<u>EXEMPTION ISSUES UNDER BAPCPA</u>

<u>522(b)(3) - The 730 Day Residency Requirement</u>

522(b)(3) provides that a debtor may exempt property under state or local law at the place "in which the debtor's domicile has been located for the 730 days immediately preceding the date of filing of the petition, or if the debtor's domicile has not been located in a single State for such 730-day period, the place in which the debtor's domicile was located for 180 days immediately preceding the 730-day period, or for a longer portion of such 180-day period than in any other place."

- 36 states have opted out - federal exemptions (and the wildcard) are ***not*** allowed.

- What happens to a debtor who moved to Texas in the last 730 days from an opt out state (ie, Nebraska) and bought a house here?

    -The debtor is prohibited from taking the Texas exemptions, so the Texas homestead is not available.
    -The Nebraska homestead exemption doesn't apply to dirt located in Texas.
    -Nebraska has opted out so the debtor can't use federal exemptions.

    See the savings clause at the end of 522(b)(3) - "If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt property that is specified under subsection (d)."

There are no post-BAPCPA cases which have addressed extraterritorial application of homestead exemptions. There are a few pre-BAPCPA cases, but do not get in a big hurry to rely on any of them. See <u>In re Drenttel</u>, 403 F.3d 611 (8th Cir.2005) which held that the debtors could claim the Minnesota homestead exemption for real property located in Arizona. See, also, <u>In re Arrol</u>, 170 F.3d 934 (9th Cir.1999) which held that the debtor could claim the California homestead exemption for real property located in Michigan.

Judge Gargotta addressed this issue in <u>In re Camp</u>, 396 B.R. 194 (Bankr.W.D.Tex.2008), in a case where a debtor moved to Texas from Florida within the 730 day period prior to filing and resided in Florida during the 180 period preceding the 730 day period. Judge Gargotta held that notwithstanding the language in the Florida statute which limits its application to "residents" of the state of Florida, it was Congress' intent when they passed BAPCPA that the opt out provision in state laws be preempted by the choice of law provision in 522(b)(3). In effect, state law becomes part of federal law by mandate of BAPCPA. Judge Gargotta was reversed by Judge Yeakel citing <u>In re Stephens</u>, 402 .B.R. 1 (10th Cir.BAP 2009). That decision is currently on appeal to the Fifth Circuit.

I think this is one of those cases where Judge Gargotta reached the result Congress intended, but not

the result Congress provided for. When Congress said you have to use the exemptions from the state you came from, that should mean that you use those exemptions with any conditions and restrictions they may contain, i.e., residency. If Congress intended to abrogate some of those conditions and restrictions, they should have more clearly said so. (One has to assume this is simply one of those issues that nobody thought through all the way when the legislation was being drafted.) See, for comparison, In re Zibman, 268 F.3d 298 (5th Cir.2001) which rejected the so-called snapshot rule for exemptions and held that courts must look to all the law and facts that exist when the case is filed. In that case, the debtors sold their homestead prior to filing, were holding the proceeds on the date of filing, and failed to reinvest the proceeds in a new homestead within six months and lost their exemption with respect to the proceeds.

Judge Lief Clark has also addressed this issue in a case where a debtor moved to Texas from Florida within the 730 day period prior to filing and resided in Florida during the 180 day period preceding the 730 day period. Judge Clark held that because the Florida exemptions are only available to "residents" of the state of Florida and the debtor was a former resident of the state of Florida on the date of filing, the debtor was entitled to use federal exemptions because the statute does not bar non-residents from using the federal exemptions. In re Battle, 06-50454-LMC-13 (W.D.Tex.12/12/06). (The author would note that Judge Clark made no mention of the savings clause. Not surprising in this case as his interpretation of Florida law made resort to the savings clause unnecessary.)

In In re Smith, 2009 WL 1109831 (Bankr.S.D.Tex.2009) Judge Schmidt ruled that a debtor who was domiciled in Texas for less than 730 days and was domiciled in Louisiana for the 180 day period preceding the 730 day period was limited to Louisiana exemptions (Louisiana is an opt out state) following Judge Gargotta's opinion in Camp and allowed the debtors to claim a $25,000 exemption on Texas property under Louisiana law. In In re Garrett, 429 B.R. 220 (Bankr.S.D.Tex.2010), Judge Isgur held that debtors who had moved to Texas from North Carolina were required to use North Carolina exemptions, notwithstanding that North Carolina exemption statute prohibited extra-territorial application of the homestead exemption, and that North Carolina statute was pre-empted to the extent it conflicted with the Bankruptcy Code. (He also held that the savings clause which says if you don't get any exemptions, you fall back to federal, is only to be used as a "last resort.") As a result, debtors were limited to $70,000 exemption of Texas residence under North Carolina statute. (Pending the outcome of the appeal in Camp, these opinions are at least suspect.)

In a case going the other way, an Oregon bankruptcy court held that an Oregon debtor could not claim a homestead exemption for property located in Oregon under Texas law because the Texas exemption statute specifically provides that it applies to "homesteads in this state" and this is part of the statute itself, not a choice of law provision. (The same analysis applies with respect to most state exemption statutes. See, e.g., Florida's statute which says a "resident" of the state of Florida may claim specific exemptions.) In re Tate, 2007 WL 81835 (Bankr.D.Or.2007)

There has been a rush of case law on this issue, most from or involving Florida. See, In re West, 2006 WL 2848140 (Bankr.M.D.Fla.2006); In re Jewell, 347 B.R. 120 (Bankr.W.D.N.Y.2006); In re Crandall, 346 B.R. 220 (Bankr.M.D.Fla.2006); and In re Underwood, 342 B.R. 358 (Bankr.N.D.Fla.2006). In West, the court held that a debtor who moved from Indiana to Florida

within the 730 day period was not entitled to Indiana exemptions which were only available to residents of Indiana, was not entitled to Florida exemptions because he had not been a resident for the required 730 period, so was entitled to federal exemptions under 522(b)(3) even though Florida is an opt out state. In Jewell, the court held that debtors who had moved from Colorado to New York within the 730 day period were not entitled to Colorado exemptions which were only available to residents of Indiana, were not entitled to New York exemptions because they had not been residents for the required 730 day period, were entitled to federal exemptions under 522(b)(3) even though both Colorado and New York are opt out states. Crandall and Underwood reached the same result as West, although different states were involved. (New York to Florida in Crandall and Colorado to Florida in Underwood.)

In an odd twist involving a couple who filed jointly in North Carolina, the husband was required to take state exemptions and the wife was required to take federal exemptions, notwithstanding 522(b)(1) because in this case the debtors were required to use those exemptions, there was no "election." (Husband had been a resident of North Carolina for more than 730 days, but wife had moved to North Carolina from Florida within 730 days and Florida restricts use of its exemptions to residents so she defaulted to federal.) In re Connor, 419 B.R. 304 (Bankr.E.D.N.C.2009).

522(n) - The $1,171,650 IRA Cap

Just for grins - 522(n) limits a debtor's interest in an IRA (*not including rollovers from specified accounts*) to $1,171,650 [but remember 522(m) - each debtor in a joint case gets their own exemptions] with a striking exception: "such amount may be *increased* if the interests of justice so require." I am trying to formulate the argument I am going to make to Judge Gargotta on this one. "My client needs to keep more than $1 million in his IRA because .....?????...... he needs the extra money to keep up his country club membership. Or maybe he is really sick and it is going to be really expensive." (That is about the only one I could come up with that might work. I don't see most judges agreeing with that.)

Much to my surprise, there is actually a case on 522(n), but the only issue in that case was whether the 401(k) rollover exception means what it says. (The debtor was claiming two IRAs valued at $1,117,375 as exempt when the statutory limit was $1,095,000.) The court concluded that the "without regard to amounts attributable to rollover contributions" under specified IRC sections means what it says and that "without regard to" means "without counting." In re Dixon, 2009 WL 5110664 (Bankr.N.D.Ca.2009).

522(o) - Use of Proceeds of Fraudulent Asset Transfers to Acquire Homestead Interest

522(o) provides the value of an interest in "real or personal property that the debtor or a dependent of the debtor uses as a residence" or "real or personal property that the debtor or a dependent of the debtor claims as a homestead" shall be reduced "to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10-year period ending on the date of filing of the petition with the intent to hinder, delay or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the

debtor has held the property so disposed of."

This is one of those sections that went in to effect in April, 2005 rather than October. The first case to address this provision was <u>In re Maronde</u>, 332 B.R. 593 (Bankr.D.Minn.2005). The debtor filed Chapter 13 on April 20, 2005. In June, 2003 the debtor purchased a home for $334,900 with a lien of $200,000 and the balance from the proceeds of the sale of a prior home. In October, 2003 the debtor took out a home equity line of credit. In December, 2005, the debtor drew $43,335 on the line which he used to purchase a truck and trailer. In February, 2004 the debtor drew down the remaining $5,888 on the line. Between November, 2004 and February, 2005 the debtor opened several new credit card accounts. Based upon the advice of a friend (not a lawyer), the debtor opened the credit card accounts with the intention of paying secured debt and then settling the new unsecured debt for less than the full amount. After meeting with an attorney in March, 2005, the debtor sold the trailer for cash and traded in the truck and received $13,708 back as part of the deal. On April 11, 2005 the debtor used $19,130 to pay the equity line to zero. None of these transactions were disclosed on the statement of financial affairs.

In analyzing the application of Sec. 522(o), the court first notes that Congress provided no definition for "intent to hinder, delay, or defraud a creditor." The court went on to note that the language is similar if not identical to Sec. 548(a)(1) and 727(a)(2) and that it is a "elemental" that similar words within a statutory body should be interpreted with the same meaning. The court also noted that since direct evidence of wrongful intent is rare, the court may infer intent from badges of fraud which the court enumerated as follows:

1. The transfer or obligation was to an insider;
2. The debtor retained possession or control of the property transferred after the transfer;
3. The transfer or obligation was disclosed or concealed;
4. Before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;
5. The transfer was of substantially all the debtor's assets;
6. The debtor absconded;
7. The debtor removed or concealed assets;
8. The value of the consideration received by the debtor was not reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;
9. The debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;
10. The transfer occurred shortly before or shortly after a substantial debt was incurred; and
11. The debtor transferred the essential assets of the business to a leinor who transferred the assets to an insider of the debtor.

In this case, the debtor's stated plan was to obtain new credit card debt in order to pay down the secured debt on his homestead. When that plan failed because the credit card companies cut him off, the debtor went to Plan B which was to sell his non-exempt trailer and partially exempt truck to pay off his homestead line of credit, all within days of filing of the case. The court held that the debtor's

conversion of nonexempt assets was "part and parcel of an overall scheme to defraud his creditors" so his homestead exemption was reduced by the amount of the proceeds of the truck and trailer he used to pay down his homestead.

Maronde was followed soon after by In re Lacounte, 342 B.R. 809 (Bankr.D.Mont.2005). In that case Mrs. Lacounte had a gambling problem (which she claimed resulted from job pressures) and over a two year period she accumulated $180,000 in unsecured debt. Mr. Lacounte apparently only learned of her debts when the house of cards collapsed in August, 2004. At that time, the debtors' daughter sought advice from two bankruptcy attorneys. As a result of that advice, the debtors sold three vehicles and a future interest in his mother's farm. In January, 2005 the debtors sold assets generating $42,800 and used $42,500 to pay down the debt on their homestead. Finally, in April, 2005, Mrs. Lacounte transferred her undivided interest in her mother's home back to her mother because of the risk that she might lose it as a result of the debtors' bankruptcy. A Chapter 7 petition was filed on April 21, 2005.

The Lacounte court went through much the same analysis as the Maronde court. The court reached much the same result based in part upon Mr. Lacounte's testimony that he was angry with the financial situation he found himself in through no fault of his own and that he could not justify giving up assets he had worked so hard for when he could simply sell those assets and apply the proceeds to his home loan.

Maronde and Lacounte have been followed in subsequent cases which have essentially adopted the same analysis. See, In re Agnew, 355 B.R. 276 (Bankr.D.Kan.2006) and In re Lyons, 355 B.R. 387 (Bankr.D.Mass.2006). In Agnew, the debtor acquired an interest in a homestead from his mother in exchange for non-exempt real property and all of debtor's farm equipment which was only partially exempt. Although the transfer occurred only five days prior to the debtors' Chapter 7 filing, the court declined to limit the debtors' homestead exemption because the uncontroverted testimony was that the transaction had been planned for some time for estate planning reasons and that the bankruptcy only influenced the timing of the transaction, not the substance of the transaction. The court also found it significant that the transfers in question were for reasonably equivalent value. (Agnew also includes a laundry list of potential badges of fraud.)

I would note that although none of the cases which provide a list of factors includes when the debtor first obtained legal advice related to the filing of a bankruptcy, but all of these courts mention the issue in analyzing the debtor's intent. (I can say from personal experience that most judges want to know the answer to this question.)

Lyons involves a much easier question. In that case, the debtor purchased a homestead in April 1997, but only filed a homestead designation on August, 2004, two weeks after a creditor was granted an attachment on the property. The court concluded that the filing of the homestead designation did not fall within Sec. 522(o) as no property was disposed of by the debtor. (The creditor also argued that the debtor should be prohibited from claiming the homestead exemption because the debtor acquired the homestead interest within 1215 days of the filing. The court rejected this argument as well, because the filing of the homestead was not an acquisition of an interest in

the homestead property.)

Texas cases which have addressed 522(0) have generally followed the analysis in Maronde and Lacounte and looked to cases under 727(a)(2) and 548(a)(1) for what constitutes intent to hinder, delay or defraud creditors. In In re Fehmel, 2008 WL 2151797 (Bankr.W.D.Tex.2008) Judge Monroe held that a debtor's use of a corporate line of credit to make a down payment on the purchase of a personal homestead was not fraudulent as to creditors (and in particular to the bank that issued the line of credit) because although the loan officers "never meant" for the corporate line of credit to be used for personal expenses, there was apparently no contractual restriction prohibiting the debtor from doing so. Judge Monroe looked to the Texas Uniform Fraudulent Transfer Act, Tex. Bus. & Com. Code Sec. 24.001, et seq. for its list of badges of fraud and although several of the enumerated badges were present, the debtor's business was profitable when the transfer was made, they were not insolvent at the time, and there was no pattern of sharp dealing so the court found that the debtors did not intend to hinder, delay of defraud. (Fehmel was appealed, but only on 522(p) as discussed below.)

Judge Bohm has written what are unquestionably the most detailed cases on 522(o). The first case was In re Sissom, 366 B.R. 677 (Bankr.S.D.Tex.2007) in which he sustained a 522(o) objection in part and overruled it in part. The debtor entered into a contract to sell non-exempt stock in a company he owned in February, 2006 for $200,000 and obtained a loan from the buyer for $50,000. Although the stock sale was by the debtor in his individual capacity, the debtor deposited $100,000 into the account of another company he owned and deposited another $50,000 into a sole management account of the debtor's spouse. In April, 2006, Ms. Sissom purchased a new homestead and paid $61,540.99 toward the purchase price in the form of two cashier's checks for $50,000 and $11,540.99. A few days later, $75,000 from the sale of their prior home was wired to her account.

Judge Bohm identified four elements which must be proven to satisfy 522(o):

1. The debtor disposed of property within 10 years preceding the bankruptcy filing;
2. The property the debtor disposed of was nonexempt;
3. Some of the proceeds from the sale of the nonexempt property were used to buy a new homestead, improve an existing homestead, or reduce the debt associated with an existing homestead, or, alternatively, to buy a new principal residence used by dependents of the debtor, or reduce the debt associated with a pricipal residence used by dependents of the debtor; and
4. The debtor disposed of the nonexempt property with the intent to hinder, delay or defraud a creditor.

Judge Bohm held that the creditor satisfied the first two elements, as the debtor disposed of the nonexempt stock within ten years prior to filing, and partially satisfied the third element at least with respect to the $50,000 payment which was traceable to the stock sale. With respect to the intent issue, Judge Bohm looked to the Texas Uniform Fraudulent Transfer Act, Tex. Bus. & Com. Code Sec. 24.001, et seq. for its list of badges of fraud and found that eleven of the thirteen enumerated badges were present. The debtor asserted several defenses which were dubious at best (and primarily

of interest for entertainment purposes, i.e., that the nonexempt cash became exempt when it was commingled with exempt cash. Really?) In order to balance the interest of the debtor to avoid a forced sale of the homestead and the interest of the trustee in liquidating the nonexempt asset, Judge Bohm gave the debtor 120 days to pay the $50,000 to the trustee.

Judge Bohm's second 522(o) case was In re Presto, 376 B.R. 554 (Bankr.S.D.Tex.2007). Mr. Presto had the unfortunate distinction of being a vice-president at Enron North America, a subsidiary of Enron Corp. He was also one of several executives to receive a "lucrative" bonus payment several weeks prior to Enron's Chapter 11 filing. (In his case, $2,000,000.) Between 2001, when he recived the bonus, and 2005, when the Enron bankruptcy court ruled the bonuses were fraudulent transfers, Mr. Presto spent or lost the bonus money so his only remaining asset was his $500,000+ homestead. The Official Employment-Related Issues Committee of Enron Corp. (sure sounds official) objected to his homestead claim. On May 18, 2006, the debtor sold his prior homestead and netted $675,000. On the same day, he purchased his new homestead for $521,800 cash. On July 31, 2006, he filed Chapter 7. In the meantime, he made $119,102 in improvements to the new homestead (including $72,000 on a pool), which he valued at $550,000 in his schedules. The Committee offered no evidence of what the value of the property was or what portion of the value was attributable to the improvements, so Judge Bohm was essentially left with the debtor's valuation of $550,000 and held that $28,200 was nonexempt under 522(o). But see the analysis of 522(p) below.

Assuming Texas bankruptcy courts will uniformly follow the same general analysis as Maronde and Lacounte, attorneys should be familiar with Fifth Circuit case law interpreting 548(a)(1) and 727(a)(2). The leading Fifth Circuit case interpreting 548(a)(1) is In re Moody, 862 F.2d 1194 (5th Cir.1989). You might want to look at the district court opinion, too, which is found at 77 B.R. 566 (D.S.D.Tex.1987). With respect to 727(a)(2), see In re Reed, 700 F.2d 986 (5th Cir. 1983); In re Bowyer, 932 F.2d 1100 (5th Cir.1991); and In re Bowyer, 916 F.2d 1056 (5th Cir.1990). At the bankruptcy court level, see In re Rothrock, 96 B.R. 666 (Bankr.N.D.Tex.1989); In re Womble, 289 B.R. 836 (Bankr.N.D.Tex.2003); In re Lee, 309 B.R. 468 (Bankr.N.D.Tex.2004); and In re Jones, 327 B.R. 297 (Bankr.S.D.Tex.2005).

522(p) - Cap on Homesteads Acquired Within 1215 Days of Filing

522(p) provides that a debtor who elects to use state exemptions "may not exempt any amount of interest that was acquired by the debtor during the 1215-day period preceding the date of the filing of the petition that exceeds in the aggregate $146,450 in value in

> (A) real or personal property that the debtor or a dependent of the debtor uses as a residence;
>
> (B) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;
>
> (C) a burial plot for the debtor or a dependent of the debtor; or
>
> (D) real or personal property that the debtor or dependent of the debtor claims as a

homestead."

There are two statutory exceptions listed in 522(p)(2):

(A) The limitation does not apply "...to an exemption claimed... by a family farmer for the principal residence of such farmer."

(B) The limitation does not include "...any interest transferred from a debtor's previous principal residence (which was acquired prior to the beginning of such 1215-day period) into the debtor's current principal residence, if the debtor's previous and current residences are located in the same State."

One of the issues courts have grappled with is what constitutes "acquiring" an "interest" in a homestead. See, e..g., In re Rogers, 354 B.R. 792 (D.N.D.Tex.2006). In that case the debtor inherited a tract of land in 1994. She subsequently married, she and her husband purchased a home, and then they divorced in 2004. After the divorce, she moved to the inherited tract. She then filed a Chapter 7 in September, 2005 and claimed the property valued at $359,000 as her homestead. A creditor objected because the property had not been her homestead for 1215 days prior to filing. The bankruptcy court denied the objection and the district court affirmed because it interpreted the meaning of an "interest" as being an ownership interest in the property and does not encompass the classification of the property as a homestead. Because it resolved the case on that issue, the court declined to reach the issue of what "acquire" means. Rogers was affirmed at both the district court In re Rogers, 354 B.R. 792 (D.W.D.Tex.2006) , and Fifth Circuit. In re Rogers, 513 F.3d 212 (5th Cir.2008). See, also, In re Lyons, 355 B.R. 387 (Bankr.D.Mass.2006), an early and oft cited case which reached the same result.

The Rogers court relied in part on In re Rasmussen, 349 B.R. 747 (Bankr.M.D.Fla.2006) which addressed the issue of whether appreciation in value of the property during the 1215 day period constituted an interest in the property. In that case, the debtors purchased the property in June, 2002 for $350,000 and filed Chapter 7 in September, 2006 - 1,210 days later. (Apparently, their bankruptcy attorney couldn't count or he would have waited six more days to file.) By the time of the filing, the house was worth $750,000, but was subject to a lien of $575,00 leaving equity of $175,000. The trustee contended that the joint debtors were only entitled to an exemption of $125,000 under 522(p) and that any appreciation in value of the property during the 1215 day period was an interest acquired. The court rejected both of these arguments. First, 522(m) provides that "this section shall apply separately with respect to each debtor in a joint case." The trustee contended that the $125,000 cap applied to the homestead rather than the debtors, but the court rejected that argument.

Second, the court held that the acquisition of equity during the 1215 day period was the acquisition of an interest in the property, but distinguished equity obtained by "active conduct on the part of the debtor" (making a down payment or paying down the mortgage) and passive conduct (appreciation) and held that the "by the debtor" after "acquires" requires active conduct by the debtor so appreciation in value is not subject to the $125,000 cap. See, also, In re Sainlar, 344 B.R. 669 (Bankr.M.D.Fla.2006) which held that equity gained during the 1215 day period, whether as a result

of appreciation or a decrease in secured debt, is not acquired and is not subject to the cap.

Judge Bohm addressed the acquisition issue in In re Presto, discussed above under 522(o). The 522 issue arose because the debtor acquired his current homestead within the 1215 day period and had rolled the prior equity from another homestead located in Texas. The wrinkle is that he had acquired his ex-wife's ½ community property interest in the prior homestead incident to a divorce within the 1215 day period. Judge Bohm held that the conveyance from her to him by Special Warranty Deed transferred an "interest" which he "acquired" during the 1215 day period. The court did hold, however, that his community interest in the property was acquired more than 1215 days prior to filing, so his one-half interest was not subject to the $125,000 cap. Judge Bohm then undertakes a detailed analysis of what portion of the total value of the property, if any, is subject to the cap. (Judge Bohm even admits that he had to "fashion a value from circumstantial evidence in the record" and that he had "no better evidence " of the amount of the lien on the property than the balance at the time of the divorce some months ago. Essentially, this was all an educated guess.) At the end of the analysis, Judg Bohm concluded that the final nonexempt portion of the homestead pursuant to 522(p) was $105,000.

Judge Hale in In re Blair, 334 B.R. 374 (Bankr.N.D.Tex.2005) distinguished between acquiring "equity" in a home and acquiring "title" (the title theory versus the equity theory) and opined that one does not actually "acquire" equity, one acquires title. He held that increased equity "acquired" by paying down the mortgage during the 1215 day period is not subject to the cap.

Contrast Rogers with In re Greene, 346 B.R. 835 (Bankr.D.Nev.2006), which holds that under Nevada law, a homestead interest is a separate property interest from fee title and that because the debtor established his homestead on the property within the 1215 day period, it was subject to the cap. In that case the debtor purchased a 67 acre tract of unimproved land in 1994. In August, 2004 he moved a travel trailer onto the property and filed a homestead declaration and filed a Chapter 13 two weeks later, having never occupied the property. A creditor objected to the claimed exemption and the debtor voluntarily dismissed the case in February, 2005. In October, 2005 he filed a Chapter 7 and the same creditor objected to the homestead exemption. The court held that because he was actually occupying the property, he was entitled to the homestead exemption, but that because he acquired the homestead interest (as opposed to fee title) within the 1215 day period, his homestead was capped at $125,000. This decision turns on interpretation of Nevada law and is included here as a reminder that cases may have completely different results if the decision is based on state law, so don't assume anything from reading cases from other states.

There is one twist on appreciation in value during the 1215 day period. In In re Fehmel, 2008 WL 2151797 (Bankr.W,D.Tex.2008), reconsideration denied, 2008 WL 2736890 (Bankr.W.D.Tex.2008), Judge Monroe was faced with a situation where the debtors acquired a piece of property during the 1215 day period and made substantial improvements to the property, i.e., "extensively remodeled the main house ... built a 50' by 50' barn, 1,620 sq. ft. enclosed workshop and an 1,100 sq. ft. guest apartment with full kitchen and bath." The property was purchased for $375,000 in May, 2005 and was valued at $700,000 when the Chapter 7 was filed in August, 2007. Adopting the "title theory", Judge Monroe held that if a homestead is acquired within the 1215 day

period, the cap applies unless one of the two statutory exceptions applies. Any increase in equity during the 1215 day period is subject to the cap, regardless of the source. (i.e., market appreciation or improvements.)

Judge Monroe also addressed the issue of whether the debtors could claim the benefit of the rollover exception. In this case, the debtors acquired their new homestead prior to selling their old homestead. When they sold the old homestead, they deposited the proceeds in a corporate bank account, out of which some of the improvements to the new homestead were made. Judge Monroe first held that the debtors had the burden of tracing the proceeds of the old homestead into the new homestead and because the funds were commingled with other monies, they debtors were unable to meet that burden. More importantly, Judge Monroe held that it is "horn book law" that if a debtor purchases a new homestead, any remaining proceeds of a prior homestead are instantly rendered nonexempt. Because the debtors acquired the new homestead prior to selling the old homestead, any proceeds ultimately received from the old homestead were nonexempt.

On appeal, the debtors argued that Judge Monroe should have used the "equity theory" rather than the title theory and focused their argument more on the effect of "market forces" which increased the value of their homestead. The district court declined to expressly adopt either the title theory or the equity theory, concluding that Judge Monroe's decision could be upheld under either theory because the increase in value of the property (from $370,000 to $700,000) was "more likely than not" from the $200,000+ in improvements made to the property during the 1215 day period. In re Fehmel, Civil Action 6:08-cv-00215-WSS (D.W.D.Tex.2008).

The Fifth Circuit "agreed" with the debtors that the value of the improvements and market forces acted "synergistically" to increase its value more than the cost of the improvements, but that once the creditor met its burden of showing that the exemption is improperly claimed, the burden then shifts to the debtor to show by "unequivocal evidence" what amount was attributable to market forces and they failed, in this case, to meet that burden. In re Fehmel, 2010 WL 1287618 (5th Cir.2010).

Contrast In re Anderson, 374 B.R. 848 (Bankr.D.Kan.2007), which adopted the title theory and held that the cap does not apply to a homestead acquired more than 1215 days prior to filing, even if the debtor substantially increases his equity during the 1215 day period. In that case, the debtor acquired his homestead in 1998 for $350,000. In July 2005, the debtor paid $240,000 to reduce his mortgage balance, then filed Chapter 7 three months later. (Why this isn't a 522(o) case rather than a 522(p) case is beyond me.)

Judge Paul got the dubious opportunity to address one of the goofiest 522(p) cases. (Actually, we aren't sure it's a 522(p) case because the objection did not state a statutory basis. Judge Paul guessed, and we are simply adopting her guess.) In In re Fadhli, 2009 WL 2461037 (Bankr.S.D.Tex.2009), a creditor objected to the debtors' homestead exemption because it was acquired within 1215 days and it exceeds the value of the debtors' prior homestead. A few small problems, however. The debtors listed the value of the property as $175,000 with a lien of $169,649, so they only had equity of $5,350. The debtors also elected to use federal exemptions. The 522(p)

cap applies only if the debtor elects to use state exemptions. (Oops.) In addition, the cap at the time was $136,875, well above the value of the equity. (Apparently, the creditor's argument was based upon the value of the property, not the value of the equity. Oops.) Not surprisingly, debtor wins this one.

Judge Hale got the dubious opportunity to address one of the more bizarre homestead cap cases in In Re Kim, Adv. 08-03440 (Bankr.N.D.Tex.2009). In that case Mr. Kim filed a Chapter 7 and claimed his homestead valued at $1,127,880 as fully exempt. A creditor objected and Judge Hale ruled that his homestead claim was capped at $136,875 pursuant to 522(p), but left open the issue of whether and to what extent Mrs. Kim, who did not file, was entitled to a homestead exemption. Mr. Kim then sued Mrs. Kim seeking declaratory relief to determine what interest his bankruptcy estate had in the property and to determine her rights to the property. (The creditor intervened.) Judge Hale ruled that because the property was property of the estate, the Bankruptcy Code determines which exemptions are available and that the exemption under the Code was limited to $136,875. Judge Hale then ruled that only a debtor is entitled to claim exemptions, relying in large part on In re McCombs, 2007 WL 4411909 (Bankr.S.D.Tex.2007). Since the case was before the court on cross motions for summary judgment, Judge Hale declined to rule on whether Mrs. Kim had a separate property interest or resulting trust interest based upon her *alleged* payment of part of the purchase price with her separate property.

Judge Monroe got the scary case for debtor's attorneys. In re Green, 2007 WL 1093791 (Bankr.W.D.Tex. 2007), new trial denied, 2007 WL1308311, involved an involuntary Chapter 7 filed by the debtor wife's aunt who held a $550,000 judgment against her niece and the niece's husband. In a prior Chapter 7, the aunt objected to the debtors' discharge and Judge Monroe found violations of 727(a)(2)(A) and 727(a)(4)(A). This involuntary case was filed by the aunt to take advantage of the 522(p) cap on homestead. In 2004, the debtors sold their home in California, liquidated an investment account netting "$300,000 plus", and along with spare change of $60,000 they had lying around, purchased a homestead in Texas for $1,440,000 cash. (The only issue addressed in this opinion was how many creditors each debtor had and whether the sole petitioning creditor could file an involuntary. If you are ever inclined to file an involuntary, don't; but if you feel like you just absolutely have to, read this opinion first.) This is the scary case for debtor's attorneys because it raises the ugly question of whether creditors can effectively use involuntary cases as a means to attack homesteads, even where there was no "bad" conduct on the part of the debtor.

Judge Bohm (in a rare fit of brevity) took only ten pages to dispose of a similar issue in McCombs. In that case, the debtor and his spouse were estranged. He filed a Chapter 7. The homestead was sold and the wife, the IRS and a judgment creditor all took the position that they had first claim to the proceeds in excess of the $125,000 cap. The wife was claiming that they had agreed to a partition of the property and she was entitled to all of the proceeds, or that it was gift from him to her, or that it an agreement incident to a divorce, or that her homestead rights trumped everyone else's claim under state law. Judge Bohm ruled that the "partition" was invalid under Texas law. (And questioned the veracity of the partition because a different version of the document appeared half way through the litigation. Don't you hate it when that happens?) He also ruled that the partition agreement did

not evidence a gift and that it was not an agreement incident to a divorce for the apparently not obvious enough reason that there was no divorce. Finally, he ruled that only a debtor may claim exemptions, otherwise any couple could do what this couple did: have only one spouse file and let the non-filing spouse avoid the cap of 522(p), clearly not the result Congress intended.

There have been several unreported cases in Texas involving the 522(p) cap issue, many of which have involved unfortunate fact patterns in which the debtor acquired the money to acquire the homestead as a result of a gift from parents or as a result of an inheritance. The source of the funds to acquire the homestead is not relevant.

Be very careful about older clients who have a valuable homestead with significant equity. I have seen several clients who had transferred their homestead into one of the those "avoid probate" trusts. The problem is the debtor no longer owns the property - the trust does. Arguably, the debtor is not entitled to claim a homestead exemption in a trust asset. My practice has always been to have the client revoke the trust and deed the property back to themselves individually. I am concerned that under the new law, that constitutes the "acquiring" of an interest in the property. Judge Monroe ruled in a pre-BAPCPA case that the transfer into the trust had no legal effect, so the debtor could still claim the homestead. That ruling was appealed and affirmed at the district court level. In re Basedow, Case 1:06-cv-002420LY (D.W.D.Tex.2006). Judge Yeakel's decison was appealed to the Fifth Circuit, but that appeal was dismissed.

See, for comparison, In re Khan, 375 B.R. 5 (1st Cir. BAP 2007), which affirmed a bankruptcy court opinion that a transfer from a self settled trust back to an individual debtor was the acquisition of an interest in property. (This is the scary result I am worried about.) See, also, In re Buonopane, 2006 WL 2347746 (Bankr.M.D.Fla.2006) which holds that under Florida law, any beneficial ownership interest (i.e., under a trust) would support a claim of homestead, but since the debtor never used the property as a primary residence until within the 1215 day period, his homestead was capped at $125,000.

522(q) - The Catch All Cap

522(q)(1) limits a debtors homestead to $146,450 if -

(A) the court determines, after notice and a hearing, that the debtor has been convicted of a felony (as defined in section 3156 of title 18), which under the circumstances, demonstrates that the filing of the case was an abuse of the provision of this tile; or

(B) the debtor owes a debt arising from -

(i) any violation of the Federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934), and State securities laws, or any regulation or order issued under Federal securities laws or State securities laws;

(ii) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 11934 or under section 6 of the Securities Act of 1933;

(iii) any civil remedy under section 1964 of title 18; or

(iv) any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years.

522(q)(2) provides that paragraph 1 shall not apply "to the extent the amount of an interest in property ... is reasonably necessary for the support of the debtor and any dependent of the debtor."

There actually are a few cases under this section. Judge Bohm also ruled on 522(q) claims in In re Presto, discussed previously under 522(o) and 522(p). In this case, the debtor received a tax refund check payable to both him and his ex-wife pursuant to an amended tax return he filed and signed for her. He then cashed the refund check. He later notified her of its receipt, but tendered payments rather than tendering the full amount due her. The Committee, which had nothing to do with the issue, objected under 522(q)(1)(B)(ii) because the debtor owed his ex-wife a fiduciary duty under their divorce decree and his conduct constituted fraud, deceit or manipulation with respect to her. Judge Bohm sustained that objection and limited the debtor's homestead exemption under 522(q) to $125,000.

See, also, In re Larson, 513 F.3d 325 (1st Cir.2008), which held that a state court's finding that a debtor was criminally liable for negligent vehicular homicide triggered the cap under 522(q)(1)(B)(iv). In that case, the debtor admitted the facts to the court which made the determination and continued the case for a year. (This is apparently the Massachusetts form of deferred adjudication.) No conviction was entered. Ms. Larson admitted that she was attempting to take a shortcut through a parking lot and turned in front of a motorcycle striking the motorcycle and causing the death of one of the riders. This was not a drunk driving case. This was a "I just didn't see them" case. The bankruptcy court held that the statute, by its terms, applies not only to intentional crimes, but crimes of negligence as well, and that the language of the statute does not require a conviction.

Contrast In re Burns, 395 B.R. 756 (Bankr.M.D.Fla.2008), which was a case where the debtors' dog ran out into the street and caused a motorcyclist to crash, resulting in serious injury. (The dog died , too.) The court held that the creditor must prove "highly unreasonable conduct, involving an extreme departure from ordinary care, in a situation where a high degree of danger is present." The court rejected the contention that the accident was the result of reckless misconduct where the dog in question had no prior history of chasing motorcycles or aggressive behavior.