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Various methods used to conceal assets

By RICHARD P. FINKEL

What happens when debtors fail to disclose assets on their bankruptcy petitions? Creditors are left holding the bag. The bankruptcy system in the United States is designed to provide a fresh start to debtors in financial distress who are unable to meet their financial obligations. Through liquidation or reorganization, creditors may receive a pro-rated share of unencumbered assets of the debtor, but not always.

Federal law requires debtors to make full disclosure of assets and liabilities through the submission of various schedules as part of the bankruptcy petition. Unfortunately, some debtors fail to make full disclosure. 18 USC §152 defines concealment and sets forth penalties, including fines and imprisonment of not more than five years for the criminal concealment of assets.

In *United States v. Wagner*, 382 F.3d 598 (6th Cir. 2004), the court found that concealment means not only secreting, falsifying and mutilating, but also includes preventing discovery, fraudulently transferring or withholding knowledge or information required by law to be made known.

Although there are countless schemes by which debtors attempt to hinder, delay, or defraud their creditors, FBI statistics indicate that more than 70 percent of bankruptcy fraud cases involve concealment of assets. Concealment of assets can take many forms.

Failure to list assets on bankruptcy schedules: Examples of assets not listed might include ownership interest in a non-debtor entity, securities, bank accounts,

precious metals, collectables, real estate and personal injury lawsuits.

Misrepresentation of asset values: Debtors may undervalue assets in an attempt to persuade creditors that particular assets are worthless and should not be liquidated.

Improper transfer of assets: The debtor may transfer assets pre-petition for less than adequate consideration. The transfer may be to a friend, a family member or a straw man with the expectation that the assets will be returned to the debtor after the bankruptcy is over.

Post-petition transfers may be made without court approval and without sufficient consideration. Once again, there may be an agreement to return the property to the debtor at some future date.

In a bizarre 2005 Louisiana case, two women were charged with bankruptcy fraud, including concealment of assets.

The indictment alleges that the two women posed as husband and wife, both on their bankruptcy petition and under oath before a bankruptcy trustee. They are alleged to have concealed more than \$18,000 worth of jewelry and more than \$138,000 that one of the women inherited upon her mother's death shortly before the bankruptcy filing. In addition, one of the women sold her personal residence during the bankruptcy, converted the proceeds into a series of cashier checks and used the checks to acquire real estate. The women face up to 40 years in jail and fines of up to \$2 million.

In a case closer to home, an individual debtor failed to disclose ownership of a condominium in California. While reviewing the debtor's canceled checks, we at BlumShapiro discovered a

check payable to Pacific Bell with a phone number noted on the front of the check. We were suspicious, since the debtor's bankruptcy schedules did not list any property in California. A quick check of a reverse phone directory supplied the address, which allowed us to confirm with the local assessor's office that the debtor owned the property. We later discovered a relative living there rent-free.

In another New England case, a business owner purchased a yacht with company funds, hid the payments through various journal entries in the books and records and failed to disclose the existence of the yacht on the company's bankruptcy schedules. During our review of the company's payroll records, we raised questions about an employee living in Florida. We ultimately determined that this employee was actually the yacht captain and that the yacht was purchased with company funds. In the end, not only was the yacht auctioned for the benefit of the creditors, but the business owner was sued and forced to repay several years of wages paid to the boat's captain.

As the numbers of bankruptcy filings continue to increase, debtors will continue to invent new, creative, sophisticated ways to conceal assets from their creditors. Creditors must be proactive in fighting asset concealment, if they don't want to be left holding the bag.



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