homestead is not subject to § 522(q)(1) because it is "reasonably necessary" for his support under § 522(q)(2) due to the fact that he needs a pool to relieve his arthritic condition. For the reasons stated below, the Court rejects each of these defenses and finds that the Debtor is limited to a $125,000.00 exemption by § 522(q)(1)(B)(ii).

B. Findings of Fact

1. On May 13, 2005, the Debtor and Evelyn Presto entered into the Divorce Decree. [Comm. Ex. 3-B.3.] The Divorce Decree states:

> [I]f a refund is made for the overpayment of taxes for any year during the parties' marriage in which a joint federal income tax return was filed that each party shall be entitled to one-half of the refund and the party receiving the refund check is designated as a constructive trustee for the benefit of the other party to the extent of one-half of the total amount of the refund, and shall pay to the other party one-half of the total refund check within five days of receipt of the endorsed refund check. It is further ORDERED that the parties will cooperate executing any refund check.
>
> [*Id.*]

2. In the Fall of 2005, the Debtor prepared an amended joint tax return for 2002, a year during which the parties were married. The Prestos' amended tax return resulted in a refund for 2002.

3. The Debtor signed Evelyn Presto's name to the amended tax return without her knowledge or consent. She had no knowledge that a refund would be forthcoming. [Comm. Ex. 3-B.7 (Transcript of Evelyn Presto deposition), p. 39.]

4. On October 21, 2005, the U.S. Treasury issued a tax refund check in the amount of $24,568.00 made payable to "Kevin M. & Evelyn L. Presto." [Comm. Ex. 3-B.5.]

5. Upon receipt of the tax refund check, the Debtor endorsed the check with his own name and, again without her knowledge or consent, signed the name of Evelyn

Presto. [Comm. Ex. 3-B.5.] On October 25, 2005, the Debtor deposited the tax refund check into his Wells Fargo account. [Comm. Ex. 10, WF-0042.]

6. On July 31, 2006, the date that the Debtor filed his Chapter 7 petition, Evelyn Presto had not received any payment from the Debtor for her half of the tax refund. The Debtor did not schedule Evelyn Presto as a creditor, and she did not file a proof of claim for this debt because she had no knowledge of the tax refund. [Comm. Ex. 3-B.7 (Transcript of Evelyn Presto deposition), p. 99 - 100.]

7. On November 30, 2006, the Debtor sent an email to Evelyn Presto informing her for the first time of the existence of the amended tax return and refund check. This email states, in pertinent part:

> I have been subject to numerous discovery requests that involve digging up years worth of old bank statements, sources and uses of cash, tax returns, etc. As I was going through the various documents, including old tax returns, I came across a situation whereby it appears you never received the $12,284 [check] for 50% of the restated 2002 tax return refund resulting from a 2004 loss carryback. This return was restated in the fall of 2005 (post divorce), and I acted as your constructive trustee (as the decree calls for on page 43), endorsed the return on your behalf and endorsed the refund check on your behalf. However, the Wells Fargo statements suggest that you never received the 50% of the refund that you were entitled too [sic] per the decree. If you recall, I had just paid you $30,000 in November 2005 pursuant to the decree and this was about the same time I received the IRS refund check. I don't recall what happened, but I thought I had sent you both checks at the same time ($30,000 and $12,284), but the Wells Fargo bank statements only showed the $30,000 check clearing in November 2005 . . . I'm pretty certain I mailed the check, but nothing ever hit my account.
>
> [Presto Ex. G.]

The Debtor then offered to satisfy the debt by making a $2,000.00 payment on December 1, 2006 and a $1,000.00 payment for each of the next 12 months. [*Id.*]

8. Evelyn Presto expressly rejected the Debtor's offer to pay in installments and demanded immediate payment of the entire $12,284.00. The Debtor failed to do so, but began mailing the monthly payments as set forth in his email of November 30, 2006. [Comm. Ex. 3-B.7 (Evelyn Presto Deposition), Ex. 6.] Evelyn Presto accepted a $2,000.00 check in December 2006 and a $1,000.00 check in January 2007.

9. On December 7, 2006, the Debtor executed an amended Schedule F which did not include the tax refund debt owed to Evelyn Presto. [Docket No. 159.]

10. On January 30, 2007, Evelyn Presto sent an email to the Debtor which inquired, "Will you be mailing the remainder of tax refund as discussed? I did not/have not agreed to monthly payments, and would like what's owed to me in full." [Comm. Ex. 3-B.7 (Evelyn Presto Deposition), Ex. 9.]

11. On February 10, 2007, the Debtor sent Evelyn Presto a letter regarding satisfaction of the tax refund debt. The Debtor testified that his counsel for this matter, Michael Colvard, actually drafted this letter. This letter reads, in pertinent part, as follows:

> I have tendered the first and second installments, bringing a [sic] total payments that you have received to $3,000. Pursuant to follow-up emails and verbal discussions, I understand that you prefer to be paid off the final balance in a lump sum, which I have agreed to do. Therefore, the following agreement has been reached:
>
> 1. I agree to pay the total sum of $10,000 in consideration for any remaining balance owed to you for the IRS refund. A check for that amount is enclosed herein. By endorsement of this check, you agree to the following terms:
>
> a. The receipt and payment of said sum constitutes full and final satisfaction of any and all claims you have to any remaining sums due for the income tax refund;
>
> . . .

c. You will assert no future claims in law or in equity, whether criminal or civil, in relation to the receipt and endorsement of the refund check;

d. That payment of the enclosed $10,000 check, together with two prior installments of $2,000 and $1,000, respectively for a total of $13,000, compensates you in full for all claims of principle [sic], interest or other in relation to your rights to one-half of the tax refund;

[Presto Ex. H.]

12. On February 16, 2007, the Committee filed a Supplemental Objection to Debtor's Claim of the Homestead Exemption. [Docket No. 107.] This Supplemental Objection raised the issue of the Debtor's conduct regarding the tax refund proceeds for the first time.

13. On February 20, 2007, Evelyn Presto endorsed the $10,000.00 check contained in the February 10, 2007 letter. With her receipt of the $10,000.00, the tax refund debt was fully satisfied. [Comm. Ex. 3-B.7 (Transcript of Evelyn Presto Deposition), p. 101.]

14. On March 8, 2007, the Debtor executed an affidavit, attached to his Motion for Summary Judgment, stating, "Upon receipt of the tax refund check in October 2005, I made a check payable to my former wife, Evelyn Presto, for exactly one-half of the entire amount of the refund check. I recall preparing that check because I prepared another check in the amount of $30,000 payable to Evelyn Presto *on that same date*." [Docket No. 128, Ex. 6, ¶ 14 (emphasis added).]

15. On March 30, 2007, the Debtor executed an amended version of the same affidavit, which was attached to his Objection to one of the Committee's Motions for Summary Judgment. This second affidavit states, "I recall preparing that check because I

prepared other checks payable to Evelyn Presto *on or about that same date* in the amounts of $30,000 and two checks for $600 each." [Docket No. 145, Ex. 6, ¶ 14 (emphasis added).]

16. Check number 2093 in the amount of $30,000.00 is dated October 25, 2005. The two $600 checks, numbers 2097 and 2098, are dated October 28, 2005. [Comm. Ex. 17; Comm. Ex. 10, WF-000167-169.] The next check, number 2100, is dated November 10, 2005. [Comm. Ex. No. 10, WF-0050.]

17. The monthly statement of the Debtor's Wells Fargo account shows the following checks being honored:

Check Number	Date Cashed	Amount
2093	**10/31**	**$30,000.00**
2094	11/02	$200.00
2095	11/16	$1,000.00
2096	10/31	$2,600.00
2097	**11/01**	**$600.00**
2098	**11/01**	**$600.00**
2100	11/14	$1,100.00

[Comm. Ex. No. 10, WF-0050.]

18. The Debtor testified that he wrote check number 2099 to Evelyn Presto within one or two days of the other three checks that benefitted her, but that it must have been lost in the mail.

19. The Debtor testified that all four checks to Evelyn Presto (numbers 2093, 2097, 2098 and 2099) were written and mailed from his place of work in the Marathon Tower in Houston, Texas.

20. The Debtor testified that he did not mail all four checks together in one envelope. The two $600.00 checks were child support payments that went to a state

disbursement agency, not directly to Evelyn Presto. At the June 20, 2007 hearing, when asked by his own counsel on direct examination why the $30,000.00 check and the check for the tax refund were not mailed in the same envelope to Evelyn Presto, the Debtor testified, "I had [the tax refund check to Evelyn Presto] sitting in a separate envelope on my desk counter at my former employer and I just . . . I guess I was maybe worried about the funds in there or something . . . I don't know . . . but it didn't get mailed on the same date." He further testified that he specifically remembered writing all four checks close together in time because he "was not happy that [he] was writing checks for that amount of money to [his] ex-wife."

21. The Debtor testified that he did not discover that check number 2099 was missing until November 2006 while preparing bank statements as part of document production in this case. The Debtor further testified that this year-long oversight was due to "sloppy" balancing of his checkbook and the stress of the avoidance action litigation.

22. The daily balance of the Wells Fargo account during the time when check number 2099 could have been written was as follows:

Date	Balance
10/31	$11,494.95
11/01	$9,365.09
11/02	$8,890.79
11/03	$5,608.22
11/04	$5,550.74
11/07	$5,467.66
11/08	$5,044.09
11/09	$4,880.09

[Comm. Ex. 10, WF-0054.]

23. At the end of November 2005, the balance of the Wells Fargo account was $3,063.06 [Comm. Ex.10, WF-0049], and at the end of December 2005 the balance was $3,865.11. [Comm. Ex. 10, WF-0055.]

24. The Debtor testified that he suffers from a severe arthritic condition, and that he uses his pool and spa for approximately one hour each morning in order to alleviate the pain of his arthritis. The Debtor presented no expert testimony regarding his medical condition.

25. In order to construct the pool, the Debtor needed the approval of the homeowners' association in the Royal Oaks development. The association had a standard 45-day waiting period before approving any proposals. In an attempt to expedite the approval process, the Debtor sent an email to members of the association explaining his need to have construction on the pool begin sooner than the standard 45 days. The email reads, in pertinent part:

> "I would still like to explain in writing my personal situation. Again, I am not asking for special treatment, just a little 'push' if possible as a favor to me for the reasons outlined below.
>
> I went through a nasty divorce last summer which involved a custody battle as well. I currently have my children the entire 80 day summer and basically all holidays. My children arrive on June 2, 2006 and leave on August 12, 2006. I have sold my current house which had a swimming pool that my children loved dearly and swam in literally every day of every summer. My children are ages 8 and 5 and have been swimming since they were 1 year old. This is the first summer I will have the children by myself, and the first time they have seen me in a different house. I want my children to be happy with their situation and be excited about having a slide, hot tub, nice pool, etc. to use in their backyard for as much of the summer as possible. *If I didn't have my beautiful young children to please, I would not be asking for accelerated approval*, but please understand (like all good Daddy's [sic]), I want to put a big smile on my children all summer

> and Mike has designed a beautiful backyard haven that I want them to enjoy all summer."
>
> [Debtor Ex. R; Docket No. 165, Ex. C (emphasis added).]

This email makes absolutely no mention of the Debtor's arthritic condition, which he testified was so severe that without the aid of a pool that he was occasionally unable to leave the house.

26. The Debtor is currently employed by Bear Energy, an affiliate of Bear Stearns Companies Inc. His annual salary is $175,000.00, with a guaranteed $100,000.00 bonus in the first year and potential bonuses in future years.

C. Conclusions of Law

1. Section 522(q)(1)(B)(ii) requires the Committee to prove that (a) the Debtor owed Evelyn Presto a fiduciary duty; and (b) he committed fraud, deceit, or manipulation while acting in this fiduciary capacity.

Section 522(q)(1)(B)(ii) provides, in pertinent part:

> (1) As a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) which exceeds in the aggregate $ 125,000 if–
>
> . . .
>
> (B) the debtor owes a debt arising from–
>
> . . .
>
> (ii) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 1934 or under section 6 of the Securities Act of 1933;

The Committee interprets § 522(q)(1)(B)(ii), based on the placement of commas, or the lack thereof, to mean that the phrase "in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities and Exchange Act of 1934 or under section 6 of the Securities Act of 1933" modifies only "manipulation" and does not apply to

"fraud" or "deceit." In other words, the Committee contends that a debt arising out of *any* kind of fraud or deceit is sufficient for § 522(q)(1)(B)(ii). The Court disagrees.

Similar language appears in §§ 523(a)(19)(A)(i) and (ii), which except from discharge any debt that is for:

> (i) the violation of any of the Federal securities laws (as that term is defined in section 3(a)(47) of the Securities Exchange Act of 1934), any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or
>
> (ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security

This section added a new type of nondischargeable debt as part of the Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, § 803(3), 116 Stat. 745. *Sherman v. SEC* (*In re Sherman*), Case No. 03-56601, 2007 U.S. App. LEXIS 15833, at *70 (9th Cir. July 3, 2007); *Smith v. Gibbons* (*In re Gibbons*), 289 B.R. 588, 589 (Bankr. S.D.N.Y. 2003). The addition of § 523(a)(19) was designed to close a "loophole" which allowed debtors convicted of securities fraud or other securities violations to discharge the debt owed to their victims. *Gibbons*, 289 B.R. at 592 (citing comments of Senator Patrick Leahy, 148 CONG REC. S 1787 (daily ed. March 12, 2002) and the Committee Report, S. RRP. No. 107-146 (2002)). The purpose of adding § 523(a)(19) was not to prevent the discharge of a debt arising from any common law fraud, but only those debts arising from securities related fraud.

Sections 522(q)(1)(B)(ii) and 523(a)(19) contain similar language, the difference being that Congress inserted the phrase "in a fiduciary capacity" between "fraud, deceit or manipulation" and "the purchase or sale of any security." 11 U.S.C. § 522(q)(1)(B)(ii). Congress has consistently

linked the phrase "fraud, deceit or manipulation" to securities violations.[41] Nothing about the addition of "in a fiduciary capacity" warrants a severance of this connection.[42] Thus, instead of accepting the Committee's interpretations of § 522(q)(1)(B)(ii), the Court interprets this provision to require that the "fraud, deceit, or manipulation" must have occurred while the Debtor was acting *either* in a fiduciary capacity *or* in connection with the purchase or sale of any registered security. Since there are no facts relating to the purchase or sale of any securities, the Committee bears the burden of proof on two elements in order to sustain its objection to the Debtor's homestead exemption under § 522(q)(1)(B)(ii): first, the Committee must establish that the Debtor owed Evelyn Presto a fiduciary obligation in relation to the tax refund proceeds; and second, the Committee must show that the Debtor committed fraud, deceit, or manipulation while acting in that fiduciary capacity.

2. The Debtor's receipt of the tax refund proceeds created a fiduciary obligation to Evelyn Presto.

The Committee argues that although the marital fiduciary relationship terminated after the divorce, the language of the Divorce Decree created a new fiduciary duty that first came into existence when the Debtor received the tax refund check.[43] The Divorce Decree states that "the party

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[41] The language "fraud, deceit, or manipulation" has been used by Congress in other instances, each within the context of securities regulation. For example, the Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 102-409 § 101, 104 Stat. 931, 932-33 (codified at 15 U.S.C. § 77t(d)), has a multi-tiered penalty system that includes the phrase "fraud, deceit, manipulation, or a deliberate or reckless disregard of a regulatory requirement." 15 U.S.C. § 77t(d)(2)(B); *see also SEC v. Kern*, 425 F.3d 143, 153 (2nd Cir. 2005). Section 804 of the Sarbanes-Oxley Act extended the statute of limitations to bring claims for "fraud, deceit, manipulation or contrivance in contravention of a regulatory requirement concerning the securities laws." *Newby v. Enron* (*In re Enron Corp. Secs.*), 465 F. Supp. 687, 711 (S.D. Tex. 2006).

[42] Although corporate directors and officers have fiduciary obligations, the language of § 522(q)(1)(B)(ii) does not limit its application to corporate settings. The statute simply uses the term "in a fiduciary capacity" which encompasses a wide range of fiduciary relationships.

[43] The fiduciary relationship between husband and wife terminates upon divorce. *In re Marriage of Notash*, 118 S.W.3d 868, 872 (Tex. App.—Texarkana 2003, no writ) (citing *Grossnickle v. Grossnickle*, 935 S.W.2d 830, 846 (Tex. App.—Texarkana 1996, writ denied)); *see also Bass v. Bass*, 790 S.W.2d 113, 119 (Tex. App.—Fort Worth 1990, no writ) ("Although marriage may bring about a fiduciary relationship, such a relationship clearly does not continue when a husband and wife hire numerous independent professional counsel to represent them respectively in a contested divorce

receiving the [tax] refund check is designated as a constructive trustee for the benefit of the other party to the extent of one-half of the total amount of the refund." [Comm. Ex. No. 3-B.3.] The Committee characterizes this language as creating an ordinary trustee-beneficiary relationship, citing case law generally holding that a trustee owes a fiduciary duty to the trust beneficiaries. A constructive trust, however, is unlike other trusts. "Under Texas law, a constructive trust is not actually a trust, but rather an equitable remedy imposed by law to prevent unjust enrichment resulting from an unconscionable act. . . . The two circumstances that generally justify the imposition of a constructive trust are actual fraud and the *breach of a confidential or fiduciary relationship*." *Haber Oil Co. v. Swinehart* (*In re Haber Oil Co.*), 12 F.3d 426, 436 (5th Cir. 1994) (emphasis added) (citations omitted). The breach of a pre-existing fiduciary relationship gives rise to a constructive trust; whereas, in a traditional trust, the pre-existing trust gives rise to the existence of a fiduciary duty. Thus, the Court concludes that the language in the Divorce Decree designating the Debtor as a constructive trustee is insufficient to establish a fiduciary relationship.

However, in the instant case, Texas law imposes a fiduciary relationship notwithstanding any language in the Divorce Decree. In a divorce, the court may award one spouse title to future property that will come into the sole possession of the other spouse. The Texas Family Code further provides, "The subsequent actual receipt by the non-owning party of property awarded to the owner in a decree of divorce or annulment creates *a fiduciary obligation* in favor of the owner and imposes a constructive trust on the property for the benefit of the owner." TEX. FAM. CODE ANN. § 9.011(b) (Vernon 2006) (emphasis added). "[This section][44] specifically provides that subsequent, later

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proceeding." (citation omitted)). Therefore, after their divorce on May 13, 2005, the Debtor did not owe a fiduciary duty to Evelyn Presto.

[44] Prior to renumbering in 1997, Tex. Fam. Code § 9.011 appeared at Tex. Fam. Code § 3.75.

receipt by a party of property that has been awarded to the rightful owner creates a fiduciary obligation in favor of the owner." *Jeffcoat v. Jeffcoat*, 886 S.W.2d 567, 570 (Tex. App.—Beaumont 1994, no writ); *see also Echols v. Echols*, 900 S.W.2d 160, 162 (Tex. App.—Beaumont 1995, writ denied). The Court sees no reason that the statute would not apply in this situation. The tax refund was future property that the parties divided in the Divorce Decree and, therefore, the statute applies.

Since half of any potential tax refund was awarded to Evelyn Presto, the Court finds that Tex. Fam. Code § 9.011(b) created both a fiduciary obligation *and* a constructive trust between the Debtor and Evelyn Presto upon the Debtor's receipt of the tax refund proceeds on October 25, 2005. Therefore, the Committee has met its burden of showing the existence of a fiduciary relationship.

3. The Debtor committed fraud, deceit, or manipulation while acting a fiduciary capacity.

Second, the Committee must show that the Debtor committed either fraud, deceit, or manipulation while acting in this fiduciary capacity. These three terms have distinct meanings in the context of securities law, but those definitions do not apply here because there is no allegation of a connection to the purchase or sale of any security.[45] Instead, the Court defines each of the three terms in § 522(q)(1)(B)(ii) as they are used to modify the phrase "fiduciary capacity" independent of their securities law meaning.[46]

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[45] For example, the term manipulation has a longstanding definition in the context of § 10(b) of the Securities and Exchange Act of 1934. The Supreme Court has described manipulation as "virtually a term of art when used in connection with securities markets" and listed examples "such as wash sales, matched orders, or rigged prices, that are intended to mislead investors by artificially affecting market activity." *Sante Fe Indus., Inc. v. Green*, 430 U.S. 462, 476 (1977) (quoting *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199 (1976)). In the case at bar, the term manipulation is not being used in connection with securities and it would be impossible to adopt this market-based definition in the broader context of all fiduciary duties.

[46] If the Court instead faced a § 522(q) objection based on a securities transaction, it would apply the definitions developed by the Supreme Court for dealing with § 10(b) violations.

a. Fraud and deceit in a fiduciary capacity

Fraud requires proof of six elements: (1) a material representation, (2) that was false, (3) that the speaker knew was false or was made recklessly without knowledge of its truth or falsity, (4) with the intent to have the other party rely, (5) actual reliance by the other party, and (6) damages. *T.O. Stanley Boot Co. v. Bank of El Paso*, 847 S.W.2d 218, 222 (Tex. 1992) (citing *Stone v. Lawyers Title Ins. Co.*, 554 S.W.2d 183, 185 (Tex. 1977)); *see also Southwestern Packing Co. v. Cincinnati Butchers' Supply Co.*, 139 F.2d 201, 203 (5th Cir. 1943). Fraud and deceit are essentially synonymous. *See* RESTATEMENT (SECOND) OF TORTS § 525 (deceit and fraudulent misrepresentation listed as the same cause of action); *Meyers v. Moody*, 693 F.2d 1196, 1214 (5th Cir. 1982) (the elements of common law fraud or deceit are identical under Texas law); *see also Southwestern Packing Co., Inc. v. Cincinnati Butchers' Supply Co.*, 139 F.2d 201, 203 (5th Cir. 1943). Thus, despite § 522(q)(1)(B)(ii) listing fraud and deceit separately, the Court interprets both words to require proof of the same elements. Additionally, the fraudulent actions must have occurred while the Debtor owed a fiduciary duty to Evelyn Presto. As stated above, the Debtor's fiduciary duty only arose upon his actual receipt of the tax refund proceeds. Thus, while the Court believes that the Debtor's two acts of forgery—on the tax return and the refund check—were deplorable and patently fraudulent, the applicable time frame for this analysis is after the Debtor cashed the refund check on October 25, 2005.

This is a case of intentional concealment where there was a duty to disclose. *Chiarella v. U.S.*, 445 U.S. 222, 230 (1980). The Divorce Decree required that the Debtor cooperate in the execution of any refund check and that the Debtor remit to Evelyn Presto one-half of any refund amount within five days of its receipt. [Comm. Ex. 3-B.3.]

The Debtor's argument is that he lacked fraudulent intent because he immediately wrote and mailed a check to Evelyn Presto for her half of the tax refund and, through no fault of his own, the check was "lost in the mail." The Court was immediately skeptical of such a trite defense, and the Debtor presented no persuasive evidence to overcome the Court's initial skepticism. For the reasons stated below, the Court finds that the Debtor either (a) never wrote a check, or (b) wrote the check but later decided not to mail it. Under either circumstance, the Debtor's concealment of the existence of the tax refund satisfies the first five elements of fraud and deceit.

The monthly statement of the Debtor's Wells Fargo account shows check number 2099 as never having been cashed. The Debtor claims that check number 2099 is the check he wrote and mailed to Evelyn Presto. Merely showing that check number 2099 was not presented for payment does not support a finding that he actually wrote and mailed a check to Evelyn Presto.

The Debtor testified that he wrote four checks for the benefit of Evelyn Presto within several days of each other in late October 2005. Check number 2093, dated October 25, 2005, was written to Evelyn Presto in the amount of $30,000.00 as part of the property settlement in the Divorce Decree. This check was cashed on October 31, 2005. The Debtor wrote two $600.00 checks (numbers 2097 and 2098) to a state agency for disbursement to Evelyn Presto as child support. Both checks were dated October 28, 2005 and cashed on November 1, 2005. The Debtor testified that check number 2099 was written within a few days after checks 2097 and 2098. The earliest that the Debtor could have written check 2099 was October 31, 2005.[47] Check number 2100 is dated

[47] The Court takes judicial notice of the fact that October 29, 2005 was a Saturday. The Debtor emphatically and repeatedly testified that he wrote and mailed all four of these checks from his place of work. Although it is conceivable that the Debtor was at work on that Saturday, it is more likely that the earliest date that check number 2099 could have been written was October 31, 2005, the next Monday.

November 10, 2005. Thus, if check number 2099 was actually written to Evelyn Presto, it would have been written between October 31 and November 9, 2005.

The daily balance of the Wells Fargo account during this time period was as follows:

Date	Balance
10/31	$11,494.95
11/01	$9,365.09
11/02	$8,890.79
11/03	$5,608.22
11/04	$5,550.74
11/07	$5,467.66
11/08	$5,044.09
11/09	$4,880.09

At the end of November 2005, the balance was $3,063.06, and at the end of December 2005 it was $3,865.11. Thus, during the nine day period when check number 2099 could have been written, and the several months that followed, the account never had sufficient funds to clear a check for $12,284.00 (i.e., the amount due to Evelyn Presto as a result of the tax refund). This fact also contradicts the Debtor's testimony that he was unaware that the $12,284.00 had not been withdrawn from his Wells Fargo account because of "sloppy" bookkeeping and the stress of the avoidance action litigation. If this account regularly had a substantial balance, it is conceivable that an uncashed check for $12,284.00 could go unnoticed. However, given that the balance in the account was less than the amount of the check, the Debtor's alleged oversight crosses the line into fraud.

The Debtor's testimony implied his awareness of this problem. On direct examination, counsel for the Debtor inquired why the allegedly missing check was not mailed in the same envelope as the other checks that were written to Evelyn Presto at approximately the same time. The Debtor responded, "I had [the tax refund check to Evelyn Presto] sitting in a separate envelope on my desk counter at my former employer and I just . . . *I guess I was maybe worried about the funds*

in there or something . . . I don't know . . . but it didn't get mailed on the same date." (emphasis added). This small slip of the tongue went largely unnoticed at trial, but the Debtor seemed to acknowledge that if he had written and mailed a check to Evelyn Presto for her half of the tax refund, the check would have been denied for insufficient funds. The Debtor also testified that he distinctly remembered writing these four checks because he "was not happy that [he] was writing checks for that amount of money to [his] ex-wife." The Court is left with only two possible conclusions: either the Debtor never wrote a check to Evelyn Presto, or the Debtor did write check number 2099 to Evelyn Presto but decided not to mail it.

Additionally, the Court has a lingering question regarding the Debtor's intent: if the Debtor intended to immediately write a check to Evelyn Presto for her half of the tax refund, why would he forge her name on both the tax return and the refund check? This is just one example of the Debtor's continuing concealment. The Divorce Decree clearly states that the parties must "cooperate" in the execution of any refund check. Without Evelyn Presto's knowledge or consent, the Debtor executed the tax return and the refund check. Under no circumstances would these actions be considered cooperation.

The Debtor's intentional concealment of the tax refund satisfies the first five elements of fraud. The remaining element is damages. Although the Debtor did not specifically address the element of damages, he did argue that he had, post-petition, paid the tax refund debt in full, and therefore did not owe a debt as required by § 522(q). In other words, the Debtor's argument is that Evelyn Presto was not damaged because she received full payment of her half of the tax refund.

The Debtor asserts that "owes," as used in § 522(q)(1)(B), indicates that the debt in question must exist at the time that an objection to exemption is filed. It is undisputed that the Debtor paid Evelyn Presto the complete balance owed from the tax return by a check dated February 10, 2007,

which was deposited by Evelyn Presto on February 20, 2007. The Committee filed the Supplemental Objection, asserting an objection under § 522(q) for the first time, on February 16, 2007. Thus, the Debtor asserts that his payment of the debt to Evelyn Presto prior to the Committee filing the Supplemental Objection precludes the application of § 522(q) because he did not owe any debt related to the tax return on the date that the Committee first objected under § 522(q).

Section 522(q) has both a deterrent and punitive effect. The statute sends a message to debtors who have violated securities law or other fiduciary duties, or caused serious physical injury to another: not only will such debts not be discharged in bankruptcy, but homesteads may be in jeopardy due to the actions giving rise to these debts. Under the Debtor's interpretation, a debtor can conceal such debts by not scheduling or otherwise disclosing them and, after such debts are uncovered, avoid the impact of § 522(q) by simply paying off that debt.[48] The Debtor's reading of § 522(q) would eviscerate the effect of the statute. The Court finds that the better policy is to not allow post-petition payment of a debt described in § 522(q)(1)(B) to terminate a debtor's liability under the statute. In sum, the Court interprets "owes," as it is used in § 522(q)(1)(B), to mean that the debt was owed on the date of the petition without regard to any payments on the debt that were made post-petition.

The Court's reading is consistent with the Fifth Circuit's rule that "the right to exemptions is determined by facts as they existed on the date of the original bankruptcy petition." *Lowe v. Sandoval* (*In re Sandoval*), 103 F.3d 20, 23 (5th Cir. 1997) (citations omitted); *see also Zibman*, 268 at 302. The effect of § 522(q) is to limit a debtor's homestead exemption. If the right to an exemption is determined on the petition date, then whether a debt is owed for purposes of § 522(q)

[48] In the case at bar, the Debtor did not schedule this debt. The Debtor testified that the first time he realized this debt was still owed to Evelyn Presto was when he was preparing documents in response to the Committee's discovery request; in other words, after litigation had begun.

should be viewed on that same date. The Debtor does not dispute that he owed a debt to Evelyn Presto on the petition date, and therefore it is appropriate for the Court to apply § 522(q) to his claimed homestead exemption.

The same analysis applies to the issue of damages, which must be determined on the petition date and not the date that the objection to exemption was filed. The Court finds that the element of damages is present because, on the petition date, the Debtor was still concealing the existence of the tax refund from Evelyn Presto. On the petition date, Evelyn Presto's damages were the full $12,284.00 that she was owed. The fact that the Debtor fully paid this debt post-petition has no bearing on whether damages existed on the petition date. Thus, all the elements of fraud or deceit have been satisfied.

b. Manipulation in a fiduciary capacity

Manipulation is not defined in the Code and the Court is unaware of any state law or federal common law cause of action for manipulation. As discussed above, the securities law definition relates to actions taken with the intent to alter market perceptions and has no application to the fiduciary duty in this case. The Court therefore looks to the common meaning of the word.[49]

The most applicable dictionary definition of manipulation is "to change by artful or unfair means so as to serve one's purpose." MERRIAM-WEBSTER'S COLLEGIATE DICTIONARY 706 (10th Ed. 2001). This definition establishes a much lower standard of proof than common law fraud, and the facts described above under the fraud analysis also satisfy manipulation. Concealing the existence of the tax refund from Evelyn Presto in violation of the terms of the Divorce Decree is serving one's own purpose by "unfair means." The Debtor did not send Evelyn Presto the money

[49] The only definition in Black's Law Dictionary is the securities law usage. BLACK'S LAW DICTIONARY 975 (7th Ed. 1999).

because, as he testified, he was unhappy about giving so much money to his ex-wife, or, as evidenced by his Wells Fargo account statements, he had already spent the funds and could not afford to send her a check for that amount. Both circumstances would serve the Debtor's own purpose. Thus, the Court finds that the Debtor's concealment was manipulation in a fiduciary capacity.

4. The Debtor's Necessity Defense

Section 522(q)(2) provides that:

> Paragraph (1) shall not apply to the extent the amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) is *reasonably necessary* for the support of the debtor and any dependent of the debtor (emphasis added).

The Debtor argued that the Royal Rose Property is "reasonably necessary" for his and his children's support. The Debtor testified that the pool on the Royal Rose Property is a medical necessity due to his severe arthritic condition. Without doing exercises and stretches in his pool and spa, the Debtor contends, his pain is so insufferable that he would not be able to go to work. The Court rejects the Debtor's defense because § 522(q)(2) is not focused on the necessity of the real property itself; rather, the test under § 522(q) is whether the *equity* in the homestead is reasonably necessary for the support of the Debtor or his children. Earlier, the Court discussed the meaning of "amount of an interest" as used in § 522(p) and held that the phrase "amount of" preceding the word "interest" meant that the interest must be quantified by a monetary figure, i.e. equity in the homestead. Thus, when the statute states that "Paragraph (1) shall not apply to the extent the amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) is reasonably necessary for the support of the debtor," the Court must determine if the equity in the homestead is necessary for the Debtor's support.

The Court draws its analysis of the § 522(q)(2) exception from cases interpreting the phrase "reasonably necessary for the support of the debtor" in §§ 522(d)(10) and (11). "Determination of the quantum that is needed for support is entrusted to the sound discretion of the bankruptcy court." *Carmichael v. Osherow* (*In re Carmichael*), 100 F.3d 375, 380 (5th Cir. 1996). "The 'reasonably necessary' standard requires that the Court take into account other income and exempt property of the debtor, present and anticipated, and that the appropriate amount to be satisfied for the debtor ought to be sufficient to sustain basic needs, not related to his former status in society or the lifestyle to which he is accustomed, but taking into account the special needs of the debtor." *In re Grant*, 40 B.R. 612, 613-14 (Bankr. N.D. Tex. 1984) (citing *In re Taff*, 10 B.R. 101, 107 (Bankr. D. Conn. 1981)); *see also In re Goff*, 706 F.2d 574, 580 n. 15 (5th Cir. 1983) (reversed on other grounds) (citing *In re Kochell*, 26 B.R. 86 (Bankr. W.D. Wisc. 1982)) (listing age, health, future earnings capacity, and necessary expenditures as factors for the court to consider).

The Court finds that the Debtor's equity in the Royal Rose Property is not reasonably necessary for his and his children's support. The Debtor is currently employed by Bear Energy, a subsidiary of Bear Stearns Companies Inc. He makes an annual salary of $175,000.00 and, pursuant to the terms of his employment agreement, is guaranteed a bonus of $100,000.00 after his first year of employment. In addition to the generous base salary, the Debtor has the ability to earn more bonuses in the future. The Debtor seems to be stubbornly holding on to his previous lifestyle in the heady days of pre-bankruptcy Enron.[50] Is it *reasonably* necessary for the Debtor, whose children

[50] For example, the Debtor testified that he purchased five televisions for the Royal Rose Property sometime during the three months preceding the petition date—a time when the Debtor was in contemplation of bankruptcy and negotiating to settle the Committee's $2 million judgment. Counsel for the Committee asked the Debtor why, as a single person, he needed so many televisions. The Debtor responded that his home had that many rooms that needed televisions—media room, family room, game room, master bedroom and guest room. This is just one of many examples presented at trial of the Debtor's cavalier spending in the months preceding his Chapter 7 petition.

only stay with him during the summer, to live in a two-story 3400 square foot house in a gated community with a country club? Surely not. Such a lifestyle for a single man far exceeds his "basic needs." Even assuming that the Debtor was truthfully testifying about his medical need for a pool, § 522(q)(2) would not protect the Royal Rose Property.[51] The only question this condition would raise is whether the Debtor has sufficient income and other assets to afford *any* house, not this specific house, that can provide a pool. In Houston, Texas in the year 2007, there are ample living options that include a pool for far less than $521,800.00. Thus, in light of the Debtor's substantial income and future earning capacity, the Court finds that the equity in the Royal Rose Property is not reasonably necessary for the support of the Debtor and his children.

In conclusion, the Court finds that the Royal Rose Property is not protected by § 522(q)(2). Therefore, § 522(q)(1)(B)(ii) applies to limit the amount of interest the Debtor may exempt in his homestead.

5. Calculation of the Non-Exempt Portion of the Royal Rose Property under § 522(q)

Unlike §§ 522(o) and (p), each of which requires the current market value to calculate the exempt amount, § 522(q) does not require the precise current market value of the Royal Rose

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[51] There are two reasons to doubt the veracity of the Debtor's testimony about the severity of his condition. First, no expert testimony was adduced regarding this condition. *See Foster v. Johnson*, 293 F. 3d 766, 773 (5th Cir. 2002). Second, an email from the Debtor to his homeowners' association, introduced into evidence by the Debtor for other purposes, casts serious doubt on the severity of his ailment. This email, sent just two days before the closing on the Royal Rose Property, was a request by the Debtor to expedite the approval process for the construction of the pool at the Royal Rose Property. The Debtor did not mention his medical condition in this email. He did not explain to the association that he would be disabled with pain if he could not use this pool or that his request for expedited consideration was made because of a medical necessity. Instead, the email focuses solely on the Debtor's desire to complete the pool early for the sake of his children. He wrote, "I want my children to be happy with their situation and be excited about having a slide, hot tub, nice pool, etc. to use in their backyard for as much of the summer as possible. *If I didn't have my beautiful young children to please, I would not be asking for accelerated approval*, but please understand (like all good Daddy's [sic]), I want to put a big smile on my children all summer." (emphasis added). If the Debtor's medical condition is really as painful as he testified, and if he really needed the pool to alleviate this pain, then it strains credulity that he would not mention his condition to the association in order to expedite the approval process.

Property to calculate the exempt amount. The Court's finding that the Debtor owes a debt arising from the conduct described in § 522(q)(1)(B) means that the Court does not need to calculate the non-exempt value of the homestead; the Debtor retains a monetary exemption in the amount of $125,000.00 and any amount exceeding $125,000.00 is property of the estate. Accordingly, the Court sustains the Committee's Objection to the extent that any value in the Royal Rose Property exceeds $125,000.00.[52]

VII. Conclusion

The Court sustains the Committee's Objections to the Debtor's homestead exemption under § 522(o) in the amount of $28,200.00; under § 522(p) in the amount of $105,000.00; and under § 522(q) to the extent that the value of the Royal Rose Property exceeds $125,000.00. The Court considered, but rejected, combining the Committee's objection under § 522(o) with its objections under § 522(q)—i.e., reducing the Debtor's homestead exemption to $125,000.00 under §§ 522(q) and then deducting the $28,200.00 for which the Debtor is liable under § 522(o).[53] Combining the Committee's objections in this way would undermine Congress' intent to allow a minimum homestead exemption under §§ 522(p) and (q) of $125,000.00.[54] Instead, the Court sustains the Committee's Objection under § 522(q), which renders the property non-exempt but allows the Debtor to retain a $125,000.00 interest. Alternatively, if the Court's interpretation of § 522(q) is

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[52] The Debtor scheduled the Royal Rose Property as having a value of $550,000.00 and testified that it had a value of $521,800.00. Whatever the actual current market value of the Royal Rose Property is, it exceeds $125,000.00.

[53] Whereas §§ 522(p) and (q) allow the Debtor to retain an exemption in the first $125,000.00 of equity in his homestead under any circumstances, Section 522(o) allows an absolute reduction to the homestead exemption and does not reference any base amount that the Debtor may exempt.

[54] However, if the Debtor was liable under § 522(o) alone for an amount that exceeded the amount sustained under §§ 522(p) or (q), then the Court would instead sustain the objection under § 522(o). This would not be a case of combining multiple objections; rather the objection would be sustained under § 522(o) because it was the largest amount of the objections.

incorrect, the Court sustains the Committee's Objection under § 522(p) in the amount of $105,000.00. Finally, if the Court is also incorrect in its interpretation of § 522(p), then the Court sustains the Committee's Objection under § 522(o) in the amount of $28,200.00.

In *Sissom*, the Court sustained the Trustee's objection under § 522(o) in the amount of $50,000.00. *Sissom*, 366 B.R. at 705. To ensure recovery of these funds, the Court granted the Trustee an equitable lien of $50,000.00 against the debtor's homestead. *Id.* (citing *In re Keck*, 363 B.R. 193 (Bankr. D. Kan. 2007)). In the case at bar, an equitable lien in favor of the Trustee is not necessary because of the differences in language between § 522(o) and § 522(q).

Section 522(o) requires that the value of a debtor's homestead exemption "shall be reduced to the extent such value is attributable" to any nonexempt property fraudulently disposed of within the last ten years. At least in the state of Texas, with its unlimited homestead exemption as to value, if an objection under § 522(o) is sustained, the debtor retains possession of his homestead as exempt property, but will be liable to the estate for any amounts that satisfy the elements of § 522(o). Conversely, § 522(q) states that if a debt is owed due to the actions described in the statute, "a debtor may not exempt any amount of interest . . . which exceeds in the aggregate $125,000." Congress apparently intended that, if an objection is sustained under § 522(q), the claimed homestead is property of the estate, and the debtor's allowed interest in the property is limited to the first $125,000.00. In short, under § 522(o), the Royal Rose Property is the Debtor's exempt property subject to the amount of the lien held by the Trustee; but under § 522(q), the Royal Rose Property is the estate's property subject to the Debtor's interest in the first $125,000.00.[55]

[55] Even if this Court, out of deference to Texas' longstanding tradition of favoring homesteads, wanted to allow the Debtor to keep the Royal Rose Property as his homestead and merely grant the Trustee a lien on this property, the Court could not do so in light of the indefiniteness of the recovery under § 522(q). A lien may only be granted in a specific amount. It is not possible to grant the Trustee a lien under § 522(q) because the recovery for the estate is unknown until the property is actually sold and the first $125,000.00 is paid to the Debtor.

Accordingly, since the Court has found that the Committee has satisfied the elements of an objection under § 522(q), the Royal Rose Property is property of the Debtor's Chapter 7 estate, subject to the Debtor's allowed exemption of $125,000.00. In *Sissom*, the Court granted the Trustee an equitable lien because the debtor retained ownership of his homestead, but was liable to the Trustee, under § 522(o), for $50,000.00. In the case at bar, the Court does not need to grant the Trustee an equitable lien on the Royal Rose Property because the Royal Rose Property is owned by the estate and not the Debtor.

Signed on this 5th day of October, 2007.

Jeff Bohm
U.S. Bankruptcy Judge