

APR 07 2006

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U.S. BKCY. APP. PANEL  
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL  
OF THE NINTH CIRCUIT

In re: ) BAP No. WW-05-1318-SRKR  
 )  
 ANTHONY MICHAEL CARTER and ) Bk. No. 05-11933  
 JESSICA C. CARTER, )  
 )  
 Debtors. )  
 )  
 \_\_\_\_\_ )  
 ANTHONY MICHAEL CARTER and )  
 JESSICA C. CARTER, )  
 )  
 Appellants, )  
 )  
 v. ) **MEMORANDUM<sup>1</sup>**  
 )  
 PETER H. ARKISON, Chapter 7 )  
 Trustee, )  
 )  
 Appellee. )  
 \_\_\_\_\_ )

Argued and Submitted on  
March 24, 2006 at Seattle, Washington

Filed - April 7, 2006

Appeal from the United States Bankruptcy Court  
for the Western District of Washington

Honorable Thomas T. Glover, Bankruptcy Judge, presiding

Before: SMITH, RUSSELL<sup>2</sup> and KIRSCHER,<sup>3</sup> Bankruptcy Judges.

<sup>1</sup> This disposition is not appropriate for publication and may not be cited except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel. See 9th Cir. BAP Rule 8013-1.

<sup>2</sup> Hon. Barry Russell, Chief Bankruptcy Judge for the Central District of California, sitting by designation.

<sup>3</sup> Hon. Ralph B. Kirscher, Chief Bankruptcy Judge for the District of Montana, sitting by designation.

1 Billie Renee Clark, Mindy Anne Wortner, Estelle Leanne  
2 Hillard, and Anthony and Jessica Carter (collectively, "Debtors")  
3 separately and independently appeal final orders entered June 23,  
4 2005,<sup>4</sup> which sustained the objections to exemption filed by the  
5 chapter 7<sup>5</sup> trustee, Peter H. Arkison.<sup>6</sup> Debtors' motions for  
6 reconsideration were denied on July 22, 2005 and timely notices  
7 of appeal were filed. We REVERSE and REMAND.

8 **I. FACTS**

9 On February 17, 2005, Debtors, all represented by the same  
10 attorney, filed separate individual chapter 7 petitions. Their  
11 § 341 creditors' meetings were held on April 11, 2005, at which  
12 time each stated that their respective schedules of assets and  
13 liabilities were correct. However, upon further and more direct  
14 questioning by the trustee regarding possible tax refunds, each  
15 responded that they either had received refunds after signing the  
16 bankruptcy schedules or were expecting to receive tax refunds.  
17 Following the meeting, they amended schedules B and C to list the  
18 refunds as assets and to claim them as exempt.<sup>7</sup>

19 \_\_\_\_\_  
20 <sup>4</sup> The order against Estelle Leanne Hillard was entered on  
June 24, 2005 - a day after the other orders were entered.

21 <sup>5</sup> Unless otherwise indicated, all chapter, section, and rule  
22 references are to the Bankruptcy Code, 11 U.S.C. §§ 101-1330, and  
23 to the Federal Rules of Bankruptcy Procedure, Rules 1001-9036.

24 <sup>6</sup> An order was entered by the Clerk of the BAP on October 5,  
2005 providing for a joint hearing in these matters.

25 <sup>7</sup> Debtors each amended their schedules to reflect the tax  
26 refunds as follows:

27	Billie Renee Clark	\$3,060
	Mindy Anne Wortner	\$4,524
28	Estelle Leanne Hillard	\$6,137

(continued...)

1 The trustee timely objected to the exemptions, asserting  
2 that Debtors should not be allowed to claim an exemption on  
3 property which they attempted to conceal from the trustee.<sup>8</sup>  
4 According to the trustee, Debtors acted to conceal the tax  
5 refunds by 1) failing to disclose them in their bankruptcy  
6 schedules in the first instance, 2) falsely representing to the  
7 trustee that the schedules were accurate, and 3) only revealing  
8 their existence when specifically asked about them by the  
9 trustee.

10 Debtors opposed the objections, alleging that the tax  
11 refunds were inadvertently omitted as a result of their  
12 attorney's failure to emphasize the necessity of scheduling tax  
13 refunds not yet received.<sup>9</sup> They denied any intent to conceal the  
14 refunds, and in this regard, requested an evidentiary hearing in  
15 order to prove the veracity of their statements to the court.

16 The trustee viewed the attempt to shift the blame onto  
17 Debtors' attorney with skepticism, pointing out that Debtors' tax  
18 returns, all signed prior to the bankruptcy filings, clearly  
19 reflected entitlement to refunds. The trustee maintained that  
20 because Debtors knowingly omitted the tax refunds from the  
21 schedules, the objections to exemption should be sustained.

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22 <sup>7</sup>(...continued)

23 Anthony and Jessica  
24 Carter

\$2,368

25 <sup>8</sup> In conjunction with the objections to exemption, the  
26 trustee also filed motions to deny the tax refunds as exempt  
27 property. The basis for the motions was identical to the  
objections, and because the bankruptcy court treated the matter  
as one, we shall do the same.

28 <sup>9</sup> Debtors each filed declarations that support the facts  
alleged herein.

1 A hearing on the matter was held on May 25, 2005. Although  
2 the bankruptcy court initially granted Debtors' oral request for  
3 an evidentiary hearing, it ultimately concluded that a further  
4 hearing was not required and sustained the exemption objections,  
5 stating

6 The Court: I think it's, as far as I'm concerned,  
7 today, on these cases. I'm not going to hear any  
8 oral testimony on these things.

9 Mr. Cleland,<sup>[10]</sup> these are sizable amounts of  
10 money for consumers to -- and to say that  
11 they somehow forgot it or didn't know is  
preposterous to me. And it seems to me, in  
each instance, that any exemption claim  
should be denied and the property should be  
turned over to the trustee.

12 Transcript of Proceedings, May 25, 2005, p. 7.

13 Debtors appeal.

## 14 II. ISSUE

15 Whether the bankruptcy court erred in disallowing the  
16 exemptions of debtors who failed to list tax refunds on their  
17 original bankruptcy schedules and who later amended the schedules  
18 to claim the refunds exempt only after the trustee's inquiry.

## 19 III. JURISDICTION

20 Federal subject matter jurisdiction is founded under 28  
21 U.S.C. §§ 1334 and 157(b)(1) and (2)(B). We have appellate  
22 jurisdiction over final orders pursuant to 28 U.S.C. §§ 158(b)(1)  
23 and (c)(1).

## 24 IV. STANDARD OF REVIEW

25 We review legal issues de novo and the bankruptcy court's  
26 factual findings under a clearly erroneous standard. In re

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27  
28 <sup>10</sup> Mr. James Cleland, Jr. represented Debtors at the hearing  
and serves as their counsel in this appeal as well.

1 Arnold, 252 B.R. 778, 784 (9th Cir. BAP 2000). The bankruptcy  
2 court has no discretion to disallow amended exemptions unless the  
3 amendment was done in bad faith or caused prejudice to third  
4 parties, i.e., creditors. Id.; Matter of Doan, 672 F.2d 831, 833  
5 (11th Cir. 1982). Issues with regard to the right of a debtor to  
6 claim an exemption is a question of law we review de novo,  
7 however, questions as to the debtor's intent are factual and  
8 subject to the clearly erroneous standard. In re Arnold, 252  
9 B.R. at 784; In re Cataldo, 224 B.R. 426, 28-29 (9th Cir. BAP  
10 1988).

## 11 **V. DISCUSSION**

12 Rule 1009(a) provides that "a voluntary petition, list,  
13 schedule, or statement may be amended by the debtor as a matter  
14 of course at any time before the case is closed." A debtor may  
15 amend his schedules at any time before the case closes, absent a  
16 showing of bad faith or prejudice to creditors. In re Wolfberg,  
17 255 B.R. 879, 883 (9th Cir. BAP 2000); In re Andermahr, 30 B.R.  
18 532, 533 (9th Cir. BAP 1983) ("an exemption should be allowed no  
19 matter when it is claimed absent a showing of bad faith by the  
20 debtor or prejudice to creditors"). In this case, the record  
21 does not support a finding of either bad faith or prejudice to  
22 third parties.<sup>11</sup>

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23  
24  
25 <sup>11</sup> At oral argument, the trustee urged the panel to expand  
26 the circumstance under which a debtor can be denied an exemption  
27 to include, in addition to bad faith and prejudice to creditors,  
28 negligence, or at the very least, gross negligence in failing to  
disclose all assets. We believe the common law rule as it  
currently stands is sufficient, and therefore, decline the  
invitation to modify or expand it.

1           A. Bad Faith

2           Bad faith is typically found in circumstances where a debtor  
3 intends to hide assets. In re Arnold, 252 B.R. at 785. Stated  
4 otherwise, the conduct in question must involve an active  
5 concealment of assets, i.e., something more than mere negligence.  
6 In re Andermahr, 30 B.R. at 533.

7           In Arnold, the chapter 7 trustee successfully negotiated the  
8 settlement of the debtor's personal injury claim. The debtor,  
9 who had previously mentioned the lawsuit in his statement of  
10 affairs but had not listed the claim on his schedules of assets  
11 or exemptions, amended the schedules to claim the settlement  
12 proceeds exempt. The trustee objected on the grounds of bad  
13 faith and prejudice to creditors. The bankruptcy court rejected  
14 the debtor's assertion that he failed to list the claim because  
15 he did not understand that the claim constituted an asset of the  
16 estate. It concluded that by burying information about the  
17 lawsuit in the statement of financial affairs and omitting them  
18 from the schedules, the debtor acted in bad faith. On appeal,  
19 the panel reversed, holding that

20                   [G]iving due regard to the bankruptcy court's  
21 assessment of [the debtor's] credibility, and  
22 accepting that he knew that the State Court  
23 Action was an asset, the record still [could  
24 not] support a finding that [the debtor]  
25 intended to hide this asset.

26 In re Arnold, 252 B.R. at 786 (emphasis added).

27           While the trustee in this case concedes that bad faith was  
28 not explicitly raised by him or the court, he maintains that his  
principal argument regarding intentional concealment, and the  
court's response to it, sufficiently addressed the issue, as

1 evidenced by the following colloquy:

2 Mr. Arkison [the trustee]: That's a  
3 significant amount of money, Your Honor, that  
4 I'm looking at in terms of -- for a lot of  
5 these people, that's probably almost a  
6 month's salary that's coming back as a tax  
7 return. And I don't know if the attorney  
8 isn't asking the questions, Debtors are  
9 zoning out and not thinking about it, they  
10 don't know that it's a -- I mean, Your Honor,  
11 the problem is, when do we get to put our  
12 hand up and say, We want this money?

13 The Court: I think it's, as far as I'm  
14 concerned, today, on these cases. I'm not  
15 going to hear any oral testimony on these  
16 things.

17 Mr. Cleland, these are sizeable amounts of  
18 money for consumers -- and to say that they  
19 somehow forgot it or didn't know is  
20 preposterous to me. And it seems to me, in  
21 each instance, that any exemption claim  
22 should be denied and the property should be  
23 turned over to the trustee.

24 Transcript of Proceedings, May 25, 2005, p. 7.

25 An objective examination of the record tends to support  
26 Debtors' contentions that their failure to disclose the refunds  
27 was inadvertent and not an attempt to conceal the assets. In  
28 their declarations, Debtors each stated

29 When reviewing the bankruptcy paperwork I  
30 signed on February 9, 2005, and the property  
31 that was "Other contingent and unliquidated  
32 claims of every nature . . .", [sic] I did  
33 not understand that this meant money I hadn't  
34 gotten yet, and Mr. Cleland did not explain  
35 this to me.

36 Mr. Cleland DID explain to me that I had far  
37 less property than the maximum allowed by  
38 law, and that I should feel free to list all  
39 of my property.

40 Had I known what the questions meant, I would  
41 have certainly listed the tax refund, as I  
42 knew from what my attorney told me that I  
43 would keep it.

1 Further, upon the trustee's inquiry regarding the tax  
2 refunds, Debtors answered honestly and followed up with an  
3 appropriate amendment to their schedules. A mere delay alone is  
4 not sufficient to support a finding of bad faith. In re Arnold,  
5 252 B.R. at 786.

6 Finally, confusion among debtors over the reporting of tax  
7 refunds is apparently not a new circumstance for the court.  
8 Apparently, the court had, in the previous year, chastised  
9 certain attorneys and their clients for neglecting to schedule  
10 tax refunds in their initial schedules, but had not denied their  
11 exemptions. Although Mr. Cleland was not privy to "the  
12 speech,"<sup>12</sup> the court's earlier leniency in other unrelated cases  
13 may have been a factor in the court's decision to deny Debtors'  
14 request for an evidentiary hearing.<sup>13</sup>

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15  
16 <sup>12</sup> Reference to the court's earlier "speech" appears in the  
17 following colloquy between the trustee and the court:

18 Mr. Arkison: All of them are basically the same issue  
19 of the tax refunds not being listed. And there's a  
20 point in time . . . when we have to raise the issue and  
21 draw a line. I believe a year ago you -

22 The Court: I gave them a speech.

23 Mr. Arkison: - you gave your speech.

24 The Court: I remember the speech.

25 Mr. Arkison: I mean, I'm back again a year later.

26 Transcript of Proceedings, May 25, 2005, p. 3-4.

27 <sup>13</sup> During the course of the hearing, the following exchange  
28 took place between the court and Mr. Cleland:

Mr. Cleland: Normally, I wouldn't ask for oral  
testimony . . .

(continued...)



1 B. Prejudice to Creditors

2 Neither the trustee's exemption objections nor the court's  
3 ruling appear to have been based on prejudice to creditors.  
4 Accordingly, we need not address the issue.

5 **VI. CONCLUSION**

6 Based on the foregoing, we conclude that the factual record  
7 does not sufficiently support the disallowance of Debtors'  
8 exemptions as to the tax refunds on the basis of intentional  
9 concealment, i.e., bad faith. Accordingly, we REVERSE the  
10 decision of the bankruptcy court and REMAND with instructions  
11 that it 1) conduct an evidentiary hearing on the issue of bad  
12 faith and 2) issue findings of fact and conclusions of law  
13 following the hearing.

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<sup>13</sup>(...continued)

19 The Court: Okay.

20  
21 Mr. Cleland: That's awfully short notice for  
my clients to get off work, sir.

22 The Court: Well, I know. But these are  
23 serious things. You now, I let everybody out  
24 last year.

25 Mr. Cleland: Sir, I wasn't privy to it. I  
didn't know you chastised --

26 The Court: It doesn't make any difference. I  
27 was being gracious last year. This one --  
the first case out --

28 Transcript of Proceedings, May 25, 2005, p. 5-6.