¶ 12.02 Prebankruptcy Planning—Generally

The term "prebankruptcy planning" is often a misnomer. Generically, it refers to the process whereby a debtor facing significant claims protects his assets. This process can occur regardless of whether the debtor eventually finds himself in bankruptcy, voluntarily or involuntarily. This planning must take into account the fraudulent transfer laws under state and federal law. Generally, the only type of prebankruptcy planning that does not violate the fraudulent transfer laws is converting nonexempt assets into exempt assets. Whether applicable law allows a debtor to convert nonexempt assets into exempt assets depends on a variety of factors and varies from jurisdiction to jurisdiction.

Prebankruptcy planning is often attacked on the following grounds:

1. The transaction constitutes a fraudulent transfer and should be set aside. From the point of view of the creditors, this is one of the best results, since it can lead to the satisfaction of their claims.
2. Denial of discharge. This is often a pyrrhic victory, since it may leave creditors with unsatisfied claims. In this regard, if property is exempt, it remains so even after bankruptcy.
3. Denial of an exemption. This is also a favorable creditor result, but is rarely invoked. Many courts have questioned whether the Bankruptcy Code authorizes such a result. Some state laws dictate this result under a variety of circumstances.
4. Dismissal of the petition, which often depends on the debtor's resources.

Although these are discrete remedies, the analytical framework to resolve these issues is often the badges of fraud under the fraudulent transfer laws. Consequently, for example, the reasoning of cases considering a denial of an exemption will be similar to cases that deal with a denial of discharge. [877] An exception to this observation is the dismissal of a bankruptcy petition, in which, among other things, the resources of the debtor are considered.

If the pre-bankruptcy planning crosses the line into criminal or fraudulent conduct, then the attorney-client privilege may be lost. [878] Further, even if such planning is not criminal or fraudulent it can trigger liability under the rules relative to Debt Relief Agencies. [879]

¶ 12.02[1] Bankruptcy and State Law Allow Prebankruptcy Planning

The legislative history accompanying **Section 522 of the Bankruptcy Code** (relating to exemptions) contemplates prebankruptcy conversion of nonexempt assets into exempt assets. It provides:

> As under current law [that is, pre-1978 law] the debtor will be permitted to convert nonexempt property into exempt property before filing a bankruptcy petition.…The practice is not fraudulent as to creditors, and permits the debtor to make full use of the exemptions to which he is entitled under the law. [880]

In accordance with this legislative history, virtually every federal circuit court has held that debtors have a right to convert nonexempt assets into exempt assets. Under both the Bankruptcy Code and state law, this conduct is not fraudulent even if the conversion occurs in contemplation of bankruptcy and even if the conduct is undertaken for the express purpose of placing those assets beyond the reach of creditors. [881] However, "there must not only be an intent to convert non-exempt assets, but also an *actual* conversion." [881.1]

The Ninth Circuit addressed the issue in *In re Stern*. [882] In this case, the debtor converted $1.4 million of a partially exempt or nonexempt individual retirement account (IRA) into an exempt IRS qualified plan on the eve of bankruptcy. (California's exemption for IRAs is subject to the reasonably necessary standard, whereas a corporate-sponsored IRS qualified plan is absolutely exempt. [883])

The bankruptcy trustee attempted to have the transfer set aside as a fraudulent transfer.

The *Stern* court noted the general rule that a conversion of nonexempt assets into exempt assets is not fraudulent per se. In ruling for the debtor on a motion for summary judgment, the court effectively held that there were no genuine issues of material facts where the "principal evidentiary inference relied upon by the Trustee is that nonexempt assets were converted to exempt assets immediately prior to bankruptcy." [884]

The majority in *Stern* so held, notwithstanding many indicia of alleged fraud cited by the vigorous dissent, as follows:

> Trustee and the dissent cite as "badges of fraud" the facts that Stern:
>
> 1. Was sued and lost the arbitration before transferring the funds to the Plan;
> 2. Testified inconsistently as to his motive for transferring the funds to the Plan;
> 3. May have, as a result of the 4.5 million dollar arbitration award levied against him, been insolvent when he made the transfer;
> 4. Transferred the funds to the Plan to benefit him and his wife;
> 5. Transferred all or substantially all of his property into the Plan; and
> 6. Retained control of the funds following the transfer. [885]

In response to this assertion, the majority in *Stern* stated:

> With the exception of the arbitration loss and the speculative insolvency, the other articulated badges of fraud are simply restatements of the accusation that Stern converted nonexempt assets into exempt assets, an accusation that cannot support a finding of fraud. [citation omitted] A similar fate awaits the claim that [the debtor] 'may have been insolvent.' We have consistently discounted speculative assertions when raised in defense of a summary judgment motion. [citation omitted] We are left with the fact that Stern lost a multimillion dollar arbitration. That single unspectacular fact does not meet a preponderance of the evidence burden of proof. [886]

The majority's assertion that the debtor's insolvency was "speculative" is surprising in the face of the debtor's bankruptcy. Similarly, it would be difficult to characterize as "unspectacular" the debtor's loss of a multimillion dollar arbitration, since it likely caused the debtor to file for bankruptcy. The *Stern* opinion would have been on firmer ground if it had pointed out that insolvency and an event such as loss of an arbitration ordinarily accompany prebankruptcy planning; consequently, such circumstances should not affect a debtor's right to convert nonexempt assets into exempt assets.

This approach was taken by the Bankruptcy Court in *In re Crater*, [887] which clarified which badges of fraud should be used in assessing the propriety of prebankruptcy planning. (In *Crater* the issue was whether the debtor would be denied discharge.) In this case, the court noted that if prebankruptcy planning is not fraudulent per se, then only those indicia of fraud that intrinsically indicate fraud should be used to determine whether discharge should be denied. Under this view, only the following badges of fraud are intrinsically indicative of fraud: (1) the debtor retained possession or control of the property transferred after the transfer; (2) the transfer or obligation was concealed; (3) the debtor absconded; and (4) the debtor removed or concealed assets. [888] The remaining badges should not be considered. The following badges do not implicitly suggest fraud but do suggest there must have been a motivation other than the transaction itself because it was not an economically rational decision for a debtor to make but for its effect to hinder or delay creditors: (1) the transfer or obligation was to an insider; (2) 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; (3) he debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

[889]

The *Crater* court's analysis is useful and is the beginning of an orderly approach to prebankruptcy planning, which may be used and refined by other courts. Other factors have also been used by court's to deny discharge for prebankruptcy planning.

The Ninth Circuit BAP revisited prebankruptcy planning in *In re Beverly*, [890] where the court characterized as fraudulent a common pattern of asset protection in the context of a divorce; namely, a division of assets whereby the debtor spouse receives exempt assets and is allocated liabilities, and the nondebtor spouse receives other, nonexempt, assets. In so holding, the *Beverly* court relied on correspondence that discussed the asset protection intention of the parties, who planned in the shadow of pending litigation and who executed the agreement after a judgment had been entered against the debtor. The court held that the allocation of assets was a fraudulent transfer, noting that in the absence of the marital agreement each spouse would have received one half of each asset.

Notwithstanding the foregoing authority and the clear expression contained in legislative history, there is a tendency on the part of some courts, especially in Florida, to thwart debtors who convert nonexempt property into exempt property on the eve of bankruptcy. Courts adhering to this view either ignore or give only lip service to the legislative history.

¶ 12.02[2] Use of Fraudulent Transfer Laws to Attack Prebankruptcy Planning

The use of fraudulent transfer laws to frustrate prebankruptcy planning is difficult to reconcile with the clear directive in the legislative history that eve of bankruptcy conversion is not fraudulent. Nonetheless, courts have avoided transfers on the basis of both the federal fraudulent transfer laws [891] and equivalent state law. [892] Further, some courts believe that the mere act of planning for bankruptcy is sufficient to warrant the denial of an exemption or other penalties associated with improper prebankruptcy planning.

The leading case adhering to this view, although apparently ambiguously, is the Eleventh Circuit's decision in *In re Levine*. [893] In this case, the court upheld a lower court's finding that a conversion of nonexempt assets into exempt assets—i.e., annuities that are exempt under Florida law—was accomplished with fraudulent intent. The facts of the case were unusually poor for the debtor in that three of the annuities had been cashed in accordance with the terms thereof. [894] The case is notable for holding that the fraudulent transfer laws apply to prebankruptcy planning and could result in either (1) setting the transfer aside or (2) a denial of the exemption. [895] The breadth of the court's opinion is unclear. In affirming the lower court's finding of fraudulent intent, the Eleventh Circuit did not depart from the views of all other courts that have held that a prebankruptcy conversion of nonexempt into exempt assets is not fraudulent per se. Even these cases consistently hold that the presence of fraudulent intent will doom the conversion.

If the *Levine* court's opinion in fact applies the fraudulent transfer laws to prebankruptcy conversions, it not only departs from existing law but imposes a substantial impediment to prebankruptcy planning, at least in the Eleventh Circuit. Constructive fraud is a category of fraudulent transfers that requires, among other things, a transfer without consideration (as determined from the creditor's point of view) at a time the debtor is insolvent or rendered insolvent thereby. Virtually every prebankruptcy conversion would result in constructive fraud, which is determined without regard to intent.

The *Levine* court did not consider this aspect of its decision. This may suggest that it has not departed from the general view, especially since the decision did not refer to the plethora of cases that enunciated the rule that a conversion is not fraudulent per se.

The Eleventh Circuit reaffirmed its negative view of prebankruptcy planning by affirming the Bankruptcy Court in *In re Chauncey*. [896] In this case, the debtor converted proceeds of a personal injury settlement to a homestead when she paid down the mortgage. In denying the debtor a discharge, the lower court relied on the badges of fraud; notably, that the conversion occurred before the bankruptcy petition was filed and because the debtor retained the benefit of the transferred property. The *Chauncey* decisions are disturbing because prebankruptcy always closely precedes the filing of a bankruptcy petition, and the debtor always retains an interest in the property transferred, i.e., converted. These decisions failed to analyze which badges of fraud should be considered in denying a discharge. [897] Similarly, the court, in *In re Delcorso*, [898] imposed sanctions on an attorney for, among other things, attempting to convert a nonexempt asset into an exempt asset.

One court has applied the fraudulent transfer laws to vitiate prebankruptcy planning when nonexempt property was sold for inadequate consideration and the proceeds thereof used to acquire exempt property. In *In re Kemmer*, [899] the process of conversion required a fire sale of certain property. The *Kemmer* court held that the proceeds of the sale were not reasonably equivalent value. Because the debtor was insolvent at the time, the transaction was voidable as constructive fraud under the Bankruptcy Code provisions. [900] The *Kemmer* court so held even though it acknowledged that converting nonexempt property into exempt property was not fraudulent per se and was within the bounds of acceptable exemption planning.

A fraudulent transfer that benefits the debtor, however, will not be avoided because, in that circumstance, creditors would not be harmed. [901]

¶ 12.02[2][a] Relation Between ERISA and Fraudulent Transfer Laws

ERISA [902] includes a broad preemption provision, which generally supersedes state laws that “relate to” ERISA employee benefit plans. [903] This preemption provision may override state fraudulent transfer laws and perhaps the parallel Bankruptcy Code provisions. ERISA also includes an antialienation provision. [904] This is commonly known as a spendthrift clause, which has the effect of preventing creditors from reaching the interest of a beneficiary of an ERISA retirement plan. ERISA's spendthrift clause is effective under state law [905] and in bankruptcy. [906]

ERISA's preemption provisions clearly apply to state laws but, by ERISA's terms, do not apply to federal laws. Therefore, the fraudulent transfer laws reflected in federal law, primarily the Bankruptcy Code and the Debt Collection Procedures Action of 1990, [907] should not be preempted by ERISA. As noted, and discussed below, however, ERISA's policy of protecting retirement interests of beneficiaries may neutralize even federal law, without reference to ERISA's preemption provision.

¶ 12.02[2][a][i] State fraudulent transfer laws preempted.

Application of state fraudulent transfer laws affect the funding of a plan, and, therefore, under case law, seem to “relate to” or makes “reference to” ERISA and to engage ERISA's preemption provision. [908]

Authority dealing directly with the issue, however, is unclear. *In re Shailam*, [909] held that the fraudulent transfer laws are laws of general application, neutral, and therefore not preempted by ERISA. [910] (Other authority in a different context supports the *Shailam* view. [910.1]) *In re Loomer*, [911] held to the contrary, providing that contributions to an ERISA plan may not be recovered from the plan under Bankruptcy Code § 550 (which refers to the liability of the transferee in the avoided transfer) because of ERISA's antialienation provision. [912] Neither of these cases considered the possibility that application of the fraudulent transfer laws are preempted on the grounds that it interferes with the funding of an ERISA plan. As noted below, a law that interferes with the funding of an ERISA plan is ordinarily preempted by ERISA.

Notwithstanding the foregoing division of authority on the preemption issues, both *Shailam* and *Loomer* agree that ERISA's policy of protecting retirement benefits neutralizes application of both state and federal fraudulent transfer laws. Thus, the *Loomer* court supported it decision to protect the debtor's interest in an ERISA retirement plan with reliance on the Supreme Court's decision in *Guidry v. Sheetmetal Pension Fund*. [913] (*Guidry* held that even the interest of a participant who stole from the retirement plan would be entitled to ERISA protection; the participant's wrongful conduct cannot result in a loss of benefits in violation of ERISA's antialienation provision.) The *Loomer* decision is notable because it held that “even if the debtor's acts were motivated by an actual intent to hinder, delay or defraud creditors, or were preferential as to other creditors, such acts would not justify an exception to the” Supreme Court's decision in *Guidry*, which held that ERISA's antialienation provisions are to be strictly enforced even as to a remedial provision of federal law. [914] The *Loomer* court also held that ERISA protection applies even though the transfer may otherwise be avoided under 11 USC §§ 544, **547**, and **548** (relating to the bankruptcy trustee's powers to avoid transfers). Thus, under *Loomer*, ERISA's antialienation provision overrides even federal fraudulent transfer laws. Under this reasoning, ERISA's antialienation provision would override state fraudulent transfer laws without reference to ERISA's preemption provisions.

The *Shailam* court also cited *Guidry* to support its ultimate decision that interest in the plan was protected, i.e., ERISA's anti-alienation provision shielded the interest from creditors. [915]

Under *Loomer*, a creditor would still have several avenues. First, the property could be recovered from the persons who benefited from any fraudulent transfer. [916] But satisfaction of that liability could be recovered only from nonexempt property, which would not include ERISA retirement plans. Depending on applicable state law, nonexempt property could, however, include distributions from such plans. [917] The court also indicated that a debtor who converted nonexempt assets into exempt assets could be denied discharge or have his bankruptcy petition dismissed for abuse. The *Loomer* court further suggested that, when an ERISA account is held under fraudulent conditions, the account may be recovered under the federal common-law theory that fraud in the inducement allows rescission of a contract. [918]

Federal common law applies, if at all, when there is a “gap” in ERISA's text. [919] No such gap exists if ERISA specifically and clearly addresses the issue. [920] When such a gap exists, the federal common law must be limited to the intention of ERISA, which is to allow only “equitable relief,” i.e., only that relief that equity would permit, which precludes personal liability relative to a contractual obligation. [921] Equitable relief can include restitution; there is a difference, however, between legal restitution and equitable restitution. The former seeks to impose personal liability on the defendant, whereas the latter seeks to recover plaintiff's property or funds that are traceable to property or funds held by the defendant. [922] Thus, federal common law can be applied to provide equitable remedies. [923]

Under this rule, a claim for unjust enrichment is not allowed because it generally provides for personal liability, which is legal in nature rather than equitable. [924]

¶ 12.02[2][a][ii] Laws affecting funding of ERISA plan preempted.

The funding of a plan “relates to” ERISA; consequently, a law that attempts to govern the funding of an ERISA plan is preempted. [925] Application of the fraudulent transfer laws affects the funding of a plan and, therefore, “relates to” ERISA. Accordingly, the application of the fraudulent transfer laws to the funding of an ERISA plan would be preempted, that is, rendered void. [926]

A number of cases appear to allow seizure of funds contributed to an ERISA retirement plan, but none of them considered the funding of plans or the protection afforded a participant's interest under *Guidry.* [927]

¶ 12.02[3] State Statutory Restrictions on Prebankruptcy Planning

Some states have enacted special legislation to prevent the conversion of nonexempt assets into exempt assets. For example, a Florida statute provides that the conversion of an asset that results in proceeds of the asset being exempt from the claims of a creditor can constitute a fraudulent transfer, regardless of whether the creditor's claim arose before or after the conversion of the asset, if the conversion was made with the intent to hinder, delay, or defraud the creditor. [928] For this restrictive statute to apply, the transferor must be the debtor at the time of the conversion of nonexempt into exempt assets. [929]

The Eleventh Circuit in *In re Levine*, [930] held that the Florida statute was merely a clarification of existing law and that a conversion, in any event, was subject to the fraudulent transfer laws, both before and after the enactment of that statute. Further, Florida law provides that property acquired as the result of a fraudulent transfer will not be exempt. [931] (This Florida statute, however, does not prevent a debtor from acquiring an exempt homestead, which is authorized under the Florida Constitution. [932]) Statutes that are aimed at restricting prebankruptcy planning have been enacted in several states, including: Texas, [933] Wyoming, [934] Ohio, [935] Kansas, [936] New Jersey, [937] New York, [938] Maine, [939] and Illinois. [940] The basis for determining whether the transfer was made with fraudulent intent is the “badges of fraud.” [941]

As indicated, these types of state laws will not likely be applied to exemptions that are granted by state constitutions, primarily on the grounds that legislatures may not restrict constitutionally granted rights without amending the constitution. [942] Further, if the acquisition of the exempt property predates the involvement with the creditor, the exemption will be upheld even if later payments increase the value of the exempt property. [943]

¶ 12.02[3][a] Possible Federal Preemption of State Restrictions on Exemptions

It is unclear whether federal preemption of state restrictions on exemptions also invalidates these restrictions in bankruptcy court.

In bankruptcy court, the debtor's federal right to claim exemptions will often supersede state restrictions. For example, a series of cases have held that **11 USCA § 522(c)**, which authorizes debtors to claim exemptions in bankruptcy, overrides the provisions of a state statute excepting from the debtor's homestead exemption contractual obligations incurred prior to the acquisition of the homestead. [944] The First Circuit Court of Appeals held that the state law restriction on the homestead exemption was preempted by § 522(c), which generally provides that exempt property is not liable for any prepetition debt, except certain specified debts such as taxes, alimony, and liens that cannot be avoided. In so holding, the court noted that Congress “has plenary power to enact uniform federal bankruptcy laws pursuant to the Constitution of the United States.” [945] The authority, however, is not uniform. [946]

Also to be considered is the U.S. Supreme Court's decision in *Owen v. Owen*. [947] In this case, the Court held that a judicial lien could be avoided even if the property was not exempt under state law as to the lien. The *Owen* Court considered **11 USCA § 522(f)**, which provides in part that “the debtor may avoid the fixing of a lien on an interest of the debtor in property to the extent that such lien impairs an exemption to which the debtor would have been entitled under subsection (b) of this section.” The *Owen* Court observed that: “Nothing in subsection [522](b) (or elsewhere in the [Bankruptcy] Code) limits a State's power to restrict the scope of its exemptions; indeed, it could theoretically accord no exemptions at all.” [948] It has been observed that the state can impose any restriction on *state* exemptions, provided that those restrictions do not conflict with the Bankruptcy Code. [949] Thus, the question is whether the right to prebankruptcy planning is contained in the Bankruptcy Code and whether a state law that conditions an exemption on the absence of such planning conflicts with any right under the Bankruptcy Code.

The right to an exemption is contained in § 522; and the legislative history thereof comments on the right of a debtor "to convert nonexempt property into exempt property before filing a bankruptcy petition." [950] Thus, there appears to be an argument that a state restriction that conditions an exemption on the absence of prebankruptcy planning conflicts with the Bankruptcy Code. [951]

The Court in *Owen* ignored the state law restriction on the exemption that impaired the homestead exemption with respect to liens that arose before the homestead was acquired, i.e., *Owen* allowed the lien to be removed pursuant to § 522(f) since it impaired the exemption. If the right of debtors to engage in prebankruptcy planning (pursuant to § 522(b) or otherwise) is commensurate with the right to a § 522(f) lien avoidance, then similarly state law should not operate to deny the debtor the right to convert nonexempt property into exempt property.

The validity of state law restrictions on prebankruptcy planning may also depend on whether the version of the fraudulent transfer law that is applied is taken from the Bankruptcy Code or applicable state law. Generally, the federal statute applies to transactions that occur within two years of filing the petition for bankruptcy, while transactions beyond the two-year period are governed by applicable state law. (Before April 20, 2006, the reach-back periods of §§ 548(a) and 548(b) were one year. [952])

Where federal law applies, state restrictions appear to be preempted by federal law under the reasoning of cases such as *In re Weinstein*. [953] Where state law applies, however, this result seems less likely, since the Bankruptcy Code specifically directs that state law applies. [954]

¶ 12.02[4] Denial of Discharge

The most draconian of the prebankruptcy planning penalties is a denial of discharge. The denial of discharge is purely a federal question and can be imposed even where the debtor is entitled to an exemption under state law. [955] Where the court holds that the debtor is entitled to a state exemption, denial of discharge may be the only means a court has to prevent prebankruptcy planning. The standard of denial of discharge in Section 727(a)(2) [956] of the Bankruptcy Code is similar to that of the actual intent category of the fraudulent transfer laws—that is, a transfer made with the intent to defraud, hinder, or delay; however, the use of this standard is often much more restrictive when applied to denial of discharge issues. [957] Thus, there is an implication that courts are subjecting the debtor's conduct to an unstated equitable standard that makes prebankruptcy planning problematic at best. [958] In this regard, one Bankruptcy Court held that, although prebankruptcy conversion does not automatically result in a denial of discharge, a lesser level of conduct than fraud is all that is required to render the conversion unsuccessful and result in a denial of discharge. [959] As a consequence, a denial of discharge will be imposed even if creditors are not harmed by the debtor's conduct. [960] It is possible that a more liberal view is taken with regard to favored assets such as a debtor's residence.

Certain conduct clearly is fraudulent and will result in a denial of discharge. For example, transferring property to an actual or implied trust with the intention of receiving the property after filing the bankruptcy petition establishes a fraudulent purpose. [961] Acquiring property in the name of another or a wholly owned corporation will similarly result in a denial of discharge, [962] as will an attempt to conceal assets by transferring them to a spendthrift trust [963] or to a dummy corporation. [964] Other courts, while reluctant to deny discharge on the grounds of prebankruptcy planning, point to a mélange of events and acts, which taken separately might not warrant a denial of discharge. [965]

Beyond these kinds of obvious examples, a multitude of factors and patterns of behavior are assessed in determining whether conduct is fraudulent. Many of the factors are badges of fraud reflected in the fraudulent transfer laws. Other factors or circumstances are unique to resolving the denial of discharge issue.

¶ 12.02[4][a] Badges of Fraud

The presence of badges of fraud may result in a denial of discharge. The same general inquiry is relevant in determining whether a transfer is voidable under the applicable fraudulent transfer laws. [966] (Although this section deals with denial of discharge, as noted, some courts have blurred the distinctions between the various remedies to thwart prebankruptcy planning, i.e., avoidance as a fraudulent transfer or a denial of the exemption. Thus, it is possible that a court could use the same elements to support those remedies.) Whether indicia of fraud are present is inherently factual and lower courts will not be overruled absent a clear error. Usually, the debtor's conduct before filing is examined to determine the existence of fraudulent intent. However, conduct occurring after the filing of the petition can indicate fraudulent intent as well. [967] The factors considered in determining whether prebankruptcy planning is accompanied by fraud are numerous, and there is disagreement among the courts as to the relevance of some of these factors. Often the decision turns on whether the debtor's conduct, taken in its totality, warrants a denial of discharge.

As noted previously, the Bankruptcy Court in *Crater*, [968] noted that only those badges of fraud that are intrinsically indicative of fraud should be used in assessing whether a conversion of nonexempt assets into exempt assets results in a denial of discharge. [969] (Those factors are: (1) the debtor retained possession or control of the property transferred after the transfer; (2) the transfer or obligation was concealed; (3) the debtor absconded; and (4) the debtor removed or concealed assets.) The *Crater* analysis rejected the other factors often used to deny discharge for prebankruptcy planning on the grounds that such factors imbue planning with unnecessary uncertainty and are beyond the court's authority. [970] These other factors, many of which are not reflected in the fraudulent transfer law, include (1) whether the debtor engaged in a pattern of sharp dealings; (2) whether the amount converted is excessive; and (3) whether the exempt property acquired is used for its intended purpose.

¶ 12.02[4][a][i] Pattern of sharp dealing.

A debtor who engages in prebankruptcy planning must be scrupulous in his dealings with creditors in order to avoid a denial of discharge. If the debtor misrepresents facts or engages in clandestine activities, then he may be condemned to a denial of discharge of all debts. Even if the deception is mild, once a misrepresentation (or other form of deception) is present, the degree of dishonesty is not relevant. [971] Consequently, a debtor contemplating conversion of assets into exempt assets is better off not saying anything rather than making any comment or statement that could be characterized as deceptive. A debtor, however, does not have the duty to volunteer information. [972]

Even if the debtor has not been deceptive, extrinsic fraud (i.e., fraud beyond or extrinsic to the mere conversion of assets from nonexempt to exempt) may be found if sufficient other indicia of fraud are present. Cases variously define “extrinsic fraud.” One case listed the following as evidence of extrinsic fraud: (1) “conduct intentionally designed to materially mislead or deceive creditors about the debtor's position; [(2) the] use of credit to buy exempt property; [(3)] [c]onverting a very great amount of property could also be an indication of fraud; [(4)] [t]he existence of conveyances for less than adequate consideration.” [973] Similarly, in *In re Reed*, [974] the court relied on the following factors to deny discharge:

- Arranging to postpone payment on a loan (which also results in hindering and delaying a creditor)
- Diverting funds from a business to an account unknown to creditors
- Converting borrowed money into exempt property

In another case, handling matters in a clandestine manner such as instructing a real estate agent not to disclose the debtor's interest in property and lying to the bank about the debtor's inability to make payments on loans, which gave the debtor time to convert property into exempt homestead, supported the denial of discharge. [975] The failure to disclose relevant transactions, such as the conversion of nonexempt property into exempt property, is also an indicium of fraud. [976]

In one case, simply promising to make payments that were not made, without making any misrepresentation, was considered in rejecting and punishing prebankruptcy planning. [977]

¶ 12.02[4][a][ii] Amount of exempt property.

A number of cases have held that the excessive amount of an exemption is extrinsic fraud that is sufficient to support a denial of discharge. This is particularly true in situations where assets are converted into exempt assets pursuant to prebankruptcy planning. For example, in *In re Zouhar*, [978] the debtor obtained a loan pledging stock in his professional corporation. The loan was approximately $45,000 and “instead of paying his debts, he purchased an annuity with the funds. The annuity was structured so that the payments were directed to the holder of the note and security interests encumbering the stock in the professional corporation.” [979] The purpose of this transaction was to shield the assets from his creditors. In considering this course of action the court stated the following:

> While it has generally been held that the transmutation of nonexempt assets into exempt assets on the eve of bankruptcy is not fraudulent per se, those cases permitting such transfers generally involve considerably smaller sums than are involved here.…
>
> The difference, which seems initially to be one merely of degree, at some point as yet unspecified becomes a difference

> in kind which requires a different result. “There is a principle of too much; phrased colloquially, when a pig becomes a hog it is slaughtered.” That principle fully applies here. While a bankrupt is entitled to adjust his affairs so that some planning of one's exemptions under bankruptcy is permitted, a wholesale sheltering of assets which otherwise would go to creditors is not permissible. [980]

If the conversion had been allowed in *Zouhar*, the debtor would have been able to avoid certain obligations to his wife and retain a net worth of approximately $130,000 in 1981. Instead the court denied debtor's discharge.

Similarly, in *Norwest Bank of Nebraska, NA v. Tveten*, [981] a physician owing $19 million converted all of his assets (i.e., land, life insurance policies, annuities, salary, a Keogh plan and individual retirement fund, a corporate profit-sharing plan and an interest in a residence), which had an aggregate value of $700,000, into life insurance or annuity contracts that were exempt to an unlimited amount under state law. (Conversely, conversion of relatively minor amounts militates against a denial of discharge. [981.1]) The Eighth Circuit held that although the kind of property that is exempt is determined by reference to state law, whether the debt is to be discharged is to be determined under federal law. The court examined the underlying purpose of the exemptions, namely, to provide debtors with a fresh start with regard to “the limited amount [of the exemptions] allowed to them” and to give the debtors “a fresh start, not a headstart.” [982]

The *Tveten* court was offended by the spectre of a debtor who earns more than $60,000 annually exempting all his assets. [983] Thus, the *Tveten* decision holds that an excessive amount of an exemption is extrinsic fraud. The debtor's ability to earn significant sums also appears to have supported this conclusion.

Similarly, the Court of Appeals for the Fifth Circuit indicated that it would consider the amount of the exemption alone as extrinsic fraud. The court stated the following:

> [T]he finding of actual intent to defraud, based on evidence other than the fact of conversion, patently was not permeated with error. It would constitute a perversion of the purposes of the Bankruptcy Code to permit a debtor earning $180,000 a year to convert every one of his major nonexempt assets to sheltered property on the eve of bankruptcy with actual intent to defraud his creditors and then emerge washed clean of future obligations by carefully concocted immersion in the bankruptcy waters. [984]

The Court of Appeals for the Tenth Circuit also indicated that it would consider the amount of the exempt property as extrinsic fraud. [985] The Court of Appeals for the Second and Seventh Circuits have repudiated or not embraced the *Tveten* view. [986] An Iowa Bankruptcy Court also indicated that the amount of an exempt property is not a consideration. [987]

Although the Ninth Circuit Court of Appeals has not ruled on this precise issue, a Bankruptcy Appellate Panel suggested that the amount would not be relevant when it allowed a conversion of nonexempt property into partially exempt property. [988] Similarly, although the issue was not squarely faced, the court of appeals in *In re Stern* [989] approved the conversion of $1.4 million of a partially exempt IRA into an IRS qualified plan, which was absolutely exempt under state law. The Ninth Circuit BAP, in *In re Beverly*, [990] took the amount of conversion into account in denying a debtor discharge.

There is some authority for the principle that if applicable state laws limits the amount of the exemptions to a modest amount, then a denial of discharge is prevented in connection with a prebankruptcy conversion of nonexempt assets into exempt assets. [991] Other authority, however, indicates that whether an amount is “modest” depends on the circumstances; and if the amount protected under a conversion would have provided substantial payment to creditors, the conversion may be subject to avoidance as a fraudulent transfer. [992]

Closely related to the amount of exempt property converted is the debtor's earning ability. Courts have supported a finding of extrinsic fraud by highlighting the debtor's considerable earning power. [993]

A denial of discharge for conversion of nonexempt into exempt assets will less likely be imposed where there is a significant societal benefit in preserving the property for the debtor, such as where homestead property is at issue. [994] Further, where the surrounding facts indicate that the conversion is not abusive in light of the debtor's circumstances, then the amount of the exemption alone will not prevent a discharge. Thus, in *In re Smith*, [995] the debtor was allowed to convert $90,000 of a $100,000 settlement to purchase an exempt annuity policy that would pay him $728 per month. His past earnings were less than $5,000 per year and he was then earning $4.40 per hour. He was 25 years old and lacked a high school diploma. The *Smith* court held that providing the debtor with minimal financial security was held not abusive.

A serious problem with considering an amount as extrinsic fraud is the lack of a precise standard and the uncertainty that it engenders. Abusiveness clearly is a relative term that will vary from judge to judge and region to region. One of the purposes of allowing state exemptions is to accommodate the diversity among the various regions. It would seem that if a state wanted to impose a limit on the aggregate amount of exemptions available to a debtor, then it would do so.

¶ 12.02[4][a][iii] Use of asset for intended exempt purpose.

Some decisions have resolved the issue on the basis of whether the exempt asset is used for its intended purpose and is consistent with the debtor's lifestyle and needs.

A Florida bankruptcy court in *In re Covino* [996] has enunciated what may become the standard to determine whether prebankruptcy planning is proper or fraudulent. In that case, the debtor sought an exemption for certain settlement proceeds that were used to pay off the debtor's mortgage and to acquire an annuity. The *Covino* court established the following standard:

> If the transfer is made with a particular creditor in mind, and the debtor has attempted to remove assets from the reach of the creditor, the debtor's discharge will be denied and the debtor's conduct is actionable. However, if the debtor is merely looking to his future well-being, the discharge will be granted, and such conduct not otherwise actionable. [997]

Under this standard, the court characterized the use of proceeds to pay off the mortgage as being for the purpose of hindering and delaying creditors. Thus, the attempted conversion from nonexempt to exempt property was avoided. [998] The same standard was applied to allow an exemption for the portion of the settlement proceeds that were used to acquire the annuity. [999] But the conversion will be treated as fraudulent when the debtor's purpose in purchasing the annuity is to thwart litigation concerning entitlement to inheritance, rather than to provide debtors with a future stream of income, i.e., the legitimate purpose of an annuity. [1000]

Similarly, in *In re Lazin*, [1001] the conversion to annuities was approved where the debtor was a 79-year-old widow who needed the funds for her support. [1002] In that case, the source of the nonexempt funds was a brokerage account that had to be liquidated because it fell below the required minimum.

The *Covino* standard was applied in *Sholden v. Ditz*, [1003] where the court held that conversion of nonexempt funds into a residence was intended to hinder and delay creditors and was, therefore, fraudulent. In this case, a 90-year-old debtor purchased a home by liquidating all of his assets, totaling $140,000 worth of certificates of deposit. Thereafter, his sole source of income was social security payments of $486 per month. Further, the debtor made improvements to the house in the form of a large deck, which was of little use to him because he had no family. [1004]

Similarly, a conversion into an exempt retirement account was considered in rejecting a plan of reorganization where the debtor was relatively young, had significant retirement accounts, and was capable of significant earnings. [1005] A variation of the *Covino* standard is where the conversion is consistent with prior patterns. Thus, a conversion of nonexempt property into exempt entireties property is not fraudulent where the parties usually held their property as tenants by the entireties. [1006]

¶ 12.02[4][a][iv] Adequacy of consideration for transferred property.

Transferring property for inadequate consideration is a badge of fraud. [1007] This factor is particularly important where the transfer is made to a close family member. [1008] Conversely, a sale for full and adequate consideration that is based on arm's-length transactions and as a result of economic factors that maximized the amounts available to creditors will not justify a denial of discharge. [1009] But if the transaction was undertaken with the intent to defraud creditors, discharge will be denied regardless of the adequacy of consideration. [1010] Further, as noted earlier, a transfer for inadequate consideration has been used to avoid a transfer as constructive fraud. [1011]

¶ 12.02[4][b] Miscellaneous Factors Used to Deny Discharge

It is apparent that many courts frown on prebankruptcy planning and attempt to discourage it. Some courts penalize prebankruptcy planning solely on the basis of the debtor's intent to place assets out of the reach of creditors. [1012] This position prevents most prebankruptcy planning, the very purpose of which is to prevent creditors from seizing the debtor's property. [1013] As of this writing, it is the minority position. [1014]

Beyond this extreme position, courts have employed numerous factors, many of which do not withstand analytical scrutiny.

¶ 12.02[4][b][i] Fraud directed at a specific creditor.

Fraudulent intent directed at a particular creditor has been the basis of a denial of discharge. [1015] Some of these cases arise in the context of an acrimonious divorce. Thus, in *In re Gepfrich*, [1016] the debtor attempted to convert a marital asset (an investment) into an exempt annuity. The debtor's wife sought to enforce her rights under a divorce decree. The court denied a discharge because the proceeds, which were converted into exempt property, were obtained from marital assets in which the wife had an interest. In addition, the court looked to the debtor's conduct of misleading both his wife and the state court as to the availability of funds as well as making gifts to his children of a previous marriage.

The *Gepfrich* court held that the conversion was fraudulent, since it was directed at a specific creditor. In so holding, the court noted: "Where the nonexempt property [converted into exempt property] . . . is tied to a claim of a specific creditor, then the debtor's conduct will be objectionable under **11 USC § 727(a)(2)**." [1017]

Where the exempt property is used for its intended purpose, this factor seems much less important. A debtor that engages in prebankruptcy planning will virtually always have a creditor (or creditors) in mind. Accordingly, this element seems at best marginally relevant. [1018]

¶ 12.02[4][b][ii] Converting borrowed funds and assets relied on by creditors.

Converting borrowed funds can also effectively result in fraud directed at a particular creditor that will result in a denial of discharge. Thus, in *In re Armstrong*, [1019] the debtors encumbered certain property to assist a related party to generate cash that was used by debtors to acquire exempt property. In denying discharge, the Bankruptcy Court stated that "if a debtor was only 'looking to his future well being,' a discharge would be granted but if the debtor had a particular creditor in mind in trying to remove his assets from that creditor's reach, then a discharge would be denied." Further, using borrowed funds to purchase exempt property is treated as an indicium of extrinsic fraud. [1020]

Borrowing money to acquire exempt property may constitute a fraud on the lender. It is unlikely that one would loan a debtor money for the purpose of acquiring exempt property. This offense may be more a matter of nondisclosure rather than fraud. In either event the lender may have an equitable lien or constructive trust on the exempt property, which could result in an effective denial of the exemption. [1021]

¶ 12.02[4][b][iii] Conversion of business assets.

Business assets are often relied on when business creditors extend credit. Converting such assets into exempt assets effectively denies those assets to a specific group of creditors who reasonably relied on their availability to satisfy all or a portion of their debt. Consequently, this conduct has been an indicium of fraud that has supported a denial of discharge. For example, in *In re Collins*, [1022] the debtor transferred $55,000 from his business resources and converted the funds into homestead property. The *Collins* court held that conversion was improper. In commenting on the propriety of converting exempt assets into nonexempt assets the court noted the following:

> Some transfers [that accomplish a conversion of nonexempt to exempt property] certainly are permissible and should be encouraged. However, in cases with a factual scenario which reveal that business assets which belong to creditors are being used to delete individual debts will not be permitted. [1023]

Business assets have been broadly defined to include not only those used in one's business, but also those relied on by business creditors. For example, in *In re Mackey*, [1024] the court held that the conversion of nonbusiness property into exempt property is treated the same as the conversion of business property because the debtor personally guaranteed the debts, and, as a consequence, all of her nonbusiness property became business property.

The fraudulent taint associated with converting business assets into exempt property is ameliorated by the passage of time. Thus, in *In re Elliott*, [1025] the use of business assets to satisfy a mortgage on a residence was not fraudulent in that there was no attempt to conceal the payment and "the most important factor" was that it occurred two and one-half years before bankruptcy rather than on the eve of bankruptcy.

This kind of debtor conduct may also result in a constructive trust or an equitable lien. [1026] Further, if the business assets liquidated are used as collateral for a loan, the conduct may also result in a breach of contract that gives rise to a nondischargeable debt. [1027]

¶ 12.02[4][b][iv] Other indicia and factors supporting fraud.

Other discrete kinds of conduct by the debtor have been used to support a finding of fraud. But usually the factors considered in determining whether to deny discharge are numerous and no single factor is dispositive. This is illustrated by *In re Fine*, [1028] wherein the court found that prebankruptcy planning did not warrant a denial of discharge. In so holding, the *Fine* court considered the following factors: (1) the objecting creditor had a "special equity" in the nonexempt property that are converted into exempt property; (2) the debtor and the transferee enjoyed a family, friendship, or close associate relationship; (3) the debtor retained the possession, benefit, or use of the property in question; (4) the debtor engaged in a sharp pattern of dealing immediately before bankruptcy; (5) the debtor became insolvent as a result of the transfers (financial condition); (6) the conversion occurred after the entry of a large judgment against the debtor; and (7) the debtor received inadequate consideration. [1029] In assessing insolvency as a factor, the *Fine* court held that deepening insolvency was an indicium of fraud. Thus, only becoming insolvent as the result of the transfer is an indicium of fraud. [1030]

The following are other discrete factors that have been considered as a badge of fraud.

- A "special equity" that a creditor may have in nonexempt property that is converted into exempt property can result in the creditor being treated as the party from whom such funds were fraudulently obtained. This can also result in an effective denial of the exemption or a portion thereof under applicable state law. [1031]
- The debtor deliberately spends money so that it does not fall into the hand of creditors. [1032]
- Failure to disclose the timing of any prebankruptcy planning. [1033]
- Consulting a lawyer for the purpose of engaging in prebankruptcy planning. [1034] It is doubtful that much judicial support will be generated for this element.
- Converting nonexempt into exempt property for the specific purposes of placing the assets out of the reach of creditors. [1035] This is usually the intent of prebankruptcy planning.
- Pending litigation at time of conversion to exempt assets. [1036] This factor is usually present in prebankruptcy planning.
- Prepayment for work to be performed on exempt property. [1037]

¶ 12.02[4][c] Conduct Not Constituting Fraud

Conversion or transfers of substantial sums will not constitute fraud under a variety of circumstances, including, without limitation, where the payments are customary in the debtor's lifestyle or were made in reliance on the advice of an attorney.

¶ 12.02[4][c][i] Customary payments.

Common or customary transfers made in order to maintain one's household is not an indicium of fraud. [1038] Moreover, payments made pursuant to a continuing pattern, whether monthly allowances to relatives or vacations, will not support a finding of intent to defraud so as to bar discharge. In so holding, one court stated the following:

> There was no proof that when [the debtor] continued to make the usual payments to his family and when he took a skiing vacation in Utah, he did so with the express intent to tap his assets to the detriment of his creditors. The debtor simply continued a pattern of living to which he was accustomed until he learned that . . . his largest creditor, after accelerating his indebtedness in obtaining a summary judgment in state court, was going to reach his bank accounts. [1039]

But where payments exceed the amounts necessary or customarily used to maintain the debtor's household, such excess payments will constitute an indicium of fraud. [1040]

¶ 12.02[4][c][ii] Reliance on attorney.

For purposes of denial of discharge in bankruptcy, case law is divided, with some cases holding that good faith reliance excuses fraudulent transfer and others cases holding that it does not constitute an excuse. [1041] The Court of Appeals for the Ninth Circuit has held that reliance on an attorney will preclude a denial of discharge due to fraud where the debtor acts in good faith. [1042] There must, however, be a complete disclosure. [1043]

In general, whether reliance on advice of counsel will vitiate fraudulent intent depends on the circumstances. [1044] Debtors planning to establish the reliance-on-counsel defense must demonstrate, among other things, that the reliance was reasonable “and that counsel's interpretation of the law was neither frivolous nor wholly unreasonable.” [1045] The debtor's knowledge that the transfer is being made for the purpose of delaying, hindering, or defrauding creditors precludes the reliance-on-counsel defense. [1046]

Where the circumstances are complex and the intention is not clear, it is possible that reliance on counsel will constitute a defense, [1047] provided that all of the elements of the defense are established. According to one commentator, the elements of reliance-on-counsel defense require that the debtor “(1) accurately relied, (2) in good faith, (3) on advice of competent counsel, (4) concerning a question of law, (5) acted with due or reasonable care, and (6) disclosed all of the facts to his or her attorney.” [1048] Even if the debtor establishes that he relied on counsel, that may be only one factor to consider. [1049]

The distinction between “good” and “bad” faith may be the difference between whether an act is inherently and manifestly wrong to all persons regardless of their training, and whether the act is wrong only under technical requirements of a statute, that is, the difference between *malum in se* and *malum prohibitum*. Thus, where transfers made to avoid a creditor are inherently wrong since both a lawyer and any client would recognize the wrongful nature of the conduct, such transfers would be indicia of fraud. [1050]

¶ 12.02[4][c][iii] Miscellaneous conduct not considered fraudulent.

Other common patterns of conduct that have been held insufficient to establish fraud include the following:

- An honest mistake or conduct resulting from ignorance. [1051]
- The intention to benefit some creditors over others, although that may result in an avoidable preference. [1052]
- A mere failure to volunteer information. [1053]
- Delegating financial matters to a spouse did not constitute a reckless indifference sufficient to deny a discharge, at least where the delegating spouse had no understanding of financial matters. [1054]
- Rolling over retirement benefits into an individual retirement plan, even where pursuant to the process the funds are maintained in a personal checking account for a short period. [1055]
- Converting property before forming the intent to file for bankruptcy. [1056]
- Converting savings into exempt property. [1057]
- Transactions in the ordinary course of business. [1058]

¶ 12.02[4][d] Purging the Fraudulent Taint

If the debtor has engaged in fraudulent conduct, there is a division of authority as to whether the debtor can purge the fraud. The Court of Appeals for the Ninth Circuit holds that the fraudulent taint can be purged, whereas the Courts of Appeals for the First, Seventh and Eleventh Circuits hold that the taint cannot be purged and that the fraudulent conduct results in a denial of discharge, regardless of the debtor's attempts to reverse the fraudulent conduct.

The Ninth Circuit's position is set forth in *In re Adeeb*. [1059] In this case, the debtor, faced with numerous creditors, consulted an attorney who told him to transfer his property to third parties who could be trusted for no consideration. He acted in accordance with this advice. Thereafter, he sought advice from another attorney who advised him to reverse the transfers, which he did. These transactions were disclosed to his creditors. The question was whether the conduct, which admittedly evidenced actual intent to hinder and delay his creditors, would result in a denial of discharge.

The *Adeeb* court interpreted the requirement that property be "transferred" to mean "transferred and remain transferred." [1060] It held that the only kind of transfer that justified a denial of discharge for all debts was a transfer that had "the effect of keeping assets from creditors,which is a transfer in which the property remains transferred at the time the bankruptcy petition is filed." [1061] This is in keeping with the purpose of the Bankruptcy Code, that is, to afford creditors the maximum amount to satisfy their claims and to give the debtor a fresh start. In addition, allowing a debtor to unwind a fraudulent transaction would encourage debtors to reverse fraudulent transfers, thereby promoting an equitable distribution of the estate among creditors and allowing an honest debtor to rectify his conduct.

The *Adeeb* court stated that this result would be available only if the debtor recovers substantially all of the property before he files his petition. In *Adeeb*, however, an involuntary petition was filed prior to recovery of substantially all of the property. The court held that it would be "inequitable" to punish a debtor who had not recovered substantially all of the property prior to the filing of an involuntary petition. Accordingly, the court modified its ruling, holding that the debtor must "actually recover the property within a reasonable time after the filing of the involuntary petition." [1062]

But where the property is recovered as a result of the actions of the bankruptcy trustee, rather than by reason of the debtor's action, the ruling in *Adeeb* will not apply and discharge will be denied. [1063]

The Court of Appeals for the Eleventh Circuit declined to follow *Adeeb*. In *In re Davis*, [1064] the court held that a fraudulent transfer of a residence by a debtor to his wife and the retransfer of the residence back to the debtor immediately before a petition was filed constituted a fraudulent transfer that resulted in a denial of discharge. The *Davis* court held that the statute in question was plain and unambiguous and that it was not free to adopt the Ninth Circuit's interpretation of the term "transferred."

The Eleventh Circuit was joined by the First Circuit in *In re Bajgar* . [1065] The *Bajgar* court specifically rejected *Adeeb*, although it noted that, unlike *Adeeb* where the retransfer occurred before the debtor filed the bankruptcy petition and after the creditors filed an involuntary petition, the retransfer in *Bajgar* occurred after the petition was filed. Thus, the *Bajgar* court was not faced with an honest but unfortunate debtor, but rather one who fully knew what he was doing and merely attempted to retransfer the property when he was faced with the prospect of being denied discharge.

The Seventh Circuit also rejected *Adeeb*. [1066]

¶ 12.02[5] Denial of Exemption Under State Law

Although a denial of discharge is determined under federal law, the debtor's entitlement to the laundry list of state exemptions is determined under applicable state law. [1067]

Applicable state law will sometimes impose the denial of exemption. For example, if exempt property was obtained exclusively with fraudulently obtained funds, case law indicates that the exemption will be denied as a matter of state law. [1068] If the fraudulently obtained funds are merely used to improve the property or pay for only part of the acquisition cost of such property, then the exemption will not be lost. [1069] Other fraud may also result in a denial of the exemption. [1070] As noted previously, bankruptcy law may preempt certain state restrictions on exemptions. [1071]

¶ 12.02[6] Denial of Exemption in Bankruptcy

An exemption can be denied in bankruptcy under § 522(g), including some prebankruptcy planning maneuvers. [1072] In addition, some courts have held that an exemption can be denied in bankruptcy pursuant to the Bankruptcy Court's equitable powers [1073] or pursuant to the bankruptcy provision allowing a debtor to claim an exemption. [1074] Other courts have raised the possibility of this result stating that although the general rule allows a debtor to convert exposed assets into exempt assets this rule "is not absolute [and w]here the debtor acts with actual intent to defraud creditors, his exemption will be denied." [1075]

Other courts point out that the Bankruptcy Code provides no basis for disallowing a state law exemption simply because exempt property was acquired in order to hinder, delay, or defraud creditors. Consequently, these courts have held that the exemption cannot be denied except pursuant to applicable state law. [1076]

¶ 12.02[7] Dismissal of Bankruptcy Petition

A bankruptcy petition may be denied under a variety of circumstances. This inquiry will be limited to dismissal in the context of prebankruptcy planning, wherein the debtor retains significant assets. Depending on the circuit in which the controversy arises, this factor will support the dismissal of a bankruptcy petition. Prebankruptcy planning has been the grounds for characterizing a Chapter 7 petition as abusive, resulting in dismissal of the petition. [1077]

A Chapter 7 petition may be dismissed if the debtor's obligations are primarily consumer debts and it would constitute a substantial abuse to grant relief. [1078] Some courts have employed the "totality of circumstances test" to resolve this issue. [1079] One of the elements of this test is the debtor's ability to repay debts. The Second Circuit Court of Appeals, in *In re Kornfield*, employed this test in considering the dismissal of an allegedly abusive Chapter 7 petition. [1080] *Kornfield* relied on, among other factors, the earning power of the debtor. [1081] Thus, the *Kornfield* court found the filing abusive in that these debtors enjoyed substantial income but sought to transfer the cost of an unnecessarily extravagant lifestyle to creditors. Under the totality of the circumstances test, a pension plan, even though exempt, would be taken into account in evaluating the debtor's circumstances. That kind of asset would be "at least relevant to a debtor's need to put aside portions of future income to provide for old age." [1082]

The sentiments expressed in *Kornfield* were echoed in *In re Koch*, [1083] where the court noted that the substantial abuse concept "focuses primarily on debtor's ability to pay; indeed substantial ability to pay creditors standing alone warrants dismissal of a Chapter 7 petition for substantial abuse. Second, ability to pay for [11 USC] Section 707(b) purposes, is measured by evaluating debtor's financial condition in a hypotheticalChapter 13 proceeding." [1084] The *Koch* court also noted that exempt income not reasonably needed for support becomes disposable income under a Chapter 13 plan. The First Circuit has also adopted the totality of the circumstances test. [1085]

Some courts have also dismissed a Chapter 7 under **Section 707(a)** for bad faith. That section allows a court to dismiss a Chapter 7 petition "for cause," including "three enumerated circumstances." [1086] In *In re Zick*, [1087] the court held that the phrase "including" meant that the three enumerated circumstances were not exclusive and could include an absence of good faith or bad faith. The *Zick* court held that this could be established where the debtor has substantial resources with which to satisfy his outstanding obligations (i.e., similar to a dismissal under **Section 707(b)** in connection with consumer debts). In *Zick* the court found bad faith where the debtor had sufficient assets for the following reasons:

1. His monthly net income was at least $7,000.
2. His business gross income was $361,000 for the year of filing.
3. He had approximately $90,000 in other assets exclusive of real estate and household goods.
4. His spouse had additional income.

Sufficient cause for dismissal under **Section 707(a)** was described in *In re Bilzerian*. [1088] In this case, the court dismissed on motion of the SEC on the grounds that the debtor filed for bankruptcy only to thwart the collection efforts of the SEC. The *Bilzerian* court adopted a totality of the circumstances test and noted that the significant debt to the SEC was nondischargeable, [1089] and Bilzerian was facing incarceration on a contempt proceeding, which he hoped to avoid by filing a Chapter 7 petition. [1090]

The Ninth Circuit, however, rejected a dismissal on the basis of bad faith under **Section 707(a)**, noting that the statutory language of Chapter 7 did not require good faith, whereas the statutory language relative to Chapters 11 and 13 specifically requires good faith. [1091] The Eighth Circuit has adopted a similar view. [1092]

¶ 12.02[8] Preferential Treatment for Residence

Although the attempt to conceal ownership of a residence is fatal, [1093] debtors have considerable latitude in arranging to retain access to their homes without sustaining a denial of discharge. For example, a sale and leaseback was approved in *In re Adlman*. [1094] In that case, the debtor sold property to her husband's aunt and uncle and used the proceeds to repay loans on insurance policies and to pay a premium on those policies. The residence was then leased back to the debtors, who continued to reside there. The net proceeds from the sale of the residence were approximately $60,000 in 1976. In approving the transaction, the court stated that in the absence of extrinsic fraud, the denial of discharge would be improper. [1095]

Another case allowed the debtors to transfer their home for fair and adequate consideration where the transferee, the debtor's father, allowed them to use the house. The court said that it was not fraudulent to allow the debtors to live in the house rent free and that it was simply up to the transferee, the debtor's father, and the debtor's use of the property is not necessarily fraudulent. [1096]

In addition, the homestead exemption can be bolstered by reducing the mortgage on the eve of bankruptcy, provided that no business assets are used and no debts are incurred that could not be paid as part of the transaction. [1097] But when a court is intent on punishing a debtor, it can do so even if the prebankruptcy planning involves a preferred asset such as a residence. Thus, in *In re Boudrot*, [1098] the debtor converted nonexempt assets into exempt assets by paying down the mortgage on a homestead. The Bankruptcy Court in *Boudrot* held that this was improper and justified a denial of discharge under Section 727(a). In so holding, the *Boudrot* court relied heavily on the fact that the debtor made the transfer shortly after entry of the state court judgment against him "without any credible statement of an intent to engage in bona fide bankruptcy planning." [1099]

¶ 12.02[9] Summary

Debtors who engage in prebankruptcy planning to convert nonexempt property into exempt property play a high-risk game. The rewards for playing are shielding assets as exempt property, and the punishment for crossing the nebulous line of improper prebankruptcy planning is the denial of discharge for all debts or denial of the exemption. In light of some of the seemingly inconsequential conduct that is characterized as fraud for purposes of denying discharge, this punishment seems harsh, especially so in light of great divergence of opinions on the matter. Often the result will depend on the circuit in which the case arises and the inclinations of the judge before whom the matter is heard.

[877] See, e.g., Hanson v. First Nat'l Bank, 848 F2d 866, 868 (8th Cir. 1988) (although a denial of exemption case, the court cited many denial discharge cases to support its decision).

[878] See, generally, **¶ 12.01[7][b]**. See, e.g., In re Grand Jury Proceedings, G.S., F.S., 609 F3d 909, 914 (8th Cir. 2010) (Crime-fraud exception to both attorney-client privilege and work product privilege applied where debtors transferred virtually all of their non-exempt property, worth hundreds of thousands of dollars, to close relatives, and after bankruptcy was complete debtors recovered the assets. If debtors "had a secret agreement with their relatives to retrieve their property post-bankruptcy, as the circumstances tend to suggest, it is also arguable that their conduct involved illegal concealment of assets.")

[879] See, **¶ 12.01[1][b]**.

[880] HR Rep. No. 595, 95th Cong., 1st Sess. 361 (1977), reprinted in 1978 USCCAN 5963, 6317; S. Rep. No. 989, 95th Cong., 2d Sess. 75, reprinted in 1978 USCCAN 5787, 5862.

[881] Wudrick v. Clements, 451 F2d 988 (9th Cir. 1971) ; Grover v. Jackson, 472 F2d 589, 590 (9th Cir. 1973) ; Forsberg v. Security State Bank, 15 F2d 499 (8th Cir. 1926) ; In re Adlman, 541 F2d 999, 1003 (2d Cir. 1976) ; Norwest Bank of Neb., NA v. Tveten, 848 F2d 871, 873–874 (8th Cir. 1988) ; In re Bowyer, 916 F2d 1056, 1059 (5th Cir. 1990) ; Ford v. Poston, 773 F2d 52, 54 (4th Cir. 1985) ; In re Reed, 700 F2d 986, 991 (5th Cir. 1983) ; In re Smiley, 864 F2d 562, 566 (7th Cir. 1989) ; Hansen v. First Nat'l Bank, 848 F2d 866, 868 (8th Cir. 1988) ; In re Carey, 938 F2d 1073, 1076 (10th Cir. 1991) (conversion is insufficient to result in denial of discharge, no fraud extrinsic to mere conversion and relatively minor amounts); In re Roosevelt, 176 BR 200, 207–208 (9th Cir. BAP 1994) , aff'd, 87 F3d 311 , modified, 98 F3d 1169 , cert. denied, 117 S. Ct. 1691 (1997) (debtor's right to convert nonexempt property into exempt property includes the transfer of property that, although nonexempt, cannot be levied upon, such as education and the medical practice); In re Holt, 894 F2d 1005 (8th Cir. 1990) (court upheld lower court finding of no fraud in connection with the conversion of nonexempt funds into reasonable amount of exempt insurance; the court confirmed that a debtor may convert nonexempt assets into exempt assets on the eve of bankruptcy; the conversion, however, must not be done with intent to defraud creditors as manifested by extrinsic evidence); Schwartzman v. Wilshinsky, 50 Cal. App. 4th 619, 629, 57 Cal. Rptr. 2d 790 (1996) (transfer of assets to a retirement plan "which might otherwise be fraudulent is permitted if the funds qualify for an exemption"); In re Bogue, 240 BR 742, 750 (Bankr. ED

Wis. 1999) (prebankruptcy conversion of assets from nonexempt to exempt within a year of filing a bankruptcy petition is not necessarily fraudulent to creditors, and to find such fraudulent intent there must be “extrinsic signs of fraud”); In re Sholdan, 217 F3d 1006, 1010 (8th Cir. 2000) (mere conversion is not itself fraudulent; to be fraudulent “there must appear in evidence some facts or circumstances which are extrinsic to the mere facts of conversion of nonexempt assets into exempt and which are indicative of such fraudulent purpose”); In re Wadley, 263 BR 857, 859–861 (Bankr. SD Ohio 2001) (the court once again confirmed that the mere conversion of nonexempt assets into exempt assets does not, by itself, establish fraud: “the intent to effect such a transfer is merely the intent to exercise a valid right [i.e., use of an exemption] rather than an intent to defraud,” citing In re Armstrong, 931 F2d 1233, 1238 (8th Cir. 1991) ; the court also noted absence of concealment or attempt to mislead creditors and a full disclosure was made to the bankruptcy trustee; further the amount involved was modest. *Wadley*, supra, at 860–861.). In re Kemmer, 265 BR 224, 231–232 (Bankr. ED Cal. 2001) (mere act of conversion not fraudulent; and actual fraudulent intent not established by fire sale undertaken solely in an attempt to convert nonexempt assets into exempt assets, which “did not exceed the bounds of acceptable exemption planning.”). In re Robinson, 271 BR 437, 441 (Bankr. NDNY 2001) (conversion of nonexempt real property into exempt annuities for $5,000 made seven months before filing a petition and the advice of counsel was allowed under the following circumstances: lack of evidence of extrinsic fraud, debtors were elderly and insolvent but paid fair consideration, husband was 74 years old and was continuing to work to support his family, his wife was in ill health, the annuities were purchased in anticipation of their future needs, the conversion was made seven months before the bankruptcy petition was filed). In re Bradley, 294 BR 64, 68-69 (8th Cir. BAP 2003) (“under the Code, the conversion of nonexempt assets into exempt assets, without more, will not deprive a debtor of the right to claim the exemption to which he is otherwise entitled;” relying, among other cases, In re Holt, 894 F2d 1005, 1008 (8th Cir. 1990) ; the court so held even though (1) substantially all of the debtor's assets were converted and (2) he was insolvent at the time and he had obtained legal advice that acquiring exempt property would reduce his exposure). In re Vangen, 334 BR 241, 248 (Bankr. WD Wis. 2005) (conversion of nonexempt into exempt assets was not improper absent evidence of fraud extrinsic to the very act of conversion; limitations on amount of funds converted is for the legislature to determine, not the courts; accordingly, debtor was allowed to convert $136,000 into an exempt annuity, which the court characterized as “not particularly sizeable”). In re Martiny, 378 BR 52 (Bankr. WDNY 2007) (prebankruptcy planning was approved whereby debtors increase equity in homestead by using nonexempt assets to reduce the mortgage; court held that absent fraud, such planning and execution was not improper). But see In re Levine, 134 F3d 1046 (11th Cir. 1998) (discussed at length below); In re Butts, 45 BR 34, 38 (DND 1984) (the legislative history is either “erroneous or merely ambiguous”); Mickelson v. Anderson, 31 BR 635 (D. Minn. 1982) (in denying the exemption, the court characterized the legislative history as irrelevant and without authority); In re Swecker, 157 BR 694, 695–696 (Bankr. MD Fla. 1993) (the court suggested that a conversion of nonexempt assets into exempt assets could be fraudulent where there is “an imminent threat of levy, attachment, garnishment, or execution on a judgment just prior to the debtors' conversion of assets,” although there was no such evidence in this case). In re Addison, 540 F3d 805 (8th Cir. 2008) (conversion of $11,500 of nonexempt assets into a homestead was proper even though (1) a transfer was made to an insider, (2) debtor retained control of the property, (3) debtor was insolvent; none of which constituted evidence of fraud extrinsic to the very conversion; the only such evidence, i.e., transaction occurred in the face of litigation, was insufficient to result in a denial of the exemption; the court ruled the same with respect to debtor's $4,000 IRA; the court also declined to deny debtor's discharge, ruling that the “the same standard applies to determine whether a discharge should be denied or whether a transfer of nonexempt property to exempt property should be voided; both require proof that the debtor acted with the intent to hinder, delay, or defraud a creditor.”). In re Danduran, 438 BR 658, 661 (8th Cir. BAP 2010) (the conversion of nonexempt property into exempt property was allowed in the absence of fraud by the debtor).

881.1

In re Danduran, 657 F3d 749, 753 (8th Cir. 2011) rev'g, In re Danduran, 438 BR 658 (8th Cir. BAP 2010) (Emphasis added).

882

In re Stern, 317 F3d 1111 (9th Cir. 2003) (Alarcón, senior circuit judge, concurring in part, dissenting in part), opinion amended and superseded on denial of reh'g by 345 F3d 1036 (2003) .

883

See Cal. Civ. Proc. Code § 704.115(e); In re Cheng, 943 F2d 1114, 1116 (9th Cir. 1991) .

884

In re Stern, 345 F3d 1044 (9th Cir. 2003) .

885
In re Stern, 345 F3d 1044–1045 (9th Cir. 2003) .

886
In re Stern, 345 F3d 1044–1045 (9th Cir. 2003) .

887
In re Crater, 286 BR 756 (Bankr. D. Ariz. 2002) .

888
In re Crater, 286 BR 764 (Bankr. D. Ariz. 2002) .

889
The following badges of fraud may be innocent in themselves, or are merely timing factors that become suspicious only when combined with other factors: (1) before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit; (2) the transfer was of substantially all of the debtor's assets; (3) the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred; and (4) the transfer occurred shortly before or shortly after a substantial debt was incurred. In re Crater, 286 BR 764–765 (Bankr. D. Ariz. 2002) .

890
In re Beverly, 374 BR 221 (9th Cir. BAP 2007) . aff'd, on this point, In re Beverly, 551 F3d 1092 (9th Cir. 2008) .

891
In re Barker, 168 BR 773, 778 (Bankr. MD Fla. 1994) (although right to convert nonexempt assets into exempt assets upheld, transfer was voided under **11 USC § 548** as a fraudulent transfer); cf. In re Davidson, 178 BR 544, 548 (SD Fla. 1995) (conversion to exempt annuity because debtor feared that creditors would attach nonexempt assets was sufficient to result in a denial of discharge under **11 USC § 727(a)(2)**, which is a question of federal law). In re Ganier, 403 BR 79, 86 (Bankr. D. Idaho 2009) ("amount" of transfer constituted extrinsic fraud even though it was approximately $60,000 because that amount would have been sufficient to provide substantial payment to creditor, i.e., "'magnitude of transfer' issue must be viewed as case specific"; further, the amount together with the nondisclosure of the conversion of non-exempt assets into homestead and IRA was sufficient at the pleading stage to state a claim for fraudulent transfer for prebankruptcy planning).

892
In re Beahm, 179 BR 329, 334 (Bankr. SD Fla. 1995) (conversion avoided under trustee's strong arm power where it violated state fraudulent transfer law); In re Covington, 171 BR 294, 295 (Bankr. MD Tenn. 1994) (conversion into exempt property and transfer of remainder interest could be voided under trustee **Section 544(b)** powers where applicable state law specifically provided that such conversions undertaken for the specific purpose of placing assets beyond reach of creditors constitutes a fraudulent transfer); In re Strehlow, 84 BR 241, 245 (Bankr. SD Fla. 1984) (under Florida law).

893
In re Levine, 134 F3d 1046 (11th Cir. 1998) .

894
In re Levine, 134 F3d 1046, 1048 (11th Cir. 1998) .

895
In re Levine, 134 F3d 1046, 1052 (11th Cir. 1998) . *Levine* was cited with apparent approval in In re Havoco, 790 So2d 1029 (11th Cir. 2001) contrasting the exemption for annuities with the constitutional exemption for Florida homesteads.

896

In re Chauncey, 308 BR 97, 105-106 (Bankr. SD Fla. 2004) ; discharge was also denied under 11 USC § 727(a)(3) (failure to preserve records; doctor claimed that she lost all the books and records), aff'd, Slip Copy, 2005 WL 2456223 (SD Fla. 2005) aff'd on these issues, 454 F3d 1292, 1295 (11th Cir. 2006).

897
See ¶ 12.02[4][a].

898
In re Delcorso, 382 BR 240 (Bankr. ED. Pa. 2007) (transfer of residence by wife to wife and husband as tenants by the entireties was held to be both actual and constructive fraudulent transfer under the Bankruptcy Code as well as the fraudulent transfer act under applicable state law; the case is notable because the debtor's counsel was ordered to disgorge fees and was sanctioned, and the court characterized the transaction as “one of the grossest, law school examination examples of a fraudulent transfer that one might see”; the court pointed to numerous factors including a failure to disclose the prebankruptcy planning and the attorney's lack of experience, i.e., he never litigated a fraudulent transfer case).

899
In re Kemmer, 265 BR 224, 231–232 (Bankr. ED Cal. 2001) .

900
See **¶ 3.04[2]**.

901
See **¶¶ 3.03[2][b]**, **3.03[2][b][i]**, 3.03[2][b][ii]; In re Arbaney, 345 BR 293 (Bankr. D. Colo. 2006) (transfer of real property to the debtor was not fraudulent because the net effect was that the creditors received more than they would have without the transfer, which was part of a plan to, among other things, sell an easement for a tax credit, the proceeds of which were applied to reduce outstanding debt; court examined what would have happened if the transaction had not occurred).

902
The Employee Retirement Income Security Act of 1974, as amended; see **29 USC §§ 101** et seq.

903
29 USC § 1144(a) (ERISA “supersedes any and all State laws insofar as they may now or hereafter relate to any employee benefit plan”).

904
29 USC § 1056(d)(1) (“Each pension plan shall provide that benefits provided under the plan may not be assigned or alienated.”).

905
See, e.g., General Motors Corp. v. Buhau, 623 F2d 455 (6th Cir. 1980) .

906
11 USC § 541(c)(2) (trust subject to antialienation provision enforceable under applicable nonbankruptcy law is excluded from estate).

907
28 USC §§ 3001–3307.

908
See, **¶ 12.02[2][a][ii]**.

[909] In re Shailam, 144 BR 626, 629 (Bankr. NDNY 1992) .

[910] See generally **¶ 13.03[4][c]** (laws of general application that are not designed to affect ERISA plans are not preempted).

[910.1] Central States, Southeast and Southwest Areas Pension Fund v. LaCasse, 254 F.Supp.2d 1069, 1072 (ND Ill. 2003) ("Whether it is viewed as a state or a federal common law claim, then, the plaintiffs' fraudulent conveyance claim is not preempted by ERISA"); Central States, Southeast and Southwest Areas Pension Fund v. Minneapolis Van & Warehouse Co., 764 F.Supp. 1289, 1295–96 (ND Ill. 1991) ("This Court accordingly exercises its equitable powers under ERISA to impose a constructive trust on the distributed assets (or on the sale price of any assets distributed and then sold) for the benefit of Pension Fund" (citations omitted)). As the LaCasse court noted, the reason that state law fraudulent conveyance claims are not preempted is that "ERISA provides no mechanism for the enforcement of judgments, [and thus] 'state-law methods for collecting money judgments must, as a general matter, remain undisturbed by ERISA.' " LaCasse, 254 F.Supp.2d 1071 (quoting Mackey v. Lanier Collection Agency, & Service, Inc., 486 US 825, 843 (1988)); Oregon Laborers-Employers Health & Welfare Trust Fund v. All State Indus. and Marine Cleaning, Inc., 850 F.Supp. 905, 909, 910 (D. Or. 1994) (employee trust funds obtained a judgment relative to contributions that were required to be made; "The fraudulent conveyance statutes in the State of Oregon are state laws of general applicability and do not relate to any employee benefit plan. The claims of the Trusts for fraudulent conveyance are not preempted by ERISA." Citing Mackey for the proposition that "Congress did not intend to forbid the use of general state laws for executing judgments against ERISA welfare benefit plans.…The*Mackey* court also stated that other state law procedures could be used against ERISA plans, citing Fed.R.Civ.P. 69(a), which defers to state law to provide procedures for collecting judgments." Citations omitted); In re Consol.Lit. Concerning Intern. Harvester's Disp. Of Wis. Steel, 681 F.Supp. 512, 525 (ND Ill. 1988) ("This court does not believe that Congress intended to preempt state fraudulent transfer law from applying to a PBGC [i.e., Pension Benefit Guaranty Corporation] claim for employer liability. Consider a hypothetical situation where an employer, just before termination of his pension plan, conveys all his assets to a nominee for $1, leaving himself with a net worth of $100. If the PBGC could not take advantage of fraudulent conveyance principles its claim against this employer would be limited to $30, 30% of his net worth."); Klemme v. Shaw, Not Reported in F.Supp.2d, 2007 WL 838958 (D. Nev. 2007) (In the context of a corporate liquidation that diverted funds from funding an ERISA plan; employees of former corporation were allowed to maintain claim for fraudulent transfer, which was not preempted by ERISA.;state UFTA "is a law of general applicability governing the debtor-creditor relationship that functions irrespective of the existence of ERISA plans. While ERISA may provide the context in which the debtor becomes liable to the creditor, the fraudulent transfer statute is a procedural mechanism by which a creditor may attempt to ensure assets exist against which to enforce a judgment. As such, it is similar to other state laws of general application relating to the enforcement of judgments which ERISA does not preempt, such as garnishment or a payment bond remedy").

But see, Central States, Southeast and Southwest Areas Pension Fund v. Marquette Bank, Minneapolis, N.A., 836 F.Supp. 673, 676-677 (D. Minn. 1993) (UFTA claim by pension plan against bank to whom payments were made by participant corporation; the claim was for funds that corporation was otherwise required to fund an ERISA plan, i.e., for withdrawal liability; Thus, the fraudulent transfer claim was "an alternative to collect[ing] the withdrawal liability of the pension defendants, an obligation which is established and enforced under ERISA. Thus, at their core, the claims against Marquette Bank arise under ERISA and seek to satisfy liability imposed by ERISA." preemption applied because "the enforcement scheme ERISA provides for withdrawal liability is an exclusive remedy." "The court concludes that ERISA's remedies for collecting withdrawal liability were meant to "supplant any remedy that otherwise would be available" to the plan." Noting also that the rights sought to be enforced were ERISA rights).

[911] In re Loomer, 198 BR 755 (Bankr. D. Neb. 1996) .

[912] **29 USC § 1056(d)(1)**. See also **11 USC § 541(c)(2)** (trust subject to antialienation provision enforceable under applicable nonbankruptcy law is excluded from estate).

[913]

Guidry v. Sheetmetal Pension Fund, 493 US 365 (1990) ; In re Loomer, 198 BR 755, 759–760 (Bankr. D. Neb. 1996) .

914

In re Loomer, 198 BR 755, 761 (Bankr. D. Neb. 1996) ; Guidry v. Sheetmetal Pension Fund, 493 US 365, 375–376 (1990) ; see also SEC v. Johnston, 922 F. Supp. 1220, 1222–1223 (ED Mich. 1996) (interest in an ERISA plan could not be reached to satisfy a claim—namely, a disgorgement of profits order), rev'd on the ground that debtor was sole owner of sponsor, 143 F3d 260 (6th Cir. 1998) .

915

In re Shailam, 144 BR 626, 631 (Bankr. NDNY 1992) . (It is not clear how this portion of the *Shailam* court's decision would apply if it had found that the transfer to the plan constituted a fraudulent transfer. In this regard, the court held that the fraudulent transfer laws were not preempted by ERISA. But, in this case, the professional corporation, which made the contribution to the pension plan, did not commit a fraudulent transfer; presumably the court would have still followed *Guidry*, and the plan would have been protected by ERISA's anti-alienation provision. (*Shailam* held that the transfer to the plan, which was made by debtor's professional corporation, did not constitute a fraudulent conveyance and that piercing of the corporate veil or disregard of the corporate entity was not justified)).

916

11 USC § 550(a)(1).

917

See **¶ 13.03[3][c]**.

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In so noting, the court cited Nash v. Trustees of Boston Univ., 946 F2d 960 (1st Cir. 1991) .

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Cooperative Ben. Adm'rs, Inc. v. Ogden, 367 F3d 323, 330 (5th Cir. 2004) .

920

See, e.g., Ogden, 367 F3d 330 (5th Cir. 2004) .

921

ERISA § 503(a)(3); **29 USCA § 1132(a)(3)**.

922

Great-West Life & Annuity Ins. Co. v. Knudson, 534 US 204, 213-214 (2002) ; Rego v. Westvaco Corp. 319 F3d 140, 145 (4th Cir. 2003) (damages measured by the difference in valuation on the date plaintiff was entitled to distribution and date plaintiff received distribution did not constitute equitable restitution since there was no property or funds that belonged to plaintiff; he was simply seeking a share of plan assets).

923

Rego v. Westvaco Corp., 319 F3d 140, 145 (4th Cir. 2003) (damages measured by the difference in valuation on the date plaintiff was entitled to distribution and date plaintiff received distribution did not constitute equitable restitution since there was no property or funds that belonged to plaintiff; he was simply seeking a share of plan assets); Cooperative Ben. Adm'rs, Inc. v. Ogden, 367 F3d 323 (5th Cir. 2004) (plan administrator's legal action not allowed); cf., Pacificare Inc. v. Martin, 34 F3d 834, 836 (9th Cir. 1994) ("the Ninth Circuit has expressly refused to create federal common law causes of action under ERISA" for unjust enrichment, although federal common law exists relative "to rights and obligations under the ERISA plan and not to causes of action.."); Shipley v. Arkansas Blue Cross and Blue Shield, 333 F3d 898 (8th Cir. 2003) (no ERISA section provides for rescission, therefore, "federal common law allows for the equitable rescission of an ERISA-governed insurance policy that is procured through the material misstatements or omissions of the insured"); Sec. Life Ins. Co. of Am. v. Meyling, 146 F3d 1184, 1191 (9th Cir. 1998) (equitable rescission allowed); Davies v. Centennial Life Ins. Co., 128 F3d 934, 943-944 (6th Cir.1997) (equitable rescission based on misrepresentation); Hauser v. Life Gen.

Sec. Ins. Co., 56 F3d 1330, 1333-1335 (11th Cir. 1995) (assuming that a right of rescission exists under ERISA-created federal common law); **Griggs v. E.I. DuPont de Nemours & Co., 385 F3d 440 (4th Cir. 2004)** (effective rescission of an election to receive type of distribution allowed, noting that it was similar to equitable rescission, which is allowed with regard to ERISA).

924

Pacificare Inc. v. Martin, 34 F3d 834, 836 (9th Cir. 1994) ("the Ninth Circuit has expressly refused to create federal common law causes of action under ERISA" for unjust enrichment, although federal common law exists relative "to rights and obligations under the ERISA plan and not to causes of action.."); Provident Life & Accident Ins. Co. v. Cohen, 423 F3d 413 (4th Cir. 2005) (fiduciary's rights are limited to equitable remedies and preclude legal remedy of unjust enrichment).

925

Calif. Div. of Labor Standards Enforcement Calif. Div. of Labor Standards Enforcement v. Dillingham Const., N.A., Inc., 519 US 316, 326, 328 (1997) (funded plan is subject to ERISA, whereas a plan that is not funded is not subject to ERISA; state's wage law relative to an apprenticeship program was not preempted by ERISA, because, among other things, it "can be approved whether or not its *funding apparatus* is of a kind as to bring it under ERISA. [citation omitted]… it is indifferent to the *funding*, and attendant ERISA coverage, of apprenticeship programs. Accordingly, California's prevailing wage statute does not make reference to ERISA plans." (Emphasis added)); Oregon Columbia Brick Masons Joint Oregon Columbia Brick Masons Joint Apprenticeship Training Committee v. Gardner, 448 F3d 1082, 1087 (9th Cir. 2006) (in assessing whether an apprentice program was preempted by ERISA, the court focused on "is whether it 'is indifferent to the funding, and attendant ERISA coverage, of apprenticeship programs'"); Associated Builders and Contractors of Associated Builders and Contractors of Southern California, Inc. v. Nunn, 356 F3d 979 (9th Cir. 2004) (same as to state's minimum wage and benefits requirement); Prudential Ins. Co. of America v. National Park Medical Center, Inc., 154 F3d 812, 821 (8th Cir. 1998) (considered same with reference to health care provider programs); American Cleaners and Laundry Co. Inc. v. Textile Processors, Service Trades, Health Care Professional and Technical Employees Intern. Union Local 161, 482 F.Supp.2d 1103, 1115 (ED Mo. 2007) (in assessing whether a claim for unjust enrichment is preempted by ERISA, the court stated: "that the state common law unjust enrichment claim does not make a specific reference to ERISA, and therefore is not preempted under the first prong", and quoting Dillingham, 519 U.S. 327 "'The California law is indifferent to the funding, and attendant ERISA coverage, of apprenticeship programs. Accordingly, California's prevailing wage statute does not make reference to ERISA plans.'").

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But see In re Shailam, 144 BR 626, 629 (Bankr. NDNY 1992) (state fraudulent transfer laws are laws of general application, neutral, and therefore not preempted by ERISA). See also, discussion of *Shailam* and cases that support the*Shailam* view at **¶ 12.02[2][a][i]**.

927

Payments made to the retirement plans within one year of bankruptcy could be voided as so-called preference payments. In re Pulaski Highway Express, Inc., 41 BR 305, 309–312 (MD Tenn. 1984) (eve of bankruptcy payment to satisfy arrearages to pension plan could be subject to preference, no discussion of ERISA preemption, court held that return of funds did not violate ERISA provision that prohibited inurement to benefit of employer). See also In re Deprizio Constr. Co., 86 BR 545, 553–554 (ND Ill. 1988) , aff'd in part, 874 F2d 1186 (7th Cir. 1989) (*Pulaski* followed, no discussion of preemption); In re Ottawa Cartage, Inc., 55 BR 371 (ND Ill. 1985) (to the same effect, although the court also noted that ERISA's preemption clause did not require subordination of federal preference payment provision to ERISA's prohibition against inurement to employer); In re Sterling Die Casting Co., 118 BR 205, 208 (Bankr. EDNY 1990) (*Pulaski* followed).

It is possible that the so-called "ordinary business exception" would apply. This exception to the preference rules applies where the debt was incurred "ordinary course of business or financial affairs of the debtor and the transferee, and such transfer was-

(A) Made in the ordinary course of business or financial affairs of the debtor and the transferee; *or*

(B) made according to ordinary business terms."

11 USCA § 547(c)(2)(emphasis added). See, **¶ 3.07[6][a]**.

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Fla. Stat. Ann. § 222.30 (the time limitation is four years after conversion).

929

In re Scott Wetzel Services, Inc., 293 BR 791, 794 (Bankr. MD Fla. 2003) (Fla. Stat. § 222.30, provides relief to party the claims the debtor fraudulently converted nonexempt assets into exempt assets; an attempt to apply this section to the ex-spouse of the principal shareholder of the debtor corporation was unsuccessful since the ex-spouse was not the debtor at the time she converted the cash received an converted it into an exempt annuity; the court held, however, that a constructive trust action could be maintained, see **¶ 4.06[2]**)

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In re Levine, 134 F3d 1046 (11th Cir. 1998) .

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Fla. Stat. Ann. § 222.29.

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Havoco of Am. v. Hill, 790 So. 2d 1018 (Fla. 2001) .

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Tex. Prop. Code Ann. § 42.004 (conversion with fraudulent intent results in loss of exemption, where limitation period is two years after transaction from which claim arose). In re Coates, 242 BR 901, 906–907 (Bankr. ND Tex. 2000) (relying on Tex. Prop. Code Ann. § 42.004, the court prevented debtors from paying down a lien against automobiles that were exempt under Texas law, but noted that the statute applied only to personal property and not real property; consequently, the debtor's homestead exemption was unaffected). Tex. Ins. Code Ann. § 1108.053(1) (exemptions for certain insurance and annuity benefits are not applicable to payments of premium “made in fraud of a creditor,” subject to the applicable limitations period relative to recovery thereof); In re Soza, 542 F3d 1060 (5th Cir. 2008) (Tex. Ins. Code Ann. § 1108.053(1)—“fraud” resulting in denial of an exemption includes both intentional fraud and “conduct less than intentional fraud,” although it does not include “constructive fraud” of the UFTA; court used the badges of fraud of the UFTA to determine whether debtor's conduct constituted “fraud”; court concluded that although “intentional fraud” was not present, that the eve of bankruptcy purchase of an annuity constituted “fraud” based on the badges of fraud, i.e., creditors would have been denied most of their claims, retention by the debtors of control of the annuity, use of the annuity to avoid an inquiry into an inheritance rather than for the purpose of allowing debtor to gain a fresh start).

934

Wyo. Stat. Ann. § 26-15-132(a)(i) (annuity exempt except as to amounts paid “with intent to defraud creditors”); In re Baker, 273 BR 892 (Bankr. D. Wyo. 2002) (conversion of nonexempt property into annuity constitutes a fraudulent transfer where prohibited intent present as evidence by standard badges of fraud).

935

Ohio Rev. Code § 3911.10 (“the amount of any premium upon such contracts, endowments, or annuities, paid in fraud of creditors, with interest thereon, shall inure to their benefit from the proceeds of the contracts”).

936

Kan. Stat. Ann. § 40-414 (restricts exemption for life insurance policies acquired within a year of bankruptcy or judgment).

937

A transfer to a trust that qualifies under various Internal Revenue Code provisions such as retirement plans and IRAs, can be avoided if they constitute fraudulent transfers. **NJ Stat. Ann. § 25:2-1**: “Conveyances of personal property in trust for use of persons making them void as to creditors . . .

> b. Notwithstanding the provisions of any other law to the contrary, any property held in a qualifying trust and any distributions from a qualifying trust, regardless of the distribution plan elected for the qualifying trust, shall be exempt

from all claims of creditors and shall be excluded from an estate in bankruptcy, except that:

(1) no exemption shall be allowed for any preferences or fraudulent conveyances made in violation of the ‘Uniform Fraudulent Transfer Act, § R.S.25:2-20 et seq., or any other State or federal law;

. . . For purposes of this section, a ‘qualifying trust' means a trust created or qualified and maintained pursuant to federal law, including, but not limited to, **section 401**, **403**, **408**, **408A**, **409**, **529** or **530** of the federal Internal Revenue Code of 1986 (26 U.S.C. § 401, 403, 408, 408A, 409, 529 or 530.”); see also NJ Stat. Ann. 17B:24-7(a)(1) (excluding from exemption “amounts paid, with intent to defraud creditors”).

938

NY CPLR § 5205(c)(5) (exemptions for, among other things, retirement plans, not applicable where addition to otherwise exempt trust violates fraudulent transfer law and where made 90 days before “the interposition of the claim on which . . . judgment was entered”).

939

Me. Rev. Stat. Ann. tit. 14, § 4423 (property converted into exempt property within 90 days of attachment or filing of the bankruptcy petition is not exempt). See also Me. Rev. Stat. Ann. tit. 14, § 4422 (where property had been fraudulently transferred it cannot be exempt).

940

735 Ill. Comp. Stat. 5/12-1001. “Personal property exempt. The following personal property, owned by the debtor, is exempt from judgment, attachment, or distress for rent: [enumerating exempt property]

If a debtor owns property exempt under this Section and he or she purchased that property with the intent of converting nonexempt property into exempt property or in fraud of his or her creditors, that property shall not be exempt from judgment, attachment, or distress for rent. Property acquired within 6 months of the filing of the petition for bankruptcy shall be presumed to have been acquired in contemplation of bankruptcy.”

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See, e.g., In re Mueller, 867 F2d 568, 570 (10th Cir. 1989) (state statute allowed exemption except for claims filed within one year after the date the policy is issued if the policy was obtained by the debtor for the purpose of defrauding one or more of the debtor's creditors; in affirming a denial of the exemption it noted the following badges of fraud: “(1) the debtor was insolvent when he purchased the policy; (2) the policy was purchased one week prior to the filing of his petition in bankruptcy; (3) the debtor used his last nonexempt assets to make the acquisition; (4) the debtor had two other unencumbered life insurance policies; (5) although the debtor contended he purchased the last policy to provide for his daughter's education, the named beneficiaries are the ‘then living children of the insured, and the then living children of any child of the insured who is not then living, per stirpes'”).

942

See, e.g., Havoco of Am. v. Hill, 790 So. 2d 1018 (Fla. 2001) ; In re Young, 235 BR 666, 671, 672 (Bankr. MD Fla. 1999) .

943

Society of Lloyd's v. Collins, 284 F3d 727, 730 (7th Cir. 2002) (continuing to pay premiums on long-standing insurance policy purchased before involvement with creditor could not be set aside).

944

In re Weinstein, 164 F3d 677, 683 (1st Cir. 1999) (applicable state law allowed an exemption for a homestead, “except…or a debt contracted prior to the acquisition of said estate of homestead.”), cert. denied sub nom. Patriot Portfolio, LLC v. Weinstein, 119 S. Ct. 2394 (1999) ; see also In re Fracasso, 222 BR 400, 401 (BAP 1st Cir. 1998) , aff'd, 187 F3d 621 (1st Cir. 1999) (unpublished opinion); In re Leicht, 222 BR 670 (BAP 1st Cir. 1998) .

945

In re Weinstein, 164 F3d 682 (1st Cir. 1999) ; see also In re Maddox, 15 F3d 1347, 1351 (5th Cir. 1994) (lien avoidance under § 522 (f) is not limited by state exceptions); In re Opperman, 943 F2d 441, 443 (4th Cir. 1991) (state homestead statute invalidated to the extent that it conflicted with § 522(f)); In re Crowell, 138 F3d 1031, 1035 (5th Cir. 1998) (bankruptcy court was not bound to follow Texas procedure for designating the debtor's homestead; governing law is Bankruptcy Code, which incorporates state law "to the extent that it allows a debtor to claim a state-law exemption under Section 522(b)(2)(A)"); In re Skjetne, 213 BR 274, 277–279 (Bankr. D. Vt. 1997) (state law that limited increase in homestead exemption to debts created after effective date of legislation could not limit debtor's exemption; Federal law expands the rights of debtors to exemptions under applicable state law, specifically, to "any property that is exempt under…state or local law that is applicable on the date of the filing of the petition." 11 USC Section 522(b)(2)(A)). In re Evans, 362 BR 275 (Bankr. DSC 2006) (Bankruptcy Code preempts state law that limits exemptions to those existing at date contract is executed; debtor may claim exemptions that exist under applicable state law on the date of the filing of the petition, **11 USCA § 522(b)(3)(A)**). Skjetne was rejected in In re Lewis, 400 BR 417 (Bankr. D. Vt. 2009) (§ 522(c) did not preempt Vermont statute limiting debtor's state law homestead exemption by providing that it would not be effective to prevent execution for debts existing at time debtor acquired homestead; also rejecting In re Euber, 217 BR 448 (Bankr. D. Vt. 1998) , and following In re Banner, 394 BR 292, 303-04 (Bankr. D. Conn. 2008) (§ 522(c) does not preempt state exemption).

946

In re Norkus, 256 BR 298, 304 (Bankr. SD Iowa 2000) (court declined to follow *Weinstein*, and instead held that the antecedent debt exception to the Iowa homestead exemption was not preempted by bankruptcy law); In re Fishman, 241 BR 568 (Bankr. ND Ill.1999) (rejecting *Weinstein*, relying on the Seventh Circuit's decision in In re Ondras, 846 F2d 33, 34 (7th Cir. 1988) — statute limiting exemption to claims not arising from tort claims — although Ondras did not consider **11 USCA § 522(c)** in its analysis). In re Lewis, 400 BR 417 (Bankr. D. Vt. 2009) (Vermont homestead was not effective with respect to pre-existing debts, i.e., debts owed by the debtor before he acquired the homestead, 27 VSA **§ 107**; **11 USCA § 522(c)**, which provides that property exempted by debtor shall not be liable, during or after the case, for any debt arising prepetition, did not expand the exemption under state law; following In re Banner, 394 BR 292, 303-04 (Bankr. D. Conn. 2008) (§ 522(c) does not pre-empt state exemption)); see also, CFCU Comm. Credit Union v. Hayward, 552 F3d 253 (2d Cir. 2009) (state law determines the available homestead exemption and **11 USCA § 522(c)** does not pre-empt state law to modify the exemption).

See also, **¶ 12.03[3][b][iv]** (lien that exists before or simultaneously with the acquisition of exempt property is not subject to removal under **11 USCA § 522(f)**).

947

Owen v. Owen, 500 US 305, 111 S. Ct. 1833, 114 L. Ed. 2d 350 (1991), on remand to 961 F2d 170 (11th Cir. 1992) .

948

Owen v. Owen, 500 US 308, 111 S. Ct. 1833 (1991) .

949

In re Konnoff, 356 BR, 206-207 (*Owen* does not prevent the loss of a homestead exemption as the result of a postpetition failure to reinvest proceeds that were exempt at the time the petition was filed because the state can impose conditions on the exemption, and indeed provide no exemption at all, so long as it does not conflict with the Bankruptcy Code; "Nothing in the Code prevents a state from imposing a time limit as a condition for allowing an exemption.").

950

See **¶ 12.02[1]**.

951

Cf., In re Weinstein, 164 F3d 677, 682-683, 687 (1st Cir. 1999) (held restriction on homestead exemption for previously contracted debts was preempted by § 522(c); the exceptions of § 522(c)(1)-(3), i.e., certain taxes, alimony, certain liens, were exclusive list, and because exception for previously contracted debts was not listed in § 522(c), the state provision was preempted by Bankruptcy Code).

952 Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (2005 Bankruptcy Act) § 1404(b)(2).

953 In re Weinstein, 164 F3d 677, 683 (1st Cir. 1999).

954 See 11 USCA § 544(b) ("The trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable*under applicable law* …." [Emphasis added]).

955 See, e.g., In re Reed, 700 F2d 985, 991 (5th Cir. 1983) (Texas exemption for homestead allowed, but discharge denied where conversion occurred with intent to defraud creditors); Norwest Bank of Neb., NA v. Tveten, 848 F2d 871, 873–874 (8th Cir. 1988) (debtor allowed exemption where only evidence is of prebankruptcy conversion of assets into exempt assets; but, the debtor's protection of $700,000 violated federal public policy and resulted in a denial of discharge).

956 See **¶ 12.04[1]**.

957 For example, a so-called pattern of sharp dealing has been treated as an indicium of fraud (**¶ 12.02[4][a][i]**).

958 See, e.g., Bank Leumi Trust Co. v. Lang, 989 F. Supp. 883, 889 (SD Fla. 1995) (conversion of approximately $1 million partially into exempt annuity held fraudulent because, among other things, debtors were not intended to be protected thereby; the court also relied on the time of the conversion, which was shortly before creditor obtained a judgment).

959 In re Segal, 227 BR 191, 195 (Bankr. SD Fla. 1998) .

960 See, e.g., In re Smiley, 864 F2d 562, 569 (7th Cir. 1988) ; In re Adeeb, 787 F2d 1343 (9th Cir. 1986) .

961 Arenz v. Astoria Sav. Bank, 281 F. 530 (9th Cir.) , cert. denied, 260 US 740 (1922) (debtor sold stock to his father who returned the stock after the bankruptcy); In re Holstein, 114 F. 794 (Conn. 1902) (transfer of money to a party to hold was characterized as a "concealed trust" and the purpose of regaining the money at a later date resulted in a denial of discharge).

962 In re Kaiser, 722 F2d 1574, 1583 (2d Cir. 1983) (acquiring property in this way will also cause imposition of a constructive trust).

963 In re Hazen, 37 BR 329, 332 (Bankr. Fla. 1983) .

964 In re Kaiser, 722 F2d 1574, 1583 (2d Cir. 1983) .

965 See, e.g., In re Warren, 512 F3d 1241 (10th Cir. 2008) (court was "most reluctant" to use prebankruptcy conversion of nonexempt assets into exempt as a basis to deny a discharge on the grounds of fraud; instead the court relied on debtors' failure to list as assets certain prepayments, the "peculiar transaction" whereby debtors acquired a homestead and returned it within months, debtors'

motivation to keep a certain creditor from obtaining anything through bankruptcy, the sale of coin collection for half its cost, which sale the court manifested as "(1) an effort to keep creditors from realizing the full value of their collection or (2) failure to report accurately how they disposed of the collection, an inference suggested by the absence of detailed records of the transactions, which the [debtors, who were both CPA's] could be expected to have kept.").

966

See **¶ 3.04[1][d]**. See, e.g., In re Pulliam, 279 BR 916, 923 (Bankr. MD Ga. 2002) (conversion into exempt asset, although not fraudulent per se, was characterized as fraudulent when accompanied by indicia of fraud, namely: the same custodian was used, there was retention of ownership, the transfer was made 10 days before the defendant filed for bankruptcy, the defendant was insolvent and unemployed, the defendant had few if any other unencumbered assets, and he offered to use his IRA distribution check to pay a family member).

967

Farmers Coop. Ass'n v. Strunk, 671 F2d 391, 395 (10th Cir. 1982) ("[f]raudulent intent of course may be established by circumstantial evidence, or by inferences drawn from a course of conduct"; the court relied on the fact that the debtor continued to write numerous checks on his account as supporting the assertion that he fraudulently concealed funds); see also In re Johnson, 124 BR 290 (Bankr. D. Minn. 1991) (debtor's postbankruptcy liquidation of exempt assets into which nonexmpt assets were converted supported finding that the exemptions were abused and resulted in a denial of discharge).

968

In re Crater, 286 BR 756 (Bank. D. Ariz. 2002) .

969

In re Crater, 286 BR 756, 764 (Bank. D. Ariz. 2002) .

970

In re Crater, 286 BR 767–773 (Bank. D. Ariz. 2002) ("'Debtors deserve more definite answers' than 'each bankruptcy judge's sense of proportion.'…Without more definite answers, 'debtors will be unable to know in advance how far the federal courts will allow them to exercise their rights under state law.'…The result will be that some debtors who relied on well intentioned advice of counsel may be denied a discharge, the bankruptcy equivalent of the death penalty, while others receive an unconscionable benefit, perhaps through ignorance or perhaps through cunning. And . . . for the judiciary to deny an exemption that the legislature has provided simply because the judge finds it out of proportion is to invade the province of the legislative branch."

"Congress did not invite bankruptcy judges to grant or deny the discharge based on an amorphous, individualistic finding such as 'reasonable' or 'good faith.'").

971

In re Smiley, 864 F2d 562, 569 (7th Cir. 1989) (debtor not only failed to volunteer information, but misrepresented the value of his assets to prevent them from filing an involuntary bankruptcy petition, which was intended to hinder and delay creditors). In re Maronde, 332 BR 593, 601 (Bankr. D. Minn. 2005) (sale of nonexempt assets and use of proceeds to reduce mortgage on homestead was characterized as fraudulent and resulted in a denial of the homestead pro tanto; court found actual fraud on the basis of debtor's failed attempt to accomplish same goal by use of credit cards; "In this case, debtor engaged in a scheme to defraud his creditors by using his (at the time) good credit to obtain a number of credit cards, use the cash advances, in the form of balance transfers, from those cards to pay off his equity credit line. He then intended to liquidate his truck and trailer to raise cash that he could offer to settle with his new creditors for less than he owed. That he failed and had to resort to Plan B and put the proceeds from the sale of the truck and trailer into his home does nothing to erase the original intent of the scheme: don't pay creditors in full and surely do not make an honest attempt to do so.")

972

In re Smiley, 864 F2d 562, 568 (7th Cir. 1989) , cited with approval in In re Bowyer, 916 F3d 1056, 1058 (5th Cir. 1990) .

[973] In re Addison, 540 F3d 813–814 (8th Cir. 2008) . See also In re Wilmoth, 397 BR 915 (8th Cir. BAP 2008) (prebankruptcy planning upheld; although there were some badges of fraud, there was no extrinsic evidence of fraud).

[974] In re Reed, 700 F2d 991–992 (5th Cir. 1983) .

[975] McKormick v. Security State Bank, 822 F2d 806 (8th Cir. 1987) ; In re Armstrong, 931 F2d 1237 (8th Cir. 1991) (intent to deceive and mislead is an indicium of fraud); In re Smiley, 864 F2d 568 (7th Cir. 1989) (misrepresenting the value or other misrepresentations that prevented creditors from filing an involuntary petition resulted in a denial of a discharge); In re Fine, 89 BR 167, 174 (Bankr. D. Kan. 1988) ; In re Swift, 3 F3d 929 (5th Cir. 1993) (conduct included: (1) debtor prepaying $5,000 in alimony or property settlement to his ex-wife; (2) debtor prepaying remaining liability on his vehicle; (3) debtor underreporting earnings due; (4) debtor transferring an insurance policy to his son, who in turn borrowed against it and transferred the funds to the debtor's ex-wife, and the ex-wife then loaned the funds back to the debtor, who gave her a promissory note on the day before bankruptcy; and (5) debtor's daughter loaning him money in exchange for a promissory note and a security interest in furniture, fixtures, renewal commissions, and certain personal property); In re Holt, 894 F2d 1005 (8th Cir. 1990) (conversion of nonexempt funds into reasonable amount of exempt insurance policy allowed, noting that the debtors did not engage in sharp practices); In re Cravitz, 225 BR 515, 521 (Bankr. D. Mass. 1998) (sharp practices doomed a conversion where, among other things, debtor mortgaged her property to secure a nonexistent debt, transferred property to trust to place it beyond the creditor's reach, violated the court injunction by transferring inherited property to her brother for $100, and simultaneously declared non-Florida property as her homestead, which declaration affected her Florida declaration); In re Segal, 227 BR 191, 195–196 (Bankr. SD Fla. 1998) (conversion failed where debtor engaged in sharp practices, which included lying to certain creditors for the purpose of delaying them, omitting a debt from a mortgage application for homestead property, and failing to make full disclosure in the bankruptcy petition); In re Carletta, 189 BR 258, 262 (Bankr. NDNY 1995) (in allowing discharge they noted that the debtors did not engage in sharp dealings, act in a secretive manner, or make misrepresentations to creditors; debtors clearly revealed their actions and simply followed counsel's advice in effectuating their rights of exemption). In re Warren, 512 F3d 1241 (10th Cir. 2008) (court was “most reluctant” to use the prebankruptcy conversion of nonexempt assets into exempt as a basis to deny a discharge on the grounds of fraud; instead the court relied on debtors' failure to list as assets certain prepayments, the “peculiar transaction” whereby debtors acquired a homestead and returned it within months, debtors' motivation to keep a certain creditor from obtaining anything through bankruptcy, the sale of coin collection for half its cost, which sale the court manifested as “(1) an effort to keep creditors from realizing the full value of their collection or (2) failure to report accurately how they disposed of the collection, an inference suggested by the absence of detailed records of the transactions, which the [debtors, who were both CPA's] could be expected to have kept.”). In re Anderson, 386 BR 315 (Bankr. D. Kan. 2008) (paying down mortgage was not accomplished with fraudulent intent for purposes of **11 USCA § 522(o)**; in holding the matter to be a close case, the court pointed to the following: (1) debtor did not use borrowed funds; (2) he did not engage in sharp practices, e.g., he did not conceal the payment; (3) the transfer of $240,000 did not render him insolvent; (4) he received fair consideration for the transfer, i.e., the reduction of his mortgage; and (5) his difficulties were simply a business setback and not, for example, the result of gambling).

[976] In re Mackey, 158 BR 509, 512–513 (Bankr. MD Fla. 1993) (conversion of nonexempt into exempt property was not disclosed until after the examination of debtor, whereupon debtor amended her petition). In contrast, see, In re Channon, 424 BR 895, 898, 899, 903 (Bankr. D.N.M. 2010) (conversion of nonexempt funds into an exempt Roth IRA was allowed: (i) debtor made full disclosure, (ii) the amount was limited to $10,000, (iii) he did not borrow funds to purchase exempt assets, and (iv) his age made it appropriate to provide for retirement and debtor testified that he intended to use funds for retirement).

[977] In re Przybylski, 340 BR 624, 630 (Bankr. ED Wis. 2006) (rejected Chapter 12 plan based in part on prebankruptcy planning that included misleading contact, which consisted of promises that were not kept, even though there were no misrepresentations).

[978] In re Zouhar, 10 BR 154 (Bankr. NM 1981) (denial of discharge for conversion of significant amount into exempt property).

979
In re Zouhar, 10 BR 154, 156 (Bankr. NM 1981) .

980
In re Zouhar, 10 BR 154, 157 (Bankr. NM 1981) .

981
Norwest Bank of Neb., NA v. Tveten, 848 F2d 871 (8th Cir. 1988) (Arnold, J., dissenting); see also In re Tveten, 402 NW2d 551, 558–560 (Minn. 1987) (exemption for money payable by a fraternal benefits society was unconstitutional because it was not limited in amount as is required under the state constitution).

981.1
Cf., In re Hall, 464 BR 896, 909 (Bankr. D. Idaho 2012) (in the context of a denial of an exemption, the court stated: “Realistically, nothing [debtors] owned by way of personal assets would come even close to paying that amount of debt. Rather, Debtors guaranteed themselves a relatively minimal stream of income through their investments,” by purchasing an annuity close to filing for bankruptcy and “Trustee has not demonstrated by a preponderance of the evidence that Debtors wilfully intended to defraud their creditors by converting non-exempt assets to a potentially exempt annuity in 2009”).

982
Norwest Bank of Neb., NA v. Tveten, 848 F2d 875 (8th Cir. 1988) .

983
Norwest Bank of Neb., NA v. Tveten, 848 F2d 876 (8th Cir. 1988) .

984
In re Reed, 700 F2d 992 (5th Cir. 1983); cf. In re Reed, 11 BR 683, 688 (Bankr. ND Tex. 1981) (bankruptcy exemptions are allowed only to give the debtors a fresh start “and to provide the debtor with minimum exemptions”).

985
In re Carey, 938 F2d 1073, 1077 (10th Cir. 1991) .

986
Cf. In re Adlman, 541 F2d 999 (2d Cir. 1976) ; In re Smiley, 864 F2d 567 (7th Cir. 1989) (the actual amount claimed as the exemption should be disregarded and debtor should be allowed to fully use all available exemption); see also Forsberg v. Security State Bank of Canova, 15 F2d 499 (8th Cir. 1926) .

987
In re McCabe, 280 BR 841, 844–845 (Bankr. ND Iowa 2002) (mere conversion of nonexempt assets to exempt assets is not fraudulent per se, and to set aside such a conversion as fraudulent, the creditor must establish some evidence extrinsic to the mere conversion; purchased shotgun was exempt and court noted that there is no dollar limit on the use of the exemption and that it was up to the legislature to impose a dollar limit).

988
In re Cataldo, 224 BR 426 (9th Cir. BAP 1998) (allowed the transformation of approximately $2 million into tenants by the entireties, a type of property that, depending on the circumstances, is generally exempt from creditor attachment).

989
In re Stern, 317 F3d 1111 (9th Cir.) , opinion amended and superseded on denial of reh'g by 345 F3d 1036 (2003) .

990
In re Beverly, 374 BR 221, 245 (9th Cir. BAP 2007) (amount as an indicium of fraud was embraced by the BAP in Beverly for

purposes of denial of discharge); aff'd in part and rev'd in part on different issues, In re Beverly, 551 F3d 1092 (9th Cir. 2008) .

991 In re Moore, 177 BR 437, 441 (Bankr. NDNY 1994) (where exemptions are modest and the ability of debtor to shield assets is controlled, conversion will be allowed).

992 In re Ganier, 403 BR 79, 86 (Bankr. D. Idaho 2009) (amount as indicium of extrinsic fraud was apparently established even though it was approximately $60,000 because the that amount would have been sufficient to provide substantial payment to creditor, i.e., "'magnitude of transfer' issue must be viewed as case specific"). In re Channon, 424 BR 895, 899 (Bankr. D.N.M. 2010) (conversion of nonexempt funds into an exempt Roth IRA was allowed, court point pointed to, among other things, the amount was limited to $10,000).

993 Norwest Bank of Neb., NA v. Tveten, 848 F2d 871 (8th Cir. 1988) ; In re Reed, 700 F2d 986, 992 (5th Cir. 1983) .

994 In re Johnson, 880 F2d 78, 82–83 (8th Cir. 1989) ; see also In re Haggerty, 448 NW2d 363, 366 (Minn. 1989) (unlimited value of homestead exemption was proper where the area was limited).

995 In re Smith, 113 BR 579, 587 (Bankr. DND 1990) . In re Przybylski, 340 BR 624, 631 (Bankr. ED Wis. 2006) (rejected Chapter 12 plan taking into account, among other things, the purpose of the conversion was solely to protect assets, unlike debtors in other circumstances that sought to secure their retirement (in this regard, the debtors were relatively young and had significant retirement accounts that were capable of significant earnings); court also thought that amount of conversion ($150,000) was excessive).

996 In re Covino, 187 BR 773 (Bankr. SD Fla. 1995) .

997 In re Covino, 187 BR 773, 779, 780 (Bankr. SD Fla. 1995) ; In re Anderson, 259 BR 687 (8th Cir. BAP 2001) (in holding that annuity was exempt, court relied, in part, on fact that purchased annuity was designed and intended to be wage substitute, which is purpose for which annuity exemption is allowed).

998 In re Covino, 187 BR 773, 779 (Bankr. SD Fla. 1995) .

999 In re Covino, 187 BR 773, 780 (Bankr. SD Fla. 1995) .

1000 In re Soza, 542 F3d 1060 (5th Cir. 2008) (in finding that eve of bankruptcy conversion of assets into exempt annuity was fraudulent, the court, among other things, noted that the declared purpose of the purchase of the annuity was to prevent litigation over the proceeds rather than to provide debtors with a future stream of income, which latter purpose would have been consistent with the purpose of the exemption and the Bankruptcy Code, i.e., to provide the debtor with a fresh start).

1001 In re Lazin, 221 BR 982 (Bankr. MD Fla. 1998) .

1002

See also Kelly v. Armstrong, 206 F3d 794, 799 (8th Cir. 2000) (conversion of moneys to exempt annuity was not proof of fraud where the debtors testified that they had no knowledge that the annuities were exempt and further testified that they had not had a savings account for over 40 years and always used annuities as a savings tool). In re Channon, 424 BR 895, 903 (Bankr. D.N.M. 2010) (conversion of nonexempt funds into an exempt Roth IRA was allowed, court point pointed to, among other things, debtor's age made it appropriate to provide for retirement and debtor testified that he intended to use funds for retirement).

1003
Sholden v. Ditz, 108 F3d 886 (8th Cir. 1997) .

1004
See also In re Phillips, 206 BR 196 (Bankr. ND Cal. 1997) (exemption for retirement plan denied on, among other grounds, the fact that the plan was funded with a residence in which the debtor resided without paying rent; thus, the assets, in part, were not for retirement purposes).

1005
In re Przybylski, 340 BR 624, 631 (Bankr. E.D. Wis. 2006) (rejected Chapter 12 plan taking into account, among other things, the purpose of the conversion was solely to protect assets, unlike debtors in other circumstances that sought to secure their retirement in this regard, the debtors were relatively young and had significant retirement accounts that were capable of earning significant sums).

1006
In re Allen, 203 BR 786, 792, 793 (Bankr. ND Fla. 1996) .

1007
In re Ingersoll, 124 BR 116, 122 (MD Fla. 1991) (transfer of property worth $200,000 to debtor's father for $10,000 where the debtor also maintained control over the property and paid all expenses and received all the income therefrom was a fraudulent transfer resulting in denial of discharge); In re Armstrong, 931 F2d 1237 (8th Cir. 1991) ; In re Fine, 89 BR 167, 174 (Bankr. D. Kan. 1988) .

1008
In re Fine, 89 BR 174 (Bankr. D. Kan. 1988) .

1009
In re Moreno, 892 F2d 417, 420–421 (5th Cir. 1990) .

1010
In re Ingersoll, 124 BR 116 (MD Fla. 1991) ; Arenz v. Astoria Sav. Bank, 281 F. 530 (9th Cir. 1922) .

1011
In re Kemmer, 265 BR 224 (Bankr. ED Cal. 2001) .

1012
In re Davidson, 178 BR 544, 550, 552 (SD Fla. 1995) (the conversion of nonexempt assets into exempt assets for the specific purpose of placing assets out of the reach of creditors is sufficient to result in a denial of discharge under federal law and to deprive a debtor of his right to claim that property as exempt under state law); In re Smith, 157 BR 37, 39 (Bankr. MD Fla. 1993) (intent to place assets beyond reach of creditors alone results in denial of discharge); In re Schwab, 150 BR 470, 473 (Bankr. MD Fla. 1992) .

1013
This position is particularly harsh because it appears that, where many motivations are present, any fraudulent purpose will result in a denial of discharge, loss of exemption, or both. See **¶ 3.04[1][c]**; In re Davidson, 164 BR 782, 785 (Bankr. SD Fla. 1994) , aff'd in part, remanded in part, 178 BR 544 (SD Fla. 1995) (where facts indicate that there were several purposes to prebankruptcy planning, the court will not balance the purposes; if only one purpose was to hinder and delay or defraud, that would be sufficient to deny discharge).

1014

See, e.g., In re Smiley, 864 F2d 562, 567 (7th Cir. 1989) (debtor should be allowed full use of exemption absent extrinsic evidence of intent to hinder delay or defraud); In re Reed, 700 F2d 986, 991 (5th Cir. 1983) (motivation to place asset beyond reach of creditors is purpose of prebankruptcy planning conversion and is proper absent actual intent to defraud); Norwest Bank of Neb., NA v. Tveten, 848 F2d 871, 873 (8th Cir. 1988) ; In re Miller, 113 BR 98, 104 (Bankr. D. Mass. 1990) (cannot be fraudulent, since purpose of exemptions is placing property out of reach of creditors); In re Barker, 168 BR 773, 776 (Bankr. MD Fla. 1994) (exemption cannot be denied on finding of fraudulent intent in establishing exemption, regardless of whether exemption is valid under applicable state law); In re Carletta, 189 BR 258, 262 (Bankr. NDNY 1995) (the court observed that a majority of debtors filed bankruptcy after engaging in prebankruptcy planning).

1015

See generally Shacter, "Bankruptcy Estate Planning: Grounds for Denial of Discharge Under Section 727(a)(2)(A)," 7 Bankr. Devs. J. 199, 207 (1990).

1016

In re Gepfrich, 118 BR 135 (Bankr. SD Fla. 1990) .

1017

In re Gepfrich, 118 BR 135, 138 (Bankr. SD Fla. 1990) ; see also In re Oberst, 91 BR 97 (Bankr. CD Cal. 1988) (court denied a discharge on the grounds that the debtor engaged in conduct designed to deny her ex-husband any part of her estate, including preferential transfers, prepaying items for future benefits, and attempting to shield assets with a particular creditor in mind); In re Edwards, 56 BR 582, 584–585 (Bankr. D. Md. 1986) (transfer by husband to his current spouse and himself as tenants by the entirety was denied discharge where the transfer was undertaken to prevent his ex-spouse, who was his only creditor, from obtaining any equity in the property).

1018

See Cf., **In re Rucker, 570 F3d 1155, 1158, 1161 (9th Cir. 2009)** (An exemption for a retirement plan under California was denied for abuse where the debtor had one major creditor and admitted that he did not want to pay his "black hole" judgment; he also overfunded the plan in violation of IRS/IRC rules, secretly funding the plans using a wholly owned offshore corporation and a foreign bank account and one of the plan purchased property on which the debtor resided rent free; the court concluded that debtor used the plans to shield assets from creditors rather than for retirement purposes).

1019

In re Armstrong, 97 BR 565, 568 (Bankr. D. Neb. 1989) , aff'd, 931 F2d 1233, 1239 (8th Cir. 1991) ; see also In re Zouhar, 10 BR 154 (Bankr. NM 1981) (borrowing against interest in a professional corporation).

1020

In re Smiley, 864 F2d 562, 567 (7th Cir. 1988) ("We look, however, for extrinsic signs of fraud. Such signs include: (1) that the debtor obtained credit in order to purchase exempt property; (2) that the conversion occurred after the entry of a large judgment against the debtor; (3) that the debtor had engaged in a pattern of sharp dealing prior to bankruptcy;…and [(4)] that the conversion rendered the debtor insolvent."); In re Reed, 700 F2d 986, 991 (5th Cir. 1983) ("evidence that the debtor, on the eve of bankruptcy, borrowed money that was then converted into exempt assets would suffice to support a finding of actual intent to defraud"). In re Przybylski, 340 BR 624, 630 (Bankr. ED Wis. 2006) (rejected Chapter 12 plan based in part on debtor's acquisition of exempt assets with borrowed funds). In re Channon, 424 BR 895, 903 (Bankr. D.N.M. 2010) (conversion of nonexempt funds into an exempt Roth IRA was allowed, court point pointed to, among other things, debtor did not borrow funds to purchase exempt assets); In re Bronk, 444 BR 902, 916-917 (Bankr. WD Wis. 2011) (debtor borrowed on his homestead to provide a college fund for grandchildren did not vitiate pre-bankruptcy planning, quoting *Bogue*, 240 BR 751 (Bankr. ED Wis. 1999) (in allowing an exemption, the court noted that "[t]his is not a case of debtors borrowing money to purchase exempt property and then selling the assets and using the sale proceeds to acquire exempt annuities" or "a case of debtors obtaining funds by theft and then converting the funds into exempt property"); and concluding that "[t]he purpose and reasoning behind the conversion [,i.e., to provide for his grandchildren's education] is understandable and hardly deserves to be labeled 'fraudulent.'").

[1021] See **¶ 12.03[6][b]**. In re Anderson, 386 BR 315 (Bankr. D. Kan. 2008) (paying down mortgage was not accomplished with fraudulent intent for purposes of **11 USCA § 522(o)**; in holding the matter to be a close case, the court pointed to the following: (1) debtor did not use borrowed funds; (2) he did not engage in sharp practices, e.g., he did not conceal the payment; (3) the transfer of $240,000 did not render him insolvent; (4) he received fair consideration for the transfer, i.e., the reduction of his mortgage; and (5) his difficulties were simply a business setback and not, for example, the result of gambling).

[1022] In re Collins, 19 BR 874 (Bankr. ND Fla. 1982) .

[1023] In re Collins, 19 BR 874, 877 (Bankr. ND Fla. 1982) ; In re Gepfrich, 118 BR 138 (Bankr. SD Fla. 1990) (conversion of business assets is an indicium of fraud).

[1024] In re Mackey, 158 BR 509, 512 (Bankr. MD Fla. 1993) (when debtor personally guarantees debt then her nonbusiness assets are relied on by her business creditors).

[1025] In re Elliott, 79 BR 944, 946 (Bankr. D. Fla. 1987) .

[1026] See **¶ 12.03[6][b]**.

[1027] See **¶ 12.04[1][f]** (discussing willful and malicious conduct).

[1028] In re Fine, 89 BR 167 (Bankr. D. Kan. 1988) .

[1029] In re Fine, 89 BR 167, 174 (Bankr. D. Kan. 1988) . A confluence of factors was considered in In re Channon, 424 BR 895, 898, 899, 903 (Bankr. D.N.M. 2010) (conversion of nonexempt funds into an exempt Roth IRA was allowed (1) debtor made full disclosure, (2) the amount was limited to $10,000, (3) he did not borrow funds to purchase exempt assets, and (4) his age made it appropriate to provide for retirement and debtor testified that he intended to use funds for retirement).

[1030] In re Fine, 89 BR 167, 175 (Bankr. D. Kan. 1988) ("On the contrary, a review of the debtor's bankruptcy schedules indicates that Fine's debts far exceeded his assets long prior to the transfers.").

[1031] Exchange State Bank v. Poindexter, 137 Kan. 101, 19 P2d 705, 708–709 (1933) (life insurance exemption denied where funds used to pay premiums were fraudulently obtained); Dock v. Tuchman, 497 NE2d 945, 947 (Ind. Ct. App. 1st Dist. 1986) (*Poindexter* distinguished on the grounds that fraudulently obtained funds could not be directly traced to exempt property); but see In re Mart, 75 BR 808, 811 (Bankr. SD Fla. 1987) (where part of funds used to purchase home were fraudulently obtained, the entire homestead will not be denied and the remedy of a creditor from whom funds were fraudulently obtained and used to, in part, acquire homestead property is to proceed in state court to recover funds), on remand, 90 BR 547 (Bankr. SD Fla. 1988) ; In re Moody, 862 F2d 1194, 1200 (8th Cir. 1989) (homestead acquired with fraudulently obtained funds can be impressed with a constructive trust and equitable lien, whereas if homestead is merely improved with fraudulently obtained funds, those remedies will not be allowed).

1032

In re Rice, 109 BR 405, 408 (Bankr. ED Cal. 1989) (spending money on advice of counsel and transferring money to mother), aff'd, without published opinion, 126 BR 823 (1991) ; In re Lubin, 61 BR 511, 514 (Bankr. SDNY 1986) (funds transferred to a child in order to pay for a trip to Europe and to pay child's automobile loan held to be fraudulent transfer resulting in denial of discharge); In re Swift, 3 F3d 929 (5th Cir. 1993) (prepaying alimony and automobile payments sufficient to deny discharge).

1033

In re Barker, 168 BR 773, 780 (Bankr. MD Fla. 1994) (although there was full disclosure, evidence that timing of the conversion was not disclosed; the court speculated that debtor “gambled that creditors would not inquire into the time of the transfer”).

1034

In re Schwab, 150 BR 470, 472 (Bankr. MD Fla. 1992) (consulting lawyer was one of several factors); In re Levine, 134 F3d 1046, 1049 (11th Cir. 1998) (lower court considered consultation with attorney to engage prebankruptcy conversion improper); cf. In re Anderson, 259 BR 687 (8th Cir. BAP 2001) (prebankruptcy planning will affect whether exemption will be allowed, in this case a retirement plan). In re Stewart, 373 BR 736 (Bankr. MD Fla. 2007) (prebankruptcy planning was disregarded where spouses acted in tandem, hiring the same lawyer taking essentially the same steps).

1035

In re Schwab, 150 BR 470, 473 (Bankr. MD Fla. 1992) .

1036

In re Swecker, 157 BR 694, 695–696 (Bankr. MD Fla. 1993) (the court suggested that a conversion of nonexempt assets into exempt assets could be fraudulent where there is “an imminent threat of levy, attachment, garnishment, or execution on a judgment just prior to the [d]ebtors' conversion of assets,” although there was no such evidence in this case).

1037

In re Jennings, 349 BR 897, (Bankr. M.D. Fla. 2006) (prepayment of $130,000 for work on homestead when contract called for installment payments was treated as an indicium of fraud justifying denial of discharge based on a fraudulent transfer); aff'd, In re Jennings, 533 F3d 1333 (11th Cir. 2008) , denial of rehearing en banc, 309 Fed. Appx. 386 (Table) (11th Cir. 2008) .

1038

In re Glaser, 49 BR 1015, 1019 (Bankr. NY 1985) (transferring money to spouse in order to meet ongoing household expenses does not warrant denial of discharge).

1039

In re Bernard, 99 BR 563, 572 (Bankr. SDNY 1989) ; see also In re Dennis, 330 F3d 696, 702 (5th Cir. 2003) (continuing pattern of payments to minor child coupled with relatively minor amounts thereof did not support denial of discharge).

1040

In re Ramos, 8 BR 490 (Bankr. Wis. 1981) (transfers to wife of $2,200 in one month and $5,800 in another month for personal expenses where monthly expenses were approximately $1,900 was fraudulent and supported a denial of discharge).

1041

In re Adeeb, 787 F2d 1343 (9th Cir. 1986) (reliance on attorney for making a fraudulent transfer did not result in denial of discharge where transfer reversed); In re Bajgar, 104 F3d 495 (1st Cir. 1997) (debtor cannot cure a fraudulent transfer for purposes of denial of discharge under **11 USC § 727(a)(2)(A)** by retransferring the property after filing for bankruptcy); In re Davis, 911 F2d 560 (11th Cir. 1990) (discharge denied where debtor acted on the advice of his lawyer in making the fraudulent transfer).

1042

In re Adeeb, 787 F2d 1339, 1342 (9th Cir. 1986) .

1043

In re Zouhar, 10 BR 158 (Bankr. NM 1981) . In re Villani, 2012 WL 3755525 (1st Cir. BAP 2012) (reliance on attorney was not a defense to denial of discharge for fraud under 11 USCA § 727(a)(2)(A) where debtor failed “to disclose the transfers [of assets to his girlfriend/bookkeeper] in his Statement of Financial Affairs”).

1044

See generally Maggs, “Consumer Bankruptcy Fraud and the ‘Reliance on Advice of Counsel' Argument,” 69 Am. Bankr. LJ 1 (1995); Hawes & Sherrard, “Reliance on Advice of Counsel as a Defense in Corporate and Securities Cases,” 62 Va. L. Rev. 1 (1976); Longstreth, “Reliance on Advice of Counsel as a Defense to Securities Law Violations,” 37 Bus. Law. 1185 (1982); Preston, “Advice of Counsel as a Defense,” 28 Va. L. Rev. 26 (1941); Note, “Reliance on the Advice of Counsel,” 70 Yale LJ 978 (1961). In re Nichols, 447 BR 97, 112-113 (Bankr. NDNY 2010) (family farmer's Chapter 12 petition reliance on counsel negated inference of fraud relative to inaccurate financial statements and tax returns; debtor credibly testified that he placed blind faith and absolute trust in his advisors).

1045

See, e.g., Manor Nursing Ctr., Inc., 458 F2d 1082, 1102 (2d Cir. 1972) ; In re Bateman, 646 F2d 1220 (8th Cir. 1981) (defense rejected on grounds that reliance was unreasonable); In re Tully, 818 F2d 106 (1st Cir. 1987) ; Norwest Bank of Neb., NA v. Tveten, 848 F2d 871, 876 (8th Cir. 1988) (defense rejected on the grounds that reliance was unreasonable). In re Stanton, 457 BR 80, 96 (Bankr. D. Nev. 2011) (in the context of a 522(o) determination, stating: “If a professional counsels a client to make a transaction that the professional knows will hinder or delay creditors, and which the client knows or should know would have the same effect, the transaction is made with the requisite intent regardless of the intercession of the professional.…a debtor cannot blindly rely on advice of others as a shield; good faith requires any reliance to be reasonable…[debtor] knew the purpose of the transactions was to keep assets away from a legitimate creditor”).

1046

In re Adeeb, 787 F2d 1339, 1343 (9th Cir. 1986) .

1047

Compare In re Murray, 116 BR 473 (Bankr. ED Va. 1990) (transfer of inventory subject to security interest on the admittedly erroneous advice of counsel was not willful and malicious where reliance was in good faith) with In re Ketaner, 149 BR 395, 401 (Bankr. ED Va. 1992) (violation of noncompetition agreement was excepted from discharge as willful and malicious and, therefore, reliance-on-counsel defense was rejected; “Simply being able to construct a legal argument to support one's actions is insufficient to invoke the protection” of the defense). In re Levine, 970 F2d 681, 689 (10th Cir. 1992) (relying on advice of attorney is an excuse to bankruptcy fraud; defendants “could not be convicted if they were strictly following the advice of counsel believing it to be correct”).

1048

Maggs, “Consumer Bankruptcy Fraud and the ‘Reliance on Advice of Counsel' Argument,” 69 Am. Bankr. LJ 1, 10 (1995). See also SEC v. Savoy Indus., Inc., 665 F2d 1310, 1314 n.28 (DC Cir. 1981) . United States v. United Med. & Surgical Supply Corp., 989 F2d 1390, 1404 (4th Cir. 1993) (failure to disclose all material facts precluded good faith reliance on advice of counsel); C.E. Carlson, Inc. v. Sec. & Exch. Comm'n, 859 F2d 1429, 1436 (10th Cir. 1988) ; United States v. Eisenstein, 731 F2d 1540, 1543 (11th Cir. 1984) (“In order to take advantage of [the defense of good faith reliance on the advice of counsel], the defendant must show that he relied in good faith after first making a full disclosure of all facts that are relevant to the advice for which he consulted the attorney.”).

1049

SEC v. Savoy Indus., Inc., 665 F2d 1310, 1314 n.28 (DC Cir. 1981) (SEC injunction to prevent further violations of securities laws; compliance with those laws cannot be avoided simply by relying on counsel); Linden v. United States, 254 F2d 560, 568 (4th Cir. 1958) ; SEC v. Manor Nursing Ctr., Inc., 458 F2d 1082, 1101–1102 (2d Cir. 1972) .

1050

In re Adeeb, 787 F2d 1343 (9th Cir. 1986) (both client and attorney knew the transfer was intended to defraud creditors; consequently, reliance on counsel defense was unavailable for denial of discharge proceeding).

1051
In re Scarbaci, 34 BR 344 (Bankr. Fla. 1983) (sale of items subject to a security agreement in violation thereof was done out of ignorance rather than with the intent to hinder, delay, or defraud a creditor; accordingly, discharge was allowed).

1052
See **¶ 3.07**.

1053
In re Smiley, 864 F2d 568 (7th Cir. 1989) ; cf. Continental Bank & Trust Co. v. Winter, 153 F2d 397 (2d Cir. 1946) , cert. denied, 329 US 717 (1947) .

1054
In re Dee, 6 BR 784 (Bankr. WD Pa. 1980) (where debtor-spouse to whom financial matters were delegated requested her to sign a deed transferring home to her parents within one year of the petition, such conduct was not accomplished with sufficient knowledge or in reckless disregard of the truth, and did not result in a denial of discharge).

1055
In re Cottrill, 118 BR 535, 538–539 (Bankr. SD Ohio 1990) ; see also In re Horath, 116 BR 835 (Bankr. MD Fla. 1990) (transferring $5,000 to an IRA was held a valid conversion of nonexempt property into exempt property under Florida law).

1056
In re Bowyer, 932 F2d 1100, 1101 (5th Cir.) , reh'g denied, 940 F2d 657 (1991) .

1057
In re Bowyer, 932 F2d 1100 (5th Cir.) , reh'g denied, 940 F2d 657 (1991) .

1058
Sender v. Mann, 423 F. Supp. 2d 1155, 1169 (D. Colo. 2006) (although transfer in the ordinary course of business is not a defense to a fraudulent transfer it may negate an element of actual fraudulent intent).

1059
In re Adeeb, 787 F2d 1339 (9th Cir. 1986) .

1060
In re Adeeb, 787 F2d 1344 (9th Cir. 1986) .

1061
In re Adeeb, 787 F2d 1345 (9th Cir. 1986) .

1062
In re Adeeb, 787 F2d 1346 (9th Cir. 1986) .

1063
In re Smiley, 864 F2d 566 (7th Cir. 1989) .

1064
In re Davis, 911 F2d 560 (11th Cir. 1990) .

1065

In re Bajgar, 104 F3d 495 (1st Cir. 1997) (debtor cannot cure a fraudulent transfer for purposes of denial of discharge under **11 USC § 727(a)(2)(A)** by retransferring the property after filing for bankruptcy).

1066

Village of San Jose v. McWilliams, 284 F3d 785 (7th Cir. 2002) (transfer and concealment of property resulted in denial of discharge even though debtor later made disclosure; although the *McWilliams* court attempted to distinguish *Adeeb*).

1067

See, e.g., Norwest Bank of Neb., NA v. Tveten, 848 F2d 871, 874 (8th Cir. 1988) .

1068

Exchange State Bank v. Poindexter, 137 Kan. 101, 19 P2d 705, 708–709 (1933) (life insurance exemption denied where funds used to pay premiums were fraudulently obtained); Dock v. Tuchman, 497 NE2d 945, 947 (Ind. Ct. App. 1st Dist. 1986) (*Poindexter* distinguished on the grounds that fraudulently obtained funds could not be directly traced to exempt property); In re Moody, 862 F2d 1194, 1200 (8th Cir. 1989) (homestead acquired with fraudulently obtained funds can be impressed with a constructive trust and equitable lien, whereas if homestead is merely improved with fraudulently obtained funds, those remedies will not be allowed); In re Walgamuth, 144 BR 465, 474–475 (Bankr. DSD 1992) , aff'd, **14 F3d 32 (9th Cir. 1994)** (constructive trust imposed on a homestead of the debtor where the debtor used moneys fraudulently obtained and subject to the constructive trust to purchase a home; the property was not part of the debtor's bankruptcy estate); In re Lapes, 254 BR 501, 507–508 (Bankr. SD Fla. 2000) (converted collateral used to purchase a homestead resulted in denial of homestead exemption; homestead cannot be used as an instrumentality of fraud).

1069

In re Mart, 75 BR 808, 811 (Bankr. SD Fla. 1987) (where part of funds used to purchase home were fraudulently obtained, the entire homestead will not be denied and the remedy of a creditor from whom funds were fraudulently obtained and used to, in part, acquire homestead property is to proceed in state court to recover funds), on remand, 90 BR 547 (Bankr. SD Fla. 1988) ; In re Moody, 862 F2d 1194, 1200 (8th Cir. 1989) (homestead acquired with fraudulently obtained funds can be impressed with a constructive trust and equitable lien, whereas if homestead is merely improved with fraudulently obtained funds, those remedies will not be allowed).

1070

In re Curry, 160 BR 813, 817 (Bankr. D. Minn. 1993) (under applicable state law only fraud sufficient to constitute a fraudulent transfer will justify a denial of homestead exemption). In re Maronde, 332 BR 593, 600 (Bankr. D. Minn. 2005) (sale of nonexempt assets and use of proceeds to reduce mortgage on homestead was characterized as fraudulent and resulted in a denial of the homestead pro tanto; court found actual fraud on the basis of debtor's failed attempt to accomplish same goal by use of credit cards; "In this case, Debtor engaged in a scheme to defraud his creditors by using his (at the time) good credit to obtain a number of credit cards, use the cash advances, in the form of balance transfers, from those cards to pay off his equity credit line. He then intended to liquidate his truck and trailer to raise cash that he could offer to settle with his new creditors for less than he owed. That he failed and had to resort to Plan B and put the proceeds from the sale of the truck and trailer into his home does nothing to erase the original intent of the scheme: don't pay creditors in full and surely do not make an honest attempt to do so.")

1071

See **¶ 12.02[3][a]**.

1072

See **¶ 12.03[9][d]**.

1073

11 USC § 105(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."); In re Davidson, 164 BR 782, 788 (Bankr. SD Fla. 1994) (court declined to deny exemption “because there has been no ‘strong showing of abuse' by the Debtors”); In re Spoor-Weston, Inc., 139 BR 1009 (Bankr. ND Okla. 1992) , aff'd, 13 F3d 407 (10th Cir. 1993) (exemption denied upon a strong showing of abuse; in so holding the court stated: “Normally, objection to claim of exemption concerns the basic right to or measure of an exemption under the law creating the exemption—in this instance, a matter of State statutory law. But in abnormal circumstances, objection to exemption might concern the abuse of an exemption in the context of a bankruptcy case—a matter purely of bankruptcy law, which encompasses equity. It must appear that the debtor's hands are unclean; that, even in the peculiar context of a bankruptcy case, the debtor is not doing such equity as would entitle him to receive equity—that debtor has converted nonexempt property to exempt property, not in the ordinary course of debtor's affairs or for other reasons unconnected with bankruptcy, but outside the ordinary course of debtor's affairs, on special occasion or in unusual amount, deliberately enlarging his exemptions in contemplation of bankruptcy—that debtor has acted in a way that distorts the combined operations of bankruptcy receivership and injunction, offends bankruptcy policy, abuses the jurisdiction of the Bankruptcy Court, threatens the public interest, and may be described as unconscionable, outrageous, disreputable, or shocking to one's conscience. The classic example would ‘have the [debtor] . . . with guidance from his attorney . . . convert his [nonexempt] assets into cash and then use that cash in such a way as to [shelter] it from his creditors, even while his attorney is busy typing up the bankruptcy schedules.' But of course there must be no casual interference with exemptions prescribed by the legislature; so a strong showing of abuse, sufficient to invoke the court's general equitable powers, must be required.” *Spoor-Weston*, supra, at 1015–1016.).

Mansell v. Carroll, 379 F2d 682, 685 (10th Cir. 1967) (husband and wife denied homestead exemption where they both participated in a fraudulent transaction that involved the residence on grounds that they could “come into a court of equity and assert another's homestead right as a defense for their own wrongful conduct, although alternative state grounds were present); cf. In re Hogan, 214 BR 882 (Bankr. ED Ark. 1997) (court denied exemption where it characterized conversion of nonexempt assets into exempt assets as fraudulent, although the statutory basis for holding was unclear). It appears that *Hogan* was reversed by In re Bradley, 294 BR 64, 69 (8th Cir. BAP 2003) (no legal basis to deny homestead exemption on the ground that debtor converted nonexempt assets into exempt assets; under applicable state law the purchase of a homestead is not a fraud on creditors).

1074

11 USC § 522. In re Schwab, 150 BR 470, 473 (Bankr. MD Fla. 1992) (the conversion of nonexempt assets into an exempt asset for the specific purpose of placing assets out of the reach of creditors is sufficient to deprive a debtor of his right to claim that property as exempt under the Bankruptcy Code); In re Coplan, 156 BR 88, 92 (Bankr. MD Fla. 1993) (exemption for homestead denied, apparently on basis of Bankruptcy Code § 522, although, under Havoco of Am. v. Hill, 790 So. 2d 1018 (Fla. 2001) the homestead would now be allowed); see also In re Hogan, 214 BR 882, 884 (Bankr. ED Ark. 1997) (sale of existing homestead to purchase a new homestead for considerably more money could result in denial of discharge, although creditor only objected to extent of increase homestead; the statutory basis for conclusion was unclear); but see In re Bradley, 294 BR 64, 69 (8th Cir. BAP 2003) (no legal basis to deny homestead exemption on the ground that debtor converted nonexempt assets into exempt assets; under applicable state law the purchase of a homestead is not a fraud on creditors).

1075

Hansen v. First Nat'l Bank, 848 F2d 866, 868 (8th Cir. 1988) .

1076

In re McCabe, 280 BR 841 (Bankr. ND Iowa 2002) (“Iowa law is applied to determine whether an exemption for a rifle or shotgun should be allowed. [citation omitted] When the debtor claims a state created exemption, the scope of the claim is determined by state law.”); In re Swift, 124 BR 475, 482 (Bankr. WD Tex. 1991) (“In the absence of a statutory basis for denying a debtor's exemption . . . , this court is reluctant to conclude that exemption claims can be disallowed solely based on a theory of impermissible prebankruptcy planning.”).

1077

In re O'Brien, 373 BR 503 (Bankr. ND Ohio 2007) (eve of bankruptcy planning supported dismissal of a Chapter 7 petition on grounds of abuse under 11 USCA § 707(b), namely, purchasing a home and a new car within three months of filing the petition; court cited In re Mitchell, 357 BR 142, 155 (Bankr. CD Cal. 2006) as another case dismissing a petition under similar grounds).

1078

11 USC § 707(b).

1079
See, ¶ 12.01[2][b][iii].

1080
In re Kornfield, 164 F3d 778 (2d Cir. 1999) .

1081
The factors were:

1. The debtors incurred substantial debts due to an extravagant lifestyle.
2. They refused to alter that lifestyle when faced with lower income.
3. One debtor had an established medical practice that would yield substantial, if diminished, future income.
4. Most of the present debts could have been avoided, and all of it could be repaid over time.
5. There were no mitigating factors.

1082
In re Kornfield, 164 F3d 778, 784 (2d Cir. 1999) .

1083
In re Koch, 109 F3d 1285 (9th Cir. 1997) .

1084
In re Koch, 109 F3d 1285, 1288 (9th Cir. 1997) . In re O'Brien, 373 BR 503 (Bankr. ND Ohio 2007) (eve of bankruptcy planning supported dismissal of a Chapter 7 petition on grounds of abuse under 11 USCA § 707(b), namely, purchasing a home and a new car within three months of filing the petition; court cited In re Mitchell, 357 BR 142, 155 (Bankr. CD Cal. 2006) as another case dismissing a petition under similar grounds).

1085
In re Lamanna, 153 F3d 1, 3 (1st Cir. 1998) (substantial abuse for discharge under **§ 707(b)**, consumer debts, was resolved by totality of circumstances and whether debtor could repay debts in a hypothetical Chapter 13); see also In re Bilzerian, 276 BR 285, 294 (MD Fla. 2002) (Chapter 7 petition was dismissed for cause under **IRC § 707(a)**; court rejected good faith rule and embraced totality of circumstances test, relying on the fact that $103 million of the approximately $140 million of the debt listed on the debtor schedule was nondischargeable and that another $9 million was owed to the IRS; further, the debtor had no intention of turning over any assets, since he listed a no asset estate).

1086
11 USC § 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 under 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**).

1087
In re Zick, 931 F2d 1124, 1126–1127 (6th Cir. 1991) ; In re Tamecki, 229 F3d 205, 207–208 (3d Cir. 2000) (debtor incurred debt of 10 times his income before he filed for bankruptcy for no apparent reason and debtor's exemption for entireties property would shortly be lost by imminent divorce; held, these facts were sufficient to shift burden of proof to debtor to prove good faith for filing bankruptcy petition, which he failed to do).

1088

In re Bilzerian, 258 BR 850 (Bankr. MD Fla. 2001) , stay denied by, 264 BR 726 (Bankr. MD Fla. 2001) , order aff'd, 276 BR 285 (MD Fla. 2002) , aff'd, Bilzerian v. SEC, 82 Fed. Appx. 213, 2003 WL 22075379 (11th Cir. 2003) .

1089

The court stated that "cause" under **Section 707(a)** would include facts establishing a denial of discharge under Section 727 or a showing that the debt is nondischargeable under Section 523.

1090

In re Bilzerian, 258 BR 850, 857–858 (Bankr. MD Fla. 2001) , stay denied by, 264 BR 726 (Bankr. MD Fla. 2001) , order aff'd, 276 BR 285 (MD Fla. 2002) , aff'd, Bilzerian v. SEC, 82 Fed. Appx. 213, 2003 WL 22075379 (11th Cir. 2003) .

1091

In re Padilla, 222 F3d 1184, 1192–1193 (9th Cir. 2000) .

1092

In re Huckfeldt, 39 F3d 829, 832 (8th Cir. 1994) (stating that while some conduct giving rise to dismissal under **Section 707(a)** can be characterized as bad faith, the issue is properly whether the petition should be dismissed "for cause").

1093

In re Kauffman, 675 F2d 127 (7th Cir. 1981) ; see also In re Olivier, 819 F2d 550 (5th Cir. 1987) ; In re Martin, 698 F2d 883 (7th Cir. 1983) .

1094

In re Adlman, 541 F2d 999, 1005 (2d Cir. 1976) (Moore, J., dissenting).

1095

In re Adlman, 541 F2d 1004–1005 (2d Cir. 1976) .

1096

In re Armstrong, 931 F2d 1238 (8th Cir. 1991) .

1097

In re Olsen, 45 BR 501, 506 (Bankr. D. Minn. 1984) ; see also In re Bowyer, 932 F2d 1100 (5th Cir.) , reh'g denied, 940 F2d 657 (1991) (withdrawal of savings to reduce mortgage approved); In re Meyer, 244 F3d 352, 355 (4th Cir. 2001) , cert. denied sub nom. Shaia v. Meyer, 122 S. Ct. 212 (2001) (use of a $168,000 bequest to prepay mortgage payments was held to be valuable consideration and, therefore, not a fraudulent transfer).

1098

In re Boudrot, 287 BR 582, 587 (Bankr. WD Okla. 2002) .

1099

In re Boudrot, 287 BR 582, 587 (Bankr. WD Okla. 2002) .