

## **An Inherited Problem: Trusts, Estates and Bankruptcy**

By: Michael A. Sabella, Esq.



The last thing that a person wants to think about when he or she is considering filing for bankruptcy protection is the passing of a loved one. However, this is an event that can have a potentially dramatic impact on a bankruptcy case. Typically any assets that a debtor has when he or she files his or her bankruptcy petition become property of the bankruptcy estate. 11 U.S.C. § 541 (2012). These assets can include homes, cars, bank accounts and cash. The common assumption then is that whatever is acquired after the filing date is not part of the estate, and belongs to the debtor. However, this is not always the case. After the filing a debtor may receive an inheritance in the form of either monies or items as directed by the trust or will of a loved one.

Section 541(a)(5) of the Bankruptcy Code provides, in relevant part, that property of the bankruptcy estate includes “[a]ny interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date--(A) by bequest, devise, or inheritance....” 11 U.S.C. § 541(a)(5) (2012).

In other words, if a debtor is either entitled to receive an inheritance before he or she files for bankruptcy, or the debtor is entitled to receive an inheritance within 180 days (generally 6 months) after a filing, then that inheritance is considered part of the debtor's bankruptcy estate. This provision is what is known as an after-acquired property provision of the Bankruptcy Code, and it is designed to expand a debtor's bankruptcy estate even after the filing. As a result, an unexpected inheritance can turn a no-asset bankruptcy case into an asset case.

In the context of a Chapter 7 bankruptcy filing, those funds must be turned over to the Chapter 7 Trustee, who will then use the funds to pay the debtor's creditors. Some debtors may be inclined to remain quiet in such situations in an attempt to avoid disclosing their inheritance. However, any attempt to hide the assets would be in violation of the Bankruptcy Code. This can lead to harmful consequences for the debtor, such as being subjected to costly litigation with the Chapter 7 Trustee to recover such funds, or in the more egregious cases, a denial (or possible revocation) of the debtor's discharge of his or her debts.

While the passing of a loved one can be incredibly difficult to discuss or anticipate, a person considering filing for bankruptcy should be prepared to have a discussion with his or her attorney about whether or not a loved one is ill or elderly. Such a conversation may result in the start of a larger conversation – how to adequately protect assets, specifically those assets designated to a loved one from the bankruptcy process. From that conversation it may become apparent to the debtor that additional structuring may be necessary or that legal tools should be employed to protect family wealth and potential inheritance from the bankruptcy process.

### **About the Author**

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