Law v. Siegel

Michael A. Stevenson, Moderator
Stevenson & Bullock PLC; Southfield, Mich.

Leonora K. Baughman
Kilpatrick & Associates, P.C.; Auburn Hills, Mich.

Michael E. Baum
Schafer & Weiner PLLC; Bloomfield Hills, Mich

Hon. Thomas J. Tucker
U.S. Bankruptcy Court (E.D. Mich.); Detroit

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Law v. Siegel and the Sixth Circuit's Reaction to *Law v. Siegel*

Michael E. Baum, Schafer and Weiner, PLLC
Bloomfield Hills, Michigan
with substantial assistance from Shanna M. Kaminski, Schafer and Weiner, PLLC

It is often said that bankruptcy provides relief for the "honest but unfortunate" debtor. In furtherance of that goal, the Bankruptcy Code contains provisions denying the benefits of bankruptcy to debtors who behave in a dishonest manner before or during a bankruptcy case. For example, a debtor who fraudulently conceals or transfers assets or who makes a false oath in a bankruptcy case may be denied the ultimate benefit of bankruptcy – the discharge of his or her pre-bankruptcy debts.

Although the Bankruptcy Code contains provisions that allow relief to be denied to dishonest debtors, it lacks mechanisms for compensating those harmed by the debtor's misconduct. Many times trustees discover hidden cash and such discovery results in the debtor being denied a discharge, but the trustee is unable to recoup its time and attorney's fees incurred by making the discovery and the creditors are deprived of a distribution of the hidden cash that was discovered because, for example, it was already spent by the debtor.

In an attempt to address this issue, trustees (and sometimes creditors) began to request other remedies to curb debtor misconduct and compensate those that were harmed by the debtor's misconduct. Such remedies included denial of a debtor's claim of exemption in specific property to make the property available for liquidation and distribution to creditors and surcharging the debtor's exempt assets (i.e.- reduction or elimination of the exemption amount claimed by the debtor in specific property to make that property available for liquidation and distribution to creditors).

The request for a surcharge of a debtor's claim of exemption presents a problem. The Bankruptcy Code provides that, except in certain enumerated circumstances, exempt property cannot be used to pay claims against the debtor, including administrative expense claims. *See* 11 U.S.C. §§522(c) and (k). To circumvent the Bankruptcy Code's express provisions prohibiting

the use of exempt property to satisfy claims, trustees (and creditors) asked that the bankruptcy court use its equitable powers to order a surcharge of the debtor's exemptions. The equitable powers of the bankruptcy court are set out in Section 105(a) of the Bankruptcy Code, which authorizes a bankruptcy court to "issue any order, process, or judgment that is necessary or appropriate to carry out" its provisions and take "any action necessary to prevent an abuse of process."

The question of whether Section 105(a) of the Bankruptcy Code grants a bankruptcy court the power to surcharge a debtor's exempt assets caused a circuit split to develop. The First Circuit and Ninth Circuit permitted exemptions to be surcharged as a remedy for debtor misconduct. See *Malley v. Agin*, 693 F.3d 28 (1st Cir. 2013) and *Latman v. Burdette*, 366 F.3d 774 (9th Cir. 2004). The Tenth Circuit, on the other hand, prohibited a debtor's exemptions to be surcharged for misconduct, relying on Section 522 of the Bankruptcy Code. *See In re Scrivener*, 535 F.3d 1258 (10th Cir. 2008). In *Law v. Siegel*, 134 S. Ct. 1188 (2014) the United States Supreme Court addressed this circuit split.

I. *Law v. Siegel*, 134 S. Ct. 1188 (2014)

A. Background

In 2004, Steven Law (the "Debtor") filed a Chapter 7 bankruptcy case in the United States Bankruptcy Court for the Central District of California (the "Bankruptcy Court"). Alfred Siegel (the "Trustee") was subsequently appointed to serve as trustee for the bankruptcy estate. The estate's only significant asset was the Debtor's house in Hacienda Heights, California.

In his Schedules, the Debtor valued the house at $363,348 and disclosed that the house was subject to two voluntary liens: a note and deed of trust for $147,156.52 in favor of Washington Mutual Bank, and a second note and deed of trust for $156,929.04 in favor of Lin's

Mortgage & Associates. The Debtor then claimed an exemption in the equity in the house in the amount of $75,000 under California law. Therefore, the Debtor represented that there was no equity available in the house for the estate.

Believing that the lien and deed of trust in favor of Lin's Mortgage and Associates was fraudulent, fictitious, and intended to diminish the equity in the house, the Trustee initiated an adversary proceeding to avoid the lien so that the home could be liquidated for the benefit of the estate and its creditors. A default judgment was entered in the adversary proceeding. The default judgment was subsequently vacated when a Lili Lin of China filed a motion to set aside default and default judgment.

After the default and default judgment were set aside, a Lili Lin of Artesia, California ("Lili Lin of Artesia") filed an answer in the adversary proceeding and stipulation for judgment that purported to resolve all the differences between her and the Trustee with respect to the adversary proceeding. In connection with the stipulation for judgment, Lili Lin of Artesia executed a declaration stating that she knew the Debtor and did not loan him money as set forth in the note and deed of trust. She further declared that the Debtor gave her a copy of the note and deed of trust in 1999, but never explained to her why he gave her the document.

The Trustee filed a motion to approve the compromise with Lili Lin of Artesia. Lili Lin of China filed an objection to the motion to approve the compromise arguing that she had not settled with the Trustee. The Bankruptcy Court ruled that Lili Lin of China lacked standing to oppose the motion to approve the compromise. The Bankruptcy Court noted that Lili Lin of China had never actually appeared in court in person and had not furnished evidence to the court that she was the lienor. In contrast, there was Lili Lin of Artesia's evidence that she had been involved in the grant of the lien in 1999.

The Bankruptcy Court determined that the evidence proffered by the Trustee was sufficient to grant the motion to approve the compromise and that approval of the stipulated judgment in favor of the Trustee was fair and equitable, and in the best interests of the estate. The stipulated judgment provided that the transfer to Lili Lin of Artesia was avoided under 11 U.S.C. §544(b) and California Civil Code §3439.04(a) and that interests of Lili Lin of Artesia in the note and deed of trust were deemed recovered by the Trustee under 11 U.S.C. §550(a).

This did not end the litigation. Lili Lin of China continued to claim to be the true beneficiary of the disputed note and deed of trust. Over the next five years, Lili Lin of China managed- despite supposedly living in China and speaking no English- to engage in extensive litigation, including several appeals, contesting the avoidance of the deed of trust and the Trustee's subsequent sale of the house.

Finally, in 2009, the Bankruptcy Court entered an order concluding that "no person named Lili Lin ever made a loan to [the Debtor] in exchange for the disputed deed of trust." *In re Law*, 401 B.R. 447, 453 (Bankr. C.D. Ca. 2009). The court found that "the loan was a fiction meant to preserve [the Debtor's] equity in his residence beyond what he was entitled to exempt" by perpetrating "a fraud on his creditors and the court." *Id.* With regard to Lili Lin of China, the court declared itself "unpersuaded that Lili Lin of China signed or approved any declaration or pleading purporting to come from her." *Id.* Rather, it said, the "most plausible conclusion" was that the Debtor himself had "authored, signed, and filed some or all of these papers." *Id.* It also found that the Debtor had submitted false evidence "in an effort to persuade the court that Lili Lin of China- rather than Lili Lin of Artesia- was the true holder of the lien on his residence." *Id.*

Prior to the Bankruptcy Court making this determination, the Trustee had filed a motion to surcharge the debtor's exemption in the house in the amount of $75,000. At the time the motion to surcharge was filed, the Trustee had spent over 1,500 hours of his time uncovering the fraudulent note and deed of trust and had incurred approximately $500,000 in attorney's fees. The surcharge request was an attempt to recover a portion of the attorney's fees and the stated basis for the surcharge was the debtor's willful and knowing attempt to defraud his creditors by removing equity from the property. The Trustee argued that courts have allowed trustees to surcharge exemptions in "extraordinary circumstances" utilizing its power under Section 105(a) of the Bankruptcy Code. *Id.*

The Bankruptcy Court, relying on the Ninth Circuit's opinion in *Latman v. Burdette*, 366 F. 3d 774 (9th Cir. 2004), allowed the surcharge. The court in *Latman* held that Section 105(a) of the Bankruptcy Code allows a court to "equitably surcharge a debtor's exemptions when reasonably necessary both to protect the integrity of the bankruptcy process and to ensure that a debtor exempts an amount that is no greater than what is permitted by the exemption scheme of the Bankruptcy Code." Both the Ninth Circuit Bankruptcy Appellate Panel and the United States Court of Appeals for the Ninth Circuit affirmed the Bankruptcy Court's surcharge order, finding that the bankruptcy court had not abused its discretion when it approved the surcharge of the exemption.

B. Holding and Reasoning

The Supreme Court reversed the Ninth Circuit Court of Appeals. It held that the Bankruptcy Court exceeded the limits of its authority when it ordered that the $75,000 exemption in the house be made available to pay the Trustee's attorney's fees.

The Supreme Court explained that in exercising its powers under Section 105(a) of the Bankruptcy Code a bankruptcy court cannot contravene specific statutory provisions or override explicit mandates of the other sections of the Bankruptcy Code; a bankruptcy court may only utilize Section 105(a) of the Bankruptcy Code to "carry out" the provisions of the Bankruptcy Code. The Supreme Court reasoned that the surcharge was an impermissible extension of the Court's powers under Section 105(a) of the Bankruptcy Code because it contravened Section 522(k) of the Bankruptcy Code, which provides that a debtor's exemptions are "not liable for payment of any administrative expense," because the attorney's fees that the $75,000 were earmarked to pay were "indubitably" administrative expenses. *Law v. Siegel*,

C. The Dicta of *Siegel*

The issue before the Supreme Court in *Law v. Siegel* and the holding in *Law v. Siegel* are seemingly quite narrow: bankruptcy courts are not permitted to surcharge a debtor's claim of exemption. Despite the issue before the Supreme Court being rather narrow, in its opinion, the Supreme Court went beyond the analysis necessary to decide the case and discussed at length the equitable and inherent powers of the bankruptcy courts, which is now referred to as the "dicta" of the case. Part of this discussion was triggered by an argument made by the Trustee.

The Trustee pointed out that several courts had claimed the authority to disallow an exemption (or to bar a debtor from amending his schedules to claim exemption) based on the debtor's fraudulent concealment of the asset alleged to be exempt and argued that "those decisions reflect a general, equitable power in bankruptcy courts to deny exemptions based on a debtor's bad-faith conduct." *Id.*

In response to the Trustee's argument the Supreme Court asserted that "the Bankruptcy Code admits no power" and that "***federal law* provides no authority for bankruptcy courts to deny an exemption on a ground not specified in the Code**." *Id.* The Supreme Court added that "when a debtor claims a *state-created* exemption, the exemption's scope is determined by state law, which may provide that certain types of debtor misconduct warrant the denial of the exemption." *Id.*

This "dicta" has been interpreted by numerous courts, including the United States Court of Appeals for the Sixth Circuit, as a blanket prohibition on denying a debtor's exemptions (or the debtor's ability to amend his or her exemptions) on the basis of bad faith, prejudice to creditors, or any other equitable consideration, unless the debtor is utilizing a state exemption and the state exemption's scope allows the denial of the exemption for equitable reasons.

II. The Sixth Circuit's Reaction to Law v. Siegel

Prior to the Supreme Court's decision in *Law v. Siegel*, bankruptcy courts in the Sixth Circuit routinely denied properly claimed exemptions based upon equitable considerations relying on *Lucius v. McLemore*, 741 F.2d 125 (6th Cir. 1984). In *Lucius v. McLemore*, the United States Court of Appeals for the Sixth Circuit held that, despite Fed. R. Bankr. P. 1009's clear language permitting a debtor to amend his or her schedules any time before the bankruptcy case is closed, bankruptcy courts may nevertheless refuse to allow a debtor to amend his or her exemptions where the debtor has acted in bad faith or prejudice to creditors would result if the amendment is permitted.

After *Law v. Siegel* was decided, trustees in the Sixth Circuit continued to object to properly claimed exemptions on the basis of bad faith, but debtors began to argue that *Law v. Siegel*

abrogated the authority of bankruptcy courts to deny a debtor's claims of exemption on equitable grounds, such as bad faith or prejudice to creditors, as they had done in the past.

In 2014, the question was raised in the United States Bankruptcy Court for the Eastern District of Michigan on a few different occasions. The question was first raised in In re Baker, Case No. 08-43175, before Judge Tucker.

In *Baker*, the Bakers filed a Chapter 13 case shortly after they lost their home in foreclosure proceedings. The case was later converted to a Chapter 7 proceeding. At no point during the bankruptcy proceedings did the Bakers list in their schedules or otherwise disclose any legal claims related to the foreclosure, but after they received a discharge and their bankruptcy case was closed, the Bakers filed successive wrongful foreclosure actions in state court. The Bakers did not reopen their bankruptcy case to report the claims.

Subsequently, Chapter 7 trustee, Douglas Ellmann, learned of the Bakers' claims and filed a motion to reopen the bankruptcy case. The bankruptcy court ultimately reopened the bankruptcy case. After the case was reopened, the Bakers filed amended schedules reporting their wrongful foreclosure claims to be worth $3,000,000 and claiming a wildcard exemption of $5,300 each. The trustee objected to the amended claims of exemption in the wrongful foreclosure claims on the grounds that the Bakers had failed to disclose the claims for several years and had thereby interfered with the administration of the estate, relying on the theory expressed in *Lucius v. McLemore* that the bankruptcy courts may use their equitable powers to disallow exemptions (or amendments to exemptions) to redress inequitable conduct.

Judge Tucker recognized that the law at the time the trustee filed the objection to the claims of exemption permitted the court to disallow the exemptions due to the Bakers failure to disclose the wrongful foreclosure claims, but concluded that *Law v. Siegel*, which was decided after the

trustee filed his objection to the claims of exemption, precluded him from doing so. The trustee appealed.

The United States District Court for the Eastern District of Michigan affirmed the bankruptcy court's decision in *Ellman v. Baker (In re Baker)*, 514 B.R. 860 (E.D. Mich. 2014). The District Court reasoned that "[t]here is no doubt that *Siegel* curbs the power that bankruptcy courts formerly exercised under *Lucius* to disallow amendments to remedy debtors' bad faith, reckless, or dilatory conduct" and held that "courts must follow *Siegel* even though *Lucius* was not expressly overruled." The trustee again appealed.

While the *Baker* case was pending before the United States Court of Appeals for the Sixth Circuit, the issue of whether, after *Law v. Siegel,* bankruptcy courts may still deny exemptions based on equitable considerations was raised before Judge Shapero in the case *In re Woolner*, 2014 Bankr. LEXIS 5048 (Bankr. E.D. Mich. Dec. 15, 2014).

In *Woolner*, the debtors amended their claims of exemption for a 1990 Chevrolet Corvette ZR01 and 2013 federal and state income tax returns. Chapter 7 trustee, Charles L. Wells, III, objected to the amended exemptions on the basis that the debtors intentionally undervalued the assets in bad faith. In response, the debtors argued that *Law v. Siegel* abrogated the authority of bankruptcy courts to deny debtor's claims of exemption on the basis of bad faith.

Judge Shapero granted the trustee's objection. He reasoned that *Law v. Siegel* was "not dispositive of the present situation or fully supportive of the debtors' arguments because, in that case, the validity of the debtor's claim of exemption was not directly contested or challenged, rather the issue was whether the bankruptcy court had authority to "surcharge" an already allowed exemption because the debtor's bad acts" and that "notwithstanding *Law v. Siegel*, [the

bankruptcy court] has the authority to disallow an amendment to an exemption due to bad faith" based upon *Lucius v. McLemore*.

The debtors filed a motion for reconsideration of the order granting the trustee's objection to their amended claims of exemption. In response, Judge Shapero issued an order requesting that the debtors and the trustee address the applicability of Fed. R. Bankr. P. 4003(b)(2) to the case. Fed. R. Bankr. P. 4003(b)(2) permits a trustee to file an objection to a claim of exemption at any time prior to one year after the closing of the case if the debtor fraudulently asserted the claim of exemption.

After the debtors and trustee submitted supplemental briefs on the issue, Judge Shapero issued an opinion denying the debtors' motion for reconsideration. Judge Shapero reasoned that an objection to a debtor's claim of exemptions on the basis of bad faith "is substantially synonymous with (and not meaningfully different from) the "fraudulently asserted" language in" Fed. R. Bankr. P. 4003(b)(2). Judge Shapero pointed out that Fed. R. Bankr. P. 4003(b)(2) was not examined in *Law v. Siegel*, likely because the Rule was not in effect at the time the case was decided, and that until a binding decision is issued reconciling *Law v. Siegel* with the Rule, the question of whether a debtor's exemptions can be denied on the basis of bad faith "should not be answered purely by implication arising out of *Siegel*."

Judge Shapero further reasoned that *Law v. Siegel* should not be relied upon in determining whether a debtor's exemptions can be denied on the basis of bad faith because "there is a material and decisive difference between the Bankruptcy Court (a) having the authority to surcharge a previously allowed exemption and (b) not having the authority to disallow an exemption in the first place because it was initially claimed fraudulently or in bad faith."

Finally, Judge Shapero reasoned that a finding that Siegel prohibits bankruptcy courts to deny exemptions on the basis of bad faith "could arguably act as an open invitation for debtor to commit fraud in claiming exemptions," noting that this result is inappropriate as a matter of public policy and that there is a "very basic need for the Bankruptcy Court to maintain and enforce the integrity of the entire system."

After *Woolner* was decided, the Sixth Circuit Court of Appeals' decision was issued in *Ellmann v. Baker (In re Baker)*, 2015 U.S. App. LEXIS 11437 (6th Cir. July 2, 2015). The Sixth Circuit Court of Appeals affirmed the District Court and held that *Law v. Siegel* abrogated *Lucius v. McLemore* and prohibits the bankruptcy court from disallowing the debtor's claimed exemptions because of bad faith or fraudulent conduct.

The Sixth Circuit Court of Appeals also addressed the *Woolner* decision in its opinion. It stated that although the principle from *Law v. Siegel* that bankruptcy courts cannot deny a debtor's claim of exemption for equitable reasons has been characterized as mere dictum in cases like *Woolner*, such cases cannot be given any credence because, in the Sixth Circuit, courts have an obligation to follow dicta.

Thus, based upon the Sixth Circuit Court of Appeals decision in *Ellmann v. Baker*, in the Sixth Circuit, bankruptcy courts are no longer permitted to deny a debtor's exemptions based upon bad faith, prejudice to creditors, or any other equitable considerations.

Is there any hope for a split in the Circuits? Other Circuits' Reaction to *Law v. Siegel* and Denying Exemptions and Amendments to Exemptions for Equitable Reasons

Leonora K. Baughman, Kilpatrick & Associates, P.C.
Auburn Hills, Michigan
with substantial assistance from Shanna M. Kaminski, Schafer and Weiner, PLLC,
Bloomfield Hills, Michigan

Like the Sixth Circuit, the majority of the circuits denied exemptions and amendments to exemptions for equitable reasons prior to Law v. Siegel. The circuits that have addressed the issue of denial of exemptions on equitable grounds have determined that Law v. Siegel abrogated the previous decisions and have held that bankruptcy courts cannot deny exemptions or amendments to exemptions for equitable reasons, such as bath faith and prejudice to creditors. No courts in the Second, Eighth, or Tenth Circuits have addressed this issue since Law v. Siegel was decided.

First Circuit

Prior to the Supreme Court's decision in Law v. Siegel, the United States Court of Appeals for the First Circuit allowed both surcharging against exempt property to offset concealment of non-exempt property and the denial of amendments to exemptions as a sanction for bad faith. *See* Hannigan v. White (In re Hannigan), 409 F.3d 480 (1st Cir. 2005) (affirming denial of amendment to homestead exemption as a sanction for bad faith) and Malley v. Agin, 693 F.3d 28 (1st Cir. 2012) (affirming surcharge against exempt property to offset fraudulent concealment of non-exempt property).

To date, the United States Court of Appeals for the First Circuit has not been faced with the issue of whether Law v. Siegel prohibits the denial or limitation of an exemption as a sanction for bad faith. It has, however, in a footnote signaled that it believes that Law v. Siegel does not permit exemptions to be limited based on bad-faith conduct. In U.S. v. Ledee, 772 F.3d 21, 29 n. 10 (1st Cir. 2014), the First Circuit stated the following:

> We note that the Supreme Court has recently held that bankruptcy courts do not have "a general, equitable power . . . to deny exemptions based on a debtor's bad-faith conduct." See Law v. Siegel, 134 S. Ct. 1188, 1196, 188 L. Ed. 2d 146 (2014) (emphasis added). In Malley and the case it cites for the bad-faith principle, In re Hannigan, 409 F.3d 480 (1st Cir. 2005), we affirmed bankruptcy court orders that had relied on the debtors' bad faith to limit exemptions. See Malley, 693 F.3d at 30 (affirming surcharge against exempt property to offset fraudulent concealment of non-exempt property); In re Hannigan, 409 F.3d at 484 (affirming denial of amendment to homestead exemption as a sanction for bad faith). Although Law appears to overrule Malley and Hannigan to the extent they limited exemptions based on bad-faith conduct, the Supreme Court's ruling does not restrict the bankruptcy court's discretion concerning amendments unrelated to exemptions -- as was the situation here.

Bankruptcy courts in the First Circuit that have been asked to deny or limit exemptions based on bad faith since Law v. Siegel have been decidedly uniform in refusing to do so on the basis it is prohibited by Law v. Siegel. *See* In re Pratt, 2015 Bankr. LEXIS 1800 (Bankr. D.P.R. June 1, 2015) (Law v. Siegel bars the Chapter 7 Trustee's Objection to Debtor's Amended Schedule C based on bad faith) and Mateer v. Ostrander (In re Mateer), 525 B.R. 559, (Bankr. D. Mass. 2015) ("The Supreme Court has issued its pronouncement [in Law v. Siegel] that a debtor's fraudulent concealment of an asset is no obstacle to his exempting it and, dicta or not, I feel bound by it. Thus, despite his fraudulent concealment, Mr. Mateer is entitled to claim a[n]….exemption….").

Third Circuit

The United States Court of Appeals for the Third Circuit has not addressed the question of whether Law v. Siegel prohibits exemptions from being denied or limited based on bad faith. Bankruptcy courts in the Third Circuit that have been faced with the question have answered in the affirmative. *See* Neblett v. Gress (In re Gress), 517 B.R. 543 (Bankr. M.D. Penn. 2014) (holding that due to Law v. Siegel it "no longer has the discretion to deny a debtor the opportunity to amend his exemptions based upon equitable considerations such as bad faith or

prejudice to creditors" and that "equitable considerations cannot be used to disallow exemption that otherwise would be allowable under §522.") and Bonidie v. Pv & JC DeBlasio (In re Bonidie), 2014 Bankr. LEXIS 4852 (Bankr. W.D. Pa. Nov. 25, 2014)(relying on Law v. Siegel the court held that the failure to disclose the true amount of the proceeds of a reverse mortgage to the Trustee during the Meeting of Creditors is not a basis to limit or deny the value of the Debtors' exemption because the grounds to do so is not specified in the Code.)

Fourth Circuit

Prior to Law v. Siegel being decided, courts in the Fourth Circuit routinely denied debtor exemptions on the basis of equitable considerations such as, bad faith, misconduct, and prejudice to creditors citing Tignor v. Parkinson (In re Tignor), 729 F.2d 977 (4th Cir, 1984). After Law v. Siegel was decided bankruptcy courts in the Fourth Circuit uniformly held that Tignor was abrogated and that, based on Law v. Siegel, bankruptcy courts do not have the authority to deny exemptions or amendments to exemptions on bad faith or other equitable grounds. *See* In re Scotchel, 2014 Bankr. LEXIS 3640 (Bankr. N.D. W.Va. Aug. 28, 2014) (holding that the bankruptcy court cannot exercise its equitable powers to disallow an amended claim of exemptions based upon equitable considerations such as a debtor's bad faith or prejudice to creditors because Law v. Siegel abrogated Tignor); In re Caillaud, 2014 Bankr. LEXIS 4527 (Bankr. W.D. N.C. Oct. 21, 2014) (holding that "[i]n light of Siegel and its progeny, this bankruptcy court holds that it lacks any statutory authority or equitable power under federal law to deny an exemption based on a debtor's bad faith or misconduct"); In re Padula, 2015 Bankr. LEXIS 1450 (Bankr. E.D. Va. April 28, 2015) (holding that "under Law v. Siegel, Bankruptcy Rule 1009(a)'s explicit language permitting debtors to amend their Schedules "as a matter of course at any time before the case is closed" precludes an inquiry into the Debtor's good faith in

amending her Schedules B and C"); In re Dunaway, 2015 Bankr. LEXIS 819 (Bankr. N.D. W.Va. March 16, 2015) (holding that it was adopting the ""emerging view" interpreting the Supreme Court's decision in Law v. Siegel as having explicitly abrogated cases decided before it that held that a court could disallow a debtor's exemption or amended exemption based upon equitable considerations"); In re Davis, 2015 Bankr. LEXIS 818 (Bankr. N.D. W. Va. March 16, 2015) (holding that it could not "restrict the Debtor's otherwise unfettered right to amend her claimed exemption at any time before the case is closed" because Law v. Siegel "explicitly abrogated cases decided before it that held that a court could disallow a debtor's exemption or amended exemption based upon equitable considerations").

Fifth Circuit

Prior to Law v. Siegel being decided, the United States Court of Appeals for the Fifth Circuit held that a debtor's request to amend its exemptions could be denied based on bad faith or prejudice to creditors. *See* Sandoval v. Sandoval (In re Sandoval), 103 F.3d 20 (5th Cir. 1997). Only one court in the Fifth Circuit has addressed whether Law v. Siegel now prohibits a court from disallowing a debtor's claim of exemption or a request to amend its exemptions based on equitable considerations.

In In re Saldana, 531 B.R. 141 (Bankr. N.D. Tx. May 22, 2015), the United States Bankruptcy Court for the Northern District of Texas was asked to determine whether certain equitable theories, including bad faith, prejudice to creditors, and judicial estoppel barred the debtor from amending his exemptions. The court stated:

> Although the holding in Law v. Siegel might initially appear to be narrow-applicable only to the notice of attempting to equitably surcharge an exemption-the court believes that the Supreme Court has essentially spoken on the issue of whether a court may disallow a debtor's claim of exemption based on bad faith or delay or prejudice to creditors.
>
> [T]he court concludes that Law v. Siegel…implicitly overruled prior case law….that enabled a bankruptcy court to deny an amendment to the debtor's homestead exemption based on bad faith or prejudice to creditors.

Seventh Circuit

Prior to Law v. Siegel, the United States Court of Appeals for the Seventh Circuit recognized an equitable power to deny bad faith amendments to exemptions. See In re Yonikus, 996 F.2d 866 (7th Cir. 1993). The United States Court of Appeals for the Seventh Circuit has yet to address whether Law v. Siegel changes its precedent.

In In re Bogan, 2015 Bankr. LEXIS 1164 (Bankr. W.D. Wis. April 7, 2015), the United States Bankruptcy Court for the Western District of Wisconsin was faced with the issue of whether a debtor's amended claim of exemptions in the cash value in a life insurance policy could be denied by the court because it was made in bad faith. After discussing Judge Shapero's decision in In re Woolner, 2014 Bankr LEXIS 5048 (Bankr. ED MI, Dec. 15, 2014), the court held that Yonikus was abrogated by Law v. Siegel and that "Law v. Siegel mandates the conclusion that the bankruptcy court is without federal authority to disallow the Amended Exemption or to deny leave to amend exemptions based on Debtors' bad faith."

In In re Franklin, 506 B.R. 765 (Bankr. C.D. Ill. 2014), the United States Bankruptcy Court for the Central District of Illinois was asked by a Chapter 7 trustee to deny a debtor's claim of exemption in social security benefits on the grounds that allowing the exemption would "run afoul of the exemption's purpose or otherwise be

inequitable." *Supra*, p.770. The Court held that it could not deny the exemption on the grounds asserted by the trustee because they were equitable in nature. The Court reasoned that in Law v. Siegel the Supreme Court determined that "courts do not have a general equitable power to deny exemptions based on a debtor's bad faith conduct." *Supra*, p.771.

Ninth Circuit

Prior to Law v. Siegel, it had long been accepted in the Ninth Circuit that a debtor's right to amend his or her exemptions was not absolute and that a court had the ability to deny amendments on a showing of a debtor's bad faith or prejudice to creditors. *See* Martinson v. Michael (In re Michael), 163 F.3d 526 (9th Cir. 1998); Arnold v. Gill (In re Arnold), 252 B.R. 778 (9th Cir. BAP 2000); Latman v. Burdette (In re Latman), 366 F.3d 774 (9th Cir. 2004); Magallanes v. Williams (In re Magallanes), 96 B.R. 253 (9th Cir. BAP 1988); Andermahr v. Barrus (In re Andermahr), 30 B.R. 532 (9th Cir. BAP 1983). After the Law v. Siegel decision, the courts in the Ninth Circuit concluded that this generally accepted principle was no longer valid. *See* In re Gutierrez, 2014 Bankr. LEXIS 2637 (Bankr. E.D. Ca. June 12, 2014) ("Therefore, based on Law, this court must conclude that established case law, such as Arnold, which permits a bankruptcy court to disallow an amended claim of exemption based on bad faith and prejudice, is no longer valid."); In re Pipkins, 2014 Bankr. LEXIS 2654 (Bankr. N.D. Ca. June 16, 2014) ("In Law v. Siegel, however, the Supreme Court held that the court cannot disallow an exemption or prevent the amendment of an exemption on equitable grounds if the exemption satisfies the statutory requisites. Therefore, the court will not disallow

Debtor's exemptions, or preclude their amendment, on bad faith grounds."); In re Arellano, 517 B.R. 228, 232 (Bankr. S.D. Ca. 2014) ("Thus, although Law v. Siegel involved a facially distinct issue, that of surcharge allowing payment of administrative expenses, the Court cannot ignore the Supreme Court's clear mandate in the area of debtor exemptions: when a debtor properly asserts an exemption under section 522, it must be allowed unless the controlling law provides for disallowance. And this is true when a debtor assets the exemption at case initiation or at a later point before case closure. There is nothing in section 522 that provides for the denial or disallowance of an exemption based on a debtor's bad-faith conduct or prejudice to third parties. In short, the bankruptcy court's equitable powers are now an insufficient basis for exemption denial even if bad faith or prejudice exists."); Gray v. Warfield (In re Gray), 523 B.R. 170, 174 (9th Cir. BAP 2014) ("Albeit in dicta, the Supreme Court found no equitable power in the bankruptcy court to deny an exemption as a remedy to debtor's bad faith conduct, and in so doing, implied that the judge-made exceptions....do not survive Law v. Siegel."); Elliott v. Weil (In re Elliott), 523 B.R. 188, 194 (9th Cir. BAP 2014) (Due to Law v. Siegel "courts can no longer deny claimed exemptions or bar amendments to exemptions on the ground that the debtor acted in bad faith, when no statutory basis exists for doing so."); In re Reade, 2014 Bankr. LEXIS 5140 *6-7 (Bankr. C.D. Ca. Dec. 23, 2014) (not for publication) ("This court lacks the authority to disallow the Debtor's claimed homestead exemption based on section 105(a), whether indirectly by denying leave to amend or directly by disallowing the exemption because doing so would be clearly irreconcilable with Law."); In re Lua, 529 B.R. 766, 774 (Bankr. C.D. Ca. 2015) ("Law v. Siegel makes clear that this court lacks the authority to deny the Debtor leave to

amend her exemptions based on section 105(a).") The court in Lua acknowledged that state law may provide a basis to disallow an exemption.

Eleventh Circuit

Like the other circuits, the Eleventh Circuit recognized the bankruptcy courts had the power to deny exemptions and amendments to exemptions based on the bad faith of the debtor. Doan v. Hudgins (In re Doan), 672 F.2d 831 (11th Cir. 1982). None of the courts in the Eleventh Circuit have delved into an extensive analysis of whether Law v. Siegel limits the ability of a bankruptcy court to exercise its equitable powers.

In In re Rivera-Cintron, 2015 Bankr. LEXIS 2690 (Bankr. M.D. Fla. Aug. 12, 2015) however, the United States Bankruptcy Court for the Middle District of Florida was asked to deny the debtor's claim of exemption in an IRA based on the debtor's omission of the IRA in her schedules. The Court held that because the trustee could not identify any Code provision or state law doctrine to support denial of the debtor's exemption due to bad faith the objection had to be denied. The Court explained that the United States Court of Appeals for the Eleventh Circuit allowed bankruptcy courts to deny a debtor's claim of exemption if an asset is not initially disclosed based on a showing of the debtor's bad faith or prejudice to creditors, but that in Law v. Siegel, the Supreme Court "struck down any notice of a bankruptcy court's "general, equitable power….to deny exemptions based on a debtor's bad-faith conduct,"" holding that "federal law provides no authority for bankruptcy courts to deny an exemption on a ground not specified in the Code." * p. 10 -11.

No circuit court of appeals has ruled on the issue of whether Law v. Siegel prohibits exemptions from being denied or limited based on bad faith. However, the

bankruptcy courts in the First, Third, Fourth, Fifth, Seventh, and Ninth Circuits are going down the same path as the Sixth Circuit in Baker. Unless the Second, Eighth, or Tenth Circuits rule contrary to the rulings in the other Circuits, it is unlikely that there will be a circuit split allowing the Supreme Court to further explain its dicta in Law v. Siegel.

Objecting to Debtors' Exemptions in a Post *Law v. Siegel* World

Michael A. Stevenson, Stevenson & Bullock, PLC
Southfield, Michigan

INTRODUCTION

Until recently, the law in the Sixth Circuit and in most of the circuits in the rest of the country was that debtors in bankruptcy may amend their schedules at any time before the case is closed, except where the debtors acted in bad faith, concealed assets, or the creditors would be prejudiced by the allowance of the amendment. Federal Rule of Bankruptcy Procedure1009 (a) provides:

> [a] voluntary petition, list, schedule, or statement may be amended by the debtor as a matter of course **at any time before the case is closed.**

The U.S. Court of Appeals for the Sixth Circuit held in Lucius v. McLemore, 741 F.2d 125 (6th Cir. 1984) that a debtor **may amend his schedules at any time before the case is closed and courts do not have the discretion to reject the amendments, unless the debtor acted in bad faith or concealed assets.** *Lucius*, supra, at 126-127.

In the *Lucius* case, the debtors, Frederick and Carliss Lucius listed a Dodge van and a Buick automobile in their Schedule "B", but did not claim an exemption in the vehicles in their Schedule "C". The debtors' listed in their schedules that a bank had a security interest in the Buick. Upon further investigation, the trustee determined that obligation to the bank on the Buick automobile had been satisfied.

When the debtors failed to surrender the vehicles upon the trustee's request, the trustee filed a complaint objecting to the debtors' discharge and demanding turnover of the vehicles. Thereafter, the debtors filed a petition with the bankruptcy court requesting authority to amend their Schedule "C" to add the vehicles. The trustee objected to the petition to allow them to amend the schedule because the debtors had failed to turn the vehicles over upon his request, and had, in fact, removed the vehicles to another jurisdiction. The bankruptcy judge, standing as a master, filed a report and recommendation that the district court deny the request to amend the schedule. Over the debtors'

objection to the report, the district court denied their request to amend their schedules to add the vehicles. The debtors appealed.

The Sixth Circuit Court of Appeals reversed the decision of the district court. The Court of Appeals held that "*Rule 110* has been adopted without substantive change as *Rule 1009* of the (*new*) *Federal Rules of Bankruptcy Procedure*, effective August 1, 1983…and that the rules codify a permissive approach to the allowance of amendments. The court went on to explain:

> *This Rule continues the permissive approach adopted by former Bankruptcy Rule 110 to amendments of voluntary petitions* and accompanying papers. Notice of any amendment is required to be given to the trustee. This is particularly *important with respect to any amendment of the schedule of property affecting the debtor's claim of exemptions…*
>
> This "permissive approach", allowing amendment at any time before the case is closed and denying courts discretion to reject amendments, has been endorsed in several circuits (Citations Omitted)…
>
> Courts may still refuse to allow an amendment where the debtor has acted in bad faith or where property has been concealed. *Lucius*, supra at 127

Thus, the rule articulated by the Sixth Circuit Court of Appeals governing lower courts in the circuit that courts do not have the discretion to reject proposed amendments to the schedules by debtors prior to the closing of the case, unless the debtor acted in bad faith or concealed assets, remained the law of this jurisdiction and many others in the country until the U.S. Supreme Court decided the case of Law v. Siegel, supra.

In the *Law* case, the Chapter 7 debtor, Law, tried to avoid having his home liquidated by the Chapter 7 trustee appointed in the case by listing the value of his home to be less than the sum of the mortgages on the property plus his $75,000.00 homestead exemption. After extensive investigation, the trustee was able to determine, and the bankruptcy court later held, that the alleged obligations the debtor owed to Lili Lin of China, which allegedly was secured by mortgages against the debtor's residence was, in fact, fraudulent and interposed by the debtor to avoid the sale of his home.

As a result of having incurred fees and costs in excess of $500,000.00 in investigating and uncovering the debtor's fraudulent scheme, the trustee, who had not objected to the debtor's homestead exemption within the time allowed for objections, sought to surcharge the debtor's $75,000.00 exemption to defray the costs and fees he incurred as a result of the debtor's fraud. The bankruptcy court granted the trustee's motion to surcharge the exemption, the Ninth Circuit Bankruptcy Appellate Panel affirmed the decision of the bankruptcy court, and the Ninth Circuit Court of Appeals affirmed the decision of the Bankruptcy Appellate Panel. Mr. Law appealed to the U.S. Supreme Court.

The Supreme Court in the *Law* case reversed the Ninth Circuit Court of Appeals affirmation of the decisions of the Bankruptcy Appellate Panel and the Bankruptcy Court, holding that the bankruptcy court exceeded its authority when it allowed the trustee to surcharge the debtor's homestead exemption. The Supreme Court explained:

> We have held that a trustee's failure to make a timely objection prevents him from challenging an exemption. *Taylor v. Freeland & Kronz, 503 U.S. 638, 643-44, 112 S. Ct. 1644*, 118 L. Ed. 2d 280 (1992)…But even assuming the Bankruptcy Court could have revisited Law's entitlement to the exemption *§ 522* does not give courts discretion to grant or withhold exemptions based on whatever considerations they deem appropriate. Rather the statute exhaustively specifies the criteria that will render the property exempt. *See 522 (b), (d)*. Siegel insists that § 522 (b) says that the debtor "may exempt" certain property, rather than he "shall be entitled" to do so, the court retains discretion to grant or deny exemptions even when the statutory criteria are met. But the subject of "may exempt" in *§522 (b)* is the debtor, not the court, so it is the debtor in whom the statute vests discretion. **A debtor need not invoke an exemption to which the statute entitles him; but if he does, the court may not refuse to honor the exemption absent a valid statutory basis for doing so**. *Law v. Siegel,* supra at 1196 (Emphasis Added)

The Supreme Court's holding in the *Law* case directly overrules the Sixth Circuit Court's holding in *Lucius* to the extent that the *Lucius* holding authorizes lower courts to deny exemptions based on bad faith or for any other reason not based on a statute. The holding in *Law* leaves in place the portion of the Sixth Circuit Court's holding that debtors may amend their schedules, including

their exemption schedules, until their cases are closed. What follows is a brief survey of the cases since the *Law* decision and how they have approached objections to exemptions and objections to requests to amend exemptions based on equitable considerations, such as bad faith, equitable estoppel, judicial estoppel, and res judicata.

1. In re Gutierrez

On June 12, 2014, in the case of In re Gutierrez, 2014 Bankr. LEXIS 2637 (2014), the U.S. Bankruptcy Court for the Eastern District of California denied the Chapter 7 trustee's objection to the debtors' claim of exemption in their homestead based on the debtor's alleged bad faith, citing the *Law* case. In *Guitierrez*, the debtors failed to timely claim their full exemption in their homestead even after the trustee in the case suggested at the first meeting of creditors that they do so until months later when the trustee hired a realtor, obtained a purchaser at a price that would result in equity to the estate over and above the liens encumbering the property and the exemption the debtors originally claimed and the trustee was ready to proceed to close the sale.

The debtors further attempted to thwart the sale by filing a motion to convert to Chapter 13, the plan for which proposed no dividend to unsecured creditors and which was denied because the unsecured creditors already stood to receive a dividend from the funds the trustee was already holding from the tax refund he had liquidated and the funds he would receive from the non-exempt equity when he sold the real estate. The debtors also recorded a notice of lis pendens against the property to prevent the sale, denied access to the property for the prospective purchasers to inspect the property, and finally filed an amended claim of exemptions to claim a full exemption in the real estate and a motion to compel the trustee to abandon the real estate.

Initially, the *Gutierrez* court granted the trustee's motion to sell, disallowed the debtors' amended exemption based on bad faith, denied the debtor's motion to compel abandonment, and

granted the trustee's motion for turnover of the real estate. The debtors appealed to the Bankruptcy Appellate Panel ("BAP"). However, in the interim, before the BAP made a decision, the *Law case* was decided. Then, after the *Law* case was decided, the *Gutierrez* court determined that the bankruptcy courts do not have the authority to deny debtors' claims of exemption for bad faith and other equitable considerations under federal bankruptcy law. However, the *Gutierrez* court observed that the Supreme Court in *Law* also held that when the debtor claims state law exemptions, state law controls whether an exemption may be denied based on bad faith or other equitable considerations. According to the *Gutierrez* court:

> Nevertheless, the Court in *Law* left open the possibility that state law may offer some independent basis to disallow an otherwise appropriate exemption that was created under state law. *See id. at 1196-97 (* "It is of course true that when a debtor claims a *state-created* exemption, the exemption's scope is determined by state law, which may provide that certain types of debtor misconduct warrant denial of the exemption." (emphasis in original)).

The *Gutierrez* court then invited the parties to brief the issue of whether California law offered any grounds for denying the debtors' claims of exemptions. The court then reviewed California law as it related to the doctrines of waiver, laches, judicial estoppel, equitable estoppel, and res judicata. The court concluded that under the facts of that case, there was nothing in California law that would provide a basis to deny the debtors' amended claims of exemptions based on bad faith, waiver, judicial estoppel, equitable estoppel, or res judicata. Although the *Gutierrez* court determined that after *Law* there is no basis in federal law to deny exemptions based on equitable considerations, the court did suggest that a trustee might use 11 U.S.C. § 105 (a) and 11 U.S.C. § 704 together with Fed. R. Bankr. P. 1001, 1009 (a), and 9006 (c), to fix a bar date and limit the number and the time for filing amended exemptions:

> When asked to fix a preemptive bar date for the amendment of exemptions, the Court may also consider Rule 9006 (c), which provides, in pertinent part, that "when an act is required or *allowed to be done at or within a specified time by these*

> *Rules*..., the court for cause shown may in its discretion...order the period reduced." *Fed R. Bankr. P. 9006 (c) (1)* (emphasis added); *see also Fed. R. Bankr. P. 9006 (c) (2)* (omitting Rule 1009 (a) from the list of Bankruptcy Rules where court is prohibited from reducing the time for action). Had the trustee in this case made a timely request to fix a bar date for the amendment of exemptions, ie., before he employed the real estate broker, the court would have had an entirely different set of legal principles upon which to make a ruling.

The *Gutierrez* court's suggestion that it might have the authority to set a bar date for amendments to claims of exemptions seems to fly in the face of the express holding of *Law*.

2. In re Arellano

In the case of In re Arellano, 517 B.R. 228; 2014 Bankr. LEXIS 4304, also a California bankruptcy court case in which the debtor claimed state law exemptions, and which was decided September 26, 2014, the debtor, Isaias Arellano's application for a waiver of the filing fee was granted based on the initial schedules he filed. However, upon questioning at the creditors meeting, the trustee discovered that the debtor had failed to disclose a bank account with approximately $5,000.00 in it and an anticipated tax refund of approximately $2,000.00. As a result, the debtor amended his schedules to disclose and exempt the bank account and the income tax refund. The trustee objected to the amended claim of exemption based on bad faith, but the court overruled the objection based on the holding in *Law v. Siegel*, supra. The trustee in that case declined to brief the issue of whether there were grounds under California law to deny the exemptions based on bad faith or other equitable considerations. (*see also* In re Dunaway, 2015 Bankr. LEXIS 819 (Bankr. N.D. W.Va. March 16, 2015); In re Bogan, 534 B.R. 346; 2015 Bankr. LEXIS 1164 (2015); In re Lua, 529 B.R. 766; 2015 Bankr. LEXIS 1505; 73 Collier Bankr. Cas. 2d (MB) 1097 (2015).

3. U.S. v. Ledee

In the case of U.S. v. Ledee, 772 F. 3d 21; 2014 U.S. App. LEXIS 21106; 95 Fed. R. Evid. Serv. (Callahan) 1145, the 1st Circuit Court of Appeals held that while the *Law* case prevents the

bankruptcy courts from denying exemptions based on the debtor's bad faith, it does not prevent the U.S. attorney from prosecuting the debtor and the debtor's sister who acted as his bankruptcy attorney, for concealing assets, lying under oath, and actual fraud, even though the debtor amended his schedules to cure the deficiencies and settled the adversary proceeding brought by the Chapter 7 trustee to recover fraudulently transferred assets that belonged to the bankruptcy estate, by agreeing that the trustee could sell one of the recovered assets and use the proceeds to pay the creditors and administrative expenses, and if those proceeds were not enough to pay the creditors in full, the debtor would do so with private funds that were not property of the estate.

Notwithstanding the fact that the trustee used the funds to pay the creditors and the administrative expenses of the estate and the debtor used private funds that were not property of the estate to make sure the creditors were paid in full, the 1st Circuit Court of Appeals determined that on the facts present in that case, neither governmental waiver, equitable estoppel, nor judicial estoppel prevented the U.S. Attorney from prosecuting the debtor for bankruptcy crimes. See *Ledee* at 29, footnote 10 where the court holds:

> Although *Law* appears to overrule *Malley* and *Hannigan* to the extent they limited exemptions based on bad-faith conduct, the Supreme Court's ruling does not restrict the bankruptcy court's discretion concerning amendments unrelated to exemptions—as was the situation here.

The *Ledee* decision is directly in keeping with the Supreme Court's admonition in *Law* that bankruptcy courts have options other than denying exemptions to compel debtors to comply with the bankruptcy laws and to punish them for misconduct, such as, denying the debtor's discharge, ordering the debtor to pay sanctions in the form of costs and attorney's fees, or in egregious cases referring such debtors to the U.S. Attorney for prosecution for bankruptcy crimes.

4. **In re Woolner**

In the case of In re Woolner, 2014 Bankr. LEXIS 5048, U.S. Bankruptcy Court, Eastern District of Michigan, Southern Division, decided December 15, 2014, Judge Shapero took a different approach. He denied the debtors' motion for reconsideration of his decision to sustain the Chapter 7 trustee's timely objection to the debtor's amended claim of exemption with which the debtors sought to exempt a vehicle and federal and state tax refunds based on the trustee's assertion that the debtors intentionally undervalued the assets in bad faith. Judge Shapero reasoned that:

> [T]he Court concluding that *Law v. Siegel* is not dispositive of the present situation or fully supportive of the Debtors' arguments because, in that case, the validity of the debtor's claim of exemption was not directly contested or challenged, rather, the issue was whether the bankruptcy court had authority to "surcharge" an already allowed exemption because of the debtor's bad acts. Id. at 1196; this Court concluding that, notwithstanding *Law v. Siegel*, it has authority to disallow an amendment to a claim of exemption due to bad faith. *In re Rice,* 478 B.R. 275, 279 (E.D. Mich. 2012 (citing *Lucius v. McLemore*, 741 F.2d 125, 127 (6th Cir. 1984); Fed. R. Bankr. P. 1009 (a); Fed. R. Bankr. P. 4003.

Moreover, the *Woolner* court based its analysis on the language in Fed. R. Bankr. P. 4003 (b) (2) which provides in relevant part:

> The trustee may file an objection to a claim of exemption at any time prior to one year after the closing of the case if the debtor **fraudulently asserted** the claim of exemption. The trustee shall deliver or mail the objection to the debtor and the debtor's attorney, and to any person filing the list of exempt property and that person's attorney. (Emphasis added) Fed R. Bankr. P. 4003 (b) (2)

The *Woolner* court concluded that the trustee's objection that **the debtor intentionally undervalued the assets in bad faith** is synonymous with the language in the court rule **fraudulently asserted**. (Query: whether the Supreme Court or the 6th Circuit Court of Appeals would interpret the language of the court rule the same way, or might those courts in light of the *Law* decision view the court rule as temporal in nature and conclude that the trustee has up to a year after the case is closed to file an objection to an exemption only if there was a statutory basis separate and apart from the

fraudulent assertion? For example, if the debtor claimed an exemption in an asset in an unlimited amount, which the debtor knew he could exempt only in a limited amount, the trustee would have up to a year to object to the amount of the exemption the debtor claimed in excess of the allowed exemption because the trustee has a statutory basis to do so. However, with respect to the statutory amount the debtor would have been entitled to in the first place, the trustee would have no basis to object to that amount. In other words, the Supreme Court's decision in *Law* suggests that fraud, by itself, is not a basis to deny an exemption. Though unstated in the *Law* opinion, the Court's rationale may be that the exemptions are carefully calibrated to allow the debtor to retain the minimum amount of income and assets the debtor needs to subsist without becoming a ward of the state. Therefore, no amount of misconduct on the part of the debtor justifies forcing the debtor into such a condition. To do so would frustrate the stated purposes of the bankruptcy process.

5. Westry v. Lim (In re Westry)

In the case of Westry v. Lim (In re Westry), 591 Fed. Appx. 429; 2014 U.S. App. LEXIS 24666; 2014 Fed. App. 0951N (6th Cir. 2014), the debtor appealed the bankruptcy court's order sustaining the Chapter 7 trustee's objection to the debtor's amended claim of exemption in her worker's compensation claim. The debtor initially listed the value of the claim as "unknown" and claimed an exemption pursuant to 11 U.S.C. § 522 (d) (5) in the amount of $10,000.00, but when the claim became liquidated nearly two years later, the debtor sought to amend her exemptions and claim the full value of the claim as exempt, increasing the value of the exemption claimed pursuant to § (d) (5) and adding claims of exemption pursuant to §§ (d) (10) (C) and (d) (11) (E). The trustee objected to the amendment, alleging that there would be prejudice to the trustee and the creditors because of the late date of the amendment. The bankruptcy court found in favor of the trustee and on appeal the

district court affirmed the bankruptcy court, finding no clear error. The debtor then appealed to the 6th Circuit Court of Appeals.

The 6th Circuit reversed and remanded for further proceedings holding that there was no evidence that the debtor's delay in amending her exemptions was an unreasonable delay (the parties were waiting to determine if the debtor's employer's worker's compensation carrier was going to offer money to settle the litigation) and delay by itself does not equal prejudice. Moreover, the circuit found that there was no evidence that the trustee was prejudiced because all she did was monitor the status of the litigation every 90 days, nor was there any prejudice to the creditors because all parties agreed that the exemptions were within the exemption limits and there were no other assets to administer for the benefit of creditors.

6. Mateer v. Ostrander (In re Mateer)

In the case of Mateer v. Ostrander (In re Mateer), 523 B.R. 559; 2015 Bankr. LEXIS 473 (2015), which was decided February 13, 2015, the debtor failed to disclose that the value of the real estate he listed in his Schedule "A" was approximately $100,000.00 less than he disclosed because of damage that occurred to the home as a result of a storm. In addition to the debtor's failure to disclose any information about the damage to the property, the debtor failed to disclose that he had claims for insurance proceeds for the damage to the home in the approximate amount of $126,000.00.

After the debtor converted his case to Chapter 7 and the Chapter 7 trustee discovered the deposit of the insurance proceeds from his review of the debtor's bank statements, the debtor sought to amend his schedules to claim the homestead exemption in the amount of $125,000.00 pursuant to Massachusetts state law. The debtor also claimed that he did, in fact, disclose the true value of his interest in the real estate and the insurance proceeds because the value he disclosed in his Schedule

"A" was a combination of the value of the home after the damage from the storm plus the amount of the insurance proceeds.

After trial, the court concluded that debtor intentionally failed to disclose the true value of the real estate after the storm damage on Schedule "A", he intentionally failed to disclose the insurance proceeds on his Schedule "B", and that there was no way for the trustee to know of the existence of the insurance proceeds from reviewing the schedules. Notwithstanding those conclusions, the court determined that the debtor was entitled to amend his exemptions and claim the full homestead exemption in light of the holding in the *Law* case.

7. In re Davis

In the case of In re Davis, 2015 Bankr. LEXIS 818, the U.S. Bankruptcy Court for the Northern District of West Virginia, which was decided on March 16, 2015, the debtor disclosed various types of real and personal property assets. After applying the debtor's claim of exemptions and his calculation that there was non-exempt equity in some of the assets, the trustee filed a notice of assets and the clerk notified the creditors to file claims. Thereafter, the debtor amended her exemptions. The trustee then objected to the debtor's amended claim of exemptions. The parties resolved the objection by entering into a stipulated order which re-characterized some of the assets as a part of the debtor's divorce settlement. After the order was entered, the trustee attempted to settle some of the property issues in the family court by filing a motion to settle to which the debtor objected and again sought to amend her exemptions. The trustee objected based on equitable estoppel, laches, and res judicata. The trustee also argued that Fed R. Bankr. P. 1001 required the court to disallow the debtor's amended exemption because even though Rule 1009 (a) permits amendment of claims of exemption until the case is closed, it must be construed in light of Rule 1001, which requires the just speedy, and inexpensive determination of every case. The court rejected the trustee's argument

regarding the court rules and also concluded that *Law* decision made clear that the court had no authority to prevent the debtor from to amending her exemptions based on equitable estoppel or laches.

8. In re Scotchel

In the case of In re Scotchel, 2014 Bankr. LEXIS 3640; 2014 WL 4327947, at *2 (citing In re Romano, 378 B.R. 454, 464 (Bankr. E.D. Pa. 2007)), the trustee objected to the debtors' amended claim of exemption based on the doctrine of res judicata. The debtors initially valued their interest in a contingency fee that Mr. Scotchel, an attorney, was entitled to at $1.00 because the lawsuit was unliquidated and they did not know what is was worth. After the lawsuit was liquidated and it was determined that Mr. Scotchel's interest in the contingency fee was worth $690,000.00, the debtor's sought to amend their exemptions to claim approximately $18,000.00 of the $690,000 contingency fee as exempt. The trustee who had received the funds from the lawsuit, obtained an order for partial distribution of an amount in excess of $300,000.00, and, in fact, distributed those funds, opposed the motion. The trustee cited cases from various jurisdictions that hold that once a court has made a ruling with respect to a debtor's claim of exemption pursuant to a particular statute section the debtor is barred from subsequently asserting a claim of exemption pursuant to a different statute section even though the case remains open based on the doctrine of res judicata. The trustee cites *Scotchel* for the proposition that the doctrine of res judicata applies to disputes over exemptions and that a debtor may not amend his schedules after an exemption has been denied by the court with respect to certain property to claim a different exemption in the same property. The doctrine of res judicata requires (1) a final decision on the merits by a court of competent jurisdiction; (2) a subsequent action between the same parties or their privies; (3) an issue in the subsequent action which was litigated or which should have been litigated in the prior action; and (4) an identity of the cause of action. *In re*

Romano, supra. In addition to those four requirements the cases acknowledge a fifth requirement that the final decision on the merits not be on appeal. The *Scotchel* case, quoting the *Romano* case held "Whenever…there has been a final, non-appealed ruling sustaining the trustee's objection, all of the elements of claim preclusion have been established, and so the debtor cannot later amend her exemptions to re-litigate that issue [.]" The *Scotchel* court overruled the trustee's objection, and the trustee appealed that decision to the U.S. District Court for the Northern District of West Virginia. The district court affirmed the bankruptcy court's decision on September 3, 2015 in Sheehan v. Scotchel, 2015, 2015 U.S. Dist. LEXIS 117293.

More importantly, the ruling in the *Scotchel* case has been overruled by the Supreme Court in *Law*. Therefore, unless there is a statutory basis for denying a debtor's claim of exemption, such as, the value of the specific property exceeding the value of the allowable exemption for that property, or the debtor claiming the residence exemption for property he does not use as a residence, or claiming a retirement plan exemption for a retirement plan that is not subject to E.R.I.S.A. or entitled to special tax treatment under the Internal Revenue Code, to name a few, the debtor is entitled to the exemption. See Ladd v. Ries, 450 F. 3d 751,754 (8th Cir. 2006) In the *Ladd* case, the court refused to apply res judicata when the debtor there changed his exemptions from federal exemptions to state exemptions and reasoned that the evidence required to determine the federal exemption was different from the evidence required to determine the state exemption. Moreover, there is no limitation in 11 U.S. C. § 522 that a debtor may not amend his exemption to claim a different exemption in the same property after a different claim of exemption in the same property has already been denied, and for lower courts to impute one where one clearly does not exist exceeds their authority and flies directly in the face of the holding in *Law:*

> The Code's meticulous—not to say mind-numbingly detailed—enumeration of exemptions and exceptions to those exemptions confirms that courts are not authorized to create additional exceptions. *Law*, supra at 1196 (Citations Omitted)

9. Ellman v. Baker

In the case of Ellman v. Baker, Slip Op. 14-2149; 2015 U.S. App. LEXIS 11437; 2015 WL 4033098, the debtors failed to list a cause of action against their mortgage company and its counsel for damages they suffered as a result of a defective foreclosure and subsequent eviction in their bankruptcy schedules. After the bankruptcy case was closed the debtor's filed a lawsuit claiming damages against the mortgage company and its counsel without reopening its bankruptcy case and disclosing the cause of action in its schedules or notifying the Chapter 7 trustee of the claim. When the trustee discovered the cause of action, he moved to reopen the bankruptcy case, was reappointed trustee, and took control of the litigation. Thereafter, the debtors sought to amend their schedules to disclose the claims against the mortgage company and its counsel and to exempt a portion of the claims. The trustee objected to the debtors' claim of exemption based on bad faith and prejudice to the creditors. The bankruptcy court overruled the trustee's objection to the debtors' claim of exemption based on the Supreme Court's holding in the *Law* case, and the district court affirmed the bankruptcy court's decision. The trustee appealed to the 6th Circuit and the 6th Circuit affirmed the bankruptcy court and the district court. The circuit court specifically held that bankruptcy courts do not have the authority to deny exemptions or amendments to exemptions because of bad faith or other equitable considerations:

> Applying these principles here, it is clear that *Siegel* prohibits the bankruptcy court from disallowing the debtors' claimed exemptions because of their alleged bad faith and fraudulent conduct. While *Lucius* previously held that bankruptcy courts may use their equitable powers to sanction a debtor's misconduct by disallowing exemptions in property concealed from the trustee, the Supreme Court's superseding decision unambiguously abrogates their ability to do so. Some courts have characterized these principles in *Siegel* as mere dictum, see,

Eg., *In re Woolner*, No 13-57269, 2014 WL 7184042, at *3-4 (Bankr. E.D. Mich. Dec. 15, 2014), but this court has explained that "[l]ower courts are obligated to follow Supreme Court dicta, particularly where there is not substantial reason for disregarding it, such as age or subsequent statements undermining its rationale." *Am. Civil Liberties Union of Ky. v. McCreary Cnty.*, 607 F. 3d 439, 447-48 (6th Cir. 2010) (citations and internal quotation marks omitted).

CONCLUSION

As the holdings of the cases since the *Law* decision make clear, bankruptcy courts and appellate courts reviewing bankruptcy court decisions no longer have the authority to deny debtors' claims of exemptions or requests to amend exemptions based on equitable considerations such as bad faith, equitable estoppel, judicial estoppel, and res judicata. The courts must have an express statutory basis to do so. Judge Shapero's valiant attempt to distinguish the *Law* decision on its facts and because the Supreme Court's discussion of equitable considerations as it related to denial of exemptions was not necessary to its decision in the *Law* case was dealt with squarely by the 6th Circuit in the *Ellman v. Baker* case and specifically rejected. Therefore, unless the Congress of the United States sees fit to revisit the issues of bad faith, fraudulent concealment, prejudice to creditors, and other equitable considerations as it relates to exemption of assets in bankruptcy cases and to grant more authority to bankruptcy courts to use denial of exemptions to remedy debtor misconduct (and Congress has seemed to have more of an appetite to curtail the authority of bankruptcy courts since the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, which amended the Bankruptcy Code) attorneys and judges will have no choice but to adapt to the *Law* decision and all it entails for the foreseeable future. Whether that results in courts exercising increasingly harsher remedies for litigants failing to do things right the first time, more denials of discharge and referrals to the U.S. Attorney for criminal prosecution remains to be seen.

What Remedies Are Still Available after *Law v. Siegel*, to Address Debtor Non-Disclosure or Delayed Disclosure of Assets, Other than Denial of or Surcharge Against Exemptions?

Judge Thomas J. Tucker,
United States Bankruptcy Court for the Eastern District of Michigan,
Detroit, Michigan
with substantial assistance from Ryan F. Hampstead, Law Clerk

I. Introduction:

In *Law v. Siegel*, 134 S. Ct. 1188 (2014), the Supreme Court held that the bankruptcy court "exceeded the limits of its authority" under 11 U.S.C § 105(a) and the bankruptcy court's inherent powers, and "violated" 11 U.S.C. § 522, when the court surcharged a debtor's homestead exemption to offset the Chapter 7 Trustee's attorney fees. The Chapter 7 Trustee had incurred such fees in a protracted legal battle concerning a fraudulent lien the debtor claimed existed on the homestead property. *Id.* at 1195-96. The Supreme Court found that the Bankruptcy Code does not provide bankruptcy courts with a "general, equitable power in bankruptcy to deny exemptions based on a debtor's bad-faith conduct." *Id.* at 1196.

In *Ellmann v. Baker* (*In re Baker*), 791 F.3d 677 (6th Cir. 2015), in accordance with *Siegel*, the Sixth Circuit overruled its longstanding precedent in *Lucius v. McLemore*, 741 F.2d 125 (6th Cir. 1984), and further held that the rule in *Siegel* applies equally to cases that have been reopened after being closed. *Baker*, 791 F.3d at 683.

Despite the holdings in *Siegel* and *Baker*:

> Every debtor in bankruptcy has an absolute obligation to schedule every asset on their bankruptcy schedules. 11 U.S.C. § 521(1). The duty to disclose is a continuing one that does not end once the forms are submitted to the bankruptcy court. Full and honest disclosure in a bankruptcy case is crucial to the effective functioning of the federal bankruptcy system. Full disclosure is the cornerstone and capstone of any bankruptcy case and is necessary for the successful administration of a bankruptcy estate.

In re Opra, 365 B.R. 728, 743 (Bankr. E.D. Mich. 2007) (quoting *Tennyson v. Challenge Realty* (*In re Tennyson*), 313 B.R. 402, 406 (Bankr. W.D. Ky. 2004)).

Thus, the question becomes, what *can* a bankruptcy court do in the wake of *Law v. Siegel* when a debtor fails to fulfill his or her obligation of full disclosure, particularly when a debtor attempts to conceal assets? This paper explores various options available to trustees, creditors,

and the court. As the cases indicate, many of these tools can be combined to fit the circumstances of the case, such as a dismissal for cause combined with a bar on future filings, under 11 U.S.C. §§ 707(a), 105(a), 109(g), and 349(a), so that creditors can pursue state court remedies.

Many of these tools are likely unaffected by the holding in *Siegel*, particularly in light of the Supreme Court's admonition that:

> Our decision today does not denude bankruptcy courts of the essential "authority to respond to debtor misconduct with meaningful sanctions." There is ample authority to deny the dishonest debtor a discharge. *See* § 727(a)(2)-(6). . . . In addition, Federal Rule of Bankruptcy Procedure 9011 . . . authorizes the court to impose sanctions for bad-faith litigation conduct, which may include "an order directing payment . . . of some or all of the reasonable attorneys' fees and other expenses incurred as a direct result of the violation." Fed. Rule Bkrtcy. Proc. 9011(c)(2). The court may also possess further sanctioning authority under either § 105(a) or its inherent powers. *Cf. Chambers v. NASCO, Inc.*, 501 U.S. 32, 45-49 (1991). And because it arises postpetition, a bankruptcy court's monetary sanction survives the bankruptcy case and is thereafter enforceable through the normal procedures for collecting money judgments. *See* § 727(b). Fraudulent conduct in a bankruptcy case may also subject a debtor to criminal prosecution under 18 U.S.C. § 152, which carries a maximum penalty of five years' imprisonment.

Siegel, 134 S. Ct. at 1198.

II. List of Possible Remaining Remedies (discussed in more detail below):

1. Denial of a debtor's discharge in a Chapter 7 case, under § 727(a)(2) or § 727(a)(4)(A);

    a. or revocation of a debtor's discharge in a Chapter 7 case, under § 727(d)(1) or (d)(2) (subject to timing requirements in § 727(e));

2. Dismissal of a Chapter 7 case "for cause," due to bad faith and/or "unreasonable delay by the debtor that is prejudicial to creditors," under § 707(a), or based on a finding of "abuse," due to the debtor's "bad faith" in filing the petition under § 707(b)(3)(A) or based on the "totality of the circumstances" under § 707(b)(3)(B);

   a. Dismissal of a Chapter 13 case or conversion to Chapter 7, "for cause," due to bad faith and/or "unreasonable delay by the debtor that is prejudicial to creditors," under § 1307(c)(1);

3. Monetary sanctions against the debtor, based on Federal Rule of Bankruptcy Procedure 9011(b) & (c), 11 U.S.C. § 105(a), and the court's inherent powers;

   a. Note that monetary sanctions against the debtor, in the form of a criminal fine, are also possible under 18 U.S.C. § 152, discussed below.

4. Monetary sanctions against the debtor's attorney, based on a number of provisions, including §§ 105(a), 526(a)(2), (c)(2) & (c)(5), 707(b)(4), Federal Rule of Bankruptcy Procedure 9011(b)(3) and (c), and the Court's inherent powers;

5. Barring a debtor from refiling, either for a specified period of time or permanently, under §§ 349(a), 109(g) and 105(a);

6. Objecting to a fraudulently asserted claim of exemption, under Federal Rule of Bankruptcy Procedure 4003(b)(2);

7. Objecting to a motion to reopen a closed case to amend schedules, under Federal Rules of Bankruptcy Procedure 1009(a), 4003(b), and 11 U.S.C. § 350(b);

8. Avoiding an interest in the debtor's property, when such interest is superior to a debtor's claimed exemption under applicable state law, under 11 U.S.C. §§ 544(a)(3) and 551;

9. Imprisonment or criminal fine, under 18 U.S.C. § 152.

III. Discussion of Relevant Code Provisions and Cases Applying Them:

1. Denial or Revocation of a Debtor's Discharge - 11 U.S.C. § 727

Section 727 of the Bankruptcy Code covers denial and revocation of a discharge in Chapter 7. The provisions potentially useful for dealing with a debtor who conceals assets include:

> (a) The court shall grant the debtor a discharge, **unless**—
> . . . .
>
> (2) **the debtor, with intent to hinder, delay, or defraud a creditor or an officer of the estate charged with custody of property under this title, has** transferred, removed, destroyed, mutilated, or **concealed, or has permitted to be** transferred, removed, destroyed, mutilated, or **concealed**—

> (A) property of the debtor, within one year before the date of the filing of the petition; or
>
> (B) property of the estate, after the date of the filing of the petition;
>
> . . . .
>
> (4) the debtor knowingly and fraudulently, in or in connection with the case—
>
> (A) **made a false oath or account**.
>
> . . . .
>
> (d) On request of the trustee, a creditor, or the United States trustee, and after notice and a hearing, **the court shall revoke a discharge** granted under subsection (a) of this section if—
>
> (1) **such discharge was obtained through the fraud of the debtor**, and the requesting party did not know of such fraud until after the granting of the discharge.
>
> (2) **The debtor acquired property that is property of the estate**, or became entitled to acquire property that would be property of the estate, and knowingly **and fraudulently failed to report the acquisition of or entitlement to such property**, or to deliver or surrender such property to the trustee;

(emphasis added).

***

Citing § 727(a)(2)-(6), the Court in *Siegel* noted that "[t]here is ample authority to deny the dishonest debtor a discharge." *Law v. Siegel*, 134 S. Ct. 1188, 1198 (2014).[1] One of the

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[1] *But cf. Exemption Strategies after Law v. Siegel*, American Bankruptcy Institute 2015 Northeast Consumer Forum panel presentation written materials at 840-41, (*available at*: https://abi-org-corp.s3.amazonaws.com/materials/ExemptionStrategiesLawvSiegel.pdf, last accessed 8/21/2015) ("While [denial of a discharge] may act as some deterrent to unscrupulous debtors, it in no way provides incentive for the trustee to pursue the potentially lengthy and expensive adversary proceeding against the debtor to deny the discharge. Despite very good grounds for denial of the discharge, many cases likely will never be brought due to this practical obstacle.").

leading cases on this in the Sixth Circuit is *Keeney v. Smith* (*In re Keeney*), 227 F.3d 679 (6th Cir. 2000). In that case, the court affirmed the bankruptcy court's decision to deny a debtor's discharge based on § 727(a)(2)(A) (concealed property within one year before date of filing) and § 727(a)(4) (false oath). *Keeney*, 227 F.3d at 682. Before filing bankruptcy, the debtor had purchased two different properties and put title to each in his parents' names. He made all mortgage payments and paid for improvements on both properties, and lived on each of the properties at various times. *Id.*

Regarding § 727(a)(2)(A), the court wrote that, "[t]his section encompasses two elements: 1) a disposition of property, such as concealment, and 2) 'a subjective intent on the debtor's part to hinder, delay or defraud a creditor through the act disposing of the property.'" *Id.* at 683 (quoting *Hughes v. Lawson* (*In re Lawson*), 122 F.3d 1237, 1240 (9th Cir. 1997)). "Courts have interpreted concealment under § 727(a)(2)(B) to mean 'withholding knowledge of an asset or refusal to divulge owed information.'" *Helbling v. Holmes* (*In re Holmes*), No. 08-1159, 2008 WL 6192253, at *4 (Bankr. N.D. Ohio Dec. 3, 2008) (quoting *Hunter v. Sowers* (*In re Sowers*), 229 B.R. 151, 156 (Bankr. N.D. Ohio 1998)).

In *Keeney*, the court found that the debtor had a beneficial interest in the properties, "from Keeney's payment for and use of the properties, including his rent-free residence on each and payment of all mortgage obligations," as well as the fact that "no explanation was provided as to why the properties were titled in the parents' names." *Keeney*, 227 F.3d at 683-84. To fit the debtor's conduct under subpart (A) of § 727(a)(2), the court adopted and applied the "continuing concealment" doctrine, which provides that "'a transfer made and recorded more than one year prior to filing may serve as evidence of the requisite act of concealment where the debtor retains a secret benefit of ownership in the transferred property within the year prior to

filing.'" *Id.* at 684 (quoting *Hughes*, 122 F.3d at 1240); *see also Helbling*, 2008 WL 6192253, at *4 ("Courts have found that a solitary omission is sufficient.").

The court also affirmed the bankruptcy court's denial of the debtor's discharge under § 727(a)(4)(A) (false oath), and set forth the elements for a "false oath" denial of discharge:

> In order to deny a debtor discharge under this section, a plaintiff must prove by a preponderance of the evidence that: **1) the debtor made a statement under oath; 2) the statement was false; 3) the debtor knew the statement was false; 4) the debtor made the statement with fraudulent intent; and 5) the statement related materially to the bankruptcy case.** Whether a debtor has made a false oath under section 727(a)(4)(A) is a question of fact.
>
> "'Complete financial disclosure'" is a prerequisite to the privilege of discharge. The Court of Appeals for the Seventh Circuit has explained that intent to defraud "involves a material representation that you know to be false, or, what amounts to the same thing, an omission that you know will create an erroneous impression." A reckless disregard as to whether a representation is true will also satisfy the intent requirement. "'Courts may deduce fraudulent intent from all the facts and circumstances of a case.'" However, a debtor is entitled to discharge if false information is the result of mistake or inadvertence. The subject of a false oath is material if it "'bears a relationship to the bankrupt's business transactions or estate, or concerns the discovery of assets, business dealings, or the existence and disposition of his property.'"

Keeney, 227 F.3d at 685-86 (internal citations omitted) (emphasis added).

In applying the elements of a "false oath" under § 727(a)(4)(A), the court concluded that "there was no error in finding that Keeney held a beneficial interest in the property," and that **"[b]y omitting this interest from this filings he made a false oath**." *Id.* at 686 (emphasis added).

Revoking a debtor's previously granted discharge is covered by § 727(d) (*e.g.*, "the court shall revoke a discharge . . . if— (1) such discharge was obtained through the fraud of the debtor . . ."). In *White v. Nielsen*, (*In re Nielsen*), 383 F.3d 922 (9th Cir. 2004), the court denied a

creditor's request to revoke the debtors' discharge in a no-asset Chapter 7 case. The creditor sought to revoke the discharge under § 727(d)(1) on the ground that the debtors had intentionally left the creditor's name off of the mailing matrix. *Nielsen*, 383 F.3d at 924. In affirming the bankruptcy court's decision to deny the revocation, the court reasoned:

> For Ms. White to prove that the **Nielsen's discharge was "obtained through" the fraud, she must at least show that, but for the fraud, the discharge would not have been granted.** That she cannot do. Assuming for purposes of discussion that Nielsen left [White's] name off the typed mailing list on purpose, so that she would not get notice, he and his wife would have been discharged anyway, so far as the record indicates. True, he owed her $8,000, he did not pay her, she had no opportunity to make a claim before he was discharged, and she did not get a penny. But so far as the record supports, the outcome would have been exactly the same had she received the notice to which she was entitled.
>
> . . . .
>
> Ms. White's brief makes the good point that just because a bankrupt says he has no assets, that does not make it true. The bankrupt may purposely leave a creditor off the list if that creditor would have knowledge of assets, or if, as with Ms. White, that creditor would have a larger incentive than others to look for assets or find some other reasons to thwart discharge. **Had Mr. White, in her proceeding to revoke the discharge, shown that, in truth, there were assets, or that there was some reason that the Nielsens should not have been discharged, this would be quite a different case. But she had just as much incentive to find such information prior to filing her complaint in this action as she would have had during the original proceedings, had she received proper notice.** So far as the record indicates, she has not found any such information.

Id. at 925-26 (emphasis added).

In *Comu v. King Louie Mining, LLC* (*In re Comu*), No. 3:14-cv-04163-B, 2015 WL 4507649 (N.D. Tex. July 24, 2015), a post *Siegel*-case, the district court affirmed the bankruptcy court's decision to revoke a debtor's previously granted discharge under both § 727(d)(1) and § 727(d)(2). In that case, the debtor did not challenge the bankruptcy court's finding "that he

fraudulently failed to disclose property of his bankruptcy estate." *Id.* at *4. Rather, he argued that the plaintiffs, who filed the complaint five months after the debtor was discharged, were aware of the fraudulent conduct before he was granted the discharge and therefore not entitled to relief. *Id.*

The district court noted that § 727(d)(2) does not "explicitly carry an absence of knowledge requirement," unlike § 727(d)(1), such that the question of the plaintiffs' pre-discharge knowledge was possibly irrelevant. But the court found that regardless of whether such a requirement should be read into the statute, the bankruptcy court did not err in finding the plaintiffs were not aware of "the truth of [the debtor's] financial situation, . . . [or] the scope of [the debtor's] fraud" until post-discharge. *Id.* at *5. The district court partially relied on the fact that, "'[t]he right to a discharge in bankruptcy is addressed to the sound discretion of the bankruptcy court, and appellate courts should interfere only for the most cogent, compelling reasons in situations of gross abuse.'" *Id.* at *4 (quoting *United States v. Cluck*, 87 F.3d 138, 140 (5th Cir. 1996)).

The district court also affirmed the bankruptcy court's decision to award the Chapter 7 trustee $5.8 million in damages against the debtor, based on the Bankruptcy Code's turnover provisions, 11 U.S.C. § 542(a). This award was calculated based on the cash proceeds generated from the sale of the concealed assets.

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2. Dismissal of Chapter 7 or Chapter 13 Case - 11 U.S.C. §§ 707, 1307

Section 707 provides for, among other things, dismissal of a Chapter 7 case "for cause," or if the court finds that the "the granting of relief would be an abuse of the provisions of this chapter." 11 U.S.C. § 707(a), (b)(1). Section 1307 provides for dismissal "for cause" in a

Chapter 13 case, or for conversion to a Chapter 7 case, "whichever is in the best interests of creditors and the estate." 11 U.S.C. § 1307(c).

As the cases hold, "cause" in both §§ 707(a) and 1307(c) includes a debtor's bad faith. In addition, it may be possible to fit a debtor's dilatory conduct into § 707(a)(1) or § 1307(c)(1) ("unreasonable delay"), or, where the debtor files one or more false schedules, to look to § 707(b)(3)(A), which directs the court to consider "whether the debtor filed the petition in bad faith."

11 U.S.C. § 707:

> (a) **The court may dismiss a case** under this chapter only after notice and a hearing and only **for cause**, including—
>
> > (1) **Unreasonable delay** by the debtor **that is prejudicial to creditors**;
> >
> > (2) nonpayment of any fees or charges required by chapter 123 of title 28; and
> >
> > (3) failure of the debtor in a voluntary case to file . . . the information required by paragraph (1) of section 521(a), but only on a motion by the United States trustee.
>
> (b)(1) After notice and a hearing, the court, on its own motion or on a motion by the United States trustee, trustee (or bankruptcy administrator, if any), or any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts, or, with the debtor's consent, convert such a case to a case under chapter 11 or 13 of this title, **if it finds that the granting of relief would be an abuse of the provisions of this chapter**. . . .
> . . . .
>
> > (3) In considering under paragraph (1) whether the granting of relief would be an abuse of the provisions of this chapter in a case in which the presumption in paragraph (2)(A)(i) does not arise or is rebutted, the court shall consider—
> >
> > > (A) whether the debtor **filed the petition in bad faith**; or

> (B) **the totality of the circumstances** (including whether the debtor seeks to reject a personal services contract and the financial need for such rejection as sought by the debtor) of the debtor's financial situation demonstrates abuse.

(emphasis added).

11 U.S.C. § 1307:

> (c) Except as provided in subsection (f) of this section, on request of a party in interest or the United States trustee and after notice and a hearing, **the court may convert a case under this chapter to a case under chapter** 7 of this title**, or may dismiss a case** under this chapter, whichever is in the best interests of creditors and the estate, **for cause, including—**
>
> > (1) **unreasonable delay** by the debtor **that is prejudicial to creditors**;
>
> . . . .

(emphasis added).

***

In *Marrama v. Citizens Bank of Mass.*, 549 U.S. 365, 367 n. 1, 372-74 (2007), the Supreme Court cited with approval several cases holding that that "cause" for dismissal under § 1307(c) includes bad faith conduct, and held that pre-petition bad faith conduct by the debtor, "including fraudulent acts committed in an earlier Chapter 7 proceeding," can constitute such "cause" for dismissal. (This was part of the court's reasoning as to why a debtor could be denied the right to convert a Chapter 7 case to Chapter 13 for bad faith.) In *Law v. Siegel*, the Supreme Court noted the above points from *Marrama*, with no indication of disapproval of *Marrama's* holding that bad faith can be "cause" for dismissal under § 1307(c). Rather, the court only distinguished *Marrama's* use of § 105(a) to support that case's holding about conversion. *See Siegel*, 134 S.Ct. at 1197.

A leading case in the Sixth Circuit on dismissal under § 707(a) ("for cause") is *Industrial Insurance Services, Inc. v. Zick* (*In re Zick*), 931 F.2d 1124 (6th Cir. 1991). In that case, a judgment was entered against the debtor for $600,000, for the debtor's breach of a post-employment non-compete agreement. He filed a Chapter 7 case, a few days after entry of the judgment, seeking a discharge principally for the $600,000 judgment; he reaffirmed most of his other debts. *Id.* at 1129. The former employer objected to his discharge and moved to dismiss the Chapter 7 case, alleging that "it was brought in bad faith based upon data in the Chapter 7 filing itself." *Id.* at 1126. The bankruptcy court granted the motion, and the district court and the Sixth Circuit affirmed.

The Sixth Circuit interpreted the word "including" in § 707(a) broadly, and concluded that "lack of good faith is a valid basis of decision in a 'for cause' dismissal by a bankruptcy court," despite the fact that it is not specifically listed as a ground in § 707(a). *Id.* at 1127. The court also noted that while "Chapter 7 of the Bankruptcy Code does not *explicitly* make good faith a requirement for voluntary liquidated petitions," nevertheless "good faith has evolved as a threshold requirement in all bankruptcy cases." *Id.* (citing *Markizer v. Economopoulos* (*In re Markizer*), 66 B.R. 1014 (Bankr. S.D. Fla. 1986)); *see also Zick*, 931 F.2d at 1129 (quoting *McLaughlin v. Jones*, (*In re Jones*), 114 B.R. 917, 926 (Bankr. N.D. Ohio 1990)) ("'Bankruptcy protection was not intended to assist those who, despite their own misconduct, are attempting to preserve a comfortable standard of living at the expense of their creditors. Good faith and candor are necessary prerequisites to obtaining a fresh start.'").

The *Zick* opinion sets forth a number of additional points of law regarding § 707(a) "for cause" dismissals for lack of good faith:

Regarding the bankruptcy court's discretion, and appellate review:

"A bankruptcy court decision to dismiss pursuant to 11 U.S.C. § 707(a) will be reversed only for abuse of discretion." *Zick*, 931 F.2d at 1126 (internal citation omitted).

Regarding factors to be applied:

> "The facts required to mandate dismissal based upon a lack of good faith are as varied as the number of cases." *In re Bingham*, 68 B.R. 933, 935 (Bankr. M.D. Penn. 1987). We find particular merit in what is described as the "smell test" in *Morgan Fiduciary, Ltd. v. Citizens and Southern Int'l Bank*, 95 B.R. 232, 234 (S.D. Fla. 1988). The factors relied on by the bankruptcy court are essential in appellate review, and should be set out in the bankruptcy court's decision. . . .

Zick, 931 F.2d at 1127-28 (other internal citation omitted).

Word of caution:

> Dismissal based on lack of good faith must be undertaken on an *ad hoc* basis. It should be confined carefully and is generally utilized only in those egregious cases that entail concealed or misrepresented assets and/or sources of income, and excessive and continued expenditures, lavish lifestyle, and intention to avoid a large single debt based on conduct akin to fraud, misconduct, or gross negligence. It was not an abuse of discretion to conclude that the factors found in this case amounted to a lack of good faith on the part of Zick.
>
> We believe that it was permissible on the record to attribute bad faith motivation to pre-petition activities of defendant Zick in a malicious breach of a noncompetition agreement situation. . . .

Id. at 1129 (internal citation omitted).

In re Mehlhose, 469 B.R. 694 (Bankr. E.D. Mich. 2012), involved serial filers who filed a Chapter 7 case and understated their income. After the debtors converted the case to Chapter 13, the court granted a creditor's motion to dismiss, awarded costs and attorney fees to the creditor, and barred the debtors from refiling for two years. *Id.* at 696.

Regarding the dismissal under § 1307,[2] the *Mehlhose* court found that the debtors' latest Chapter 7 case was filed only to delay the creditor's pursuit of its claim, and not for any legitimate purpose. This was because the debtors could not obtain a Chapter 7 discharge of any of their debts. All of their debts arose before they filed a prior chapter 7 case in which they were denied a discharge, (*see* 11 U.S.C. § 523(a)(10)). And the debtors had no non-exempt assets that could be used to pay creditors in a Chapter 7 case. Finally, the debtors' undisclosed true incomes would have made them eligible for Chapter 13. The court found that the debtors had deliberately understated their incomes — by a substantial amount — in their original Schedule I. The court also cited the fact that the debtors did not testify and explain themselves at the evidentiary hearing on the creditor's motion to dismiss. *Id.* at 699-706. The court stated:

> Certainly, there is cause to dismiss this case because the Debtors are guilty of "unreasonable delay . . . prejudicial to creditors," within the meaning of § 1307(c)(1). In addition, the statute's list of 11 examples of what constitutes cause to dismiss a case is not exclusive. *See Marrama v. Citizens Bank of Mass.*, 549 U.S. 365 (2007). The filing of a bankruptcy case in bad faith is also considered "cause" to dismiss a case under § 1307(c). *Alt v. United States* (*In re Alt*), 305 F.3d 413, 418-19 (6th Cir. 2002) ("[T]here is abundant authority for the notion that a bankruptcy court has the power to dismiss a Chapter 13 petition upon a finding that the debtor did not bring it in good faith.").
>
> The Sixth Circuit has "announced standards for bankruptcy courts to follow in determining the debtor's good faith." *Alt*, 305 F.3d at 419. A determination of "good faith is a fact-specific and flexible determination" which "requires consideration of the totality of the circumstances." *Copper v. Copper* (*In re Copper*), 426 F.3d 810, 815 (6th Cir. 2005). "Under the totality of the circumstances test, [courts] analyze both the prior conduct of the bankruptcy petitioner and the petitioner's present circumstances." *Society Nat'l Bank v. Barrett* (*In re Barrett*), 964 F.2d 588, 590 (6th Cir. 1992).

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[2] The refiling bar and monetary sanctions are discussed in other sections of these materials.

> The *Alt* court also noted that "[i]n considering whether a petition has been brought in good faith, other circuits have recognized factors similar to those relevant in determining whether a plan has been proposed in good faith." *Alt*, 305 F.3d at 419. The Sixth Circuit listed twelve "circumstances to be considered in determining whether a plan has been proposed in good faith":
>
> > (1) the debtor's income;
> > (2) the debtor's living expenses;
> > (3) the debtor's attorney's fees;
> > (4) the expected duration of the Chapter 13 plan;
> > (5) the sincerity with which the debtor has petitioned for relief under Chapter 13;
> > (6) the debtor's potential for future earning;
> > (7) any special circumstances, such as unusually high medical expenses;
> > (8) the frequency with which the debtor has sought relief before in bankruptcy
> > (9) the circumstances under which the debt was incurred;
> > (10) the amount of payment offered by the debtor as indicative of the debtor's sincerity to repay the debt;
> > (11) the burden which administration would place on the trustee;
> > (12) the statutorily-mandated policy that bankruptcy provisions be construed liberally in favor of the debtor.

Id. at 707-08 (some internal citations omitted). The *Mehlhose* court further noted that the list is not exhaustive, and that "'no one factor should be viewed as being a dispositive indication of the debtor's good faith.'" *Id.* at 708 (internal citation omitted).

Readers may be interested in the bankruptcy court's unpublished opinion, entitled "Opinion Regarding Debtor's Motion to Convert to Chapter 13," in *In re Phillips*, No. 14-21741 (Bankr. E.D. Mich., filed June 26, 2015 (Docket # 57) (Opperman, J.). In that case, the court, applying the *Alt* factors, found that the trustee failed to establish a lack of good faith to prevent the debtor from converting from Chapter 7 to Chapter 13, despite the fact that the debtor filed several amendments to her Schedules A and C relating to the same piece of real property.

However, the court conditioned the granting of the debtor's motion to convert "upon the acceptance by the Debtor of Chapter 7 administrative expenses which include, but are not necessarily limited to, attorney fees for the Chapter 7 Trustee, as well as the Chapter 7 Trustee's fees." *Id.* at 8.

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3. Monetary Sanctions Against the Debtor - 11 U.S.C. § 105(a), Federal Rule of Bankruptcy Procedure 9011, and the Court's Inherent Powers

Courts have statutory and inherent authority to order a debtor to pay monetary sanctions for bad faith conduct, including an award of attorney fees to an opposing party, or a civil penalty payable to the court. And as the Supreme Court noted in *Siegel*, "because it arises postpetition, a bankruptcy court's monetary sanction survives the bankruptcy case and is thereafter enforceable through the normal procedures for collecting money judgments." *Law v. Siegel*, 134 S. Ct. 1188, 1198 (2014) (citing 11 U.S.C. § 727(b)).

The relevant provisions of § 105 and Rule 9011 provide:

11 U.S.C. § 105(a):

> (a) The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

Federal Rule of Bankruptcy Procedure 9011:

> (a) Signature
>
> Every petition, pleading, written motion, and other paper, except a list, schedule, or statement, or amendments thereto, shall be signed by at least one attorney of record in the attorney's individual name. A party who is not represented by an attorney shall sign all papers.

Each paper shall state the signer's address and telephone number, if any. An unsigned paper shall be stricken unless omission of the signature is corrected promptly after being called to the attention of the attorney or party.

(b) Representations to the court

By presenting to the court (whether by signing, filing, submitting, or later advocating) a petition, pleading, written motion, or other paper, an attorney or unrepresented party is certifying that to the best of the person's knowledge, information, and belief, formed after an inquiry reasonable under the circumstances,

. . . .

(3) the allegations and other factual contentions have evidentiary support or, if specifically so identified, are likely to have evidentiary support after a reasonable opportunity for further investigation or discovery; and

(4) the denials of factual contentions are warranted on the evidence or, if specifically so identified, are reasonable based on a lack of information or belief.

(c) Sanctions

If, after notice and a reasonable opportunity to respond, the court determines that subdivision (b) has been violated, **the court may**, subject to the conditions stated below, **impose an appropriate sanction upon the attorneys, law firms, or parties that have violated subdivision (b) or are responsible for the violation.**

(1) How initiated

(A) By motion

A motion for sanctions under this rule shall be made separately from other motions or requests and shall describe the specific conduct alleged to violation subdivision (b). . . . The motion for sanctions may not be filed with or presented to the court unless, within 21 days after service of the motion (or such other period as the court may prescribe), the challenged paper, claim, defense, contention, allegation, or denial is not withdrawn or appropriately corrected, except that this limitation shall not apply if the conduct alleged is the filing of a petition in

violation of subdivision (b). If warranted, the court may award to the party prevailing on the motion the reasonable expenses and attorney's fees incurred in presenting or opposing the motion. Absent exceptional circumstances, a law firm shall be held jointly responsible for violations committed by its partners, associates, and employees.

(B) On court's initiative

On its own initiative, the court may enter an order describing the specific conduct that appears to violate subdivision (b) and directing an attorney, law firm, or party to show cause why it has not violated subdivision (b) with respect thereto.

(2) Nature of sanction; limitations

A sanction imposed for violation of this rule shall be limited to what is sufficient to deter repetition of such conduct or comparable conduct by others similarly situated. Subject to the limitations in subparagraphs (A) and (B), the sanction may consist of, or include, directives of a nonmonetary nature, an order to pay a penalty into court, or, if imposed on motion and warranted for effective deterrence, an order directing payment to the movant of some or all of the reasonable attorneys' fees and other expenses incurred as a direct result of the violation.

(A) Monetary sanctions may not be awarded against a represented party for a violation of subdivision (b)(2).

(B) Monetary sanctions may not be awarded on the court's initiative unless the court issues its order to show cause before a voluntary dismissal or settlement of the claims made by or against the party which is, or whose attorneys are, to be sanctioned.

(3) Order

When imposing sanctions, the court shall describe the conduct to constitute a violation of this rule and explain the basis for the sanction imposed.

(emphasis added).

***

In *In re Mehlhose*, discussed above, the court found that the debtors' "bad faith and abuse of the bankruptcy system" caused a creditor to incur attorney fees and costs in moving to dismiss the debtor's bankruptcy case. 469 B.R. at 711. In ordering the debtors to pay the creditor's fees and costs, the court discussed at length its inherent authority and statutory authority under 11 U.S.C. § 105(a) to order monetary sanctions against debtors.

Regarding inherent authority, the *Mehlhose* court cited the case, *John Richards Homes Building., L.L.C. v. Adell* (*In re John Richards Homes Building. Co., L.L.C.*), 404 B.R. 220, 226-27 (E.D. Mich. 2009) ("Bankruptcy courts, like all courts, have an inherent power to issue sanctions, as explained by the Supreme Court in the *Chambers* case."), and the Ninth Circuit case, *Price v. Lehtinen* (*In re Lehtinen*), 564 F.3d 1052, 1058-59 (9th Cir. 2009) ("A bankruptcy court's inherent power allows it to sanction 'bad faith' or 'willful misconduct,' even in the absence of express authority to do so."). The *Mehlhose* court also quoted a leading Supreme Court case on sanctions, *Chambers v. NASCO, Inc.*, 501 U.S. 32, 45-46 (1991):

> [A] court may assess attorney's fees when a party has "'acted in bad faith, vexatiously, wantonly, or for oppressive reasons.'" In this regard, if a court finds "that fraud has been practiced upon it, or that the very temple of justice has been defiled," it may assess attorney's fees against the responsible party, as it may when a party "shows bad faith by delaying or disrupting the litigation or by hampering enforcement of a court order[.]" The imposition of sanctions in this instance transcends a court's equitable power concerning relations between the parties and reaches a court's inherent power to police itself, thus serving the dual purpose of "vindicat[ing] judicial authority without resort to the more drastic sanctions available for contempt of court and mak[ing] the prevailing party whole for expenses cause by his opponent's obstinancy."
>
> . . . [Statutory mechanisms for imposing sanctions] are not substitutes for the inherent power, for that power is both broader and narrower than other means of imposing sanctions. First,

> whereas each of the other mechanisms reaches only certain individuals or conduct, the inherent power extends to a full range of litigation abuses. At the very least, the inherent power must continue to exist to fill in the interstices.

In re Mehlhose, 469 B.R. at 710 (quoting *Chambers*, 501 U.S. at 45-46) (internal citations omitted).

Regarding statutory authority to impose monetary sanctions, the *Mehlhose* court noted that its statutory authority under 11 U.S.C. § 105(a) "exceeds the equitable authority available under 'traditional equity jurisprudence,'" but that "such power is not limitless and must not be exercised in a way that is inconsistent with the Bankruptcy Code." *In re Mehlhose*, 469 B.R. at 710-11 (internal citations omitted). The court concluded that "[t]here is nothing in the language of § 1307(c) of the Bankruptcy Code which prevents a bankruptcy court from sanctioning a debtor, upon dismissal of the debtor's bankruptcy case for cause, for misconduct occurring during the pendency of the case," and furthermore that § 105(a) provides authority "to award attorney fees as a sanction for misconduct." *Id.* at 711.

In re Mitchell, No. 13-14494, 2014 WL 1725819 (Bankr. N.D. Ohio April 30, 2014), is a post-*Siegel* case in which the bankruptcy court somewhat begrudgingly allowed a debtor to amend her Schedule C to include a homestead exemption, despite the debtor's inconsistent representations about the ownership of the property and the amount of the claimed exemption. This case mentions monetary sanctions against the debtor as an "alternative remedy" for the debtor's misconduct, but declined to award sanctions at the time because the creditor had not moved for them:

> One alternative remedy for debtor misconduct is the imposition of sanctions under Federal Rule of Bankruptcy Procedure 9011. Sanctions available under Rule 9011 include requiring the sanctioned party to pay some or all of the reasonable legal fees and related expenses incurred by another party as a

> direct result of the sanctionable conduct. Fed. R. Bankr. P. 9011(c)(2). However, cost-shifting sanctions may only be imposed upon standalone motion. *Id.* [The creditor] has not yet filed such a motion for sanctions under Rule 9011, and, therefore, consideration of such sanctions is not properly before the Court.

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4. Monetary Sanctions Against the Debtor's Attorney - 11 U.S.C. § 105(a), Federal Rule of Bankruptcy Procedure 9011, and the Court's Inherent Powers; §§ 526(a), (c), 707(b)(4)(D)

Litigants may prefer to pursue sanctions against the debtor's attorney instead of the debtor. To impose sanctions on a debtor's attorney, courts rely on, *inter alia*, §§ 105(a), 707(b)(4), 526(a) & (c), Rule 9011, and the court's inherent authority. Section 105(a) and Rule 9011 are quoted above. Sections 526 and 707(b)(4) are quoted below, and cases relying on those sections to sanction a debtor's attorney are discussed.[3]

When reading the provisions of § 526, "Restrictions on debt relief agencies," one must keep in mind the Supreme Court's holding in *Milavetz, Gallop & Milavetz, P.A. v. United States*, 559 U.S. 229, 239 (2010), that "attorneys who provide bankruptcy assistance to assisted persons are debt relief agencies within the meaning of BAPCPA [and therefore § 526]."[4]

11 U.S.C. § 526:

> (a) A debt relief agency shall not—

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[3] *See also* G. Thomas Curran, Jr., *How Much Diligence is Due? Defining an Attorney's Duty to Perform a Pre-Petition Inquiry*, 23 Am. Bankr. Inst. J. 10, 24-25, 74 (Nov. 2013) (*available at*: https://s3.amazonaws.com/abi-org-corp/journals/2013/september/straight.pdf, last accessed 8/24/2015).

[4] The *Milvetz* court also succinctly outlined possible remedies against debtors' attorneys under § 526(c):

> Section 526(c) provides remedies for a debt relief agency's violation of § 526, § 527, or § 528. Among the actions authorized, a debtor may sue the attorney for remittal of fees, actual damages, and reasonable attorney's fees and costs; a state attorney general may sue for a resident's actual damages; and a court finding intentional abuse may impose an appropriate civil penalty. § 526(c).

Milavetz, 559 U.S. at 242-43.

. . . .

(2) **make any statement**, or counsel or advise any assisted person or prospective assisted person to make a statement **in a document filed in a case** or proceeding under this title, **that is untrue or misleading, or that upon the exercise of reasonable care, should have been known by such agency to be untrue or misleading.**

. . . .

(c)(1) . . .

(2) **Any debt relief agency shall be liable** to an assisted person **in the amount of any fees** or charges in connection with providing bankruptcy assistance to such person that such debt relief agency has received, **for actual damages, and for reasonable attorneys' fees and costs** if such agency is found, after notice and a hearing, to have—

(A) **intentionally or negligently failed to comply with any provision of this section**, section 527, or section 528 with respect to a case or proceeding under this title for such assisted person;

(B) provided bankruptcy assistance to an assisted person in a case or proceeding under this title that is dismissed or converted to a case under another chapter of this title because of such agency's intentional or negligent failure to file any required document, include those specified in section 521; or

(C) intentionally or negligently disregarded the material requirements of this title or the Federal Rules of Bankruptcy Procedure applicable to such agency.

. . . .

(5) Notwithstanding any other provision of Federal law and in addition to any remedy provided under Federal or State law, **if the court**, on its own motion or on the motion of the United States trustee or the debtor, **finds that a person intentionally violated this section, or engaged in a clear**

> **and consistent pattern or practice of violating this section, the court may—**
>
> > (A) enjoin the violation of such section; or
> >
> > (B) **impose an appropriate civil penalty against such person.**

(emphasis added).

11 U.S.C. § 707(b):

> (4)(A)The court, on its own initiative or on the motion of a party in interest, in accordance with the procedures described in rule 9011 of the Federal Rules of Bankruptcy Procedure, may order the attorney for the debtor to reimburse the trustee for all reasonable costs in prosecuting a motion filed under section 707(b), including reasonable attorney's fees, if—
>
> > (i) the trustee files a motion for dismissal or conversion under this subsection; and
> >
> > (ii) the court—
> >
> > > (I) grants such motion; and
> > >
> > > (II) finds that the action of the attorney for the debtor in filing a case under this chapter violated rule 9011 of the Federal Rules of Bankruptcy Procedure.
>
> (B) If the court finds that the attorney for the debtor violated rule 9011 of the Federal Rules of Bankruptcy Procedure, the court, on its own initiative or on the motion of a party in interest, in accordance with such procedures, may order—
>
> > (i) the assessment of an appropriate civil penalty against the attorney for the debtor; and
> >
> > (ii) the payment of such civil penalty to the trustee, the United States trustee (or the bankruptcy administrator, if any).

> (C) **The signature of an attorney on a petition, pleading, or written motion shall constitute a certification that the attorney has—**
>
> > (i) **performed a reasonable investigation into the circumstances that gave rise to the petition, pleading, or written motion; and**
> >
> > (ii) **determined that the petition, pleading, or written motion—**
> >
> > > (I) **is well grounded in fact; and**
> > >
> > > (II) **is warranted by existing law** or a good faith argument for the extension, modification or reversal of existing law and does not constitute abuse under paragraph (1).
>
> (D) **The signature of an attorney on the petition shall constitute a certification that the attorney has no knowledge after an inquiry that the information in the schedules filed with respect to such petition is incorrect.**

(emphasis added).

***

In re Opra, 365 B.R. 728 (Bankr. E.D. Mich. 2007) involved sanctions against a debtor's attorney under Federal Rule of Bankruptcy Procedure 9011(b) ("Representations to the court"). In that case, the debtor failed to disclose the fact that she had a personal injury claim arising from a prepetition motorcycle accident in which the debtor and her husband were both seriously injured. (The claim later settled for $100,000). The court found, after an evidentiary hearing, that "Debtor's failure to disclose her personal injury claim in her original Schedule B was an intentional concealment of that asset, and . . . Debtor acted in bad faith." *Id.* at 730. The court denied the debtor's attempt to amend her Schedule C to exempt the asset, because of the debtor's

concealment of the asset (this was a pre-*Siegel* case), and ordered the debtor's attorney to pay $2,000 in the form of a civil penalty to the court based on Rule 9011.

Regarding the attorney's duties, the court stated:

> At the show cause hearing [on Rule 9011 sanctions], [the attorney] professed to have very limited knowledge of Michigan's no-fault law. But he did not contend that his knowledge of Michigan law was so limited that he did not know that Debtor had *any* claims. And even if [the attorney] was not sufficiently well-versed in Michigan law to know whether Debtor had any claims, he had a duty under Rule 9011(b) to conduct a "reasonable" inquiry into that law before indicating in Debtor's Schedule B that she had *no claims*. By its terms, Rule 9011(b) imposes a duty on the attorney to conduct an "inquiry reasonable under the circumstances" into both fact and law.

In re Opra, 365 B.R. at 740 (internal citation omitted).

Regarding the type and amount of sanctions, the court discussed how Rule 9011(c) does not expressly authorize "monetary sanctions," such as payment of attorney fees for the trustee, when the Rule 9011 proceeding is initiated by the court; rather, in that situation Rule 9011(c)(2) only expressly authorizes sanctions in the form of "(1) nonmonetary 'directives;' and (2) a 'penalty' to be paid into court." *In re Opra*, 365 B.R. at 741. But the court cited several cases holding that "monetary sanctions may be imposed under 11 U.S.C. § 105(a) and under the Court's inherent authority to impose sanctions on attorneys appearing before it." *In re Opra*, 365 B.R. at 741-42 (citing *Miller v. Cardinale* (*In re Deville*), 361 F.3d 539, 550-51 (9th Cir. 2004) ("a court 'may safely rely on its inherent power' as a sanctioning tool in instances when statutes or rules prove inadequate to remedy misconduct"); *Knowles Building Co. v. Zinni* (*In re Zinni*), 261 B.R. 196, 203 (6th Cir. BAP 2001) (holding that "federal courts, including the bankruptcy court, have the inherent power to impose sanctions on a scope broader than that of Bankruptcy Rule 9011, including monetary sanctions")).

However, the court concluded that requiring the debtor's attorney "to pay a penalty into the court" was "an appropriate choice" in that case because:

> (1) the sanction amount the Court is imposing is relatively small; and (2) the Chapter 7 Trustee, and therefore the bankruptcy estate, has not suffered any net loss because of the conduct being sanctioned. Because the Court is denying Debtor's $28,550.00 claimed exemption, as discussed later in this opinion, the bankruptcy estate will recover substantially more than the $7,000 to $8,000 that it has incurred in attorney fees for the Trustee to object to Debtor's amended exemptions. In the end, therefore, the initial nondisclosure of Debtor's personal injury claim will not have caused any net loss to the bankruptcy estate, in the form of additional Trustee attorney fees.

In re Opra, 365 B.R. at 742 (footnote omitted).

In discussing the appropriate amount of the penalty, the *Opra* court noted that, under subsection (c)(2), "Rule 9011 sanctions must be limited to what is necessary to deter the offending attorney from repeating the sanctioned conduct, and to deter others from engaging in comparable conduct." *Id.* And the court noted that, "sanctions must be 'commensurate with the egregiousness of the conduct.'" *Id.* (citing *Mapother & Mapother P.S.C. v. Cooper* (*In re Downs*), 103 F.3d 472, 477 (6th Cir. 1996)); *see also In re Hale*, 511 B.R. 870, 880-81 (Bankr. W.D. Mich.2014).

The court concluded that $2,000 was an appropriate penalty, reasoning that the amount "is necessary to deter [debtor's attorney] and other attorneys from failing to properly disclose assets," yet "not so steep as to unduly damage [the attorney] and his firm." *In re Opra*, 365 B.R. at 742. The court noted that the amount is "only $1,000.00 more than the $1,000.00 fee that [the attorney] received from Debtor to file this case." *Id.* (footnote omitted). Finally, the court found that the amount was "'commensurate with the egregiousness of the conduct,'" although it may have been "too light." *Id.* at 742-43 (citation omitted).

Hills v. McDermott (*In re Wicker*), 702 F.3d 874 (6th Cir. 2012) involved sanctions ordered under 11 U.S.C. § 526(a)(2) and § 526(c)(5)(B) against a bankruptcy petitioner preparer who instructed a debtor to deny the BPP's involvement in preparing the debtor's filings. In affirming the bankruptcy court's decision to order the BPP to pay a $5,000 civil penalty, the court stated:

> The bankruptcy court also properly ordered [the BPP] to pay a civil penalty of $5,000 for intentionally violating § 526(a)(2). Section 526(a)(2) prohibits debt relief agencies, including bankruptcy petition preparers, *see* 11 U.S.C. § 101(12A), from "mak[ing] any statement, or cousel[ing] or advis[ing] any assisted person or prospective assisted person to make a statement in a document filed in a case or proceeding under this title, that is untrue or misleading. . . . ." 11 U.S.C. § 526(a)(2). If a bankruptcy petition preparer violates this provision intentionally, the court may "impose an appropriate civil penalty." 11 U.S.C. § 526(c)(5)(B). The record shows that [the debtor] initially submitted a declaration stating that she had no assistance in preparing her bankruptcy filing. [The debtor's] testimony that [the BPP] instructed her to conceal his involvement in the filing of her bankruptcy petition supports the bankruptcy court's conclusion that [the BPP] advised her to make an untrue statement in the filed declaration, and that he so intentionally. Accordingly, the court was authorized to impose a civil penalty under § 526(c)(5)(B).

In re Wicker, 702 F.3d at 878.

In *In re Casavalencia*, 389 B.R. 292 (Bankr. S.D. Fla. 2008), the bankruptcy court cited 11 U.S.C. § 526(a)(2) (untrue or misleading statements to the court) and Rule 9011 when ordering a debtor and a debtor's attorney to pay a group of creditors' costs and fees incurred in prosecuting a motion to dismiss a Chapter 13 case for bad faith. The debtor in the case filed bankruptcy after a real estate investment Ponzi scheme collapsed. The court found that the debtor intentionally filed under a different name and listed himself as single (he was married) to mislead his creditors, and that he concealed a piece of real property and a car. In the order dismissing the case, the court stated:

> I specifically find that the Debtor's bankruptcy petition was filed in bad faith and that both the Debtor and his counsel, Carlos A. Santos, II, Esquire, are responsible for that bad faith. No reasonable or responsible lawyer could have filed a petition and schedules so replete with misstatements if that lawyer had done anything approaching the "reasonable inquiry" requirements of Federal Rule of Bankruptcy Procedure 9011. Moreover, as a "debt relief agency" within the meaning of 11 U.S.C. § 101(12A), that is, a person "who provides any bankruptcy assistance to an assisted person in return for payment of money or other valuable consideration, Mr. Santos was enjoined under 11 U.S.C. § 526(a)(2) [from making untrue or misleading statements in a document filed in a bankruptcy case].
>
> The falsehoods contained in the petition and schedules filed here were untrue and misleading and at least some of them (particularly including the Debtor's nomenclature) would have been known to [the debtor's attorney] "upon the exercise of reasonable care. I find that Rule 9011 and 11 U.S.C. §§ 105(a) and 526(A)(2) provide the basis for the award of such sanctions.

In re Casavalencia, 389 B.R. at 296 (other internal citations omitted).

Other cases regarding attorney sanctions:

In re Clink, 770 F.3d 719, 722-23 (8th Cir. 2014) (holding that attorneys may be sanctioned under § 526(a)(2) "when they advise their clients to lie, regardless of whether the client takes the advice," unlike under § 7206(2) of the tax code, which requires that "a false [tax] return actually be prepared before the attorney may be sanctioned").

In re Garrard, Nos. 13-40418-JJR13, 13-40419-JJR13, 2013 WL 4009324, at *4 (Bankr. N.D. Ala. Aug. 5, 2013) (using "reasonable inquiry" standard from Rule 9011 to determine whether a debtor's attorney violated §§ 707(b)(4)(C) and 526(a)(2)).

In re Trudell, 424 B.R. 786, 792 (Bankr. W.D. Mich. 2010) (nothing that "[w]hether Rule 9011 applies to statements of affairs and schedules is debatable," but that § 707(b)(4)(D) "unquestionably imposes a duty upon the debtor's attorney to ensure the accuracy of his client's schedules").

5. Barring a Debtor from Refiling Bankruptcy - 11 U.S.C. §§ 349(a), 109(g), 105(a)

In *In re Mehlhose*, discussed above, the bankruptcy court dismissed the debtors' Chapter 13 case "for cause," and barred the debtors from refiling bankruptcy for two years, citing §§ 105(a), 109(g), and 349(a). Section 105(a) is quoted above. Sections 109(g) and 349(a) provide as follows:

11 U.S.C. § 109 ("Who may be a debtor"):

> (g) Notwithstanding any other provision of this section, no individual or family farmer may be a debtor under this title who has been a debtor in a case pending under this title at any time in the preceding 180 days if—
>
> > (1) **the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of the case**; or
> >
> > (2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided by section 362 of this title.

(emphasis added).

11 U.S.C. § 349(a) ("Effect of dismissal"):

> (a) **Unless the court, for cause, orders otherwise,** the dismissal of a case under this title does not bar the discharge, in a later case under this title, of debts that were dischargeable in the case dismissed; nor does the dismissal of a case under this title prejudice the debtor with regard to the filing of a subsequent petition under this title, except as provided in section 109(g) of this title.

(emphasis added).

***

The *Mehlhose* court explained that "'where there is sufficient cause, bankruptcy courts have the authority pursuant to 11 U.S.C. §§ 105(a) and 349(a) to prohibit bankruptcy filings in excess of 180 days.'" 469 B.R. at 711-12 (internal citation omitted). The court cited a number of cases in support of this point, including *Cusano v. Klein* (*In re Cusano*), 431 B.R. 726, 737 (6th Cir. BAP 2010) (reasoning that "[s]ection 109(g) is not . . . a limitation on the bankruptcy court's authority to impose sanctions fashioned to prevent abuse of the bankruptcy system" and finding that "[t]he record . . . demonstrate[d] sufficient cause to prohibit th[e] [d]ebtor from refiling for Chapter 13 protection for two years"); *Dietrich v. Nob-Hill Stadium Props.*, No. 05-2255, 2007 WL 579547, at *5 (6th Cir. Feb. 15, 2007) (affirming permanent bar against refiling); *Mains v. Foley*, Nos. 1:11-CV-456, 1:11-CV-740, 2012 WL 612006, at *7 (W.D. Mich. Feb. 24, 2012); *Javens v. Ruskin*, No. 99-74189, 2000 WL 1279189, at *2 (E.D. Mich. Aug. 24, 2000). *But see Frieouf v. United States* (*In re Frieouf*), 938 F.2d 1099, 1104 (10th Cir. 1991) ("[i]nterpreting section 349(a) and section 109(g) to allow bankruptcy courts to prohibit future filings for a period greater than 180 days, not only contradicts the statute's plain meaning, but encroaches on the fifth amendment's due process and equal protection guarantees.").

Finally, the *Mehlhose* court cited several cases establishing that a "bankruptcy court's finding of bad faith, or an abuse of the bankruptcy process, particularly in the case of serial filers, is generally considered sufficient cause to impose a bar to refiling for more than 180 days." *In re Mehlhose*, 469 B.R. at 712 (citing *Cusano*, 431 B.R. at 737; *In re Morris*, No. 3:10-BK-04143, 2010 WL 3943927, at *9 (Bankr. M.D. Tenn. Oct. 6, 2010); *In re Price*, 304 B.R. 769, 773 (Bankr. N.D. Ohio 2004); *Javens*, 2000 WL 1279189, at *2); *see also In re Norton*, 319 B.R. 671 (Bankr. D. Utah 2005) (granting United States trustee's motion to permanently bar debtor from

refiling pursuant to 11 U.S.C. § 349(a), where debtor filed nine petitions in nine years, all of which had been dismissed).

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6. Objecting to a Fraudulently Asserted Claim of Exemption - Federal Rule of Bankruptcy Procedure 4003(b)(2)

The authors of a February 2015 ABI Journal article, *Law v. Siegel Dicta Leads Lower Courts Astray*,[5] argue that "Fed. R. Bankr. P. 4003(b)(2) does provide clear authority for a trustee to object to fraudulently asserted claims of exemption." *Id.* at 77. They point out "[w]hile [*Law v. Siegel*] involved a debtor who engaged in fraud, the claim of a $75,000 homestead exemption was indisputably legitimate." *Id.* But attorneys practicing in the Sixth Circuit should rely on this advice with caution in light of the Sixth Circuit's holding in *Baker*, and for the reasons indicated in *In re Bogan*, No. 12-16624, 2015 WL 1598056 (Bankr. W.D. Wis. April 7, 2015), discussed below.

Federal Rule of Bankruptcy Procedure 4003:

> (a) Claim of exemptions. A debtor shall list the property claimed as exempt under § 522 of the Code on the schedule of assets required to be filed by Rule 1007. If the debtor fails to claim exemptions or file the schedule within the time specified in Rule 1007, a dependent of the debtor may file the list within 30 days thereafter.
>
> (b) **Objecting to a claim of exemptions**
>
> > (1) Except as provided in paragraphs (2) and (3), a party in interest may file an objection to the list of property claimed as exempt within 30 days after the meeting of creditors held under § 341(a) is concluded or within 30 days after any amendment to the list or supplemental schedules is filed, whichever is later. The court may, for cause, extend

[5] Neil C. Gordon & Jonathan H. Azoff, *Law v. Siegel Dicta Leads Lower Courts Astray*, 34 Am. Bankr. Inst. J. 34 (2015) (*available at*: https://s3.amazonaws.com/abi-org-corp/journals/2014/december/trustee.pdf, last accessed 8/24/2015).

> the time for filing objections if, before the time to object expires, a party in interest files a request for an extension.
>
> (2) **The trustee may file an objection to a claim of exemption at any time prior to one year after the closing of the case if the debtor fraudulently asserted the claim of exemption.** The trustee shall deliver or mail the objection to the debtor and the debtor's attorney, and to any person filing the list of exempt property and that person's attorney.
>
> . . . .
>
> (c) Burden of proof. In any hearing under this rule, the objecting party has the burden of proving that the exemptions are not properly claimed. After hearing on notice, the court shall determine the issues presented by the objections.

(emphasis added).

***

In *In re Bogan*, No. 12-16624, 2015 WL 1598056 (Bankr. W.D. Wis. April 7, 2015), a Chapter 7 trustee objected to a debtor's amended claim for exemption of benefits in a life insurance policy on the ground that the amendment was filed in bad faith. The trustee relied explicitly on Federal Rule of Bankruptcy Procedure 4003(b)(2). The court rejected the trustee's argument, reasoning:

> [A]s a general matter, the Code defines the creation, alteration or elimination of substantive rights . . . the Bankruptcy Rules [only] define the process by which these privileges may be effected." *In re Hanover Indus. Mach. Co.*, 61 B.R. 551, 552 (Bankr. E.D. Pa. 1986). Thus, the bankruptcy rules cannot authorize the court to act in the absence of a code provision creating the right. *See In re Gee*, 204 F.3d 1115 (5th Cir. 1999) ("Under 28 U.S.C. § 2075, the rules the Supreme Court was given the power to promulgate are not to 'abridge, enlarge, or modify any substantive right'"). If Congress wanted to give bankruptcy courts the power to deny bad faith exemption amendments, then it would have added a provision to § 522.

In re Bogan, 2015 WL 1598056, at *2 (some internal citations omitted); *see also, e.g.*, *In re James*, 498 B.R. 813, 822-23 (Bankr. E.D. Tenn. 2013) (denying trustee's Rule 4003(b)(2) objection to a debtor's exemption, concluding that "the single overstatement of the value of the claimed exemption [does not rise] to the level of a fraudulent assertion of an exemption.").

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7. Objecting to a Motion to Reopen Closed Case to Amend Schedules - Federal Rules of Bankruptcy Procedure 1009(a), 4003(b); 11 U.S.C. § 350(b)

At the end of its opinion in *Baker*, the Sixth Circuit affirms the rejection of the Chapter 7 trustee's argument that the debtors' requested amendment (to exempt a previously undisclosed asset) was untimely under Federal Rule of Bankruptcy Procedure 1009. *Ellmann v. Baker* (*In re Baker*), 791 F.3d 677, 683-84 (6th Cir. 2015). The Sixth Circuit concluded that the Chapter 7 trustee's untimeliness argument was itself untimely, and thus deemed waived under Federal Rule of Bankruptcy Procedure 4003(b). (The court further held that the time limit for objecting to exemptions imposed by Rule 4003(b) is jurisdictional.) *Id.* at 683.

Rule 4003(b) is quoted in the immediately preceding section. Rule 1009(a) and section 350 provide:

Federal Rule of Bankruptcy Procedure 1009(a):

> (a) General right to amend
>
> **A voluntary petition, list, schedule, or statement may be amended by the debtor as a matter of course at any time before the case is closed.** The debtor shall give notice of the amendment to the trustee and to any entity affected thereby. On motion of a party in interest, after notice and a hearing, the court may order any voluntary petition, list, schedule, or statement to be amended and the clerk shall give notice of the amendment to entities designated by the court.

(emphasis added).

11 U.S.C. § 350:

> (a) After an estate is fully administered and the court has discharged the trustee, the court shall close the case.
>
> (b) A case may be reopened in the court in which such case was closed to administer assets, to accord relief to the debtor, or for other cause.
>
> ***

On the one hand, *Baker* held that no distinction should be drawn between pending cases and cases that have been closed and reopened, in terms of whether a bankruptcy court has an equitable power to "disallow exemptions or amendments to exemptions due to bad faith or misconduct." *Baker*, 791 F.3d at 683. But on the other hand, the Sixth Circuit seemed to leave the door open for parties to object to a proposed amendment to exemptions (Schedule C) in a reopened case. The Sixth Circuit did not reach the merits of the Trustee's argument that Rule1009(a) does not apply in a reopened case:

> Because the bankruptcy case was previously closed, the trustee argued at the hearing which occurred more than thirty days after the amendments were filed, that the debtors could not make amendments under Rule 1009(a) "as a matter of course" and that any amendment made after the reopening of a case instead **is subject to disallowance at the discretion of the bankruptcy court**.
>
> . . . .
>
> We agree with the district court's conclusion that the trustee waived his Rule 1009(a) argument by failing to timely raise it in his objection. Importantly, the trustee conceded at the hearing that he never argued in his objection that Rule 1009 barred the debtors from amending their exemptions. In addition, the trustee answered "Yes" in response to the bankruptcy court's question, "Well, you had that argument available to you before [*Law v. Siegel*] was decided, didn't you?" . . . .

Id. (emphasis added) (internal citations omitted).

Moreover, in its conclusion, the *Baker* court states the following two reasons for its decision to affirm the bankruptcy court's order permitting the amended exemption: "Because *Law v. Siegel* prohibits the bankruptcy court from disallowing amendments due to a debtor's bad faith or fraud **and the trustee waived his timeliness objection to the amendments**, we affirm the district court's decision affirming the bankruptcy court's order." *Id.* at 684 (emphasis added).

Thus, litigants in the Sixth Circuit *might* still have the option to object to the timeliness of a debtor's motion to reopen a case to amend his or her schedules to exempt previously concealed assets. "A decision to reopen a case is committed to the sound discretion of the [bankruptcy] court." *In re Quinn*, No. 08-031969, 2015 WL 535533, at *1 (Bankr. N.D. Ohio Feb. 6, 2015) (citing *In re Kapsin*, 265 B.R. 778, 780 (Bankr. N.D. Ohio 2001)). Moreover, "[i]n exercising its discretion to reopen a case, 'the bankruptcy court should exercise its equitable powers with respect to substance and not technical considerations that will prevent substantial justice.'" *In re Oglesby*, 519 B.R. 699, 703 (Bankr. N.D. Ohio 2014) (quoting *In re Shondel*, 950 F.2d 1301, 1304 (7th Cir. 1991)).

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8. Avoiding an Interest in a Debtor's Property that is Superior to the Debtor's Exemption - 11 U.S.C. §§ 544(a)(3), 551; applicable state law

In a May 2014 article in the American Bankruptcy Institute Journal entitled, *Law v. Siegel: U.S. Supreme Court Limits Reach of § 105(a)*, Ferve E. Ozturk wrote that "bankruptcy trustees assessing the impact of *Siegel* should bear in mind that they may have a priority claim to property that is allegedly subject to a homestead exemption to the extent that they can avoid an interest in the property superior to the exemption under applicable state law." 33 Am. Bankr.

Inst. J. 28, 104 (2015).[6] Ms. Ozturk cited *Lassman v. OneWest Bank* (*In re Swift*), 458 B.R. 8 (Bankr. D. Mass 2011).

In *In re Swift*, the Mortgage Electronic Registration System, or MERS, erroneously recorded a discharge of the debtor's mortgage. Later, a new bank acquired the mortgage, and the debtor and the bank modified the mortgage and note and "reiterated the debtor's obligation to pay the note in full." *Id.* at 11 (footnotes omitted). About six months later, the debtor recorded a "Declaration of Homestead" for the property, and then filed a Chapter 7 petition eight days later. The Chapter 7 trustee for the case filed an adversary proceeding "seeking to (i) avoid the Mortgage pursuant to 11 U.S.C. § 544(a)(3), (ii) preserve the avoided Mortgage for the benefit of the estate pursuant to 11 U.S.C. § 551, and (iii) establish the Mortgage's priority over the Debtor's Homestead." *Id.* (footnotes omitted). The court granted the trustee's motion.

The case was primarily decided under Massachusetts law, which provides that "a debtor's homestead exemption is not effective against a mortgagee where the mortgage in question was executed before the debtor recorded a declaration of homestead," and that the holder of a mistakenly discharged mortgage holds an equitable claim for reinstatement of the mortgage. *In re Swift*, 458 B.R. at 14-15 (internal citations omitted). The court also addressed the relationship between exemptions, 11 U.S.C. § 551 and the trustee's strong arm powers under 11 U.S.C. § 544(a):

> [T]he Homestead was subordinate to the Mortgage at the time of the Debtor's filing. The fact that the Trustee subsequently avoided the Mortgage and preserved it for the estate does not change their relative priority. Again, preservation of an avoided lien "puts the estate in the shoes of the creditor whose lien is avoided. It does nothing to . . . detract from the rights of that creditor vis-à-vis other creditors." Because OneWest's interest in the Mortgage had

[6] This article is available at: https://s3.amazonaws.com/abi-org-corp/journals/2014/march/feature3.pdf (last accessed 8/24/2015).

> priority over the Homestead, the Trustee's interest in the avoided Mortgage has priority as well.
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> The Debtor argues that the Trustee's attempt to establish the Mortgage's priority over the Homestead constitutes an untimely objection to the exemption, and thus should be summarily denied. There is, however, a distinction between an objection to the Debtor's entitlement to a homestead exemption, which the Trustee does not contest, and an attempt to establish the Mortgage's priority over the Homestead. Although the Trustee's action may prevent the Debtor from enjoying the full amount of his exemption, the Trustee is not objecting to the Debtor's claim of an exemption. Rather the Trustee is merely enforcing OneWest's rights as a prior lienholder against the Debtor, as he is entitled to do pursuant to 11 U.S.C. § 551.

Id. at 15-16 (footnotes omitted).

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9. Imprisonment or fine - 18 U.S.C. § 152 – for the crime of bankruptcy fraud

The *Siegel* decision also mentions the possibility of imprisonment for "[f]raudulent conduct in a bankruptcy case" under 18 U.S.C. § 152. While trustees and creditors have no ability to bring federal criminal charges against a debtor themselves, everyone should be aware of 18 U.S.C. § 152. That criminal law section, entitled "Concealment of assets; false oaths and claims; bribery," provides:

> A person who—
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> (1) knowingly and fraudulently conceals from a custodian, trustee, marshal, or other officer of the court charged with the control or custody of property, or, in connection with a case under title 11, from creditors or the United States Trustee, any property belonging to the estate of a debtor;
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> (2) knowingly and fraudulently makes a false oath or account in or in relation to any case under title 11;
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> (3) knowingly and fraudulently makes a false declaration, certificate, verification, or statement under penalty of perjury as

> permitted under section 1746 of title 28, in or in relation to any case under title 11;
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> . . . .
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> (7) in a personal capacity or as an agent or officer of any person or corporation, in contemplation of a case under title 11 by or against the person or any other person or corporation, or with intent to defeat the provisions of title 11, knowingly and fraudulently transfers or conceals any of his property or the property of such other person or corporation;
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> (8) after the filing of a case under title 11 or in contemplation thereof, knowingly and fraudulently conceals, destroys, mutilates, falsifies, or makes a false entry in any recorded information (including books, documents, records, and papers) relating to the property or financial affairs of a debtor; or
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> (9) after the filing of a case under title 11, knowingly and fraudulently withholds from a custodian, trustee, marshal, or other officer of the court or a United States Trustee entitled to its possession, any recorded information (including books, documents, records, and papers) relating to the property or financial affairs of a debtor, shall be fined under this title, imprisoned not more than 5 years, or both.
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To prove guilt under subsection (1), the government must show that 1) the debtor knowingly and fraudulently, 2) concealed property, 3) from the trustee or creditors; 4) that belonged to the estate. *See United States v. Wagner*, 382 F.3d 598, 607 (6th Cir. 2004) (holding that a debtor violated subsection (1) when he changed the locks on three houses, thereby "concealing" the value of the properties from the trustee). In *Wagner*, the Sixth Circuit adopted a broad definition of "conceal," to cover "'*any* type of effort to keep assets from being equitably distributed among creditors.'" *Id.* at 608 (quoting *United States v. Goodstein*, 883 F.2d 1362, 1369 (7th Cir. 1989)).

In *United States v. Kurleman*, 736 F.3d 439, 452 (6th Cir. 2013), the Sixth Circuit held that a debtor could be convicted of violating both subsections (1) and (3) for the same conduct, because each requires the government to establish different elements.