Community Property

a. F.C. § 125 defines quasi-community property to mean all property, wherever situated, acquired by either spouse while domiciled outside of California which would have been community property if the spouse who acquired the property had been domiciled in California at the time the property was acquired.

b. The Law Revision Commission in 1983 made a recommendation for recodification and clarification of the law governing the rights of spouses and creditors. They felt that quasi-community property should be treated as community property for the purposes of determining liability of debts. This rule would be consistent with the public policy of California that the marital unit shares its assets and liabilities. Law Revision Commission Report, p. 11. Subsequently former Civil Code Section 5120.120 was enacted in 1984.

c. F.C. § 912 now continues former Civil Code Section 5120.120 and provides that quasi-community property is liable in the same manner and shall be treated the same in all other respects as community property. The result: quasi-community property, like regular community property, is property of the bankruptcy estate.

2. Claims Against Third Parties. Generally, claims against third parties, whether based on contract, statute or common law causes of action (including personal injury claims) are brought into the bankruptcy estate, except for very limited exclusions. Such claims may be contingent, disputed or unliquidated at the time the bankruptcy case is filed.

It is well settled that the trustee in a bankruptcy proceeding steps into the shoes of the debtor where that debtor is a plaintiff in an action for money or property, and the action itself is property of the estate. See Sierra Switchboard Co. v. Westinghouse Elec. Corp., 789 F.2d 705 (9th Cir. 1986) (emotional distress claim asserted pre-petition is property of the subsequently filed bankruptcy estate); Bronner v. Gill (In re Bronner), 135 B.R. 645 (9th Cir. BAP 1992) (lawsuit exempt to extent of proper value of exemption only; lawsuit nonetheless property of estate in control of trustee); Cain v. Hyatt, 101 B.R. 440 (E.D.Pa. 1989) (pre-petition claim for wrongful termination property of bankruptcy estate, and debtor has no standing to prosecute action on own behalf); Havelock v. Taxel (In re Pace), 159 B.R. 890 (9th Cir. BAP 1993) (debtor's and debtor's counsel's attempt to exercise control over pre-petition legal mal-practice action to exclusion of trustee, to whom control over such property runs, punishable by sanctions); Cottrell v. Schilling (In re Cottrell), 876 F.2d 540 (6th Cir. 1989) (pre-petition personal injury action belongs to Chapter 7 trustee as property of the estate, whether or not proceeds thereof are exempt).

3. Contingent, Future and Inchoate Interests

a. Rights of a Spouse in the Other Spouse's Property. What about property solely owned by one spouse during a marriage? In a non-community property state, does the other spouse have an interest in that property by virtue of possible rights in a future divorce? Should those inchoate rights supersede the rights of the bankruptcy trustee of the owning spouse, and do they pass to the bankruptcy estate of the non-owning spouse? Several cases have discussed these equitable, inchoate rights. See U.S. v. Davis, 370 U.S. 65 (1962); In re Tucker, 95 B.R. 796 (Bankr. D. Colo. 1989).

b. Contingent Interests. The bankruptcy estate also includes interests that are contingent upon the happening of a future event. For example, a debtor's contingent right to payments due upon his termination of employment was determined to be property of the estate in In re Ryerson, 739 F.2d 1423 (9th Cir. 1984). The right was contingent because the debtor was still employed on the date of the bankruptcy filing; however, the portion of the right to payment

that was attributable to pre-bankruptcy services was includable in the estate. The court concluded that the right to payment was "sufficiently rooted in the pre-bankruptcy past and so little entangled in the debtor's ability to make a fresh start that it should not be excluded from property of the estate."

Other examples of contingent interests that may be property of the estate include the debtor's possible right to recover on a tort case, an attorney's contingency fee agreement in such a case, the monies to be paid under a special support decree (which can be modified in most states at any time), and the like.

c. Future Interests. A future interest, such as the debtor's right to receive possession of land or other property in the future, if vested at the time of the filing of the bankruptcy, is property of the bankruptcy estate. For example, a debtor's remainder interest in property in which another person has a life estate is property of the estate. In re Kreiss, 72 B.R. 933 (Bankr. E.D. N.Y. 1987). Distributions from a trust, other than a spendthrift trust, may also be property of the estate. The debtor may be entitled, as of the date of the filing of a bankruptcy petition, to property bequeathed in a will or otherwise inherited. Absent valid disclaimer under state law, such an interest, which is vested due to a decedent's death, is also property of the estate. Indeed, some types of future interests, even if not vested as of the date of the bankruptcy, but subsequently vested within 180 days thereafter, are also property of the estate. See discussion of Bankruptcy Code § 541(a)(5) below. Matter of Chenoweth, 3 F.3d 1111 (7th Cir. 1993). In Chenoweth, the debtor was named as a legatee in a will, and the testator died within 180 days of the filing of the petition. The will was not admitted to probate until after the expiration of the 180-day period. The Chenoweth court specifically held that the property, so devised, was property of the estate, regardless of the date of probate or payment. Id. at 1112. The policy behind Chenoweth is sound:

"A different interpretation of the after-acquired provision would gut the provision. It often takes 180 days or more to probate a will, and a legatee who wanted to delay the probate in order to keep a legacy out of a bankrupt's estate would often be able to do so." Id. at 1113.

A right to a tax refund is also property of the estate. Segal v. Rochelle, 382 U.S. 375 (1966).

4. Property Excluded From the EstateProperty Interests Acquired After the Bankruptcy Petition Is Filed. After acquired property of an individual debtor may, or may not be, property of the estate, depending on the Chapter of the case. Before BAPCPA, the earnings of an individual debtor after the commencement of the bankruptcy case, unlike the proceeds or profits of property of the estate, did not become part of the Chapter 7 or 11 estate, but were (and are) property of the Chapter 12 and 13 estate. In a particular case under Chapter 11, the debtor may have chosen to contribute future wages to fund a plan to reorganize a business. Indeed, when the debtor has an ongoing business operated as a sole proprietorship, determining which part of post petition earnings is from personal services and which part is from income attributable to estate property (such as goodwill) is not a simple matter. See In re FitzSimmons, 725 F.2d 1208 (9th Cir. 1984); In re Cooley, 87 B.R. 432 (Bankr. S.D. Tex. 1988). With the amendments under BAPCPA, personal earnings and other property acquired by the debtor after the commencement of the case, but before conversion to a Chapter 7, are property of the estate in Chapter 11 cases under § 1115 (and continue to be so in Chapter 12 and 13 cases). However, personal earnings are still not property of the estate in Chapter 7 cases. See 11 U.S.C. § 541(a)(6).

b. Exceptions to the Rule. Certain property acquired within the 180 days after petition is, nonetheless, property of the estate even in a Chapter 7 case. Specifically, in all Chapters, property acquired by the debtor within 180 days by (a) bequest devise or inheritance, (b) as a result of a marital settlement agreement or divorce decree, or (c) or as a beneficiary of a life insurance policy or death benefit, does become property of the estate. 11 U.S.C. § 541(a)(5). There is nothing magic to the 180 day time period; by all accounts, the 180 days is an arbitrary rule designed to prevent a debtor's ability to manipulate a bankruptcy filing to exclude from its creditors substantial property.

Perhaps a good example of the subtlety of this issue was addressed in In re Robert Kirk Adams, Case No. 94-01921-B7, a case in the United States Bankruptcy Court, Southern District of California. In that case, debtor Robert Kirk Adams had been awarded, pre-petition basis, $16,000 per month in spousal support to be paid by his ex-wife, Judith Straub Adams. Mr. Adams filed a bankruptcy proceeding in an attempt to preserve the entire $16,000 per month to him as his exempt property. Upon objection by the trustee, Mr. Adams contended that the payments coming to him greater than 180 days after the filing of the case were specifically excluded from property of the estate under § 541(a)(5). The trustee countered that the right to receive the post-petition payments was itself granted pre-petition and, therefore, the payments coming due post-petition were merely proceeds of a pre-petition property right. The Court ruled in favor of the trustee.

III. Community Property Interest in Separate Property

In re Marriage of Moore, 28 Cal.3d 366, 168 Cal.Rptr. 662 (1980) and In re Marriage of Marsden, 130 Cal.App.3d 426, 181 Cal.Rptr. 910 (1982). When community property is contributed to the separate property of a spouse during marriage, the community acquires an interest in the property. This principle is known as the "Moore/Marsden rule" and addresses the apportionment of the appreciation in value to a spouse's separate property due to funds expended by the community.

Bono v. Clark, 103 Cal.App.4th 1409, 128 Cal.Rptr.2d 31 (2002). Ex-spouse had pro-tanto interest in other spouse's separate property where community property was used to pay for improvements. Cites In re Marriage of Wolfe, 91 Cal.App.4th 962 (2001), In re Marriage of Allen, 96 Cal.App.4th 497 (2002) and application of *Moore/Marsden* rule.

In re Marriage of Zaentz, 218 Cal.App.3d 154, 267 Cal.Rptr. 31 (1990). Court affirmed finding that community was entitled to $600,000 as compensation for husband's contributions to the movie "Amadeus" which was owned by SZC, a corporation which had been formed by husband prior to the parties' marriage. Case discusses the two models generally used in apportioning increased value in separate property. The *Pereira* approach is to allocate a return on the separate property investment as separate income and to allocate any excess to the community property as arising from the husband's efforts. Pereira v. Pereira, 156 Cal. 1, 103 Pac.Rptr. 488 (1909). The *Van Camp* approach is to determine the reasonable value of the husband's services and to allocate that amount as community property, and treat the balance as separate property attributable to the normal earnings of the separate estate. Van Camp v. Van Camp, 53 Cal.App. 17, 199 Pac.Rptr. 885 (1921).

In re Marriage of Koester, 73 Cal.App.4th 1032, 87 Cal.Rptr.2d 76 (1999). Husband's separate property business incorporated during marriage did not become community property, requiring calculation of respective contributions of effort and return on capital pursuant to Pereira v. Pereira, 156 Cal. 1 , 7-8, 103 Pac.Rptr. 488, 491-492 (1909), as opposed to F.C. § 2640 dollar-for-dollar reimbursement.

In re Marriage of Iredale, Cates, 121 Cal.App.4th 321, 16 Cal.Rptr. 505 (2004). Community property interest in spouse's law partnership was limited to value of spouse's partnership capital account.

IV. Sale of Co-Owned Property

11 U.S.C. § 363(h) provides the basis for a trustee to sell both the estate's interest, and the interest of any co-owner in property in which the debtor had, at the time of the commencement of the case, an undivided interest as a tenant in common, joint tenant, or tenant by the entirety, subject to certain conditions.

Property of the debtor and debtor's spouse in community property is generally property of the estate, and can therefore be sold by a trustee. 11 U.S.C. § 541(a)(2). However, if the debtor is a Registered Domestic Partner, only the debtor's interest in community property is property of the estate. Therefore, there may be no basis to sell such co-owned property under 11 U.S.C. § 363(h).

V. Reimbursement Claims

See Reimbursement Claims above.

In re Mantle, 153 F.3d 1082 (9th Cir. 1998). Sales proceeds from community property residence were property of the estate notwithstanding the non-debtor separated wife's right to reimbursement of her separate property interest.

In re Marriage of Nicholson and Sparks, 104 Cal.App.4th 289, 127 Cal.Rptr.2d 882 (2002). Separate property contributions toward payoff of community credit card debt was not reimbursable from the community even where the payoff was a prerequisite to the community's acquisition of real property, in that it was unrelated to improvement of the property. F.C. § 2640.

VI. Post-Petition Earnings

In re Goldstein, WL 19702632007 (Bankr. C.D.Cal. 2007). Pursuant to 11 U.S.C. § 1115(a)(2), post-petition earnings of individual Chapter 11 debtor are property of the estate. The court authorized the appointment of two special counsel to represent joint debtors in dissolution proceedings.

VII. Distribution of the Estate to Creditors

In addressing the distribution of property of the bankruptcy estate, issues are raised regarding whether any of the debtor's debts are his/her separate debts, i.e., what happens if most of the debtor's debts are post-separation obligations for which the non-debtor's share of the community property is not liable? In that event, the non-debtor spouse's share of the community property is not liable for the debts incurred by the debtor after separation but prior to dissolution or prior to the division of community property. Should the non-debtor spouse seek relief from stay to proceed in the Superior Court to determine the respective interests in the community property?

The bankruptcy estate is required to segregate community property for distribution purposes; community property is distributed first to holders of community claims. 11 U.S.C. § 726(c).

In re Merlino, 62 B.R. 836 (Bankr. W.D. Wa. 1986). Creditor bank commenced involuntary Chapter 7 against debtor in his separate capacity and filed creditor claim, to which objection was

filed claiming that it was not a "community claim" and not allowable against community assets. Held that § 726(c) did not entitle bank to distribution of community property for separate debt of husband-debtor. This case also sets forth the four "sub-estates" created by § 726(c)(2)(A)-(D).

VIII. Filing and Allowance Claims

Although 11 U.S.C. § 726 controls the distribution of proceeds of the estate, §§ 501-510 relate to various issues which must be determined before a distribution of estate proceeds can be made. It is important to be aware of whether a proof of claim must be filed, and if so, the deadlines for filing such claims (which` vary based on the Chapter under which the case is filed). As noted previously, whether a claim will be allowed as secured, priority and/or unsecured is also an important issue which must be addressed early on in a bankruptcy case.

BAPCPA amended 11 U.S.C. § 507 to provide first priority status to DSOs. Case law interpreting 11 U.S.C. § 507 and § 523(a)(5) defining "debts in the nature of support" is useful in determining what qualifies as a DSO, although it appears that the new definition was intended to broaden the class of obligations entitled to DSO status.

Note: Priority creditors must take timely action to preserve their rights. They can play an important role in Chapter 11 and Chapter 13 cases since a plan cannot be confirmed without their acceptance or full payment of their claim. However, acceptance may be assumed if a creditor does not take timely action. Furthermore, under BAPCPA, a Chapter 13 debtor must certify that post-petition DSOs which have become due have been paid in order to receive his/her discharge, and failure to pay any DSO that becomes due after filing a Chapter 13 case is grounds for conversion or dismissal of the case.

Claim or Property Right: It is important to determine whether the non-debtor spouse or ex-spouse has a property right or a claim for money. If it is a claim for money (and not a DSO), advise the non-debtor party to investigate preserving such party's rights against the debtor in a timely manner; otherwise, any claim against the debtor may be barred by the injunction granted the debtor by the bankruptcy discharge.

IX. The Automatic Stay

It is a violation of the automatic stay to commence or continue a civil proceeding to the extent such proceeding seeks to determine the division of property that is property of the bankruptcy estate. 11 U.S.C. § 362(b)(2)(A)(iv). Section 362(b)(2) has been expanded to except from the automatic stay the commencement or continuation of a civil proceeding for the establishment of paternity, the establishment or modification of an order for domestic support obligations, actions, concerning child custody or visitation, the dissolution of marriage and/or regarding domestic violence.

Section 362(b)(2)(B) also excepts from the automatic stay the collection of a DSO from property that is not property of the estate. Whether an attorney's fee order is a DSO and therefore excepted from the automatic stay may require an evidentiary hearing and determination by either the Bankruptcy Court or the Superior Court. See In re O'Brien, 339 B.R. 529 (Bankr. D. Mass. 2006). Debtors and creditors will likely prefer different forums to make that determination.

Section 362(b)(2)(C) excepts from the automatic stay the withholding of income that is property of the estate or property of the debtor for payment of a DSO under a judicial or administrative order or a statute.

Note: The collection of arrears, however, may still be subject to the automatic stay.

See In re Gellington, 363 B.R. 497 (Bankr. N.D. Tex. 2007), which held that although the attorney general's post-petition garnishment of a debtor's wages to collect child support arrears which were to be paid through a Chapter 13 plan did not violate the automatic stay, the attorney general was bound by the terms of the debtor's confirmed plan providing for payment of the claim through the plan, and therefore, the garnished wages had to be returned and the garnishment terminated.

An individual who is injured by any willful violation of the automatic stay shall recover actual damages, including costs and attorneys' fees, and in appropriate circumstances, may recover punitive damages. 11 U.S.C. § 362(h). "Willful" means with knowledge of the bankruptcy case. In re Bloom, 875 F.2d 224 (9th Cir. 1989). Any act in violation of the automatic stay is void. In re Schwartz, 954 F.2d 569 (9th Cir. 1992).

Non-bankruptcy practitioners must pay attention to the difference between the stay imposed against property of the estate versus the stay imposed against the debtor personally. Oftentimes, the stay against the debtor has terminated, and yet the stay is still in effect as it relates to property of the estate which is still subject to administration in the case.

In re Caffey, 384 B.R. 297 (Bankr. S.D. Ala. 2008). This case should lead to caution on the part of enforcers of DSOs and their counsel. A Chapter 11 debtor who was jailed post-petition for his failure to pay past-due child support, filed an adversary complaint against the creditor-mother of a child for whom he owed support, seeking damages for the creditor's alleged violation of the automatic stay.

Although the Code contains an exception to the stay for collection of support obligations, pursuant to § 362(b)(2)(B) it only pertains to non-estate property. The court thus found that the state-court contempt order issued in connection with Chapter 11 debtor's past-due child support obligation, as well as writ of arrest issued by state court, both of which were issued postpetition, willfully violated the automatic stay and, thus, were void ab initio and were without force or effect. The court awarded the debtor significant damages for emotional distress, lost income, attorney's fees and punitive damages. The target of the court's wrath was not any particular conduct by the creditor herself, but that of the creditor's attorneys who with full knowledge of the effect of the automatic stay allowed the debtor to be jailed and money to be taken from the estate that belonged to all the creditors.

In re Gruntz, 202 F.3d 1074 (9th Cir. 2000). Any state court modification of the automatic stay would constitute an unauthorized infringement upon the Bankruptcy Court's jurisdiction to enforce the automatic stay. **Note:** Although a state court can act and/or make a ruling if it determines the act or ruling does not violate the automatic stay, the act or ruling is void if a Bankruptcy Court subsequently rules that the act or ruling violated the stay.

In re Allen, 275 F.3d 1160 (9th Cir. 2002). Wife's efforts to modify existing support order on grounds she incurred extraordinary uninsured health costs were within the plain meaning of § 362(b)(2)(A)(ii), and thus, did not violate the automatic stay imposed by the husband's Chapter 13 bankruptcy filing. **Note:** However, wife might need relief from the automatic stay to collect any increased support award from property of the estate, or based upon BAPCPA, the debtor may need to modify his Chapter 13 plan to provide for payment in order to receive his discharge.

In re Levenstein, 371 B.R. 45 (Bankr. S.D. N.Y. 2007). Automatic stay imposed against foreclosure proceedings with regard to real property in name of non-filing estranged spouse of debtor where debtor claimed interest in marital property.

Sternberg v. Johnston, 582 F.3d 1114 (9th Cir. 2009). Chapter 11 debtor commenced adversary proceeding charging ex-wife and her attorney with willfully violating automatic stay by state court proceeding to hold debtor in contempt for non-payment of spousal support. The Bankruptcy Court vacated the state court's contempt order as the violating automatic stay, but granted motion of ex-wife and attorney for directed verdict. Debtor appealed. The District Court reversed and remanded. After debtor settled with ex-wife, the Bankruptcy Court ruled on remand that attorney willfully violated automatic stay, awarded damages for debtor's emotional distress, and awarded attorney fees and costs. Attorney appealed. The Court of Appeals, held that:

> (1) attorney willfully violated automatic stay by defending overbroad state court order, and
> (2) debtor was entitled to limited award of attorney fees.

X. Abstention or Relief From Stay - Jurisdictional Issues

If a dissolution was filed before the bankruptcy and is still pending, the state court no longer has jurisdiction over property of the estate. In re Teel, 34 B.R. 762 (9th Cir. BAP 1983). Therefore, if the non-filing estranged spouse or ex-spouse of the debtor would prefer the state court to determine the respective separate and community interests in the debts and assets of the parties, relief from the automatic stay must be obtained from the bankruptcy court pursuant to 11 U.S.C. § 362, or abstention must be obtained under 11 U.S.C. § 305. The debtor may also file a motion for abstention under 11 U.S.C. § 305 and 28 U.S.C. § 1334(c). The bankruptcy court has jurisdiction over the distribution of property even if it has abstained to allow the state court to determine the rights of the spouses to a property division. In re French, 139 B.R. 476 (Bankr. D. S.D. 1992).

XI. Exemptions

An individual debtor is generally entitled to claim certain property as exempt under state law, and to retain such property to the extent it is allowed as exempt. California provides a debtor with a choice of two (2) sets of exemptions --- those provided under C.C.P. § 703.140(b) [includes a "wildcard" exemption] and those provided under C.C.P. § 704.010 et seq. [includes a homestead/dwelling exemption].

Note: See C.C.P. § 703.140(a)(2) regarding the necessity of a spousal waiver in order to use the exemptions under Section 703.140 if only one spouse files bankruptcy.

A. The Constitutionality of Bankruptcy-Specific State Exemption Laws

There is a split in the courts as to whether congress' enactment of the 11 U.S.C. § 522(b)(2) "opt-out" provision was intended to allow states to adopt bankruptcy specific provisions such as the California wildcard exemption or whether, as in other areas of Bankruptcy Code, the uniformity and supremacy clauses of the United States Constitution should preclude the adoption of state bankruptcy-specific laws.

Under the Bankruptcy Clause, Congress was granted the power to "establish ... *uniform* Laws on the subject of Bankruptcies." U.S. Const., Art. I, § 8, cl. 4 (emphasis added). The Supreme Court has acknowledged that "state laws are suspended only to the extent of actual conflict with the

system provided by the Bankruptcy Act of Congress." Butner v. U.S., 440 U.S. 48 (U.S.N.C., 1979), 55 n. 9 (1979) (citing Sturges v. Crowninshield, 17 U.S. 122, 4 L.Ed. 529, 2 Wheat. 122 (1819)).

Some courts have held that so long as the bankruptcy-specific state exemption does not conflict with the overarching purposes of the Bankruptcy Code, it is not preempted. See In re Urban, 375 B.R. 882 (9th Cir. BAP 2007) (730 day domicile rule for homestead exemption did not offend uniformity requirement); In re Morrell, 394 B.R. 405 (Bankr. N.D. W.Va. 2008) ($25,000 bankruptcy homestead exemption, that is $5,000 greater than non-bankruptcy exemption, did not offend federal supremacy); In re Brown, 2007 WL 2120380 (Bankr. N.D. N.Y. 2007) aff'd, 2007 WL 4560671 (N.D. N.Y. 2007) (distinctive homestead in bankruptcy).

In In re Regevig, 389 B.R. 736 (Bankr. D. Ariz. 2008), however, the court found that the California exemption statute which was applicable only to debtors in bankruptcy (and not debtors under other circumstances), and under which debtors were entitled to "wildcard" exemptions in an amount roughly double the amount of the Bankruptcy Code's "wildcard" exemption, was invalid, as violating the Supremacy Clause.

Under the California bankruptcy-only exemptions at the time of the Regevig case, the value for the wild card was $1,100 plus any unused portion of the homestead exemption, which was $20,725. Regevig, 389 B.R. at 738. The Bankruptcy Code's "wild card" exemption was similar, except the amount was then $1,075 plus up to $10,125 of the unused portion of the then $20,200 homestead exemption. 11 U.S.C. § 522(d)(5). The court noted that the wild card exemption was the only significant state deviation from the federal limits. Id. at 739. The court conjectured that the difference in exemptions for all other property between the California Statute were likely due to the adjustment of the amounts under the California statute according to the California cost of living under C.C.P. § 703.150 as opposed to the national consumer price index that is used by the Bankruptcy Code under § 104(b). Id.

The court essentially advanced two arguments in support of its position that the Bankruptcy code has pre-empted state legislation on the matter. Id. at 740, 741. The court maintained that Congress' intent to supersede state law altogether may be found from a general scheme of federal bankruptcy regulation that is "so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it." Id. at 740 (citing to Sherwood Partners, Inc. v. Lycos, Inc., 394 F.3d 1198, 1203-06 (9th Cir. 2005)). The court also argued that the Code's list in § 522(b)(2) of possible bankruptcy-specific exemptions that states may offer if they opt for the federal exemptions indicates that "Congress has occupied the field." Id. at 741.

But see In re Applebaum, 422 B.R. 684 (9th Cir. BAP 2009), which found no conflict between the Bankruptcy Code purpose and the bankruptcy-only statute, criticizing Regevig.

Note: This issue is still not totally determined.

B. Spousal Support Award Is spousal support a "personal" interest and therefore excluded from property of the estate, or is it "property" and therefore included in property of the estate? This issue may depend on applicable state law. See In re Anders, 151 B.R. 543 (Bankr. D. Nev. 1993) (right to receive past due maintenance property of the estate); See contra In re Wise, 346 F.3d 1239 (10th Cir. 2003) (Colorado law).

Under California law, the debtor has a right to receive alimony, support and maintenance to the extent reasonably necessary for the support of the debtor and dependents of the debtor. C.C.P. §703.140(b)(10)(D).

One of the hottest issues in divorce and exemption law is the nature and extent of the spousal support award exemption. In re Ross, 128 B.R. 785 (Bankr. C.D. Cal. 1991) (debtor has burden of proving how much of alimony and support is reasonably necessary for support under California exemption); In re Benjamin, 136 B.R. 574 (Bankr. S.D. Fla. 1992) ("lump sum alimony" was actually property division and was not exempt); In re Anders, 151 B.R. 543 (Bankr. D. Nev. 1993) (spousal support paid past 180 days after petition was exempt as "personal" interest, not property interest); In re Mehlhaff, 2013 Bankr. LEXIS 944 (Bankr. D. S.D. 2013) (debtor required to turn over alimony payments she received from her ex-husband post-petition and her right to receive those payments).

Anders was not followed in a celebrated case in the United States Bankruptcy Court, Southern District of California, In re Robert Kirk Adams, case no. 94-01921-B7 . In the Adams case, the debtor contended that payments due under a spousal support award were "personal" and not "property," therefore excluded from property of the estate. The Trustee, having objected to the debtor's attempt to keep for himself $16,000 per month in spousal support, countered that a right to money is itself a property right, and that the money so paid is merely proceeds of that property right. Whatever the result under Nevada law, as interpreted in Anders, the California bankruptcy court in Adams concluded (in a well-reasoned, unpublished opinion) that in California, like the Federal Bankruptcy Code, spousal support payments are property interests; to hold otherwise would leave the limitation of section 522(d)(10)(D) -- that such amounts are only exempt "to the extent reasonably necessary for support" -- with no meaning.

For more on this issue, See *Christopher Celentino Divorce and Bankruptcy: Spousal Support as Property of the Estate*, 28, No. 8 Cal. Bankr. J. 542 (2006).

a. Only Amounts Required for "Basic Needs" Are "Reasonably Necessary for Support." -- A State Court's Award of "Spousal Support" Does Not Establish the "Support" Amount of the Exemption

It should be noted that when a state court awards "spousal support," the amount awarded does not establish the amount "reasonably necessary for support" for purposes of the exemption. Indeed, if it did, the phrase "reasonably necessary for support" would have no function -- it would always yield an exemption equal to the full amount of the "support" award.

For example, in California, as in many states, "spousal support" awards take into account much more than the basic needs of the recipient. In particular, they often take into account the payor-spouse's ability to pay and the parties' pre-separation standard of living, factors that have no relevance to exemption law. California Family Code §§ 4320-4326. That is precisely why Bankruptcy Code § 522(d)(10)(D) is limited by the "reasonably necessary for support" language whereas other parts of § 522(d)(10), though similarly focused on future earnings, are not similarly limited. See 3 Collier on Bankruptcy ¶ 522.19 at 522-76 (15th ed. rev. 2008); Bankruptcy Code § 522(d)(10)(A) (social security and unemployment compensation), (d)(10)(B) (veterans' benefit), (d)(10)(C) (disability, illness or unemployment benefit)). "Spousal support" awards serve one set of policies; exemption "support" determinations serve entirely another.

b. Determining Amounts "Reasonably Necessary for Support" Involves a Consideration of Multiple Factors -- The Applicable Factors.

The Bankruptcy Court is charged to determine the debtor's "basic needs," measured by objective standards, to assess what portion of the spousal-support award is "reasonably necessary for [debtor's] support." To assist in that process, in the context of Bankruptcy Code § 522(d)(10)(E)'s pension exemption, the bankruptcy courts have developed a list of relevant factors. That list is, for the most part, is also relevant in the context of a spousal-support exemption determination. The list includes these items:

(1) Debtor's present and anticipated living expenses;

(2) Debtor's present and anticipated income from all sources;

(3) Age of the debtor and dependents;

(4) Health of the debtor and dependents;

(5) Debtor's ability to work and earn a living;

(6) Debtor's job skills, training, and education;

(7) Debtor's other assets, including exempt assets;[1]

(8) Liquidity of other assets;

(9) Special needs of the debtor and dependents;

(10) Debtor's financial obligations, e.g., alimony or support payments.

In re Link, 172 B.R. 707, 710-11 (Bankr. D. Mass. 1994) (citing cases); accord, In re Moffat, 119 B.R. 201, 206 (9th Cir. BAP 1990) (applying factors to C.C.P. § 704.100(c) annuity exemption), aff'd, 959 F.2d 740 (9th Cir. 1992); to similar effect, see In re Ross, 128 B.R. 785, 789 (Bankr. C.D. Cal. 1991) (applying California analogous § 522(b)(10)(D) statute).

Again, however, as the court in In re Link made clear, these factors do not exist in a vacuum: they must be applied with reference to the general principle that "[t]he exemption is not intended to continue the debtor's standard of living in the future, but is to be used to provide for the basic needs of the debtor and any dependents." Link, 172 B.R. at 711 (emphasis added).[2]

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[1] This factor is also prescribed by any analogous state law exemption statutes. For example, California law, C.C.P. § 703.115, directs that "the court shall take into account all property of the judgment debtor, . . . whether or not such property is subject to enforcement of the money judgment."

[2] One additional factor which the courts have typically included in the context of § 522(d)(10)(E)'s retirement-benefits exemption context is "the Debtor's ability to save for retirement." In re Link, 172 B.R. 707, 711 (Bankr. D.Mass 1994) ("whether the age of the debtor will permit the funding of a new retirement plan if the IRA is held to be non-exempt"). But in that context the focus is on both present need and the debtor's "ability to rebuild the retirement fund if [it is] purged" by a disallowance of the exemption. See In re Dalaimo, 88 B.R. 268, 272 (Bankr. S.D. Cal. 1988) (applying C.C.P. § 704.115(e)). See also In re Switzer, 146 B.R. 1, 4-7 (Bankr. C.D. Cal. 1992). In the spousal-support context, where there is no retirement fund at issue, that should generally not be relevant.

Thus, the court must separate the "necessary" from the "discretionary," a process which one court described usefully this way in the context of Bankruptcy Code § 1325(b):

> [T]he proper methodology is to aggregate all expenses projected by the debtor which are somewhat more discretionary in nature, and any excessive amounts in the relatively nondiscretionary line items such as food, utilities, housing, and health expenses, to quantify a sum which, for lack of a better term, will be called "discretionary spending."
>
> The task before me, therefore, is to identify how much of the Debtors' anticipated expenses are discretionary in nature and to weigh them on this scale. If the discretionary expenses in the aggregate allow the Debtors to exceed their basic needs, including a reasonable reserve for recreation and exigencies (the reasonable "cushion"), then their plan cannot be confirmed.

In re Gonzales, 157 B.R. 604, 609 (Bankr. E.D. Mich. 1993) (held $330 monthly discretionary spending -- $70 for recreation and $260 for master's program -- too large to be reasonable).

As the court held in In re Moffat, 107 B.R. 255, 262 (Bankr. C.D. Cal. 1989), aff'd, 959 F.2d 740 (9th Cir. 1992): "The measure of 'reasonably necessary' is...the objective standard of how much a debtor reasonably needs to live."

Homestead Cases

BAPCPA added § 522(o) to provide a way to reduce a debtor's homestead exemption if the equity claimed exempt was increased by disposing of non-exempt property and the proceeds used to pay down the encumbrance on the homestead with the intent to hinder, delay, or defraud a creditor, within the 10-year period prior to the bankruptcy filing.

In re Rowe, 236 B.R. 11 (9th Cir. BAP 1999). Under Nevada law, joint debtors who were living apart could claim only one homestead exemption. **NOTE:** Timing is sometimes critical one month after debtors filed for bankruptcy, they divorced.

In re Rabin, 359 B.R. 242 (9th Cir. BAP 2007). California registered domestic partners share same homestead exemption as married persons. Good discussion of interplay of bankruptcy and domestic partnership law in California.

In re Lawley, 130 B.R. 568 (Bankr. E.D. Cal. 1991). Debtor-husband, whose minor children's principal residence was with their mother (post-dissolution), was not entitled to homestead exemption as member of family unit. (Former wife objected)

In re Wilson, 341 B.R. 21 (9th Cir. BAP 2006). Debtor lacked "intent" to claim homestead exemption in residence awarded to spouse from which debtor had already been excluded, notwithstanding that he was entitled to receive almost one-half of the sales proceeds.

c. Administration of Exempt Assets to Pay Domestic Support Obligation

Prior to BAPCPA, 11 U.S.C. § 522(c) provided that "...property exempted under this section is not liable during or after the case for any debt of the debtor that arose, ... 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." Section 523(a)(1) referred to certain tax debts and section 523(a)(5) referred generally to debts in the nature of support. BAPCPA amended § 522(c)(1) by adding language that says, "(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))". Some Chapter 7 trustees have tried to assert that under BAPCPA they have the right to administer exempt property for the benefit of the domestic support creditor.

Under pre-BAPCPA law, the case of In re Davis, 170 F.3d 475 (5th Cir. 1999), held that the bankruptcy statute providing that property claimed by debtor as exempt will not be liable for any prepetition debts, except for certain nondischargeable tax and familial support obligations, does not create "liability" of exempt property for specified debts following bankruptcy, but instead permits creditors holding such claims to proceed against property after bankruptcy based on rights and remedies they would have had under state law if bankruptcy had not been filed. If the state precluded a creditor from pursuing exempt property, the creditor could not seek payment from the exempt property, notwithstanding the bankruptcy section indicating otherwise.

The newly added language seems to indicate that exempt property will be liable notwithstanding nonbankruptcy law to the contrary. If that is so, it would seem that the bankruptcy court may be the only available forum to enforce collection against exempt property (but see In re Grazieadei, below, and the cases cited therein regarding the lack of the bankruptcy court's subject matter jurisdiction over exempt property).

In re Graziadei, 32 F.3d 1408 (9th Cir. 1994). Bankruptcy Court had no jurisdiction over exempt property and no jurisdiction to order debtor to turnover sale proceeds to attorney for debtor's former wife, which fell within homestead exemption. Since order was void (no jurisdiction), money had to be returned to trustee. However, in a footnote, the court distinguished the case of Breedlove v. Breedlove, 100 Nev. 606, 691 P.2d 426 (1984), which held that a debtor is barred from using the homestead exemption as a defense against making support payments to an *ex-spouse* reasoning that the homestead exemption's very purpose was to support *family members* of the debtor. The Graziadei court stated, "By contrast, this case does not involve payments to an ex-spouse, but rather to her attorney for attorney's fees and costs." Query, whether the court would rule differently based upon the change in 11 U.S.C.§ 522(c)(1).

Since the enactment of BAPCPA, courts have generally held that a Chapter 7 trustee may not administer an asset claimed exempt which is fully exempt for the sole purpose of paying a DSO. See In re Covington, 368 B.R. 38 (Bankr. E.D. Cal. 2006), In re Vandeventer, 368 B.R. 50 (Bankr. C.D. Ill. 2007) and In re Quezada, 368 B.R. 44 (Bankr. S.D. Fla. 2007). However, where the asset is property of the estate, and the debtor claims a portion of the proceeds of sale of the asset to be exempt, it appears that depending on the application of state law to the exempt property, courts may very will allow a trustee to distribute otherwise exempt proceeds to satisfy a DSO. See dicta in In re Quezada, 368 B.R. 44 (Bankr. S.D. Fla. 2007) and In re Covington, supra.

In re Elmasri, 369 B.R. 96 (Bankr. E.D. N.Y. 2007). Although the bankruptcy court abstained from determining whether a DSO could be enforced against a debtor's homestead exemption under New York state law, and therefore denied an ex-spouse's request for the trustee to turnover otherwise exempt proceeds from the sale of the debtor's home, the court restrained the Chapter 7 trustee from distributing the proceeds to the debtor pending a determination by the state court as to whether the proceeds could be used to satisfy the domestic support obligation.

In re Galtieri, 172 Fed.Appx. 397 (3rd Cir. 2006). Not selected for publication. Not Precedential. Bankruptcy Code allowed access to otherwise exempt property to pay nondischargeable domestic support obligations. Property was distributed by trustee who held proceeds from sale of home.

XII. Trustee's Avoidance Powers

The trustee appointed to administer the debtor's estate, or the debtor-in-possession if no trustee is appointed, may avoid **preferences** (i.e. generally transfers on account of antecedent debts) made within ninety (90) days of the filing of the debtor's bankruptcy petition, or in the case of insiders (such as relatives, spouses or partners), made within one (1) year of the filing of the petition. However, bona fide DSO payments may not be avoided by a trustee. 11 U.S.C. § 547(c)(7).

The trustee or debtor-in-possession may also avoid **fraudulent transfers** made within two (2) years of the filing of the petition under federal bankruptcy law and generally within four (4) years under state law (and in some circumstances within ten (10) years if made to a "self-settled trust or similar device"), as well as **unauthorized post-petition transfers** made after the filing of the petition, and unperfected security interests under his or her **strong arm powers**.

XIII. Preference Cases

11 U.S.C. § 547. A preference is a pre-bankruptcy transfer of a debtor's interest in property made to or for the benefit of a creditor while the debtor is insolvent that allows a creditor to receive more than he/she would have received in a Chapter 7. This could be payment, perfection of a security interest, obtaining a judgment lien or other kind of transfer. In re Rhoads, 130 B.R. 565 (Bankr. C.D. Cal. 1991); Grassmueck v. Food Industries Credit Union, 127 B.R. 869 (Bankr. D. Or. 1991) (payments for car awarded debtor's spouse in the divorce within 90 days of filing were preferences). Preferences may also be transfers of community property to a third party by a debtor's spouse. Such transfers are avoidable and recoverable by the trustee if made to a non-insider within 90 days of filing or to an insider within one year of filing. Is the former spouse an insider, making the preference period one year? Trustee can generally recover payments made to wife within 1 year of filing as a preference due to the fact she is an insider under the Bankruptcy Code. 11 U.S.C. § 101(30)(A)(i). Insider is determined by the closeness of the parties and the degree to which the transferee is able to exert control or influence over the debtor. In re Schuman, 81 B.R. 583 (9th Cir. BAP 1987); In re Ishaq, 129 B.R. 206 (Bankr. D. Or. 1991); In re Whaley, 1995 Bankr. LEXIS 1898 (N.D. Miss. 1995) (preference analysis of ex-husband seeking to avoid alimony and support payment fails; wife wasn't receiving any more than she would in a hypothetical Chapter 7 situation since those obligations are nondischargeable).

In re Keller, 185 B.R. 796 (9th Cir. BAP 1995). Distribution adjustments made with respect to divorced spouses' interests in proceeds from sale of family residence made by family law court within 90 days of debtor-husband's bankruptcy filing were not preferential transfers inasmuch as debtor never had vested right in sale proceeds, so proceeds were not estate property.

In re Glass, 164 B.R. 759 (9th Cir. BAP 1994). Debtor no longer had right to claim homestead in property transferred to son less than 90 days prior to bankruptcy which trustee recovered for benefit of the estate based on 11 U.S.C.§ 522(g).

XIV. Transmutations and Other Fraudulent Transfers

Between Spouses in Fraud of Creditors' Rights. Awarding property of one spouse to the other pursuant to a divorce decree is a transfer which may in some cases be fraudulent as to creditor. Matter of Perez, 954 F.2d 1026 (5th Cir. 1992); In re Bucci, 97 B.R. 954 (Bankr. N.D. Ill. 1989) aff'd, 103 B.R. 927 (N.D. Ill. 1989) and 905 F.2d 1111 (7th Cir. 1990) (transfers, with apparent retained interest, to former spouse and son at divorce were fraudulent as to creditors. Debtor was also denied discharge); Matter of Holloway, 955 F.2d 1008 (5th Cir. 1992) (transfer of security interest to wife was fraudulent even though debtor's wife had previously made unsecured loans); In re Clausen, 44 B.R. 41 (Bankr. D. Minn. 1984) (allowing the debtor's spouse to receive all

property of the parties by default constituted a fraudulent conveyance); In re Whaley, supra, where alimony and support are at reasonable levels, they aren't fraudulent, especially since nonpayment would lead to jail for contempt of Chancery court.

Trustee Can Recover Property Transferred to Ex-Spouse. Trustee can recover property given to debtor's spouse due to the fact that debtor received less than reasonably equivalent value in the exchange or made with an intent to hinder, delay or defraud creditors, if transfer was made or incurred on or within 2 years before the date of the filing of the petition. 11 U.S.C. 548. The property transferred under a marital settlement agreement ("MSA") is not beyond the reach of the bankruptcy trustee. In re Lange, 35 B.R. 579 (Bankr. E.D. Miss. 1983); In re O'Connor, 1995 Bankr. LEXIS 300 (M.D. Fla., February 3, 1995) (Debtor was entitled to half of proceeds from sale of all stock of corporation which had been held by debtor and ex-wife. If those proceeds were transferred to ex-wife, it was fraudulent). Trustee may also seek recovery of property under 11 U.S.C. § 544(b)(1) – i.e., utilizing the applicable state law fraudulent transfer laws. See below discussion of Section 544.

Reasonably Equivalent Value. Courts do not usually overturn the valuation issues decided by the divorce courts. If the bankruptcy court had to do a detailed analysis regarding the reasonably equivalent value, it would consider all of the information considered by the divorce court and as such, the bankruptcy court should not overturn that decision. Furthermore, even if the transfer was not litigated in the divorce action, but was rather a product of debate and a stipulation of divorce, the court still would not likely overturn it as long as it appears to be within the range of likely distribution had it been fully litigated. In re Surlucco, 68 B.R. 748 (Bankr. D. N.H. 1986); Snyder v. United States, 1995 U.S. Dist. LEXIS 13283 (E.D. N.Y. 1995). A party asserting a claim of fraudulent conveyance bears the burden of establishing that the conveyance was made without fair consideration. Where the conveyance involves family members a heavier burden is placed on the grantee to demonstrate fair consideration. An agreement between spouses to remain married and continue to live together cannot, as a matter of law, constitute fair consideration.

Fair Consideration Is Reasonably Equivalent Value. A transfer of property in return for a release of future periodic payments can be considered reasonably equivalent value. Matter of Ottaviano, 63 B.R. 338 (Bankr. D. Conn. 1986). "Reasonably equivalent value does not require an exact amount." In re Riso, 102 B.R. 280 (Bankr. D. N.H. 1989).

Collateral Estoppel Applies to Divorce Orders. Husband brought action against former spouse to avoid the transfer of property she received as part of the divorce property settlement. He claimed he was rendered insolvent, received less than reasonably equivalent value and they should be recovered for his estate. In a situation like this, the court ruled that he was collaterally estopped from asserting this position due to the fact that the state court divorce determined the property settlement was fair and equitable under the same criteria used in § 548. In re Falk, 98 B.R. 472 (D. Minn. 1989); In re Capps, 1995 Bankr. LEXIS 2001 (S.D. Ala., September 29, 1995). Where the factual findings contained in a consent judgment indicated that the parties intended that the judgment operate as a final adjudication of the factual issues therein, the bankruptcy court is collaterally estopped from relitigating those issues in a subsequent dischargeability proceeding.

Trustee Has Broad Powers to Void Transfers. Debtors cannot operate in a vacuum. The trustee can look at surrounding circumstances to determine whether a transfer was fraudulent or not. In one case, debtor transferred his ½ interest in his house to his wife as "lump sum alimony." However, he remained in the home, no dissolution of marriage took place and they got back together four months after the transfer. The trustee was able to set this aside as a fraudulent transfer

since the debtor did not receive reasonably equivalent value for the transfer. Matter of Kaczorowski, 87 B.R. 1 (Bankr. D. Conn. 1988).

Trustee Can Also Use State Law to Avoid Transfers Under 11 U.S.C. 544. Most states have adopted either the Uniform Fraudulent Conveyance Act or the Uniform Fraudulent Transfer Act. Under 11 U.S.C. § 544(b), a trustee may employ applicable state law fraudulent transfer laws to recover fraudulently transferred property.

In re Chappel, 243 F.Supp.417 (S.D. Cal. 1965). Unequal division of property may be set aside as a fraudulent conveyance.

Mejia v. Reed, 31 Cal. 4th 657, 74 P.3d 166, 3 Cal.Rptr.3d 390 (2003). Provisions of the Uniform Fraudulent Transfer Act applies to marital settlement agreements ("MSAs"). Under the UFTA, a transfer can be invalid either because of "actual fraud" or "constructive fraud". One form of constructive fraud is if the transfer is without receipt of reasonably equivalent value and the debtor is insolvent or renders the debtor insolvent.

In re Beverly, 374 B.R. 221 (9th Cir. BAP 2007), aff'd, 551 F.3d 1092 (9th Cir. 2008) Pursuant to a MSA, and after a hostile divorce proceeding, debtor's spouse received $1 million in liquid community assets and debtor received the entire exempt interest in his law firm pension plan worth some $1.1 million. The court concluded that moving assets beyond the reach of creditors was part of the MSA negotiations since an adverse judgment for which the community was liable was anticipated. The court concluded that the transfer to the debtor's spouse of his half of the unencumbered $1 million in bank accounts was avoidable in that the MSA did something other than evenly divide the marital property. The court found that the MSA transfer was an actually fraudulent transfer under the UFTA not subject to the good-faith-transferee-for-reasonably-equivalent-value defense, and thus avoidable. **Note:** If the court had determined that debtor's spouse was a good faith transferee, would she have been able to defend the avoidance action since she gave up the an amount virtually equivalent in debtor's pension plan?

In re Carbaat, 357 B.R. 553 (Bankr. N.D. Cal. 2006). Debtor's ex-wife asserted that her agreement to pay her own attorneys' fees and her waiver of spousal support should have been considered value for purposes of determining whether debtor received reasonably equivalent value for transfer of home to ex-wife provided for in an MSA. The Court ruled that no value should be attributed to the waiver of spousal support based upon 11 U.S.C. § 548(d)(2)(A) and Cal. Civ.Code § 3439.03 which excludes an unperformed promise to provide future support to the debtor or another person, and the fact that the debtor's waiver of his obligation to pay future spousal support from post-petition income does not create value from a creditor's perspective. However, the ex-wife's agreement to pay her own attorney's fees did constitute value.

In re Roosevelt, 176 B.R. 200 (9th Cir. BAP 1994). There is no language in state fraudulent conveyance statute or the Bankruptcy Code to suggest the court may disregard the value of property transferred to a debtor because it may not be susceptible to attachment and execution. The Court held the community interest in debtor-husband's medical practice and legal education did not have zero value, and thus, wife (who was a good faith transferee entitled to § 548(c) defense) and who received beneficial interest in partnership and family residence had defense to avoidance action, although case was remanded to determine the value exchanged between husband and wife pursuant to the MSA, and notwithstanding fact that Bankruptcy Court found that husband had actual intent to hinder, delay and defraud his creditors. Citing Britt v. Damson, 334 F.2d 896 (9th Cir. 1964), cert. denied 379 U.S. 966, 85 S.Ct. 661, 13 L.Ed.2d 560 (1965).

In re Roosevelt, 87 F.3d 311 (9th Cir. 1996). Marital agreement was valid transmutation of husband's community property to wife's separate property, notwithstanding fact that court determined husband made transfer with intent to hinder, delay or defraud creditors, and did not provide basis for denial of debtor's discharge under § 727(a)(2) in that the transfer occurred more than one year before the bankruptcy filing. However, transfer may be avoidable under § 544.

In re Roosevelt, 220 F.3d 1032 (9th Cir. 2000). Court had determined that husband had made the transfers to wife with actual intent to hinder, delay or defraud creditors, but that wife was entitled to good faith defense. Court held that wife who exchanged interest in husband's legal education for property conveyed to her by bankruptcy debtor did not give property of value where education was not paid for with community funds and did not increase husband's earning capacity during marriage and therefore, gave no value or the transfer.

Roosevelt Facts: MSA transmuted various community and separate property interests into the separate property of each. Husband gave wife community property interest in home and separate property interest in partnership; wife gave husband her community property interest in his medical practice and CP interest in his legal education.

Roosevelt On Remand: Bankruptcy Court determined medical practice had at all times been husband's separate property, and wife's interest in husband's legal education had at all times been zero, and therefore, wife did not give husband anything.

Roosevelt Remanded Again: Regarding the community property interest in the medical practice, the Court basically held that wife did not provide evidence of value given, notwithstanding that the court had held that she took in good faith.

Compare: In re Hinsley, 201 F.3d 638 (5th Cir. 2000). Court affirmed turnover in favor of trustee for debtor-husband's bankruptcy estate with respect to assets transferred to wife pursuant to partition agreements which purported to divide community estate into separate property. Parties remained married, and alleged that partition was done at a time when divorce was contemplated, and as part of an effort at reconciliation. Court held value to be determined from the standpoint of creditors.

State Board of Equalization v. Woo, 82 Cal. App. 4th 481, 98 Cal.Rptr.2d 206 (2000). Marital agreement transmuting future earnings to separate property was not effective to prevent taxing authority from obtaining earnings withholding order against one spouse to pay other's tax debt which was incurred during the marriage. Court ruled that agreement was entered into upon learning that taxing authority intended to levy wages, and was a fraudulent transfer of community property.

Sturm v. Moyer, 32 Cal.App.5th 299, 243 Cal.Rptr.3d 556 (2019). In July 2005, Sturm obtained a determination of nondischargeability and a $600,000 judgment in bankruptcy court against Moyer. During a judgment debtor examination in July 2016, Sturm discovered that Moyer had married Jessica Schell in 2014, and that they had entered into a premarital agreement which provided that each party's earnings and income, and any property acquired during the marriage by each spouse, would be that spouse's separate property, acknowledging that these earnings, income, and property otherwise would be community property. Sturm filed suit against Moyer and Schell under the UFTA (now the Uniform Voidable Transfers Act or UVTA) to set aside the transfer of Moyer's community property interest in Schell's earnings and income. Moyer and Schell demurred, and the trial court sustained the demurrer without leave to amend and Sturm appealed. Acknowledging that parties contemplating marriage have no interest in one aother's property and future earnings, as community property rights exist only where there is a marriage, the court also noted that the

premarital agreement was effective only in the event of marriage. Holding that the statutes creating community property interests had to be read together with California's adopted version of the Uniform Premarital Agreement Act (UPAA), the court found that the question of whether the parties' disclaimers of any community interests in future earnings that would be community property but for the premarital agreement was a question of fact. If there existed no actual fraudulent intent, only constructive fraud, then the transfer was not avoidable. On this basis the court reversed and remanded for further proceedings regarding the parties' intent. Query: If constructive fraud will not suffice, yet the non-debtor fiancé seeks to protect his/her income from the debtor fiance's creditors through a premarital agreement, when would actual fraudulent intent be lacking? Should recitals or disclosures of existing debts no longer be made in premarital agreements? Are ostriches safe from predators when they bury their heads in the sand? Are star-struck lovers who do not marry guilty of fraud for failing to do so?

In re Bledsoe, No. 07-35567, 2009 U.S. App. LEXIS 13677 (9th Cir. June 25, 2009). Oregon court entered a default dissolution judgment against the debtor in husband-defendant's divorce action, according to which the husband defendant's items were valued at substantially more than the items the debtor received. The bankruptcy trustee claimed inter alia that the dissolution judgment was a voidable transfer pursuant to § 548(a)(1)(B)(1) as the "debtor received less than a reasonably equivalent value in exchange for such transfer." The Court of Appeals affirmed the lower court's ruling, and found that, in the absence of fraud, a state court's dissolution judgment which followed a regularly conducted contested proceeding conclusively establishes both ownership *and* "reasonably equivalent value" to the same extent that a foreclosure sale does for the purposes of § 548. (citing BFP v. Resolution Trust Corp., 511 U.S. 531 (1994) (holding that real estate mortgage foreclosure sales pursuant to state law establishes reasonably equivalent value as a statutory matter). Judge O'Scannlain concurred in the result, but dissented as to the reasoning underpinning the court's rejection of the trustee's § 548 action. O'Scannlain cited to Roosevelt v. Ray (In re Roosevelt), 176 B.R. 200, 207 (9th Cir. BAP 1994) to support his argument that a dissolution judgment is a tool for discovering and assigning the individual ownership of property, but not for determining its value. See also In re Erlewine, 349 F.3d 205, 213 (5th Cir. 2003) (concluding that in the absence of any collusion, sandbagging or irregularity a dissolution judgment establishes reasonably equivalent value as a matter of law).

In re Llamas, 2011 Bankr. LEXIS 4779 (Bankr. C.D. Cal. 2011). Court determined trustee was entitled to summary judgment on constructive fraudulent transfer claims under § 548(a)(1)(B), but not actual intent fraudulent transfer claims under § 548(a)(1)(A). In the preceding divorce, the former spouse insisted upon and obtained a quitclaim deed transferring the debtor's interest in the family residence to her. The California court later held that the divorce judgment did not conclusively establish the reasonably equivalent value of the property. The court distinguished Bledsoe on the grounds that: (1) California is a community property state while Oregon is not; and (2) the divorce in Llamas was not contested as in Bledsoe.

XV. Exceptions to Discharge

The filing of a bankruptcy petition will permit a debtor to discharge his or her debts, with certain exceptions. Generally, a DSO is an exception and is not discharged. 11 U.S.C. § 523(a)(5). However, whether the debt is a DSO is determined by federal law and not by the fact that a debt may be called support in an agreement or order. Prior cases interpreting what is "in the nature of support" under pre-BAPCPA law will be useful in determining whether a debt qualifies as a DSO.

Although there is no requirement that a complaint be filed in the bankruptcy court to determine whether a debt is a DSO under § 523(a)(5) or a debt that qualifies as a debt "incurred in the course

of a divorce . . ." under § 523(a)(15), especially in a Chapter 7 case, it may be important for a debtor or non-debtor to file such a complaint in the Bankruptcy Court, not only to determine if the obligation is a DSO, but also to determine if there is a basis other than § 523(a)(15) which can provide an exception to discharge in a Chapter 13 case.

When and Where to File a Complaint Objecting to Discharge of a Debt

Prior law granting concurrent jurisdiction to the Superior Court and the Bankruptcy Court to determine whether a debt is "in the nature of support" at any time (see In re Siragusa, 27 F.3d 406, 408 (9th Cir. 1994)), may likely be made applicable to whether state and federal courts have concurrent jurisdiction to determine whether a debt qualifies as one "incurred in the course of divorce . . ." under 11 U.S.C. § 523(a)(15).

In addition, debts related to division of marital property are not dischargeable in Chapter 7 or 11, but may be discharged in Chapter 13. 11 U.S.C. §§ 523(a)(15), 1328(a).

Other debts which may be nondischargeable include debts incurred by false pretenses, a false representation, or actual fraud under 11 U.S.C. § 523(a)(2), debts incurred by fraud or defalcation while acting in a fiduciary capacity under 11 U.S.C. § 523(a)(4), and debts incurred for willful and malicious injury by the debtor to another entity or property of the entity under 11 U.S.C. § 523(a)(6). Section 523(a)(2) and 523(a)(4) may be able to be used by a creditor to except from discharge in a Chapter 13 case a debt which might otherwise be discharged under § 523(a)(15). These grounds are narrowly construed and it is necessary to file a complaint against the debtor in the Bankruptcy Court within specific time limits to preserve these claims.

A non-debtor waives any right to claim a debt that is non-dischargeable based on § 523(a)(2), (a)(4) and/or (a)(6) unless a complaint is filed against the debtor not later than sixty (60) days following the first date set for the meeting of creditors [Fed. Rule Bankr. Proc. 4007(c)].

In re Heilman, 430 B.R. 213 (9th Cir. BAP 2010). Bankruptcy Court properly refused to declare that dissolution decree obligated former husband to hold wife harmless on prepetition community debt that had been discharged in former husband's bankruptcy. Court noted that debt was discharged prior to divorce agreement and that assignment to Husband was attempt to circumvent reaffirmation requirements and that the hold harmless was an attempt to revive a discharged debt. DISSENT: Judge Pappas dissented holding that the hold-harmless obligation imposed on husband was a post-bankruptcy debt that was not discharged in his Chapter 7 proceeding, and even if it were a pre-bankruptcy debt, it was excepted from discharge.

Are Creditors Entitled to Attorney's **Fees?**

Travelers Cas. and Sur. Co. of America v. Pacific Gas and Elec. Co., 549 U.S. 443, 127 S.Ct. 1199 (2007). Overturned the rule set forth in the case of In re Fobian, 951 F.2d 1149 (9th Cir. 1991) which held that attorney's fees are only recoverable in bankruptcy court for litigating issues peculiar to bankruptcy law.

In re Busch, 369 B.R. 614 (10th Cir. BAP 2007). Citing *Travelers Casualty & Surety Co. v. Pacific Gas & Electric Co.*, the court held that where a Utah statute provided for attorney's fees to be awarded when incurred in connection with enforcing provisions in a divorce decree, creditor ex-wife was entitled to attorney's fees incurred in participating in debtor's prior Chapter 13 cases and in the adversary proceeding to determine whether obligation to pay mortgage was nondischargeable support obligation.

In re SNTL Corp., 571 F.3d 826 (9th Cir. 2009). After an extensive statutory exegesis, the Court of Appeals found that an unsecured creditor may include attorneys' fees incurred post-petition but arising from a prepetition contract as part of its unsecured claim.

DSOs are nondischargeable. 11 U.S.C. § 523(a)(5). A DSO is defined in § 101 (14A).

11 U.S.C. § 523(a)(5) - Domestic Support Obligations

Shaver v. Shaver, 736 F.2d 1314 (9th Cir. 1984). Bankruptcy courts look to federal law, not state law, to decide if debts are in the nature of support for dischargeability purposes. The court will look beyond the characterizations of an agreement or order to determine the nature of the debt; principles of collateral estoppel do not bind bankruptcy courts to the label affixed to an award. Factors considered are presence of minor children, relative incomes of parties, duration of the obligation, etc.

In re Sternberg, 85 F.3d 1400 (9th Cir. 1996). In determining whether payments owed by a debtor to a former spouse are spousal support, and therefore nondischargeable, the court looks to the parties' intent at the time the agreement was made and focus on: (1) actual need, (2) income imbalance between the parties at the time of the divorce decree, (3) when the obligations terminate, (4) to whom and when payments are made, and (5) the labels given to the payments by the parties (i.e., in the agreement, on tax returns, etc.).

In re Matthew Banks Ashworth, 2012 Bankr. LEXIS 4563 (Bankr. C.D. Cal. 2012). In addition to learning that husband had an illicit (same sex) affair for which she filed for divorce, wife learned that as a result of the illicit sexual encounter, husband had contracted (and unbeknownst to wife shared with her) a case of herpes. Wife sued for divorce and using the same counsel also filed suit for $10,000,000 for personal injury damages. Ultimately both cases were settled, with husband paying $1 for the personal injury claim and agreeing to pay $305,000 as fixed and nonmodifiable spousal support, which would continue unabated even if wife remarried (she did within months). Husband commenced Chapter 13 to discharge the $305,000 obligation. Wife objected on the basis the claim was nondischargeable under Section 523(a)(5) as a domestic support obligation. The court identified In re Sternberg as controlling precedent and heavily weighed wife's state of need at the time of divorce in determining that wife had met her burden of proving, by preponderance of the evidence, that the debt obligation in the final divorce judgment was a domestic support obligation. The court also pointed to the fact that payments were made directly to the wife, paid in installments over a substantial period of time and that the parties gave the obligation the label "alimony." The court noted that while prepetition waivers of dischargeability in bankruptcy (here, of the alimony obligation) are generally contrary to public policy and unenforceable, there did not seem to be any violation to the extent that the parties agreed in the recitation of their settlement that the obligation was a DSO or other domestic relations obligation.

In re Seixas, 239 B.R. 398 (9th Cir. BAP 1999). Former spouse's contractual promise under marital settlement agreement to pay half of children's college education expenses constituted nondischargeable "child support" obligation.

In re Foross, 242 B.R. 692 (9th Cir. BAP 1999). Post-petition interest that accrues on nondischargeable child support debt during pendency of Chapter 13 case is not dischargeable.

Wisconsin Dept. of Workforce Dev. v. Ratliff, 390 B.R. 607 (E.D. Wis. 2008). The court addressed the issue of whether the Wisconsin Department of Workforce Development overpayment of food stamp benefits to debtor was a DSO entitling it to a first priority administrative claim. The court

found that as the food stamps enabled the debtor to obtain food, a basic form of support, for herself and her children, they qualified as "support" under BAPCPA definition of "domestic support obligation," notwithstanding the assertion by the debtor that because the debt was for "overpayment" of food stamp benefits, it was, by definition, for benefits in excess of those needed to support debtor and her family. 11 U.S.C. §§ 101(14A), 507(a)(1)(A), (B).

The court identified four requirements for the debt to be considered a "domestic support obligation," under 101(14(A): it must be (1) owed to or recoverable by a governmental unit; (2) in the nature of alimony, maintenance, or support (including assistance provided by a governmental unit) of such spouse, former spouse, or child of the debtor or such child's parent, without regard to whether such debt is expressly so designated; (3) established or subject to establishment before, on, or after the date of the order for relief in a case under this title, by reason of applicable provisions of an order of a court of record or a determination made in accordance with applicable nonbankruptcy law by a governmental unit; and (4) not assigned to a nongovernmental entity, unless that obligation is assigned voluntarily by the spouse, former spouse, child of the debtor, or such child's parent, legal guardian, or responsible relative for the purpose of collecting the debt. (citing In re Forgette, 379 B.R. 623, 625 (Bankr. W.D. Va. 2007).

In support of the wide-sweeping nature of 101(14A), the court cites to a passage in Collier's treatise: "This broad definition was undoubtedly intended to include debts to governmental units that were not always considered within the ambit of section 523(a)(5) under prior law." Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy ¶ 101(14A) (15th rev. ed. 2008).

In re Hickey, 473 B.R. 361 (Bankr. D. Or. 2012). Court held that the debtor's obligation to repay unlawfully obtained public assistance was not for support of debtor's spouse, former spouse, or child of the debtor or such child's parent; rather it was a debt for the return of a benefit paid to the debtor which should not have been paid in the first place and therefore did not constitute a domestic support obligation (debt still excepted from discharge under §523(a)(2)).

In re Livingston, 397 B.R. 544 (10th Cir. BAP 2008). Chiquito, the legal and putative biological father of a child, divorced the child's mother and pursuant to a court order paid domestic support for the child for six years, after which time he became suspicious that child was not his own and pursued various legal actions against the alleged biological father. In one such tortious action Chiquito obtained a monetary default judgment in which the judge stated in dicta that the defendant by his absence "apparently" admits to his paternity. Chiquito pursued the debtor-alleged father in bankruptcy court, seeking payment of the debt as a non-dischargeable DSO.

The Bankruptcy Appellate Panel applied the Ratliff 101(14A) test, and found that the default judgment was not a DSO as the state judge issuing the default judgment had not made a veritable finding as to paternity. In its opinion, however, the court conceded that a default judgment need not be issued by a family court to constitute a DSO. A state court's denomination of its award as something other than alimony, maintenance or support is, moreover, not controlling of whether the award is in the nature of a "domestic support obligation," as that term is defined in the Bankruptcy Code. Id. at 613.

In re Smith, 398 B.R. 715 (1st Cir. BAP 2008). The First Circuit Bankruptcy Appellate Panel held that an obligation that a state divorce court imposed on a debtor-husband if he failed to make alimony payments in timely fashion, for an additional $50 per day for each day that alimony payment was late was in amount sufficiently high that it could not be regarded as having been intended to compensate ex-wife for any delay in receipt of the monthly alimony that debtor-husband was to pay, in initial amount of $2,300 and decreasing over time, but was rather meant as

punitive sanction to coerce debtor-husband's compliance with separate alimony obligation under divorce decree. Id. at 724.

The court estimated that in matters where the debt at issue was owed to a spouse, the standard for determining whether a payment was in the nature of a support obligation had not changed under the BAPCPA rules. Id. at 721. A court must look at the totality of the circumstances of each particular case in deciding whether the obligation qualifies as a DSO as that term is defined in the Bankruptcy Code. Id. Prominent in the court's analysis were the following: (1) language and substance of state court's order; (2) parties' financial circumstances *at time of the order*; and (3) function served by obligation *at the time of order*. 11 U.S.C. § 101(14A). Id. at 722. (emphasis added).

In re Putnam, 2012 Bankr. LEXIS 6117 (Bankr. E.D. Cal. 2012). Debtor's breach of car lease, new car down payment, and attorney fee obligations under a dissolution judgment are nondischargeable, but only to the extent that debts represent an actual obligation to pay former spouse, as to be determined by the state court.

In re Nelson, 451 B.R. 918 (Bankr. D. Or. 2011). Court held provisions in marriage dissolution judgment awarding debtor the marital home, requiring debtor to assume mortgage and to hold ex-wife harmless were not domestic support obligations. To overcome ambiguity of the parties' intent the court considered the fact that debtor, and not non-debtor ex-wife, occupied the house, the obligation did not terminate on death or remarriage and that the parties expressly waived the right to receive spousal support.

Marvin Obligation Case

In re Doyle, 70 B.R. 106 (9th Cir. BAP 1986). The Court held that obligations arising in connection with a civil action (a "Marvin action"), do not qualify for nondischargeable treatment under Section 523(a)(5) since the parties have never been married and one of the requirements under the section is that the debt "must be payable to a spouse or child."

Note: This analysis may provide the basis to hold that "spousal" support payable to a Registered Domestic Partner is dischargeable.

Attorney's **Fees Awards - Are they DSOs?**

A majority of courts deny discharge of attorney fees if the award is "based on the need of the recipient spouse or the financial circumstances of the parties."

In re Gionis, 170 B.R. 675 (9th Cir. BAP 1994), held that an award of attorney's fees and costs in a state divorce proceeding constituted nondischargeable alimony, maintenance or support order, even though there was no spousal support award and debtor was awarded custody of the minor child. Fees awarded based upon statute which considers income and needs. Look to case for analysis and factors to consider.

In re Marriage of Harris, 158 Cal. App. 4th 430, 434, 70 Cal.Rptr.3d 51 (2007). The court distinguished the facts from Gionis in so far as the case at bar presented no evidence of a disparity between the income of the husband and wife, no discussion of the wife's need for support, and no children involved. In light of these facts the court refused to qualify the debt as non-dischargeable pursuant to § 523(a)(5) and remanded to the trial court for an equitable determination of dischargeability under § 523(a)(15).

In re Gibson, 103 B.R. 218 (9th Cir. BAP 1989), citing Civil Code §§ 4370, 4370.5 and 4801 (now F.C. 2030, 2031, 2032 and 4320), permitting a court to consider the relative financial needs and resources of a party. If the award merely resulted from an equal division of community debts, as in Gibson, the debtor may still discharge the debt. Fee awarded as sanction dischargeable. See also In re Gentilini, 365 B.R. 251 (Bankr. S.D. Fla. 2007), which held that attorney's fees payable to law firm which were in nature of support were dischargeable since debtor's ex-wife was no longer liable to law firm. Criticizes In re Chang, 163 F.3d 1138 (9th Cir. 1998).

In re Greco, 397 B.R. 102, 109 (Bankr. N.D. Ill. 2008) (distinguishing the facts and rejecting the analysis of 523(a)(5) in In re Gentilini, 365 B.R. at 254-255). The court determined that a right to payment from Chapter 7 debtor of a child representative appointed for debtor's children in divorce action was not within the scope of Bankruptcy Code's definition of "domestic support obligation" and discharge exception under § 523(a)(5) for DSOs simply by virtue of being court-ordered payment in the nature of support. The child representative must be a direct payee under the restricted post-BAPCPA definition of "domestic support obligation." § 101(14A). As the child representative was neither a "direct payee" of former spouse nor a "legal guardian" or other "governmental unit," the court found that the child representative attorney fees were dischargeable.

Priority Treatment

The same language used in § 523(a)(5) is used in § 507(a)(1) which grants priority treatment to domestic support obligations. In a pre-BAPCPA case, the court held that if a debt would be nondischargeable under § 523(a)(5), it was also entitled to priority under § 507(a). In re Chang, 163 F.3d 1138 (9th Cir. 1998).

11 U.S.C. § 523(a)(15) – "incurred in the course of a divorce or separation"

(a) "A discharge . . . does not discharge an individual debtor from any debt ---

> (15) to a spouse, former spouse, or child of the debtor and not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, or a determination made in accordance with State or territorial law by a governmental unit."

These debts are also absolutely non-dischargeable in bankruptcy, except in Chapter 13 where the plan is fully complied with.

The Congressional Record refers to In re MacDonald, 69 B.R. 259 (Bankr. D. N.J. 1986), in discussing the reasons for creating § 523(a)(15).

Although there has been very little litigation with regard to whether or not a specific debt is "incurred in the course of a divorce or separation", the fact that debts that qualify under § 523(a)(15) are excepted from discharge in Chapter 7 cases may give rise to litigation with respect to whether or not a specific debt is one "incurred in connection with a divorce . . ."

In re Schweitzer, WL 1693060 (Bankr. S.D. Ohio 2007). Hold harmless provisions in separation agreement, requiring debtor to indemnify former husband for her charges on joint credit card, created new debt from debtor to former husband which was incurred in connection with separation agreement, and were therefore excepted from discharge.

In re Corn, 2008 WL 2714404 (Bankr.W.D. Tex. 2008). Following the analysis used in Schweitzer, the court found that a joint debt to the Internal Revenue Service for 2001 individual income, and the payment of two credit card debts that had been incorporated into a final decree of divorce, were non-dischargeable pursuant to § 523(a)(15).

In re Richardson, 212 B.R. 842 (Bankr. E.D. Ky. 1997). Absent hold harmless language in separation agreement, debt to former spouse's mother which was incurred during parties' marriage and which debtor agreed to assume in connection with the parties' divorce was not a new obligation incurred in the course of divorce, and thus not within the 523(a)(15) discharge exception.

In re Short, 232 F.3d 1018 (9th Cir. 2000). Premarital loan, expressly included in parties' divorce decree as payable by debtor, held to be debt "incurred in course" of divorce or separation for purpose of § 523(a)(15).

In re Dollaga, 260 B.R. 493 (9th Cir. BAP 2001). Creditor-attorney lacked standing to sue debtor for divorce-related fees under § 523(a)(15) since attorney was neither a spouse, former spouse or dependent of the debtor.

In re Putnam, 2012 Bankr. LEXIS 6117 (Bankr. E.D. Cal. 2012). Debtor's express obligations to hold former spouse harmless from any liability on family loan debt under a dissolution judgment are nondischargeable, but only to the extent the debt represents an actual obligation to pay former spouse.

In re Marriage of Vaughn, 29 Cal.App.5th 451, 240 Cal.Rptr.3d 227 (2018). Arising in the state court in a post-dissolution proceeding, the family court concluded that the former husband's outstanding debt on a loan made by a family partnership in which his former wife had an interest was nondischargeable pursuant to Section 523(a)(15). Husband appealed. Affirming the trial court, the court reasoned that the language of the statute requiring that the debt be owing "to a spouse, former spouse, or child of the debtor" was unclear, finding "that most courts have determined that section 523(a)(15)'s language is ambiguous, and should be interpreted "broadly and liberally ..." In logic that requires turning the plain wording of the statute on end, the court reasoned that "BAPCPA was "intended to increase the scope of the discharge exception," not limit its protection to spouses, former spouses, and children." Accordingly, finding that the debt was owing to a non-individual business entity in which former wife was a 20% owner, the court reasoned that wife's interest in the partnership adequately substituted for the lack of a debt directly owing to the wife that arose from the divorce judgment. Query: How far does this reasoning extend. Had husband owed a deficiency judgment after an automobile repossession to Ford Motor Credit, and wife owned shares of stock in Ford, would the debt to Ford be nondischargeable pursuant to Section 523(a)(15)? This case being from the state court, it is not a binding precedent in a bankruptcy proceeding.

In re Gunness, 505 B.R. 1 (9th Cir.BAP 2014). The debtor filed adversary complaint against her current husband's ex-wife and the ex-wife's family law attorney, seeking determination that the debt she owed to ex-wife for attorney fees awarded in a family law case to which the debtor had been joined was dischargeable. The debtor had been joined to the divorce case by motion of the ex-wife, who had brought a fraudulent transfer case under the UFTA against her ex-husband and the debtor, and had been awarded attorney's fees against the debtor and her now-husband. Debtor sought to discharge her liability in Chapter 7. The bankruptcy court granted summary judgment in favor of the debtor. The ex-wife appealed. The BAP held that the debt lacked the requisite connection to "a spouse, former spouse, or child of the debtor," notwithstanding the fact that debtor had been joined by the state court as a party to the dissolution proceedings of her husband and his ex-wife from

which the debt arose, and so neither the discharge exception for domestic support obligations nor the discharge exception for divorce-related debts not in the nature of support was applicable. Ironically, Gunness was cited with approval in In re Marriage of Vaughn, supra, which held that a debt owing to a family partnership in which the former wife was a 20% owner was sufficiently connected to render the claim nondischargeable under 523(a)(15).

Burden of Proof

Pre-BAPCPA the Ninth Circuit held that once the creditor met his/her burden of proving a debt was incurred in the course of a dissolution, the burden of going forward shifted to the debtor to prove the debt should be discharged. See In re Morris, 193 B.R. 949 (Bankr. S.D. Cal. 1996); In re Jodoin, 209 B.R. 132 (9th Cir. BAP 1997); In re Myrvang, 232 F.3d 1116 (9th Cir. 2000). **Note:** If the debtor questions whether the debt is "incurred in the course of …" it is expected that the courts will require the debtor to bear the burden of proof.

11 U.S.C. § 523(a)(2)(A)

A debt may be nondischargeable to the extent obtained by false pretenses, a false representation, or actual fraud. 11 U.S.C. § 523(a(2). See In re Kirsh, 973 F.2d 1454 (9th Cir. 1992) for elements which must be proven to except a debt from discharge under this section.

In re Tsurukawa, 258 B.R. 192 (9th Cir. BAP 2001). Unless debtor-wife knowingly participated in her husband's fraud, or was his business partner and stood in an agency relationship with him, marital relationship alone was insufficient predicate for imputation of husband's fraud to debtor-wife for purpose of denying her discharge and excepting debt from discharge. See also In re Stearman, 256 B.R. 788 (9th Cir. BAP 2000).

In re Guske, 243 B.R. 359 (8th Cir. BAP 2000). Chapter 7 debtor's ex-wife sought nondischargeability of $30,000 property settlement pursuant to consent dissolution decree pursuant to both 523(a)(15) and, following admission by debtor that he had never intended to make the promised payment, also on 523(a)(2). Bankruptcy Court excepted debt from discharge as one for property obtained by false pretenses, false representation or actual fraud. On appeal, court reversed, ruling that debtor's admission did not provide basis for 523(a)(2) holding given complete lack of evidence that ex-wife justifiably relied on debtor's promise.

In re Sung Ho Cha, 483 B.R. 547 (9th Cir. BAP 2012). The court affirmed a lower court's finding that a prior default judgment against the debtors for unpaid rent was nondischargeable as to the wife only the extent of the debtors' community property where the bankruptcy court also determined the wife had nothing to do with the false financial statements provided by the husband when the lease was executed.

11 U.S.C. § 523(a)(4)

A debt may be nondischargeable if based on fraud or defalcation while acting in a fiduciary capacity, embezzlement or larceny. "The meaning of 'fiduciary' in § 523(a)(4) is an issue of federal law --- the broad general definition of fiduciary - a relationship involving confidence, trust and faith --- is inapplicable in the dischargeability context. The trust giving rise to the fiduciary relationship must be imposed prior to any wrongdoing [and] the debtor must have been a 'trustee' before the wrong and without reference to it. The requirements eliminate constructive, resulting and implied trust." See Ragsdale v. Haller, 780 F.2d 794 (9th Cir. 1986) (decided under California Corporations Code § 15021(1), which included the same language as F.C. § 721(b)(3) as set forth below). See

also Schlecht v. Thornton, 544 F.2d 1005 (9th Cir. 1976) for criteria that must exist in order to give rise to an express trust.

California F.C. § 721, California F.C. § 1100 et seq. and the provisions of the California Corporations Code, may provide a basis for a non-dischargeability complaint by a non-filing spouse post-separation with respect to a claim for reimbursement (not yet a debt pursuant to a court order), under either § 523(a)(4) breach of fiduciary duty, or § 523(a)(6) willful misconduct discussed below.

California F.C. § 721 provides, in part, as follows:

> "... (b) ... a husband and wife are subject to the general rules governing fiduciary relationships which control the actions of persons occupying confidential relations with each other. This confidential relationship imposes a duty of the highest good faith and fair dealing on each spouse, ... **This confidential relationship is a fiduciary relationship subject to the same rights and duties of nonmarital business partners, as provided in Sections 16403, 16404, and 16503 of the Corporations Code**, including ..." (Emphasis added.)
>
> (b)(3) "Accounting to the spouse, and holding as a trustee, any benefit or profit derived from any transaction by one spouse without the consent of the other spouse which concerns the community property."

In re Niles, 106 F.3d 1456 (9th Cir. 1997). Debt for defalcation while acting in a fiduciary capacity is nondischargeable only "where (1) an express trust existed, (2) the debt was caused by fraud or defalcation, and (3) the debtor acted as a fiduciary to the creditor at the time the debt was created." The fiduciary relationship must arise from an express trust imposed before and without reference to the wrongdoing that created the debt.

In re Stanifer, 236 B.R. 709 (9th Cir. BAP 1999). Debtor's breach of fiduciary duty with regard to pension benefits barred discharge of debt incurred as a result of failure to share benefits with ex-spouse under 11 U.S.C. § 523(a)(4) (based upon the fiduciary duty owed between spouses which incorporates the law applicable to the fiduciary duty between business partners.

In re Teichman, 774 F.2d 1395 (9th Cir. 1985). The court held that past payments owing to a spouse under the debtor's military pension (assigned under a property settlement agreement) are dischargeable while future payments from the pension are not. [Majority view is both past and future military pension payments are non-dischargeable.]

In re Boyd, 143 B.R. 237 (Bankr. C.D. Cal. 1992). Sanctions for bad faith filing, where filing based on Teichman case to avoid payment of pension benefits to spouse.

In re Rubenstein, 2009 WL 197967 (Bankr. E.D. Cal. 2009). Where debtor had concealed the existence of a promissory note of $255,000 that was part of a personal injury settlement with the estate of the decedent, the court did not find that the debt was non-dischargeable under 523(a)(2)(A) because the debt itself did not arise out of the act of fraud.

In re Lam, 364 B.R. 379 (Bankr. N.D. Cal. 2007). Court held that since under California law, spouses act as fiduciaries inter se with respect to the management and control of the community assets pursuant to F.C. §§ 1100(e) and 1101(a), these provisions make spouses fiduciaries with respect to community property for purposes of § 523(a)(4). Further, since the state court judge

concluded that debtor had breached F.C. § 915(b) which requires a spouse to make payments for a pre-marital support obligation from separate property, if available, as opposed to community property, wife's entitlement to reimbursement was nondischargeable.

11 U.S.C. § 523(a)(6) versus 11 U.S.C. § 1328(a)(4)

Exceptions to discharge based upon 11 U.S.C. § 523(a)(6) for willful and malicious conduct is available in Chapter 7, Chapter 11 and Chapter 12 cases and in Chapter 13 cases in which a debtor requests a hardship discharge pursuant to 11 U.S.C. § 1328(b).

Nondischargeability of a debt for willful and malicious injury by the debtor to another entity or to the property of another entity. In the case of Kawaauhau v. Geiger, 523 U.S. 57, 118 S.Ct. 974 (1998), the Supreme Court, construing the language "for willful and malicious injury by the debtor to another," held that a debtor's reckless or negligent misconduct does not come within the dischargeability exception, even if the debtor performed the act intentionally. Rather, the debtor must intend to cause injury (as a result, In re Cecchini, 780 F.2d 1440 (9th Cir. 1986), is no longer good law). See also In re Jercich, 238 F.3d 1202 (9th Cir. 2001) and In re Su, 290 F.3d 1140 (9th Cir. 2002), which held that, "the willful injury requirement .. is met only when the debtor has a subjective motive to inflict injury or when the debtor believes that injury is substantially certain to result from his own conduct."

In re Moffitt, 252 B.R. 916 (6th Cir. BAP 2000) - Chapter 7 debtor's ex-wife sought to except debt from discharge, as one based on "willful and malicious injury", based upon judgment entered in state court action for debtor's intentional infliction of emotional distress resulting from debtor's knowingly engaging in unprotected sexual relations during marriage at same time when he was engaging in such relations with other women, and when he had been infected with genital warts. Court held debt nondischargeable.

Burgos v. Wheeler, 2009 WL 281294, *15 (Cal.App.4th Dist. 2009). An intentional breach of contract with an intent to defraud is not sufficient to satisfy the § 523(a)(6) standards for non-dischargeability requiring a showing of "willful and tortious conduct that violates fundamental public policy."

In re Kaczmarski, 245 B.R. 555 (Bankr.N.D.Il. 2000). Chapter 7 debtor's ex-wife sought to except from discharge obligation imposed in parties' divorce decree. Court ruled debt excepted under both §§ 523(a)(15) and 523(a)(6) in that debtor's actions in withdrawing all funds from a retirement fund and borrowing funds on a home equity second line of credit, in violation of state court orders, and thereafter dissipating those assets in violation of restraining order were willful and malicious, and debtor was aware that actions were substantially certain to lead to injury of wife or her property interest. Court ruled that under Supreme Court decision in Geiger, willful or specific intent to do harm is not required, and that debtor's knowledge that injury is substantially certain will suffice.

Spousal abuse cases appear to be based upon 523(a)(6) as opposed to 523(a)(15), and therefore, a timely complaint must be filed to except these debts from discharge.

Section 1328(a)(4) is not the equivalent of 11 U.S.C. § 523(a)(6)

In re Byrd, WL 670530 (Bankr. C.D. Ill. 2007). Where there is no judgment or award in the civil action as of the date of the bankruptcy filing, it is a contingent, unliquidated debt not subject to exception from discharge. However, object to confirmation based upon the plan not being proposed in good faith (1352(a)(3), or the case not being filed in good faith. 1325(a)(7)). See also In re

Nutall, WL 128896 (Bankr. D. N.J. 2007); In re Galtieri, 2007 WL 2416425, 1 (Bankr. D. N.J. Aug. 17, 2007) (prepetition tort claim could not be excepted from the bankruptcy discharge, unless that exception were preserved by the initiation of a timely adversary proceeding pursuant to a 11 U.S.C. § 523(a)(6) allegation of willful and malicious injury to spouse).

In re Taylor, 388 B.R. 115, 122 (Bankr. M.D. Pa. 2008). The court held that willful or malicious injury that results in a personal injury gives rise to a non-dischargeable debt under Chapter 13 even if it has not yet been reduced to judgment. The court rejected the In re Nutall analysis of 1328(a)(4), finding it to be in disaccord with the construction of other exceptions to discharge and incompatible with the surrounding body of law. The court argued that there was no reason to assume that Congress intended to differentiate between creditors who were able to obtain a judgment against a debtor before the bankruptcy filing and those that were stymied in their efforts to obtain redress for their injuries by the invocation of the automatic stay.

Punitive Damage Awards

Cohen v. DeLaCruz, 523 U.S. 213, 118 S.Ct. 1212 (1998). Giving a broad construction to the language, "debt ... to the extent obtained by ... actual fraud," the Supreme Court held that § 523(a)(2)(A) bars the discharge of all liability arising from fraud, including any punitive damages and attorneys' fees to which a plaintiff may be entitled to under non-bankruptcy law. As a result, In re Levy, 951 F.2d 196 (9th Cir. 1991), is no longer good law.

In re Bugna, 33 F.3d 1054 (9th Cir. 1994). Punitive damages portion of state court judgment for fraud in a fiduciary capacity is nondischargeable under § 523(a)(4).

In re Britton, 950 F.2d 602 (9th Cir. 1991). Punitive damages excepted from discharge under 11 U.S.C. § 523(a)(6).

XVI. The Discharge Injunction

Once a debtor receives a discharge in a bankruptcy case, 11 U.S.C. § 524(a) provides certain protections to a debtor. Section § 524(a)(3), subject to exceptions set forth in § 524(b), also provides protections to a non-filing spouse regarding the collection of a debt from community property acquired after the commencement of the bankruptcy case.

In re Kimmel, 367 B.R. 166 (Bankr. N.D. Cal. 2007). Holder of community claim must take action in innocent spouse's bankruptcy case, even if his real quarrel is with the nonfiling, wrongdoing spouse. Once deadlines in first spouse's case have passed with no attempt by creditor to obtain determination of nondischargeability of debt, it is too late for creditor to collect prepetition community claim from after-acquired community property. 11 U.S.C. § 524(a)(3)

In re Strickland, 153 B.R. 909 (Bankr. D. N.M. 1993). Community property discharge operated as injunction against any action to collect or recover from after-acquired community property, but did not operate as injunction against collection from nondebtor spouse's separate property.

In re Siragusa, 27 F.3d 406 (9th Cir. 1994). State court's modification of alimony based on bankruptcy discharge of property settlement did not violate discharge injunction.

In re Marriage of Lynn, 101 Cal.App.4th 120, 123 Cal.Rptr.2d 611 (2002). Discharge in bankruptcy of one ex-spouse's property settlement obligation was not proper ground, absent

consideration of other factors, for modifying earlier spousal support order. See F.C. § 3592 and § 4320 (which lists all factors to consider).

Williams v. Williams, 157 Cal.App.3d 1215, 203 Cal.Rptr. 909 (1984). Permitting husband to offset wife's indebtedness which was discharged in bankruptcy frustrated intent and purpose of Federal Bankruptcy Act and violated federal supremacy clause.

In re Passmore, 156 B.R. 595 (Bankr. E.D. Wis. 1993). Automatic stay in debtor-husband's individual bankruptcy prevented creditors from reaching community property wages earned by husband's nondebtor spouse, even to satisfy independent claims against nondebtor spouse. Post-petition wages are community property.

In re Marusic, 139 B.R. 727 (Bankr. W.D. Wa. 1992). Fact that spouse filed previous bankruptcy and received discharge within preceding six (6) years, and therefore, would be denied discharge if he had filed with wife, made after acquired community property liable for community claim.

PART FIVE

TIMING AND THE IMPACT OF DIVORCE AND BANKRUPTCY PROCEEDINGS

I. General Observations

The issue of timing can be a crucial one in a divorce/bankruptcy interaction. Because the filing of a bankruptcy petition brings all of the debtor's interests in separate and jointly held property into the bankruptcy estate, brings all community property into the bankruptcy estate (unless it is under the sole management and control of the non-debtor and not liable for an allowable claim against the non-debtor), and stays all of the property distribution aspects of a pending divorce case, a client contemplating divorce or separation needs to be aware of the potential consequences that delay in obtaining a dissolution decree and final entry of property distribution orders may have on his or her property interests. Although there are situations in which it might be advisable for a client to delay filing bankruptcy until a divorce action has been completed, more often a family-law practitioner will be advising a client to speed up the divorce process to beat a potential bankruptcy filer to the punch. On the other hand, if a couple contemplating a separation and a joint or separate bankruptcy filing are on sufficiently amicable terms, joint planning could reap significant advantages for both spouses.

II. Bankruptcy and the "Amicable" Divorce

If a husband and wife are in the fortunate position of remaining on relatively civil terms as they contemplate a divorce and a potential bankruptcy for one or both, some advance strategic planning can improve their post-divorce financial situations. A joint bankruptcy petition filed prior to divorce can save on filing and attorney's fees, but could also reduce the total amount of property that could be exempted from the bankruptcy estate. If one spouse has significant separate property and no personal liability for some or all of the other spouses' debts, the bankruptcy of only the personally liable spouse prior to divorce may be advantageous. This will at least preserve the non-debtor spouse's separate property, and may leave more property to be considered and distributed at dissolution.

It might also be possible, if a couple determines the desirability of divorce and the imminence of bankruptcy far enough in advance, to transmute a significant amount of community property into separate property prior to the two-year avoidance window prescribed 11 U.S.C. § 548(a). However, California's four-year fraudulent transfer provisions may be applicable to the transmutation. Regardless of the time constraints, a transfer of property interests for reasonably equivalent value in the course of settlement negotiations might still allow insulation of some property from the grasp of the trustee, and may result in a lower post-divorce support burden for the debtor spouse. 11 U.S.C. § 548(a)(2)(A). A transfer of the potential debtor spouse's interest in a marital home to the other spouse in exchange for a release of future support obligations may be an example of such a transmuting transaction. However, see In re Carbaat, 357 B.R. 553 (Bankr. N.D. Cal. 2006), *supra*.

While potentially very advantageous to both the potential debtor and the non-debtor spouse, these transactions must be carefully planned in order to avoid the possibility that the trustee will be able to avoid the transfer as fraudulent and reassert control over the property. It is advisable to seek a bankruptcy practitioner's guidance before contemplating or consummating such a transaction.

Note: Counsel will need to address conflict issues that may or could exist or arise in multiple party representation, both as it applies to the bankruptcy case as well as the impact on pending or future dissolution proceedings.

In re Goldstein, 383 B.R. 496 (Bankr. C.D. Cal. 2007) WL 19702632007. The court authorized the appointment of special counsel to represent joint debtors in dissolution proceedings. On the same day that the joint debtors filed their bankruptcy petition, bankruptcy counsel for the debtors filed two motions for authorization to employ divorce counsel. Debtors stated on their employment applications that they each needed divorce counsel's services to advise the debtors concerning divorce issues that may arise from the bankruptcy case and to complete the dissolution process without interfering with the administration of the bankruptcy case.

III. When Should a Client be Advised to Hasten the Divorce Process?

Of course, not all divorce proceedings which will ultimately be impacted by bankruptcy are conducted in a spirit of cooperation. Timing in these cases becomes even more crucial. When a bankruptcy petition is filed, divorce proceedings are stayed, property division is halted, and community property comes under the control of the trustee (or debtor-in-possession) of the bankruptcy estate. If the debtor spouse files for bankruptcy before a dissolution, the non-debtor spouse's community property also becomes part of the bankruptcy estate, with the result that the trustee can sell property, such as a family home, right out from under the non-debtor spouse. In re Gorman, 159 B.R. 543 (9th Cir. BAP 1993).

Generally speaking, then, in any case in which a less-than-amicable divorce or separation proceeding is looming or actually underway and the client's spouse is a candidate for a bankruptcy filing, a client is probably well advised to obtain at least a dissolution decree as quickly as possible. It may also be prudent to obtain whatever property division orders are possible, even if there is a reservation of jurisdiction over other issues.

If a state-law judge has issued a notice of intended decision and a debtor spouse files for bankruptcy before the judgment is entered, entry of the order will be stayed. In re Willard, 15 B.R. 898 (9th Cir. BAP 1981). If the final judgment has been announced, however, and it is only the formal "ministerial" act of the entry of a judgment by the court clerk that remains undone, there is authority that the stay may not prevent the judgment from becoming effective. In re Watson, 192 B.R. 238 (Bankr. D. Nev. 1996) (state court entered judgment on day one, debtor spouse filed for bankruptcy on day 2, state court clerk files the judgment on day 6, and debtor-spouse attempts unsuccessfully to assert that the automatic stay applied to the filing of the judgment). This result however is not without uncertainty.

IV. When Should a Client be Advised to Hasten the Bankruptcy Process?

Given the nature of the family law practice, it will generally only be in relatively amicable divorce situations, in which the spouses are attempting to mutually optimize their post-divorce financial pictures as discussed *supra*, that a family law practitioner would be advising a client to hasten a bankruptcy filing. It would be the unusual situation, to say the least, in which an attorney with a client contemplating the more typically adversarial divorce would advise him or her to file for bankruptcy if the client's individual financial situation did not warrant it.

However, if a client was in dire financial straits, a pre-divorce bankruptcy filing could result in a more modest and realistic divorce settlement obligation for a potential payor, and a more realistic support award for a potential payee. Given that BAPCPA has considerably limited the dischargeability of amounts awarded in such settlements, the value of attempting to "ambush" a former spouse with a post-separation bankruptcy has considerably diminished. The relative benefits of coming before the state court with a difficult financial position already demonstrated,

and a rigorous analysis of what assets and income are actually available from which alimony, maintenance, support, or a property settlement might be paid, are thus correspondingly greater.

V. Sword or Shield?

An example of using bankruptcy as a sword often arises in cases where the sale of the family residence will yield substantial net sales proceeds which the potential debtor wants used to pay community debts. Often, the non-filing spouse refuses to sell the house or, if the parties agree to sell the house, they often do not reach agreement regarding the expenditure and/or division of the sales proceeds. Therefore, although the house may be sold, the funds retain their community property character and remain in trust pending further determination by the Superior Court. By filing a bankruptcy before the funds are divided and/or threatening to file bankruptcy, the potential debtor can often generate a settlement which will be advantageous and resolve the divorce issues without incurring further litigation expenses in the divorce case.

An example of using bankruptcy as a shield generally arises in cases where the Superior Court has made certain orders and/or the potential debtor anticipates that the Superior Court is about to make certain orders, oftentimes regarding the value of a business which is no longer valuable and/or the payment or assignment of debts. Filing a bankruptcy will stay the Superior Court proceedings - at least temporarily.

PART SIX

THE EFFECTS OF SAME-SEX MARRIAGE AND DOMESTIC PARTNERSHIPS ON BANKRUPTCY

Note: On June 26, 2013, the United States Supreme Court ruled that married same-sex couples were entitled to federal benefits and by declining to decide a California case on standing grounds, the Court effectively allowed same-sex marriage in the state of California. See below, United States v. Windsor, 570 U.S. 744 (2013) and Hollingsworth v. Perry, 558 U.S. 183 (2013). Thus, some of the issues and cases discussed in this Part Six may be impacted.

I. Consolidated and Joint Filings

In re Rabin, 359 B.R. 242 (9th Cir. BAP 2007)

This case involved a couple of same-sex debtors who had registered as domestic partners under the California Domestic Partner Rights and Responsibilities Act ("DPRRA"), and filed separate Chapter 7 petitions, in which each claimed a $75,000 homestead exemption in residential property in which they each held a one-half interest. The Bankruptcy Appellate Panel upheld the lower court's decision to sustain the Chapter 7 trustee's objection to the dual homestead exemption and subsequent determination that the proceeds from the sale of the exempted property must be divided between the partners. As DPRRA specified that, with certain limited exceptions, registered domestic partners were to be treated as "spouses" for economic purposes under California law, the court held that DPRRA dictated that they be considered as "married" persons for the purposes of applying the California homestead statute.[3]

The court also affirmed that a bankruptcy judge may exercise its discretion to order the consolidation of the filings of same-sex debtors to overcome the federal restriction under 11 U.S.C. § 302 of the benefit of the filing of a joint petition with a single filing fee to married people as a matter of federal law.[4] The court further noted that § 302 only creates a presumption that bankruptcy cases filed by "spouses" should be jointly administrated. Compare with In re Lucero, 2009 WL 2030397, 1 (Bankr. C.D. Cal. 2009) (finding that § 302(a)'s "individual and individual's

[3] The court found that DPRRA and Initiative Proposition 22, providing that "[o]nly marriage between a man and a woman is valid or recognized in California," were not in contradiction. Relying upon the analysis in Knight v. Superior Court, 128 Cal.App.4th 14, 26 Cal.Rptr.3d 687 (2005) the court distinguished between the "status" of marriage targeted by Initiative Proposition 22 and the economic rights and responsibilities associated with marriage in DPRRA. As the issue of the homestead exemption was purely economic i.e. the degree of protection from creditors to be accorded to debtors, the court held that Initiative Proposition 22 did not apply.

[4] In In re Blair, 226 B.R. 502, 505 (Bankr. D. Me. 1998), the court discussed the differences between a joint filing and a substantive consolidation and anticipated that with the passage of DOMA, recourse to substantive consolidation by same-sex couples would become more common. See also In re Roll, 400 B.R. 674, 679 (Bankr. W.D. Wis. 2008) (finding that DOMA prohibits the Court from treating a same-sex couple as married, and consequently, the separate filings of same-sex couples cannot be found to be manipulation of the system).

spouse" language precluded a joint filing of unmarried heterosexual couple and ordering the dismissal of one of the co-debtor's petition).

In re Allen, 186 B.R. 769 (Bankr. N.D. Ga. 1995). Unmarried same sex couple could not file jointly even though the court acknowledged that they had many of the same characteristics of a typical marriage between a man and woman. The court found that the term "spouse" in § 302 should be construed in the common way, which typically identifies a "spouse" in the terms of a husband and wife.

In re Balas, 449 B.R. 567 (Bankr.C.D.Ca. 2011). A bankruptcy judge in the United States Bankruptcy Court for the Central District of California recently issued a decision in this case in which the court held that the Defense of Marriage Act ("DOMA"), as applied to a same-sex couple legally married under state law, violated the couple's equal protection rights afforded under the Fifth Amendment of the United States Constitution.

Mssrs. Balas and Morales were a lawfully married couple under the laws of the State of California when they filed a joint bankruptcy petition under Chapter 13 of the Bankruptcy Code. In response to the filing, the United States Trustee ("UST") moved to dismiss the case unless Mssrs. Balas and Morales agreed to sever their cases into two (2) separate bankruptcy cases. They refused and the matter was submitted to the court. In denying the UST's motion, the court found that DOMA did not serve an important governmental interest, or advance any valid governmental interest, and could not be upheld under either heightened or rational basis scrutiny.

Following the Balas and Morales decision, twenty (20) federal judges in southern California joined together to rule that DOMA does not bar same-sex married couple from filing joint bankruptcy petitions.

Although not given as much national attention as the Balas and Morales case, a New York bankruptcy judge also denied the UST's motion to dismiss a joint Chapter 7 case filed by a same-sex couple who had been legally married. The court held that "cause" did not exist under 11 U.S.C. §707(a) to dismiss the case solely on provisions of federal legislation, DOMA, that the executive branch had declined to enforce. See In re Somers, 448 B.R. 677 (Bankr. S.D.N.Y 2011).

No formal opinion has been issued by any of the Bankruptcy Judges of the Northern District of California as to how they would rule if the matter was brought before them. However, the court did issue an announcement ("Announcement") in which it stated, in relevant part, as follows:

> It is appropriate for this court to clarify its practices regarding joint petitions, in light of the much-publicized Balas and Morales decision, ...
>
> The Balas and Morales decision is not binding in this court, because it is the decision of a court equal to this court, rather than a court superior to this court. This court may properly address the issue raised in Balas and Morales only if and when that issue is properly presented in a case before this court.

The Announcement further provided that the clerks of the bankruptcy courts in the Northern District of California would accept for filing a single bankruptcy petition by individuals representing themselves as lawfully married, and further, that the court would not, on its own initiative investigate whether any such individuals were same-sex, mixed-sex or recognized as married under state or federal law. However, the Announcement also provided that if a motion or action were filed by a party in interest objecting to such a joint filing, that the court would schedule

such proceedings as are appropriate to determine the legal and factual questions raised in the action or motion.

In re Villaverde, 540 B.R. 431 (Bankr.C.D. 2015). Two women who had entered into a California Registered Domestic Partnership (RDP) commenced a joint Chapter 13 case in the Riverside Division of the Central District of California, contending that the language of Section 302 which states that "[a] joint case ... is commenced by the filing with the bankruptcy court of a single petition ... by an individual that may be a debtor ...and such individual's spouse", included RDPs as "spouses". The Chapter 13 trustee objected to confirmation and moved to dismiss on the basis of lack of eligibility. Judge Yun first noted that while the term "spouse" was used throughout the Code in a number of sections, nowhere was the term defined. Turning to the Defense of Marriage Act (DOMA), the court noted that while it defined the term "spouse" as a marital partner of the opposite sex, in 2013 the Supreme Court had held DOMA to be unconstitutional under the equal liberty guarantee of the Fifth Amendment in the case of United States v. Windsor, 570 U.S. 744, 133 S.Ct. 2675, 186 L.Ed.2d 808 (2013). The court next turned to the ordinary meaning of "spouse", falling back on Merriam Webster's Collegiate Dictionary to hold that, irrespective of gender, a spouse is a person who is married to another. The court examined California statutes that effectively granted RDPs the same rights and duties as spouses, but concluded that, "As much as the California Legislature attempted to grant domestic partners the same rights as spouses, its intent was not to grant domestic partners the same status as spouses." Accordingly, the court dismissed one of the RDPs from the case and allowed the case to proceed as an individual Chapter 13 case by the remaining RDP.

In re Cusimano, 2013 WL 9736597. One of two women who had entered into a California Registered Domestic Partnership (RDP), commenced a Chapter 7 case in the Santa Ana Division of the Central District of California, while the parties were embroiled in a concurrent proceeding pending in the Orange County Superior Court for dissolution of the registered domestic partnership. One of the RDPs commenced an adversary proceeding to have any non-support marital debts held to be nondischargeable pursuant to Section 523(a)(15). With United States v. Windsor, supra, pending before the Supreme Court, Judge Smith deferred ruling on the issue in the hope it would provide the decision as to whether RDPs and spouses were one and the same. When it did not, she examined the same statutes as guided Judge Yun some two years later in In re Velaverde, supra. However, she concluded that "As a registered domestic partner, California Family Code section 297.5(f) provides Movant the same rights as those provided to spouses. Cal. Fam.Code § 297.5(f). Accordingly, the application of "spouse" as used in § 523(a)(15) must apply to Movant as a registered domestic partner pursuant to California Family Code § 297.5." Notably, although it predated the Velaverde decision, the unpublished Cusimano decision was not mentioned in Judge Yun's published decision.

Exemption Statutes and Same-Sex Couples

In re Townsend, 344 B.R. 915 (Bankr. W.D. Mo. 2006). A four-person household that consisted of Chapter 7 debtor, her same-sex partner, and partner's two children, one of whom was conceived by artificial insemination after debtor and her partner began living together, qualified as "family," as that term was used in the Missouri "head of the household" exemption, where debtor and her partner manifested their desire to live together in domestic relationship of indefinite duration, not

only by their decision to have child together, but by taking legal action of having their names changed so that they and the two children all had same surname. V.A.M.S. §§ 513.440.

II. Constitutional Issues Raised by the Defense of Marriage Act

United States v. Windsor, 570 U.S. ___ (2013). On June 26, 2013, in a 5-4 decision, the United States Supreme Court declared Section 3 of DOMA unconstitutional. It appears that same-sex couples that are legally married under state law may now receive all the benefits and burdens of the more than 1,000 federal laws affected by DOMA – including federal bankruptcy laws. Thus, legally married same sex-couples should be able to file bankruptcy petitions jointly. As of July 2013, thirteen states and the District of Columbia allow same sex couples to get married, a number likely to keep increasing.

In light of the U.S. v. Windsor ruling noted above, many of the cases and issues pertaining to DOMA discussed below may no longer be considered relevant or current law.

In re Kandu, 315 B.R. 123 (Bankr. W.D. Wash. 2004). In a widely discussed opinion from 2005, the Bankruptcy Court for the Western District of Washington refused to allow a lesbian couple who had married in Canada to file a joint Chapter 7 petition. In the absence of a countervailing state statute, the court held that the Defense of Marriage Act ("DOMA"), which limits "marriage" and "spouses" to opposite-sex couples for purposes of federal law, precluded the couple from filing jointly.[5] In an extensive analysis, the court found that DOMA does not violate the Tenth Amendment, the Fourth Amendment, or the equal protection[6] and substantive due process clauses of the Fifth Amendment. The court also declined to apply the doctrine of comity to recognize the couple's Canadian marriage for the purposes of § 302 governing joint cases.

In re Levenson, 560 F.3d 1145 (9th Cir. 2009); In the Matter of Karen Golinski, 587 F.3d 901 (9th Cir. 2009).

Prior to the Supreme Court decision in U.S. v. Windsor, above, the Court of Appeals for the Ninth Circuit had examined the constitutionality of DOMA in two separate internal personal grievances actions related to federal health benefits. A deputy federal public defender and staff attorney at the ninth circuit headquarters had each married same-sex partners in 2008 prior to the passage of Proposition 8. The benefits administrator refused to allow the employees to include their same-sex spouses under their employee benefits plans because of DOMA's restrictive definition of spouse. In the first case, Chief Judge Kozinski was able to avoid deciding the constitutionality of DOMA.

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[5] The Defense of Marriage Act provided that "[i]n determining the meaning of any Act of Congress, or of any ruling, regulation, or interpretation of the various administrative bureaus and agencies of the United States, ... the word 'spouse' refers only to a person of the opposite sex who is a husband or a wife." 1 U.S.C. § 7. In contrast to In re Rabin and with little analysis, the court asserted blankly that § 302 required a joint filing to consist of a debtor and "such individual's spouse."

[6] The court held that DOMA did not discriminate against a protected class. The court found that although the majority opinion in Lawrence v. Texas, 539 U.S. 558 (2003) may indicate a shift in the treatment of same-sex couples, the Supreme Court did not hold that same-sex couples constitute a suspect or semi-suspect class under an equal protection analysis. 315 B.R. at 144. As DOMA was determined not to burden a fundamental right or target a suspect class, the court analyzed DOMA under the deferential rational basis test. The court concluded that the DOMA classification of marriage bore a rational relationship to several legitimate governmental interests such as defending and nurturing the institution of traditional marriage.

He concluded that the Federal Employee Health Benefits Act ("FEHBA") was sufficiently ambiguous to allow a verbal sleight of hand to circumvent any conflict with DOMA. In the course of his opinion, however, Kozinski indicated that DOMA raised a "thicket" of serious constitutional issues in light of case law precedent in Romer v. Evans, 517 U.S. 620 (1996), Lawrence v. Texas, 539 U.S. 558 (2003), Witt v. Department of Air Force, 527 F.3d 806 (9th Cir. 2008) (holding that "don't ask don't tell" policy had to survive heightened scrutiny as to *each* service member discharged) and Sell v. U.S., 539 U.S. 166 (2003).

Circuit Judge Reinhardt, however, found that FEHBA was unambiguous in its prohibition of discrimination based on sex and sexual orientation and in direct conflict with DOMA. As a result, Reinhart examined DOMA's compliance with the equal opportunity clause of the Fifth Amendment. Although Judge Reinhardt opined that some form of heightened scrutiny should be applied, he affirmed that DOMA would not even be able to survive a rational basis analysis. According to Judge Reinhart DOMA bore no rational relationship to a legitimate government interest.

As of July 2013, thirteen states (Massachusetts, Connecticut, Iowa, Vermont, New Hampshire, New York, Maryland, Maine, Washington, Delaware, Rhode Island, Minnesota, and California) and Washington D.C. allow same-sex marriage.[7]

Hollingsworth v. Perry, 558 U.S. 183 (2013). The United States Supreme Court held that proponents of California Proposition 8 lacked standing in federal court as the only harm to proponents was ideological, which the Court stated is never enough for standing. The result is that the California federal district court ruling declaring Proposition 8 unconstitutional stands and same-sex couples in California can now marry.

As noted above, various challenges to the various state laws around the country denying marriage equality are likely in the future and the number of states legally recognizing same-sex marriages will likely increase.

III. Bankruptcy Choice of Law and Same-Sex Marriages

[7] While many state marriage statutes have been upheld, others have been invalidated on state constitutional grounds. See, e.g., Varnum v. Brien, 763 N.W.2d 862 (Ia. 2009) (barring same-sex couples from marriage violates the equal protection provisions of the Iowa Constitution. Equal protection requires marriage, rather than civil unions or some other substitute for same-sex couples); Martinez v. County of Monroe, 850 N.Y.S.2d 740 (N.Y. App. 4 Dept. 2008) (court ruled unanimously that because New York recognizes out-of-state marriages of opposite-sex couples, it must do the same for same-sex couples); In re Marriage Cases, 43 Cal.4th 757 (2008) (ruling that limiting marriage to opposite-sex couples is invalid under the equal protection clause of the California Constitution, and that full marriage rights, not merely domestic partnership, must be offered to same-sex couples); Lewis v. Harris, 908 A.2d 196 (N.J. 2006) (New Jersey is required to extend all rights and responsibilities of marriage to same-sex couples, but prohibiting same-sex marriage does not violate the state constitution); Goodridge v. Department of Public Health, 798 N.E.2d 941 (Mass. 2003) (denial of marriage licenses to same-sex couples violated provisions of the state constitution guaranteeing individual liberty and equality, and was not rationally related to a legitimate state interest); Baker v. State, 744 A.2d 864 (Vt. 1999) (Common Benefits Clause of state constitution requires that same-sex couples be granted the same legal rights as married persons).

Most of the commentary on the interaction of state marriage statutes and DOMA with the bankruptcy code has focused on provisions 11 U.S.C. §§ 302, 507, 1328. Out-of-state same sex marriages raise significant choice of law issues in the characterization of property of the estate. If, for instance, a same-sex couple that was married in Massachusetts and holds a Massachusetts home under tenancy in the entirety, subsequently moves to Florida, a state that, as of July 2013, does not recognize same-sex marriages, civil unions or domestic partnerships, and files bankruptcy shortly thereafter, the Bankruptcy court will be confronted with the issue of respecting which choice of law rules apply in defining the property of the estate. If Florida choice of law rules were to apply and they required Florida law to be used, recognition of the tenancy by the entirety in virtue of the couple's same-sex marriage might be prohibited, thereby enabling creditors to make claims on the home as property of the estate. If, however, federal choice of law rules apply, the court may choose to apply Massachusetts law.[8]

In the Ninth Circuit, federal common law choice of law rules apply in bankruptcy cases.[9] Liberty Tool & Mfg. v. Vortex Fishing Sys. (In re Vortex Fishing Sys.), 277 F.3d 1057, 1069 (9th Cir. 2002); In re Lindsay, 59 F.3d 942, 948 (9th Cir. 1995). Federal choice of law rules follow the approach of the Restatement (Second) of Conflict of Laws. Vortex, 277 F.3d at 1069.[10]

Although no published bankruptcy opinions have addressed the issue of choice of law in the context of out-of-state same-sex marriage, the Ninth Circuit's federal common law approach could enable couples married out of state to benefit from recognition in a California bankruptcy court.

In a Florida case, the bankruptcy judge held in dicta that Florida's marriage statute would prevent a Florida bankruptcy court from recognizing a same-sex marriage celebrated in another state for the purposes of a bankruptcy proceeding. In re Mercier, No. 9:03-bk-15259-ALP, 2005 Bankr. LEXIS 18 (Bankr. M.D. Fla. 2005).

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[8] For a detailed analysis of choice of law issues in bankruptcy raised by same-sex marriages see Jackie Gardiner, The Perfect Storm: Bankruptcy, Choice of Law and Same-Sex Marriage, 86 B.U.L. Rev. 881 (2006).

[9] Other circuits apply the choice of law rules of the forum state in bankruptcy cases. See, e.g., Amtech Lighting Servs. v. Payless Cashways, Inc. (In re Payless Cashways), 203 F.3d 1081, 1084 (8th Cir. 2000); Comdisco Ventures, Inc. v. Fed. Ins. Co.(In re Comdisco Ventures, Inc.), 2005 WL 1377856, at *4 (N.D. Ill. 2005); Carter Enterprises, Inc. v. Ashland Specialty Co. Inc., 257 B.R. 797, 801 (S.D. W. Va. 2001). A third set of courts recognizes the complexities of developing a coherent choice of law policy in bankruptcy and applies state choice of forum rules in the absence of an overriding federal interest. See Bianco v. Erkins (In re Gaston & Snow), 243 F.3d 599, 606 (2d Cir. 2001); Compliance Marine, Inc. v. Campbell (In re Merritt Dredging Co., Inc.), 839 F.2d 203, 206 (4th Cir. 1988); Federal Deposit Ins. Corp. v. Lattimore Land Corp., 656 F.2d 139, 150 n.16 (5th Cir. 1981).

[10] The Restatement provides that the following factors are to be considered as part of a choice of law analysis: (1) the needs of the interstate and international systems; (2) the relevant policies of the forum; (3) the relevant policies of other interested states and the relative interests of those states in the determination of the particular issue; (4) the protection of justified expectations; (5) the basic policies underlying the particular field of law; (6) certainty, predictability and uniformity of result; and (7) ease in the determination and application of the law to be applied. RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 6.

Crossover Issues re: Trusts in Bankruptcy

CPEX – 2024

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THE HONORABLE JOSHUA P. SEARCY
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1. Exclusions from Property of the Estate – Is a Debtor's Interest in a Trust Excluded?

    a. A debtor's interest in a trust that contains a restriction on transfer (spendthrift provision) that is enforceable under applicable non-bankruptcy law is excluded from the Estate. 11 U.S.C. § 541(c)(2). *See also, Patterson v. Shumate,* 504 U.S. 753 (1992); *United States Internal Revenue Service v. Snyder*, 343 F.3d 1171 (9th Cir. 2003).

    b. A debtor's powers as the trustee of a trust *of which the debtor is not a beneficiary* likely is not property of the estate. 11 U.S.C. § 541(b)(1); *see, e.g., In re Simon*, 179 B.R. 1, 5-6 (Bankr. D. Mass. 1995); *In re Poffenbarger*, 281 B.R. 379, 391-92 (Bankr. S.D. Ala. 2002) (collecting cases, and ruling that when the debtor held funds in trust for a child, but was not the beneficiary, such funds did not come into the estate); *cf.* 11 U.S.C. § 541(b)(6) (excepting certain funds placed in a Section 529 education fund from property of the estate).

    c. Bodies of applicable non-bankruptcy law

        i. ERISA - Title 29 of the United States Code.

            1. 29 U.S.C. § 1056(d)(1) provides that ""[e]ach pension plan shall provide that benefits provided under the plan may not be assigned or alienated."

            2. ERISA is applicable non-bankruptcy law sufficient to exclude retirement plans subject to and qualified under ERISA from property of the estate. *See, Patterson v. Shumate, supra*.

                a. Control. A debtor's interest in an ERISA qualified plan is not subject to alienation and is not property of the bankruptcy estate, even though the debtor holds substantial control over the timing and manner of plan distributions. *In re Connor*, 73 F.3d 258 (9th Cir. 1996).

                b. Plan not operated in compliance with ERISA may still be excluded. *McDonnell v. Gilbert (In re Gilbert)*, No. 23-2944, 2024 U.S. App. LEXIS 26872 (3d Cir. Oct. 24, 2024).

            3. Single Participant Plans Not Subject to ERISA. Plans in which the employer is the only participant are not subject to ERISA. *In re Witwer*, 148 B.R. 930 (Bankr. C.D. Cal. 1992).

a. A former spouse with an interest in the plan may qualify as the non-owner employee subjecting the plan to ERISA. *In re Metz*, 225 B.R. 173 (9th Cir. BAP 1998).

4. Do protections expire when benefits become payable – The Circuits are Split. Once a benefit from an ERISA plan becomes payable to the participant, the restriction on transfer is no longer enforceable. *N.L.R.B. v. HH3 Trucking, Inc.,* 755 F.3d 468 (7th Cir. 2014); *Hoult v. Hoult,* 373 F.3d 47, 53-55 (1st Cir. 2004); *Central States Pension Fund v. Howell,* 227 F.3d 672, 678-79 (6th Cir. 2000); *Wright v. Riveland,* 219 F.3d 905, 919-21 (9th Cir. 2000); *Robbins v. DeBuono,* 218 F.3d 197, 203 (2d Cir. 2000); *Trucking Employees of North Jersey Welfare Fund, Inc. v. Colville,*16 F.3d 52, 54-56 (3d Cir.1994).
    a. Minority Position. See, *United States v. Smith,* 47 F.3d 681 (4th Cir.1995); *Herberger v. Shanbaum*, 897 F.2d 801, 803-04 (5th Cir. 1990).

ii. State spendthrift trust laws. In California, Probate Code §§ 15300 *et seq.* California law generally enforces anti-alienation provisions on Income (Probate Code § 15300) and Principal (Probate Code § 15301).

1. From 1990 to 2017, the leading bankruptcy case interpreting California spendthrift trust laws had been *Neuton v. Danning (In re Neuton)*, 922 F.2d 1379, 1383 (9th Cir. 1990). In *Neuton*, the debtors filed bankruptcy in November 1987. On the petition date, the debtor held a contingent interest in an *inter vivos* spendthrift trust. The trust provided that debtor was to receive a share of trust income during life and that, if living at the time of the trustor's death, a greater share of the trust. One month later, the trustor died. The 9th Circuit held that 75% of the trust was excluded from the bankruptcy estate as a valid spendthrift trust. The court further recognized that CCP § 709.010 could potentially protect some or all of the remaining 25% that was not necessary for the support of the debtor.

2. *In re Reynolds*, 479 B.R. 67, 71 (B.A.P. 9th Cir. 2012) In *Reynolds*, the debtor was a named beneficiary in three family trusts, the Bypass Trust, the Marital Trust (collectively, the "Family Trust") and the Survivor's Trust ("Survivor's Trust"). Once the debtor survived his father by thirty days, he was entitled to receive distributions from both the Family Trust and the Survivor's Trust. From the Family Trust, debtor was entitled to $250,000. Additionally, as a one-third

beneficiary of the Survivor's Trust, debtor was entitled to receive $100,000 per year for ten years. Both the Family Trust and the Survivor's Trust included spendthrift trust provisions. The assets in the Survivor's trust were interests in undeveloped real property that did not generate any income. No income distributions were expected from the trusts.

Debtor filed a voluntary petition for relief under Chapter 7 of the Bankruptcy Code one day after the death of his father. Debtor's interests in the trusts were vested on the petition date subject to the contingency that he outlived his father by 30 days.

3. The California Supreme Court ruled that a creditor or bankruptcy trustee can reach 100% of principal payments that are "due and payable" to a beneficiary as of the petition date even if the funds were still in the hands of the trust and 25% of future payments that have not yet become due and payable. While the decision discusses payments of principal, the result for payments of income would appear to be the same.
    a. Open Issue: Can the bankruptcy trustee leave the case open until the future payments become due and payable and therefore intercept all payments? Section 541(c)(2) provides that a restriction on transfer is enforceable against a bankruptcy trustee. When that restriction ceases to be enforceable, however, due to the passage of time, a good argument can be made that it is no longer enforceable. The contrary argument would be that the estate's interest is fixed as of the petition date. This position, however, ignores that creditors outside of bankruptcy would be able to enforce judgments against such payments when they became due and payable.

4. Needs-based Exceptions under State Law: A beneficiary, however, may be able to reduce the amount that a creditor can reach to the extent that the trust provides protections for a beneficiary's support or education and the beneficiary needs the money for those purposes. *Carmack v. Reynolds*, 2 Cal.5th 844 (2017).

d. Debtor's Interest in Trust Determined as of the Petition Date. The nature of a debtor's interest as a beneficiary of an *inter vivos* trust is generally determined on date that bankruptcy petition is filed and a trustor's post-petition death likely does not enlarge a bankruptcy trustee's rights. *In re Kim,* 257 B.R. 680 (9th Cir. BAP

2000) [On petition date, debtor had an interest in a fully exempt public employment retirement plan. Within weeks of the petition date, debtor rolled the funds to an individual retirement account. Court held that the exemption was determined by the nature of the interest in property on the petition date and that the account was a fully exempt public employment plan].

e. Revocable Trusts. If Debtor's interest is as a beneficiary of a revocable trust, then the interest in the trust is not property of the estate. Instead, it's a mere expectancy. *In re Spencer*, 306 B.R. 328 (Bankr. C.D.Cal. 2004).

f. Section 541(a)(5) Does Not Apply. The post-petition death of the trustor causing debtor's interest in the trust to vest did not render such interest property of the estate. Furthermore, acquiring property by trust was not a bequest, devise or inheritance bringing the property into the estate under Section 541(a)(5)].

g. Self-Settled Trusts may not be enforceable under State Law or Section 548(e).

   i. California law does not enforce spendthrift provisions in self-settled trusts. California Probate Code § 15304(a). *In re Salkin* 526 B.R. 31 (Bankr. C.D.Cal. 2015), and *In re Nielson*, 526 B.R. 351 (Bankr. D.Hi. 2015).

      1. California law will not enforce a purported spendthrift provision in a revocable trust because assets held in a revocable trust remain subject to creditor claims. California Probate Code § 18200.

      2. Florida also has a strong public policy against the enforcement of self-settled spendthrift trusts which are designed to put assets out of the reach of creditors. *Mehdipour v. Rensin (In re Rensin)*, 600 B.R. 870, 880 (Bankr. S.D. Fla. 2019); *Menotte v. Brown (In re Brown)*, 303 F.3d 1261, 1266-70 (11th Cir. 2002).

      3. Texas law also voids self-settled spendthrift trusts. *Shurley v. Texas Commerce Bank-Austin, N.A. (In re Shurley)*, 115 F.3d 333, 338-39 (5th Cir. 1997).

   ii. Domestic Asset Protection Trusts. Many states now have laws permit spendthrift provisions in self-settled trusts.

      1. In most states, a spendthrift provision in a self-settled trust is invalid against creditors. There are approximately 17 states that have enacted statutes specifically authorizing self-settled spendthrift trusts including Alaska, Colorado, Delaware, Hawaii, Mississippi, Missouri, Nevada, New Hampshire, Ohio, Oklahoma, Rhode Island,

South Dakota, Tennessee, Utah, Virginia, West Virginia, and Wyoming.

2. Typical features: Must contain a spendthrift provision, be irrevocable, and not ***require*** distributions of principal or income.

3. Example: Nevada permits self-settled spendthrift trusts so long as the following requirements are met: (1) the trust is irrevocable; (2) the trust does not require that any part of principal or income be distributed to the settlor; (3) the trust is not intended to hinder, delay, or defraud known creditors; and (4) the trustee is an individual, trust company, or bank with a residence/office in Nevada. Nevada Revised Statutes §§ 166.015 and 166.040.

4. Many states also require that the majority of assets be located in the state in order for the choice of law provision to be enforceable.

5. Some states also require that at least one of the trustees be domiciled in the state and that tax returns be filed in such state.

6. Fraudulent Transfer Laws. Most states' laws allow creditors or bankruptcy trustees to avoid transfers made with actual intent to hinder, delay, or defraud creditors.

iii. Choice of Law Provisions. Courts in states that do not recognize self-settled spendthrift trusts may be unwilling to recognize a choice of law provision in a trust specifying state law that does enforce self-settled spendthrift trusts. *See e.g.*, *In re Portnoy*, 201 B.R. 685 (Bankr. S.D.N.Y. 1996) [law of state with greatest interest in litigation will prevail over choice of law provision in trust]; *In re Brooks*, 217 B.R. 98 (Bankr. D. Conn. 1998) [law of settlor's state of residence determines validity as to creation of trust notwithstanding choice of law provision which would apply if trust validly created]; *In re Lawrence*, 227 B.R. 907 (Bankr. S.D. Fla. 1998) [bankruptcy court refused to recognize debtor's unilateral specification in offshore asset protection trust that laws of the Republic of Mauritius will apply in determining extent of debtor's rights in property and whether such rights became property of bankruptcy estate]; *Dexia Credit Local v. Rogan*, 624 F.Supp.2d 970 (N.D. Ill. 2009) [court refused to honor laws of another jurisdiction specified in a trust where doing so would violate the public policy of the State of Illinois]. *See also*, *In re Huber*, 493 B.R. 798 (Bankr. W.D. Wash. 2013) [Trust had a choice of law provision which stated Alaska law would control. Debtor filed bankruptcy in Washington. The Chapter 7 trustee sought assets of the trust under the laws of the state of

Washington, but debtor contended that the choice of law provision in the trust was controlling. Debtor's choice of Alaska law designated in a trust would not be upheld as Alaska did not have a substantial relation to the trust; at the time the trust was created, the settlor and beneficiaries were domiciled in Washington, the assets and all of debtor's creditors were located in Washington. The only relation to Alaska was that it was the location in which the trust was to be administered and the location of one of the trustees. Additionally, Washington State has a strong public policy against self-settled asset protection trusts; a debtor should not be able to escape the claims of his creditors by utilizing a spendthrift trust, and a debtor's transfers made to self-settled trusts are void as against existing or future creditors.]

h. Laws Attacking Domestic Asset Protection Trusts ("DAPT").

1. State laws refusing to recognize self-settled spendthrift trusts (California Probate Code § 15304(a), Fla. Stat. § 736.0107)

2. State fraudulent transfer laws (11 U.S.C. § 544; California Civil Code §§ 3439 *et seq.*)

3. Federal fraudulent transfer laws (11 U.S.C. § 548(a) and (e))

4. FDCPA – Fair Debt Collection Procedure Act (28 U.S.C. § 3001 *et seq.)*

    a. Majority Position - Bankruptcy Trustees ***may*** use FDCPA where government is a creditor. *Vieira v. Gaither (In re Gaither)*, 595 B.R. 201, 212 (Bankr. D.S.C. 2018); *Hillen v. City of Many Trees, LLC (In re CVAH, Inc.)*, 570 B.R. 816, 824 (Bankr. D. Idaho 2017); *Gordon v. Harrison (In re Alpha Protective Services, Inc.)*, 531 B.R. 889, 906 (Bankr. M.D. Ga. 2015); *Tronox Inc. v. Kerr McGee Corp. (In re Tronox Inc.)*, 503 B.R. 239, 273-74 (Bankr. S.D.N.Y. 2013).
    b. Minority Position - Bankruptcy Trustees ***may not*** use FDCPA. *See, MC Asset Recovery LLC v. Commerzbank A.G. (In re Mirant Corp.)*, 675 F.3d 530 (5th Cir. 2012).

5. State remedies including theories of alter ego or reverse piercing or state laws that void trusts created for illegal or improper purpose (*See e.g., In re Schwarzkopf, infra*.; *Dean v. United States*, 987 F.Supp. 1160 (W.D. Mo. 1997)).

i. Shifting Trusts. Shifting Trusts that provide for forfeiture of a beneficiary's interest upon a creditor's attempted attachment or alienation may be enforceable. *In re Fitzsimmons*, 896 F.2d 373 (9th Cir. 1990).

1. Restriction on transfer in purported trust created by settlement of a personal injury action not enforceable under California law. *In re Jordan*, 914 F.2d 197 (9th Cir. 1990).

2. Spendthrift provisions may not be enforceable against the IRS pursuant to 26 U.S.C. § 6321.

2. Fraudulent Transfer Laws - Can Assets Transferred to a Trust be Avoided

a. A bankruptcy trustee can avoid prepetition transfers of assets by a debtor including transfers to a trust.

b. Bodies of Fraudulent Transfer Laws. The Bankruptcy Code contains fraudulent transfer laws in 11 U.S.C. § 548. The Bankruptcy Code further allows a trustee to use applicable non-bankruptcy fraudulent transfer laws pursuant to 11 U.S.C. § 544 which makes California's version of the Uniform Fraudulent Transfer Act set forth in Civil Code §§ 3439 *et seq.* The FDCPA may also be applicable if the government is a creditor. See above.

c. Fraudulent Transfer Law Under 11 U.S.C. § 548

i. Actual Fraud: A trustee may avoid a transfer if the debtor "made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted." 11 U.S.C. § 548(a)(1)(A).

ii. Constructive Fraud: A trustee may avoid a transfer if the debtor "received less than a reasonably equivalent value in exchange for such transfer or obligation" and the debtor meets one of the insolvency definitions. 11 U.S.C. § 548(a)(1)(B).

d. Fraudulent Transfer Law Under 11 U.S.C. § 544 and state law (for example, California Civil Code Section 3429, *et seq*.)

i. Actual Fraud: Pursuant to 11 U.S.C. § 544, a trustee may invoke provisions of state law, standing in the shoes of a creditor, to avoid a transfer of property. To recover on a transfer under Cal. Civ. Code §3439.04(a)(1), a trustee must establish that the transfer of property that was made with actual intent to hinder, delay, or defraud any creditor. An action under Cal.

Civ. Code §3439.04(a)(1) must be brought within four (4) years of the transfer. Cal. Civ. Code §3439.09(a). There is not a significant difference between a claim under §548(a)(1)(A) and a claim under Cal. Civ. Code §3439.04(a)(1). But, California Civil Code § 3439.08(a) states that "[a] transfer or obligation is not voidable under paragraph (1) of subdivision (a) of Section 3439.04, against a person that took in good faith and for a reasonably equivalent value given the debtor or against any subsequent transferee or obligee." In turn, the plain language of California Civil Code § 3439.03 provides that "[v]alue is given for a transfer or an obligation if, in exchange for the transfer or obligation, property is transferred or an antecedent debt is secured or satisfied. . ."

ii. Constructive Fraud: Under California law, a transfer is constructively fraudulent in two situations. First, as to a creditor whose claim arose before or after the transfer was made or the obligation was incurred, a transfer is constructively fraudulent if the debtor made the transfer: (2) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor either: (A) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction. (B) Intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due. Cal. Civ. Code § 3439.04(a)(2). Alternatively, under Cal. Civ. Code § 3439.05, a transfer is constructively fraudulent "as to a creditor whose claim arose before the transfer was made or the obligation was incurred if the debtor made the transfer or incurred the obligation without receiving a reasonably equivalent value in exchange for the transfer or obligation and the debtor was insolvent at the time or the debtor became insolvent as a result of the transfer or obligation." See, Cal. Civ. Code § 3439.05

e. Reach-back Period

i. Under Bankruptcy Code Section 548, the reach back period is two years prepetition.

ii. Under Bankruptcy Code Section 544 which makes California Civil Code Sections 3439 *et seq.* applicable, the reach back period is four years or one year after discovery not to exceed seven years.

iii. 10-Year Reach Back – Section 548(e)(1) extends the reach back period for a trustee to 10 years to avoid a debtor's transfer of an interest in property to a self-settled trust.

> "In addition to any transfer that the trustee may otherwise avoid, the trustee may avoid any transfer of an interest of the debtor in property that was made on or within 10 years before the date of the filing of the petition, if—
>
> > **(**A) such transfer was made to a self-settled trust or similar device;
> >
> > (B) such transfer was by the debtor;
> >
> > (C) the debtor is a beneficiary of such trust or similar device; and
> >
> > (D) the debtor made such transfer with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made, indebted."

iv. *In re Kipnis*, 555 B.R. 877 (Bankr. S.D.Fla. 2016) [chapter 7 trustee permitted to use IRS 10-year reach-back to avoid fraudulent transfer]; *In re CVAH*, 570 B.R. 816, 834-36 (Bankr. D. Ida. 2017) [chapter 7 trustee permitted to use IRS 10-year reach-back].

f. Cases interpreting Section 548(e)

i. *In re Mastro*, 2011 WL 4498834 (Bankr. W.D. Wa. September 27, 2011) [properties transferred to self-settled spendthrift trusts including an offshore asset protection trust avoided in bankruptcy commenced by creditors through filing of involuntary petition to utilize Bankruptcy Code Section 548(e)]

ii. *In re Mortensen*, 2011 WL 5025249 (Bankr. D. Alaska., May 26, 2011) [Property transferred by debtor to asset protection trust more than four years prior to bankruptcy avoided pursuant to Section 548(e). In finding actual fraudulent intent in making the transfer, the bankruptcy court relied on statements in the trust that the purpose of the trust was to preserve assets for the settlor's children. The bankruptcy court refused to apply Alaska law that specifically holds that statements of intent in a trust cannot be used to establish fraudulent intent finding that state law did not apply to Section 548(e)]

iii. *In re Porco*, 447 B.R. 590 (Bankr. S.D. Ill. 2011) [bankruptcy court refused to apply Section 548(e) to a transfer by debtor to related entity which was

attacked as a constructive or resulting trust finding that Section 548(e) applied only to express and not implied trusts]

iv. *In re Potter*, 2008 WL 5157877 (Bankr. D.N.M. 2008) [bankruptcy court found actual fraudulent intent where debtor transferred all assets to trust rendering him insolvent where trust formed after entry of a large judgment and debtor continued to reside in residence]

v. *In re Castellano*, 514 B.R. 555 (Bankr. N.D.Ill. 2014) [debtor's transfer to self-settled spendthrift trust avoidable fraudulent transfer]

vi. Note: Section 548(e) is not dependent on state law. As such, a choice of law provision specifying the law of a state with liberal laws permitting self-settled trusts may not be applicable.

(A) In 2012, the 9th Circuit BAP held that a settlor's choice of law provision can determine the bankruptcy estate's interest in a spendthrift trust. *Zukerkorn v. Zukerkorn*, 484 B.R. 182 (9th Cir. BAP 2012). In *Zukerkorn*, the court concluded that the settlor's choice of Hawaii law in a spendthrift trust was valid because Hawaii had a substantial relation to the trust. The Court also concluded that the choice of law was not a violation of fundamental policy for California. Because Hawaii offered complete creditor protection, the bankruptcy trustee was unable to reach any distributions to the beneficiary who was the son of the deceased settlor. While the Court declined to consider whether post-petition distributions of income from the trust were property of the estate under 11 U.S.C. §§ 541(a)(6) and (7) because they were raised for the first time on appeal, the Court confirmed that such distributions of income were not property of the estate under 11 U.S.C. § 541(a)(5) because distributions from an *inter vivos* trust do not constitute a bequest, devise, or inheritance.

vii. Practice Pointers.

1. Post-claim asset protection rarely avoids scrutiny as an actually fraudulent transfer

2. Post-claim asset protection may subject debtor and estate planning professional to liability including application of RICO laws

3. Alter ego and/or laws voiding trusts created for improper purposes can render asset protection trusts void long after expiration of statutes of limitations

4. Choice of law provisions will not control in all situations especially with regard to the question of whether the trust was created for a proper purpose

3. Disclaimers of Interests in Trusts

   a. California Probate Code § 283 provides "A disclaimer is not a voidable transfer by the beneficiary under the Uniform Voidable Transactions Act."

   b. *Drye v. United States*, 528 U.S. 49 (1999) [taxpayer's disclaimer occurring after debt arose ineffective as to the IRS under FDCPA].

   c. *In re Costas*, 555 F.3d 790 (9th Cir. 2009) [debtor defeated chapter 7 trustee's fraudulent transfer action establishing that prepetition disclaimer not a fraudulent transfer under Arizona law where FDCPA inapplicable].

   d. *United States SBA v. Bensal*, 853 F.3d 992 (9th Cir. April 2017) [FDCPA preempted California law that a disclaimer occurring after debt arose is not a transfer and government successfully avoided disclaimer as a fraudulent transfer].

   e. *In re Kipnis*, 555 B.R. 877 (Bankr. S.D.Fla. 2016) [chapter 7 trustee permitted to use IRS 10-year reach-back to avoid fraudulent transfer].

   f. *In re CVAH*, 570 B.R. 816, 834-36 (Bankr. D. Ida. 2017) [chapter 7 trustee permitted to use IRS 10-year reach-back].

4. Voluntary transfers result in loss of exemptions upon avoidance

   a. If a debtor makes a voluntary transfer to a trust that is later avoided by a bankruptcy trustee, the debtor loses his or her exemption in the recovered asset(s). 11 U.S.C. § 522(g). *See also*, *In re Glass*, 60 F.3d 565 (9th Cir. 1995).

   b. For example, a debtor transfers his home to an irrevocable trust for no consideration. A bankruptcy is later filed by or against the debtor. The Trustee successfully avoids the transfer as fraudulent. The debtor is denied any homestead exemption in the recovered asset. Under California law (generally), the exemption is $75,000 for a single person; $100,000 for a family unit; and $175,000 for an elderly person.

5. QPRT – Qualified Personal Residence Trusts

    a. A QPRT is used to transfer a grantor's residence out of the grantor's estate at a low gift tax value. Once the trust is funded with the grantor's residence, the residence and any future appreciation is excluded from the grantor's estate upon death if the grantor survives the term of the trust. QPRTs purport to be irrevocable split interest trusts. For at least tax purposes, the transfer of the residence to the trust constitutes a completed gift. The grantor retains the right to live in the house for a specified number of years rent free. Then, the remainder beneficiaries of the trust become fully vested. If the grantor did not have the right to live in the house post-transfer, then the value of the gift for tax purposes would be the value of the house at the time of the transfer. However, to minimize gift taxes, the Internal Revenue Code § 7520 provides a formula that takes into account the term of the trust, the life expectancy of the grantor, and a specified rate based on the month and year that the transfer was made. This determines the value of the grantor's retained interest which is applied against the value of the residence to minimize or eliminate the gift tax.

    b. For bankruptcy purposes, when the grantor subsequently files bankruptcy during the period of time that he or she has the right to live in the property, does the residence become property of the bankruptcy estate? Or, does the completed gift aspect of the transfer result in the debtor no longer having fee simple title (subject to a trustee's ability to avoid the entire transfer as a fraudulent transfer)?

    c. *In re Yerushalmi*, 487 B.R. 98 (Bankr. E.D.N.Y. 2012) [QPRT not property of grantor's bankruptcy estate]. See also, In re Earle, 307 B.R. 276 (Bankr. S.D.Al. 2002) [debtor's transfer of property to QPRT not fraudulent conveyance].

    d. *Compare*, *In re Ferrante*, 2015 WL 5064087 (9th Cir. BAP 2015). BAP affirmed Judge Albert's judgment which determined a waterfront home in Newport Beach transferred to a QPRT more than 10 years prior to bankruptcy was an asset of the estate. Decision based on actual language of the trust that provided that the QPRT would terminate if the debtor ceased to use the property as his principal residence prior to the specified term until the beneficiaries' interests vested. Court ordered Debtor to move out causing the trust to fail.

6. Exemption Planning

    a. Legislative history indicates planning is proper. H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 361 (1977), reprinted in App. Pt. 4(d)(i) infra (the conversion of nonexempt property into exempt property is not per se fraudulent).

b. Conflicting cases. Eighth Circuit cases.

i. *Hanson v. First National Bank Hanson v. First Nat'l Bank*, 848 F.2d 866 (8th Cir. 1988) and *Norwest Bank Neb., N.A. v. Tveten*, 848 F.2d 871 (8th Cir. 1988) were decided on the same day by the same panel of judges.

ii. In *Hanson*, the debtors were farmers who converted $35,000 of non-exempt property into exempt property. The Eighth Circuit affirmed the lower courts' decisions overruling the objection to the exemption based on the finding that the debtors had no fraudulent intent in making the transfers.

iii. In *Tveten*, the debtor was a physician who liquidated his nonexempt property and purchased approximately $700,000 worth of exempt annuities and life insurance policies. The Eighth Circuit affirmed the lower courts' denial of discharge because the transfers were made with fraudulent intent.

7. What works

a. Maximizing retirement plan contributions within IRS limits especially if debtors have a history of doing so

b. Maximizing cash value in life insurance or similar exemptions

c. Possibly paying down mortgage subject to Section 522 caps and if not done with fraudulent intent

d. If debtor owns a business, possibly creating a defined benefit or other plan that permits greater annual contributions

8. What doesn't work

a. Asset protection schemes rarely, if ever, work. Great risk for denial of discharge

b. Single premium deferred annuities.

i. Most courts hold that they are not exempt under state or Section 522(d). *In re Turner*, 186 B.R. 108 (9th Cir. BAP 1995)

ii. But, see *Silliman v. Cassell*, 292 Ga. 464 (2013).

9. Section 522 Caps

    a. Section 522(n) – Caps exemptions in IRAs at $1,512,350

    b. Section 522(o) – 10 year look back to avoid transfers of non-exempt to exempt property made with actual intent to hinder, delay, or defraud

    c. Section 522(p) – Caps exemptions in residences, burial plots to the extent debtor acquired such interest in the 1,215 day (3.33 year) period prior to bankruptcy. Current cap is $189,050

    d. Section 522(q) – Caps exemptions by felons or if debtor owes a debt arising from a crime, intentional tor, or reckless misconduct that caused serious physical injury or death at $189,050

10. Exemptions

    a. Exempt property protected from reach of creditors. 11 U.S.C. § 522.

    b. Exempt property not subject to payment of administrative claims of estate. 11 U.S.C. § 522(k); *Law v. Siegel*, 571 U.S. 415, 427-28 (2014) (Supreme Court held that bankruptcy court improperly surcharged dishonest debtor's homestead exemption to pay administrative expenses).

    c. Bankruptcy Code allows states to "opt out" of federal exemptions and allow debtors to use state law exemptions. 11 U.S.C. § 522(b)(2).

    d. The burden of proof may be governed by state law notwithstanding Rule 4003. *In re Diaz*, 547 B.R. 329 (9th Cir. BAP 2016) (applying the reasoning of *Raleigh v. Illinois Department of Revenue*, 530 U.S. 15, 20-21 (2000) to the burden of proof in state law exemptions: "the burden of proof is an essential element of the claim itself; one who asserts a claim is entitled to the burden of proof that normally comes with it."); *but see In re Weatherspoon*, 605 B.R. 472, 482 (Bankr. S.D. Ohio 2019) (recognizing that the Sixth Circuit follows the plain language of Rule 4003 under *Zingale v. Rabin (In re Zingale)*, 693 F.3d 704, 707 (6th Cir. 2012).

    e. California law contains exemptions for "private retirement plans." California Code of Civil Procedure §§ 703.140(b)(10)(E) and 704.115(a)(3) and (e).

    f. California law does not permit a debtor to purchase a single premium deferred annuity and exempt it under Code of Civil Procedure § 704.100 which provides exemptions for life insurance (including endowment and annuity) policies. *In re Turner*, 186 B.R. 108 (9th Cir. 1995).

g. Debtor cannot create an exemption out of whole cloth by affixing a title to an agreement or trust (i.e. the retirement plan must be designed and principally used for retirement purposes). *In re Peacock*, 292 B.R. 593, (Bankr. S.D. Ohio 2002).

h. Pre-bankruptcy planning to maximize exemptions generally permissible; however, 2005 Amendments to Bankruptcy Code placed substantial limits on the practice. For example, 11 U.S.C. § 522(o) provides that a debtor that converts non-exempt property into certain specified assets including an exempt residence if the transfer was made with actual intent to hinder, delay or defraud creditors.

11. "Pigs get fed, hogs get slaughtered:" Denial or Revocation of Discharge

a. Certain transfers or asset protection strategies may create the risk of loss of bankruptcy discharge

b. Transfers with Intent to Defraud – 11 U.S.C. § 727(a)(2)

i. Debtor transfers property within one year prior to bankruptcy with actual intent to hinder, delay, or defraud creditors

ii. "Continuing Concealment" – Debtor conceals property more than one year prior to bankruptcy and the concealment continues into the one year prior to bankruptcy. *In re Lawson*, 122 F.2d 1237 (9th Cir. 1997).

c. False oaths – 11 U.S.C. § 727(a)(4)

i. Debtor executes Schedules and Statements concealing an asset, an interest in an asset, an interest in a trust, or a pre-bankruptcy transfer of assets.

d. Failure to explain dissipation of assets – 11 U.S.C. § 727(a)(5)

e. In general terms, if a debtor conceals an asset, but the concealment is not discovered until after the debtor's discharge is entered, and the asset is material (for example, failure to disclose an eight-unit apartment complex in Long Beach, California, compared with failure to disclose $50 in debtor's wallet), the trustee may request revocation of the discharge within the time limits specified in 11 U.S.C. § 727(e).

12. Bankruptcy Crimes – 18 U.S.C. §§ 151-158

a. False oaths, concealment of assets. 18 U.S.C. § 152.

b. Bankruptcy fraud including false petition, involuntary petition, or claim. 18 U.S.C. § 157.

Faculty

Christopher Celentino is a partner with Dinsmore & Shohl LLP in San Diego, where he focuses his practice on creditors' rights, fiduciary services litigation, business reorganization and workouts, and insolvency and bankruptcy law. His bankruptcy practice emphasizes representation of creditors and court-appointed trustees in chapter 7 and 11 cases, as well as representation of debtors in chapter 11 cases. He also has knowledge of mechanic's lien law and related construction litigation matters, as well as family law and related dissolution matters. Mr. Celentino's creditors' right practice emphasizes representing lenders and borrowers in workout and restructuring of commercial loans, secured transactions and lease transactions, and the pursuit of creditors' rights in commercial litigation matters. He is Board Certified in Business Bankruptcy Law by the American Board of Certification. In 2011, Mr. Celentino was selected as one of the "Transcript 10," comprised of 10 of the most noteworthy attorneys from San Diego County, by the *San Diego Daily Transcript*. In 2012, he was president of the California Bankruptcy Forum, having served previously as treasurer and secretary; in 2018, he served as a co-chair of its annual meeting. Mr. Celentino also is a former member and past president of the board of directors of the San Diego Bankruptcy Forum. He is a member of the San Diego County Bar Association, for which he served as chair of its Bankruptcy Law Section from 1992-93, and a secretary and vice president of the California State Bar Association Insolvency Committee, as well as a former member of the board of directors of the Bay Area Bankruptcy Forum. He is also former chair of the San Diego Financial Lawyers Group and has served since 1994 as a court-appointed mediation panel member to the U.S. Bankruptcy Court for the Southern District of California. Mr. Celentino has served as both a court-appointed expert and privately-engaged expert in many cases involving unique issues of bankruptcy and divorce. He is rated AV-Preeminent by Martindale Hubbell, and has been listed in *The Best Lawyers in America* for Bankruptcy and Creditor/Debtor Rights/Insolvency and Reorganization Law since 2012. Mr. Celentino received his B.S. in 1984 from Northwestern University and his J.D. *cum laude* in 1987 from Georgetown University Law Center, where he was co-founder and editor-in-chief of the *Journal of Law and Technology*, and an associate editor of *The Georgetown Law Journal*.

Hon. Elizabeth L. Gunn is a U.S. Bankruptcy Judge for the District of Columbia in Washington, D.C., appointed on Sept. 4, 2020. A COVID-era selection and appointment, she was sworn in by Zoom from her living room. Prior to her appointment, Judge Gunn served as an Assistant Attorney General for the Commonwealth of Virginia as the bankruptcy specialist for the Division of Child Support Enforcement. She also practiced law in Richmond, Va., at Sands Anderson PC and McGuireWoods LLP. In 2017, Judge Gunn was honored as a member of ABI's inaugural class of "40 Under 40." In 2022, she was recognized by the Bar Association of the District of Columbia as its Judicial Honoree and recipient of the BADC's Suzanne V. Richards Foundation Grant. Judge Gunn serves on the advisory board of the *American Bankruptcy Law Journal* and is a coordinating and associate editor of the *ABI Journal*. In addition, she sits on the boards of the Federal Bar Association Bankruptcy Section, International Women's Insolvency & Restructuring Confederation, American Bar Association, National Conference of Federal Trial Judges and the Chesapeake Chapter of the Turnaround Management Association, and she hosts the popular American Bar Association Business Law Section Podcast "Bad Boys of Bankruptcy." She also is a member of the Walter Chandler Bankruptcy Inn of Court and is Board Certified in Consumer Bankruptcy Law by the American Board of Certification.

Judge Gunn received her B.A. *cum laude* from Willamette University and her J.D. *cum laude* from Boston College Law School.

D. Edward Hays is a founding member of Marshack Hays LLP in Irvine, Calif. He was admitted to practice in 1992. Mr. Hays has been a Certified Bankruptcy Law Specialist with the State Bar of California from 2016 to the present. He also has been selected on numerous occasions to present to national, state, county and local bar associations on various legal topics, including bankruptcy law, family law in bankruptcy cases, labor law in bankruptcy, exemptions, enforceability of spendthrift trusts, evidence, pretrial and trial practice, and recent developments in bankruptcy law. In 2011 and 2014, Mr. Hays presented at the Southern California Trust and Estate Planning annual conference on the treatment of trusts in bankruptcy. In 2018, he presented an all-day seminar on evidence to the National Association of Consumer Bankruptcy Attorneys. In 2019, he was asked to speak at the annual conference of the National Association of Bankruptcy Trustees on the administration of trusts in bankruptcy, and he was selected to present a seminar on evidence at the National Conference of Bankruptcy Judges in Washington, D.C. During that trip, he also was admitted to appear before the U.S. Supreme Court. Mr. Hays received his B.A. in business with honors from California State University at Fullerton in 1989 and his J.D. from the University of Southern California Law Center in 1992, where he was a member of the Hale Moot Court Honors program.

Hon. Joshua P. Searcy is a U.S. Bankruptcy Judge for the Eastern District of Texas in Tyler, appointed on March 1, 2021. Previously, he was an attorney with Searcy & Searcy, P.C. in Longview, Texas, where his bankruptcy practice included representing debtors and creditors in chapters 7, 11, 12 and 13, as well as chapter 7 and 11 trustees. He also represented and defended financial institutions, handled real estate matters and nonbankruptcy civil litigation, and provided general representation to a municipality, including as city prosecutor. Judge Searcy has served as secretary on the Executive Council of the Bankruptcy Section of the State Bar of Texas, is a past recipient of the Section's Romina L. Mulloy Bossio Achievement Award, and is a member of ABI's 2018 class of "40 Under 40." He is admitted to practice in the State of Texas, the U.S. District Courts for the Northern, Southern, Eastern and Western Districts of Texas, the Fifth Circuit Court of Appeals, and the U.S. Supreme Court. Mr. Searcy received his B.A. in Spanish and history from Trinity University in San Antonio and his J.D. from Baylor University School of Law in 2005.