“The Law of Reopening: Revisited”

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It seems to happen all the time. A debtor files a Chapter 7 petition and within several months receives her §727 discharge.[2/] Shortly thereafter, the bankruptcy clerk’s office closes the case pursuant to §350(a) and Federal Rule of Bankruptcy Procedure 5009 (Fed. R. Bankr. P.).

Within months, the debtor is contacted by a long forgotten landlord, credit card issuer, or relative whose debt was not listed on the schedule of creditors and who is now demanding payment of it. The nervous debtor contacts her bankruptcy counsel and explains that her failure to list the debt was a mistake, the result of forgetfulness or inadvertence. The harried attorney says “No problem,” and directs his paralegal to draft a motion to reopen this closed no-asset consumer bankruptcy case. The attorney plans to follow this by filing a motion to amend Schedule F, to add the name of the omitted unsecured creditor and the amount of that debt.[3/] The clerk’s office processes the pleadings, and in due course the bankruptcy court enters an order granting the requested relief.

Sound all too familiar? Probably, but is the time and effort taken to reopen a closed no-asset consumer Chapter 7 case and to discharge an omitted creditor necessary to provide a debtor with the full benefit of her discharge and a fresh start? Perhaps, but as the Court of Appeals for the Sixth Circuit has observed, among bankruptcy and appellate courts widespread confusion still exists concerning unscheduled Chapter 7 debts in no-asset cases and the efficacy of reopening such bankruptcy cases to include them. *In re Madaj*, 149 F.3d 467, 468 (6th Cir. 1998).[4/] This confusion is caused by decisions that erroneously hold that, once a case is closed, the debtor must reopen her case in order to discharge a prepetition debt by amending her schedules to list an omitted

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[1/]All views expressed in this article are those of the author and do not necessarily represent the views of the U.S. Trustee Program or the U.S. Department of Justice. The author is grateful to Denis W. Thomas, Ph.D. for his suggestions, comments, and editorial assistance on this article.

[2/]11 U.S.C. § 727; all section citations are to the Bankruptcy Reform Act of 1978, as amended, codified at 11 U.S.C. § 101 et. seq.(“Bankruptcy Code” or “Code”).

[3/]Official Form F--Creditors Holding Unsecured Nonpriority Claims.

[4/]See generally Michael P. Saber, Section 350(b): The Law of Reopening, 5 Bankr. Dev. J. 63 (1987) (collecting cases).

creditor.

A Chapter 7 bankruptcy case can be reopened after discharge and case closure under certain circumstances. Bankruptcy Code Section 350(b) authorizes the bankruptcy court to reopen a case for various reasons including to "administer assets, to accord relief to the debtor, or for other cause." Fed. R. Bankr. P. 5010 states: "A case *may* be reopened on motion of the debtor or other party in interest pursuant to §350(b) of the Code." (emphasis added). See *In re Chalasani*, 92 F.3d 1300, 1308 (2d Cir. 1996). *Accord In re Thompson*, 16 F.3d 576, 581–82 (4th Cir.), *cert. denied*, 512 U.S. 1221, 114 S. Ct. 2709, 129 L. Ed. 2d 836 (1994); *In re Rosinski*, 759 F.2d 539 (6th Cir. 1985); *In re Mattera*, 203 B.R. 565, 568 (Bankr. D.N.J. 1997); *In re Bianucci*, 4 F.3d 526, 528 (7th Cir. 1993); *In re Shondel*, 950 F.2d 1301, 1304 (7th Cir. 1991) (discussion of "other cause" sufficient to justify reopening Chapter 7 case).

Ultimately, however, the decision to reopen is within the discretion of the court, and merely granting a motion to reopen does not afford substantive relief but simply provides the opportunity to request further relief. *Chalasani*, 92 F.3d at 1307–08. *Accord In re Leach*, 194 B.R. 812 (E.D. Mich. 1996); *In re Germaine*, 152 B.R. 619 (B.A.P. 9th Cir. 1993).

In using its discretion to grant such a motion, "the bankruptcy court should exercise its equitable powers with respect to substance and not technical considerations that will prevent substantial justice." *Stark v. St. Mary's Hospital* (*In re Stark)*, 717 F.2d 322, 323 (7th Cir. 1983) (per curiam). *Hawkins v. Landmark Finance Company*, 727 F.2d 324, 326 (4th Cir. 1984) (involved the reopening of a case to permit a lien avoidance proceeding; the determination to reopen a case is left to the sound discretion of the court and depends upon the circumstances of the case).

Bankruptcy Code §727(b) provides that a discharge releases a debtor from personal liability for allowed claims and debts:

> Except as provided in §523 of this title*, a discharge* under subsection (a) of this section *discharges the debtor from all debts that arose before the date of the order for relief under this chapter*, and any liability on a claim that is determined under section 502 of this title as if such claim had arisen before the commencement of the case, whether or not a proof of claim based on any such debt or liability is filed under section 501 of this title, and whether or not a claim based on any such debt or liability is allowed under section 502 of this title (emphasis added).

In addition, §523(a) addresses the nondischargeability of particular debts and provides in part:

> (a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt—
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> (3) neither listed nor scheduled . . . in time to permit—
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> (A) if such debt is not of a kind specified in paragraph (2), (4), or (6), of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time for such timely filing; or
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> (B) if such debt is a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim and timely request for a determination of dischargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such filing and request.

Many bankruptcy courts routinely grant debtors' motions to amend schedules to list previously omitted creditors. See, e.g., *In re Halstead*, 228 B.R. 915, 915–16 (Bankr. S.D. Ind. 1998). The Court of Appeals for the Seventh Circuit has confirmed the expansive rule that a debtor in a no-asset case "may reopen the estate to add an omitted creditor where there is no evidence of fraud or intentional design." *Stark,* 717 F.2d at 324. See, also, *In re Moyette*, 231 B.R. 494 (E.D. N.Y. 1999) (a bankruptcy court abuses its discretion in denying to reopen a case to amend schedules to add a creditor in the absence of fraud, recklessness, or intentional design on the part of the debtor).

One line of appellate-level cases has focused on the concepts of prejudice to creditors and of fraud or intentional design in the §350(b) analysis. *Samuel v. Baitcher (In re Baitcher)*, 781 F.2d 1529 (11th Cir. 1986); *In re Rosinski,* 759 F.2d 539 (6th Cir. 1985) (extremely narrow decision addressing the propriety of reopening the debtor's case, holding that to permit a no-asset debtor to reopen her case in order to amend schedules does not prejudice the omitted creditor and emphasizing the subjective mental state of the debtor in failing to list the debt); *Hawkins*, 727 F.2d at 324; *Stark*, 717 F.2d at 322 (the right of the creditor that is protected by § 523(a)(3) is the right to timely file a proof of claim). *Accord Judd v. Wolfe,* 78 F.3d 110, 114–15 (3rd Cir. 1996); *In re Doherty*, 176 B.R. 483 (Bankr. S.D. Ill. 1994). This established line of cases holds that once a debtor's case is closed, she must have her case reopened in order to discharge the omitted debt. *Madaj*, 149 F.3d

at 468. After the case is reopened, the debtor amends her Schedule F pursuant to Fed. R. Bankr. P. 1009(a), and the now-scheduled debt is subject to the §727 discharge.[5/]

However, this practice has been criticized as "pointless" by the Sixth Circuit Court of Appeals, because the omitted debt is already discharged. Reopening the case and scheduling the omitted debt cannot alter that fact. *Madaj*, 149 F.3d at 469. Declaring the law of reopening to be "counter-intuitive," the *Madaj* court carefully examined the interplay between §727, §523(a)(3)(A), (a)(3)(B), and Fed. R. Bankr. P. 2002(e) and framed the judicial question (and its answer) by asking:

> [W]hen an otherwise dischargeable debt is omitted from the schedule in a Chapter 7 no-asset case and the debtor receives a discharge, what is the effect of reopening the case to permit the debtor to schedule the omitted debt?
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> The answer is "there is no effect." The reason that the reopening has no effect is clear. A debtor cannot change the nature of the debt by failing to list it in his petition and schedules. Section 523(a)(3)(A) excepts from discharge only those debts as to which a timely proof of claim cannot be filed because the debts were not listed *and* the creditor had neither notice nor actual knowledge of the bankruptcy in time to file a timely proof of claim. In a no-asset Chapter 7 case,

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[5/]Prior to adoption of the Bankruptcy Code, statutory and case law provided for the per se nondischargeability of any unscheduled claim, the holder of which had no knowledge of the bankruptcy case:

> A discharge in bankruptcy shall release a bankrupt from all of his provable debts, whether allowable in full or in part, except such as . . . have not been duly scheduled in time for proof and allowance, with the name of the creditor, if known to the bankruptcy unless such creditor had notice or a actual knowledge of the proceeding in bankruptcy.

Section 17a(3), Bankruptcy Act, codified at 11 U.S.C. §350(a)(3) (repealed by the Bankruptcy Reform Act of 1978), (as quoted in *In re Adams,* 734 F.2d 1094, 1098 (5th Cir. 1984)); *see, also, Birkett v. Columbia Bank*, 195 U.S. 345, 25 S.Ct. 38, 49 L.Ed. 231 (1904).

> there is no date by which a proof of claim must be filed in order to be "timely." Whenever the creditor receives notice or acquires actual knowledge of the bankruptcy, he may file a proof of claim, that claim will be timely, and the fact that the debts were not listed becomes irrelevant. Section 523(a)(3)(A) simply provides no basis for excepting an unlisted debt from discharge if the creditor has actual knowledge such that he can file a proof of claim. And once the §727 order of discharge is entered, all of the debtor's prepetition debts are either discharged or they are not discharged; nothing the debtor does after the entry of the order of discharge can change the character of those debts. *Madaj*, 149 F.3d at 472.

In other words, reopening a closed no-asset case to add a creditor has no effect on whether the omitted debt is discharged. *See Beezley v. California Land Title Co. (In re Beezley)*, 994 F.2d 1433, 1434 (9th Cir. 1993) (per curiam); *American Standard Ins. Co. v. Bakehorn*, 147 B.R. 480, 483–84 (N.D. Ind. 1992).

In general, the debtor's only articulated reason for seeking to reopen the case is to add inadvertently omitted creditors, and she often files the motion to reopen "in the mistaken belief that adding the creditor to the schedules is necessary for the debt to be discharged." Lawrence P. King, 3 *Collier on Bankruptcy* ¶350.03[2], at 350–6 (15th ed. rev. 1999); *In re Harmon*, 213 B.R. 805, 807 (Bankr. D.Md. 1997). However, in a no-asset Chapter 7 case, in which creditors will not receive any distribution from the estate, "there would be no purpose served by reopening a case to add an omitted creditor to the bankrupt's schedules." *Judd,* 78 F.3d at 115. Indeed, reopening under these circumstances "is for all practical purposes a useless gesture." *Madaj*, 149 F.3d at 468 (*quoting in re Hunter,* 116 B.R. 3, 5 (Bankr. D.D.C. 1990)).

The court's analytical approach in *Madaj* differs from the Fifth Circuit Court of Appeals' analysis in *Stone v. Caplan (In re Stone)*, 10 F.3d 285 (5th Cir. 1994). In *Stone*, the husband and wife debtors filed a no-asset Chapter 7 petition after their condominium business venture failed. The debtors neglected to list their condo sellers as creditors, although §521(1) requires debtors to do so. The sellers (creditors) first learned that the Stones had filed for bankruptcy approximately one year after the deadline for filing proofs of claim and after the deadline for filing complaints to determine dischargeability under §523(c). The creditors' sole dischargeability claim was based upon the failure-to-list provision of §523(a)(3)(A). The creditors admitted that the debtors had not engaged in fraud or intentional

design in failing to list the condo debt.

The Stones amended their schedules to include the inadvertently omitted creditors prior to the final discharge of the case, but the bankruptcy court ruled that the debt was nondischargeable under §523(a)(3). On appeal, the district court affirmed. The Stones appealed.

Acknowledging the historical and textual ambiguity of §523(a)(3)(A), the Fifth Circuit turned to the legislative history of the Bankruptcy Reform Act of 1978 for guidance, and concluded "that §523(a)(3) must be construed with an eye toward the equitable principles which underline bankruptcy law." *Stone*, 10 F.3d at 290. *See Robinson v. Mann*, 339 F.2d 547 (5th Cir. 1964). Because the debtor's failure to list the condo sellers as creditors was due solely to mistake or inadvertence and because these creditors were scheduled in time to protect their rights, §523(a)(3)(A) did not apply, and the omitted debt was dischargeable. *Stone*, 10 F.3d at 292.

Most recently in *In re Wells*, 246 B.R. 268 (Bankr. E.D. Ky. 2000), yet another bankruptcy court was confronted with a motion to reopen a Chapter 7 case to add an omitted creditor. Notwithstanding the suggestion that the omission of a $28,000 debt to the mother of the debtor's husband may have been deliberate, the court, citing *Madaj*, held that where there is no claim of nondischargeability pursuant to 11 U.S.C. §523(a)(2), (4) or (6), the discharge entered for the debtors makes it unnecessary to reopen the case and schedule the omitted debt.

Of course, in no-asset cases creditors do not need to file claims, because they will not receive any dividend from the estate. *See* Fed. R. Bankr. P. 2002(e). Consequently, omitted creditors are not prejudiced by being unlisted on Schedule F. *See Judd*, 78 F.3d at 114–15 ("An omitted creditor who would not have received anything even if he had been originally scheduled has not been harmed by omission from the bankrupt's schedules and the lack of notice to file a proof of claim."). Should assets be discovered at a later time, the bankruptcy case then may be reopened. *See Shondel*, 950 F.2d at 1306. At that time all creditors are notified and given a reasonable period in which to file their claims. *See* Fed. R. Bankr. P. 3002(c)(5); *Stark*, 717 F.2d at 324; see, also, Lawrence P. King, *3 Collier on Bankruptcy* ¶350.03[2], at 350–5 to 350–6 (15th ed. rev. 1999).

If a debt falls within a §523 exception, "reopening the case to schedule the debt does not render it dischargeable." *3 Collier on Bankruptcy*, ¶350.03[2] at 350–6. However, if the debt does

not fall within the exception, it "is discharged regardless of whether it ever was scheduled." *Id.; Wells*, 246 B.R. at 271.

Commentators and the courts have suggested various options for parties faced with the question of whether to reopen to list names of and claims for omitted creditors. *See* Lauren A. Helbling and Christopher M. Klein, *The Emerging Harmless Innocent Omission Defense to Nondischargeability under Bankruptcy Code Section 523(a)(3)(A): Making Sense of the Confusion over Reopening of Cases and Amending Schedules to Add Omitted Debts*, 69 Am.Bankr. L.J. 33, 59–63 (Winter, 1995).

In *In re Gardner*, 194 B.R. 576, 579 (Bankr. D.S.C. 1996), the bankruptcy court noted several litigation alternatives for debtors and creditors:

> First, if [the creditor] pursues a lawsuit on the claim, Debtors can assert the bankruptcy discharge as an affirmative defense and the court with jurisdiction over that lawsuit can decide whether the debt falls within any of the exceptions to discharge. Second, under Bankruptcy Rule 4007(b) either Debtors or [the creditor] can move to reopen this case for the purpose of filing a complaint to determine dischargeability. Third, Debtors or [the creditor] can bring an action in this court to enforce the discharge injunction contained in §524(a) against any creditor who is attempting to collect discharged claims. "The virtue of any of these procedures, as opposed to a motion to reopen to amend schedules, is that it will focus on the real dispute (if there is a real dispute) between the parties--the dischargeability of the debt."

See, also, In Matter of James, 184 B.R. 147 (Bankr. N.D. Ala. 1995) (the court listed three ways to litigate dischargeability after a case is closed as opposed to filing a motion to reopen to amend and add creditors).

Several courts have concluded that reopening a Chapter 7 case to add omitted creditors may provide meaningful relief to debtors. In *Judd*, the debtor alleged that it was "important for her to have all of her creditors listed so that her schedules accurately reflect the discharge of her debts," and that "as a condition of acquiring new credit, prospective lenders may require that all discharges appear on her schedules." *Judd*, 78 F.3d at 116-17. Acknowledging the possible merit of the debtor's arguments, the Third Circuit remanded the case to the district court for reference to the bankruptcy court and noted that allowing the debtor "to list

all of her discharged creditors is in keeping with the practical considerations pertinent to chapter 7 debtors, and in keeping with the primary purpose of the Bankruptcy Act of affording debtors a fresh start." *Judd*, 78 F.3d at 117. *See, e.g., In re McKinnon*, 165 B.R. 55, 57 (Bankr. D. Maine, 1994) (maintaining the accuracy of a debtor's schedules is sufficient cause to reopen a no-asset case so that debtors can "fulfill more perfectly their obligations under §521(1) and Fed. R. Bankr. P. 1007 to assure the comprehensiveness of the chapter 7 discharge."); *Matter of McDaniel*, 217 B.R. 348, 352 (Bankr. N.D. Ga. 1998) (in general, debtor's desire to amend schedules to include additional creditors, and thus accurately reflect all debts owed, constitutes sufficient cause to reopen); *In re Jones*, 191 B.R. 265, 268 (Bankr. D. Mass. 1996).

Emphasizing the importance of the debtor's right to a fresh start, the U.S. Supreme Court has long observed: "One of the primary purposes of the bankruptcy act is to 'relieve the honest debtor from the weight of oppressive indebtedness and permit him to start fresh free from the obligations and responsibilities consequent upon business misfortunes.' *Williams v. U.S. Fidelity & G. Co.,* 236 U.S. 549, 554–55, 35 S.Ct. 289, 290, 59 L.Ed. 713 (1915). In furtherance of a fresh start, debtors "are entitled to do what they can to ensure a comprehensive discharge, get the case behind them, and get on with their lives." *McKinnon*, 165 B.R. at 58. Some courts have authorized procedural guidelines to facilitate the reopening process for needy debtors.[6/]

[6/]In 2000 the U.S. Bankruptcy Court for the Northern District of Indiana promulgated the following guidelines:

STANDARD GUIDELINES FOR MOTIONS TO REOPEN BANKRUPTCY CASE

11 U.S.C. § 350(b)

"A case may be reopened in the court in which such case was closed to administer assets, to accord relief to the debtor, or for other cause."

A Practical Guide to the United States Bankruptcy Court for the Northern District of Indiana – Financial Matters (II)(B)(p. 12)

1. In General – The decision to reopen a closed bankruptcy case is within the discretion of the Court, meaning that the Court is not required to reopen a case. Our Court, in its discretion, has declined to reopen a few cases that clearly have no attainable assets to be distributed by the closed estate and no purpose to be served by adding a creditor's name to the schedules.

Notwithstanding the right of debtors to a fresh start, however, reopening a closed no-asset consumer case to add omitted creditors is not justified for at least two reasons: 1) amending schedules is "pointless" because the omitted debt is already discharged, and 2) the reopening process creates an unnecessary administrative burden on the courts, clerk's offices, creditors, bankruptcy practitioners and the United States Trustee. *See In re Thibodeau*, 136 B.R. 7, 8 n.2 (Bankr. D. Mass. 1992) (reopening to list an omitted creditor in a no-asset case just to give the debtor peace of mind does not justify the administrative burden that it would impose on the court).

Therefore, in a case where there are no assets to be distributed to creditors, no relief to be accorded to the discharged debtor, and no "other cause" shown for reopening, the courts should adopt the *Madaj* analysis and decline to reopen the debtor's Chapter 7 bankruptcy case to add an omitted creditor because of the plain language of §350(b), §727(b), §523(a) and Fed. R. Bankr. P. 2002(e). Scheduling an omitted creditor in a reopened case is irrelevant to discharging the unlisted debt. Thus, in the typical no-asset consumer case, the debtor must articulate a specific reason qualifying as "other cause" under §350(b) in order to justify reopening and obtain relief.

> However, this Court, [sic] views the third reason for reopening a case – "other cause" – quite broadly. As long as any justification can be given to the Court for the reopening, this Court usually grants the *Motion to Reopen.*
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> 2. Procedure – The reopening of a case is usually initiated by a *Motion* filed by the debtor or other party in interest. In cases under Chapter 7, 12, or 13, a trustee will not be appointed unless the court determines that a trustee is necessary to protect the interests of creditors and the debtor or to insure [sic] efficient administration of the estate.
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> 3. Reopening Fee (Omitted)
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> 4. Archive Retrieval Fee (Omitted)
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> 5. Amendment Fee (Omitted)