UNITED STATES BANKRUPTCY APPELLATE PANEL FOR THE FIRST CIRCUIT

BAP No. MW 01-031

IN RE: STEVEN A. NEWTON

Debtor

Appeal from the United States Bankruptcy Court
for the District of Massachusetts
(Hon. Joel B. Rosenthal, U.S. Bankruptcy Judge)

Before

VOTOLATO, LAMOUTTE, DE JESUS, U.S. Bankruptcy Appellate Panel Judges

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David W. Lima for the Appellant.

Steven Weiss, Shatz, Schwartz and Fentin, P.C. for the Appellee

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January 10, 2002

LAMOUTTE, Bankruptcy Judge.

The issue before the panel is whether the bankruptcy court erred in denying debtor's motion to amend his chapter 7 petition because it found that he had acted in bad faith.

Background

Debtor filed a petition for relief under chapter 7 of the Bankruptcy Code on August 23, 2000. He listed in Schedule B a 1985 Ford log truck, estimating the value at $12,000. The debtor uses the truck for self-employment. The debtor had given his son, John Newton, the title of the truck in return for a loan for its purchase; at the time of filing, the balance owed was $8,500. According to the debtor, he mistakenly believed that delivery of the title had created a lien, and therefore informed his attorney that there was a lien on the vehicle and listed John as a secured creditor. At the meeting of creditors, held on October 2, 2000, the trustee, Steven Weiss, asked about the nature of the security interest in the truck. Debtor provided the trustee with a copy of the truck's title, which listed no secured party; in fact, no lien had ever been filed with the Department of Motor Vehicles or the Secretary of the Commonwealth of Massachusetts. The trustee informed the debtor that, because the security interest was unperfected, he would move to avoid the lien for the benefit of creditors under 11 U.S.C. §§ 544 and 551. The debtor moved to amend schedules D and F to include John Newton as an unsecured creditor, and to amend schedule C to use his exemptions under 11 U.S.C. § 522(d)(5), (6) to protect his equity in the vehicle up to $9,756.00. Debtor also had the vehicle appraised in the amount of $10,000 and amended schedule B accordingly. The trustee objected to debtor's amendment of his schedules.

After an evidentiary hearing, the bankruptcy court denied the motion to amend, finding clear and convincing evidence that debtor had filed the motion in bad faith and that its allowance would

prejudice the creditors. The court entered an order on April 23, 2001, specifically finding (1) that the trustee failed to satisfy his burden of proof that debtor's son had a valid security interest for the trustee to preserve for the estate under 11 U.S.C. §§ 544 and 551; however, (2) that the trustee sustained his burden of proof by clear and convincing evidence that the debtor filed the motion to amend schedules in bad faith, and that the amendment would prejudice creditors because the debtor maintained that his son held a security interest in the truck until the trustee made a demand for it, and did not file the motion to amend until after the deadline for creditors or the trustee to object to discharge had passed. The court further found that the debtor had deliberately not kept records of the truck transaction or had concealed them. The court allowed the debtors exemption in the truck in the amount of $3,500 as originally scheduled. See Order, Appendix pp. 41-42. See also Transcript of Evidentiary Hearing, Appendix pp. 43-70.

Jurisdiction

This panel reviews the bankruptcy court's application of law *de novo* and its findings of fact under a clearly erroneous standard. Jeffrey v. Desmond, 70 F.3d 183, 185 (1st Cir. 1995); In re SPM Mfg. Corp., 984 F.2d 1305 (1st Cir. 1993). Decisions entrusted to the discretion of the bankruptcy judge are reviewed for abuse of discretion. Moretti v. Bergeron (In re Moretti), 260 B.R. 602 (BAP 1st Cir. 2001) ("Abuse occurs when a material factor deserving significant weight is ignored, when an improper factor is relied upon, or when all proper and no improper factors are assessed, but the court makes a serious mistake in weighing them." (citations omitted)).

Arguments on Appeal

The appellant/debtor argues that the bankruptcy court erred in denying his motion to amend because under Fed. R. Bankr. P. 1009, which provides that a voluntary petition, list, schedule or

statement may be amended by the debtor as a matter of course at any time before the case is closed, he has an absolute right to amend his schedules. Although he acknowledges that some courts have carved out a judicial exception to the right to amend where a debtor had acted in bad faith or the creditors are prejudiced, he argues that the debtor's right to amend should be construed liberally and motions to amend should be disallowed only in exceptional cases. Debtor argues that the facts in this case do not support a finding of bad faith and, further, that the trustee and creditors are not prejudiced by the amendment because they have always known that debtor owned the truck and would exempt its equity. According to the debtor, his amendment only seeks to use exemptions which were always available to him and which would have been claimed to protect the equity in the vehicle if he had believed the debt to be an unsecured one.

The trustee replies that the requirement that pleadings be filed in good faith underlies the entire Bankruptcy Code, and that the debtor does not have *carte blanche* to amend his schedules under any circumstances. According to the trustee, although Fed. R. Bankr. P. 1009 does not specifically require a finding of good faith, many provisions of the Bankruptcy Code do, which has led many courts to find a debtor's general right to amend schedules is tempered by a good faith requirement. The trustee argues that the bankruptcy court's findings of bad faith were factual and not clearly erroneous, and therefore should not be overturned.

Discussion

Fed. R. Bank. P. 1009 provides in pertinent part:

> (a) *General Right to Amend*. A voluntary petition, list, schedule, or statement may be amended by the debtor as a matter of course at any time before the case is closed.

This permissive approach to amendment has been construed to give courts no discretion to reject

amendments unless the debtor has acted in bad faith or concealed property, or the amendment would prejudice creditors. 9 Lawrence P. King, et al., Collier on Bankruptcy ¶ 1009.02[1] (15th ed. rev. 2001). "Bad faith" by the debtor, which may cause a court to disallow an exemption amendment, is generally identified as some sort of attempt to conceal an asset. In re Cudeyro, 213 B.R. 910, 918 (Bankr. E.D. Pa. 1997).

In determining whether the amendment would prejudice creditors, the appropriate inquiry is not whether a creditor will recover less or be adversely affected by the amendment; instead, a court must determine whether the creditor would be adversely affected by having detrimentally relied on the debtor's initial position. Collier, ¶ 1009.02[1] at 1009-3; In re Talmo, 185 B.R. 637, 645 (Bankr. S.D. Fla. 1995) ("[P]rejudice may be established by showing harm to the litigating posture of parties in interest. If the parties would have taken different actions or asserted different positions had the exemption been claimed earlier, and the interests of those parties are detrimentally affected by the timing of the amendment, then the prejudice is sufficient to deny amendment."). Prejudice has also been found to accrue where a debtor exhibits "inordinate delay" in amending his exemption schedules. Cudeyro, 213 B.R. at 920.

The right to amend the various statements and schedules does not mean that the debtor has an unfettered right to alter previously-settled rights of affected entities. Collier, ¶ 1009.02[1] at 1009-3. This issue was discussed in In re St. Angelo, 189 B.R. 24 (Bankr. D.R.I. 1995), wherein the court stated:

> Under Federal Rule of Bankruptcy Procedure 1009, a debtor may amend a voluntary petition as a matter of course anytime before the case is closed. This language comports with the well-established principle that exemptions should be liberally construed in furtherance of the debtor's right to a "fresh start," and absent bad faith or

> prejudice to creditors, courts have little or no discretion to deny leave to amend a claim of exemption.
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> The court may disallow such amendments, however, in exceptional circumstances.... Intentional concealment of estate property will bar the debtor from claiming such property as exempt, after it surfaces as an asset. Intent to conceal is a factual determination to be made by a bankruptcy court, based upon the evidence presented and inferences drawn therefrom at trial.
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> Id. at 26 (citations omitted).

Thus, the bankruptcy court must balance the right to amend under Rule 1009 with the need to administer the estate for the benefit of all creditors. Although the right to amend is broad, the debtor must assume responsibility for intentional omissions from the schedules.

The bankruptcy judge considered the standard for allowing amendments under Rule 1009, as well as the judicially-created exceptions thereto, and found that the debtor's actions showed bad faith and prejudiced the creditors. Accordingly, the court refused to allow debtor to amend his schedules. These factual findings by the bankruptcy court are reviewed under the clearly erroneous standard. Under that standard, "the bankruptcy judge's findings are to be set aside only if, on the entire evidence, we are 'left with the definite and firm conviction that a mistake has been committed.'" In re Tully, 818 F.2d 106, 109 (1st Cir. 1987), citing United States v. United States Gypsum Co, 333 U.S. 364, 395 (1948). The court in Tully further noted that "where the conclusions of the [trier] depend on its election among conflicting facts or its choice of which competing inferences to draw from undisputed basic facts, appellate courts should defer to such fact-intensive findings, absent clear error." Id., citing Irons v. FBI, 811 F.2d 681, 684 (1st Cir. 1987).

The debtor/appellant has not pointed to any specific findings as being clearly

erroneous; rather, he offers explanations of his actions. The record indicates that these arguments were also made to the bankruptcy court and were rejected. The appendix includes the complete transcript of the evidentiary hearing that the court conducted, as well as the two-page opinion that it issued. The opinion contains the court's findings and conclusions, and indicates that it considered debtor's testimony and certain exhibits. Specifically, the bankruptcy court found:

> [T]he Court finds the Trustee sustained his burden of proving by clear and convincing evidence that the Debtor filed the Motion in bad faith, and that the Debtor's proposed amendment would prejudice creditors in the Debtor's case, insomuch as the Debtor maintained that Newton held a security interest in the Truck until such time as the Trustee made demand for the Truck, and furthermore the Debtor did not file the Motion until after the deadline had passed for creditors or the Trustee to object to the Debtor's discharge. The Court also drew an inference adverse to the Debtor, based on the Debtor's testimony, that records of the cash transaction between the Debtor and Newton were either deliberately not kept or deliberately concealed.

"Order on Debtor's Motion to Amend Schedules B, C, D, and F and Chapter 7 Trustee's Objection", App. p. 42. Thus, the court found that the debtor's actions were made in bad faith and that the creditors were prejudiced by debtor/appellant's actions because the motion to amend was not filed until after the deadline had passed for them to object to discharge. These findings led the bankruptcy court to conclude that the debtor's motion to amend should be denied. The debtor has not pointed to any part of this record which illustrates why the panel should conclude that the bankruptcy court's findings of bad faith and prejudice were clearly erroneous.

Conclusion

The First Circuit Court of Appeals has previously stated:

> [T]he very purpose of certain sections of the law...is to make certain that those who seek the shelter of the bankruptcy code do not play fast and loose with their assets or with the reality of their affairs. The statutes are designed to insure that complete, truthful, and reliable information is put forward at the outset of the proceedings, so that decisions can be made by the parties in interest based on fact rather than fiction. As we have stated, '[t]he successful functioning of the bankruptcy act hinges both upon the bankrupt's veracity and his willingness to make a full disclosure.' Neither the trustee nor the creditors should be required to engage in a laborious tug-of-war to drag the simple truth into the glare of daylight. The bankruptcy judge must be deft and evenhanded in calibrating these scales.

Tully, 818 F.2d at 110 (citations omitted). The same reasoning applies to the matter before this panel. The record shows that the bankruptcy judge who heard the evidence did calibrate the scales by considering and balancing the facts presented by the debtor and the trustee, analyzed them in light of the applicable law, and found against debtor. Appellant has failed to show that the bankruptcy judge's findings were clearly erroneous, or that his legal analysis was an abuse of discretion. Accordingly, the appellant's petition is denied, and the decision of the bankruptcy court to deny debtor's motion to amend is hereby AFFIRMED.