

CONSUMER BANKRUPTCY

Debtor Amends Exemptions to Protect Homestead 19 Years Later

By **Craig D. Robins**

Since the Supreme Court decided *Law v. Siegel* in 2014, there has been a trend in which bankruptcy courts have become increasingly permissive towards debtors' efforts to use or amend their exemptions.

In *Siegel*, 134 S. Ct. 1188 (2014), the Supreme Court permitted the debtor to use the homestead exemption, despite the debtor having fabricated a lien on his home in utmost bad faith, and despite the Chapter 7 trustee having spent over \$500,000 investigating and litigating the issues surrounding the fabricated lien. The

Supreme Court held that bankruptcy courts may not override explicit mandates of the Bankruptcy Code, in particular, a debtor's rights to use exemptions. Thus, the Supreme Court determined that the bankruptcy court cannot deny an exemption based on bad conduct.

Since that decision, bankruptcy judges have uniformly held that the bankruptcy courts lack the power to disallow exemptions on the grounds of the debtor's fraud or bad faith. Generally, Bankruptcy Rule 1009(a)



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permits debtors to amend their schedules, including Schedule C – the exemption schedule — at any time while their Chapter 7 case is pending.

A recent decision, however, from Judge Carl L. Bucki, sitting in the Western District of New York, explored an extreme situation: whether to permit a debtor to amend her exemptions 19 years after her case was closed. *In re Muscato* (Bankr. W.D.N.Y. Case No. 98-14386, March 22, 2018).

In *Muscato*, the debtor had apparently

engaged in elder law planning, and deeded remainderman interests to her children in 1992 while retaining a life estate. When she filed a typical consumer Chapter 7 case in 1998, she failed to schedule her life estate as an asset. As she did not list this real estate asset, she did not take the homestead exemption. The trustee routinely closed the case as a no-asset case.

Fast forward to 2016. The debtor and her children decided to sell the property. However, the title search revealed the bankruptcy.

The exception raised by the title company
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was that even though trustees are held to abandon assets that they do not administer, when a debtor fails to disclose the asset, there is no abandonment as a matter of law. (This concept has been discussed several times in this column especially with regard to debtors who failed to disclose personal injury suits and how such debtors sometimes lose the opportunity to proceed with the suit as they technically do not have standing).

Thus, the debtor's interest in the property remained an asset of the bankruptcy estate. To resolve the title objection and proceed to closing, the debtor and her children worked out an agreement with the title company in which they would hold the entire net proceeds in escrow until such time as they could resolve the interest of the bankruptcy estate.

Almost a year later, the debtor moved to reopen her case, which was granted. The

debtor then amended her schedules to acknowledge the ownership of the life estate interest that she held at the time of filing in 1998, and to claim a homestead exemption in that interest – some 19 years later.

The Chapter 7 trustee (now a successor trustee as the original trustee had passed away) of course raised objections. First, the trustee argued that the debtor acted in bad faith as evidenced by her intentional failure to disclose a known asset. Secondly, the trustee contended that the debtor's amendment, 19 years later, should be rejected as untimely and unduly prejudicial to the bankruptcy estate.

The debtor's attorney argued that the debtor may have been unfamiliar with the concept of a life tenancy and that her initial failure to disclose the life estate was an innocent mistake that should not affect her right to an exemption.

Judge Bucki determined that the central

issue involved the extent to which the court can disallow a valid but tardily claimed exemption under the standard that the Supreme Court established in *Law v. Siegel*.

The judge concluded that *Siegel* permitted debtors to freely amend their exemption schedules without limitation as to whether the case is open or reopened after closing. He noted that Code Section 350(b), which is that provision that provides for reopening a closed case, expressly acknowledges that a proper purpose of reopening is "to accord relief to the debtor," and that this includes the right to enjoy the benefit of all allowable exemptions. Judge Bucki also noted that the Federal Rules of Bankruptcy Procedure do not require that exemption schedules be amended within a specified period. Accordingly, the debtor was entitled to reopen her case and exempt her homestead 19 years after filing even though she did

not disclose her ownership interest at the time of filing.

Practical tip: Trustees often seek to administer assets that debtors were either unaware of at the time of filing or unaware of the value, such as anticipated tax refunds. In such cases, debtor's counsel should consider whether to amend the schedule of exemptions to maximize those assets which can be protected, as *Siegel* freely permits debtors to make such amendments at any time.

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