



THE STATE BAR OF CALIFORNIA Business Law Section

Insolvency Law e-Bulletin

September 7, 2016

Dear constituency list members of the Insolvency Law Committee,

The following is a case update analyzing a recent case of interest:

SUMMARY

In *Caldwell v. Nelson (In re Caldwell)*, 545 B.R. 605 (9th Cir. BAP 2016), the BAP held that Bankruptcy Code Section 522(p)(1)'s limitation on the amount a debtor could claim as a homestead exemption did not apply based on the applicable Nevada State exemption statutes even though the Debtor only obtained legal title to the subject property within the 1215-day pre-petition period that otherwise would implicate Section 522(p)(1)'s limitation.

To read the full published decision, click here: <http://bit.ly/2bX6r5l>.

FACTS

In 1994, Patrick Caldwell (the "Debtor") and his spouse purchased residential real property in Nevada (the "Property"). At all relevant times, the Caldwells lived at the Property and paid the mortgage, taxes, insurance, and other expenses associated with homeownership. Between 1998 and 2011, the Caldwells transferred title to the Property seven times, to and from a trust in which the Caldwells were the sole trustees (the "Trust") and to a limited liability company in which the Caldwells were the sole members (the "LLC"). All of the transfers were for no consideration and described as forms of estate planning.

On October 10, 2011, the Caldwells transferred the Property from the LLC to the Trust (the "2011 Transfer"). That same day, the Caldwells recorded a declaration of homestead against the Property.

On September 5, 2014 (the "Petition Date"), 1061 days after the 2011 Transfer, the Debtor filed a voluntary chapter 7 petition. In his schedules, the Debtor claimed the full \$550,000 homestead exemption in the Property allowable under Nevada Revised Statutes (NRS) 21.090(1)(l) and 115.050.

The chapter 7 trustee objected to the exemption, seeking to limit the exemption to \$155,675 under Section 522(p)(1) of the Bankruptcy Code because the 2011 Transfer occurred during the 1215-day period preceding the Petition Date. The Debtor argued that the limitation under Section 522(p)(1) did not apply because he always retained a beneficial and equitable interest in the Property despite the numerous transfers of legal title to and from the Trust and LLC. The Debtor reasoned that such interests were retained since he and his spouse were the sole trustees of the Trust and the sole members of the LLC and thus the Debtor was "merely transferring title from himself to an entity owned by him." The Debtor also asserted that his continuous payment of all Property expenses indicated that he and his spouse continued to use and consider the Property as their own. Finally, the Debtor contended that under NRS 115.020, neither he nor his spouse needed to hold legal title to declare a homestead.

The bankruptcy court rejected the Debtor's arguments and limited the Debtor's homestead exemption to \$155,675 under Section 522(p)(1). The bankruptcy court reasoned that (1) under applicable law, the Debtor did not hold an interest in the Property while title was in the LLC's name because the LLC was a separate legal entity, and a member's interest in an LLC is personal property; (2) Nevada exemption laws required the Debtor to hold an ownership interest, rather than a general or possessory interest, in the Property; and (3) the Debtor could not claim a homestead interest in property held in the name of an LLC.

The Debtor appealed.

THE BAP'S RULING AND REASONING

The BAP reversed the bankruptcy court's ruling.

In determining whether the Debtor held an interest in the Property to support a homestead claim while the LLC held title, the BAP noted that the applicable Nevada statutes -- NRS 21.090(1)(l) and 115.005(2)(a) -- do not designate how title must be held or require an individual to hold title to property in fee simple in order for real property to qualify as a "homestead." Rather, the BAP found that, to secure the benefits of a Nevada homestead exemption, an individual must record a declaration of homestead stating that the individual is a "householder."

Pointing to a 1909 Nevada Supreme Court decision defining "householder" as "one who keeps house," the BAP concluded that a householder "must be in actual possession of the house" and must be "the occupier of a house." The BAP further noted that, under the Nevada law, a "householder" referred "to the civil status of a person, not his property, and a man may be a householder without owning real estate." Accordingly, the BAP held that because the Debtor had lived on the Property since 1994, and was at all times in actual possession of the house, he met the definition of a "householder," entitling him to claim the homestead exemption even while the LLC held legal title to the Property.

Next, the BAP turned its attention to Nevada's requirement that a homestead claimant needs to hold some type of interest in the Property to claim the "equity" exemption up to \$550,000 under NRS 115.010. The BAP explained that NRS 115.005(1) defined "equity" as "the amount that is determined by subtracting from the fair market value of the property the value of any liens excepted from the homestead exemption under NRS 115.010 or NRS 115.090." In a decision interpreting what qualifies as equity in property, the Nevada Supreme Court previously held that a person must hold more than a general interest in or right to possession, but did not otherwise limit the estate that must be owned. Based on that decision, the BAP held that, when read in the context of the definition of a "householder" and applicable case law, the type of "ownership" required is not limited to only fee simple title.

Accordingly, the BAP concluded that here the Debtor retained more than a general interest or mere right to possession in the Property after the transfer of legal title to the LLC based on his retaining all the indicia of ownership including the continuous use and possession of the Property, and payment of the mortgage, taxes and insurance, all of which maintained the "equity" protected by the homestead exemption. Therefore, the BAP held that the Debtor was not divested of all interest in the Property by the transfer of legal title to the LLC, and that his homestead rights in the Property, before and after the transfers of title, remained unchanged. In turn, the BAP ruled that the 2011 Transfer did not result in the Debtor acquiring an "interest" in the Property within the 1215-day pre-petition period so as to limit the amount of exemption under Section 522(p)(1).

AUTHOR'S COMMENTARY

Caldwell joins a string of recent decisions in which the BAP ruled in favor of protecting a debtor's interest in a claimed homestead exemption. See, e.g., *In re Calderon*, 507 B.R. 724 (9th Cir. BAP 2014); *In re Elliott*, 523 B.R. 188 (9th Cir. BAP 2014); *In re Gray*, 523 B.R. 170 (9th Cir. BAP 2014); *In re Diaz*, 547 B.R. 329 (9th Cir. BAP 2016). These decisions signal the panel's willingness to delve deeply into state exemption laws to identify legitimate statutory bases to enable debtors to utilize the homestead exemption.

Caldwell again urges bankruptcy courts and trustees to take a more comprehensive reading of state exemption schemes. The validity of homestead exemption claims under Nevada law requires a thorough analysis of the debtor's ownership interest in the subject homestead beyond the mere form of title.

With the BAP seemed to display an increased interest in policing the exemption disallowance process, chapter 7 trustees within the Ninth Circuit are advised to extensively analyze the applicable homestead exemption statutes and laws before engaging in costly litigation.

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