

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MINNESOTA
THIRD DIVISION

In

re: Chapter 7 Case

Conrad Edward Wagner and Mary Ann Wagner,
BKY Case No. 3-92-2419

Debtors.

ORDER

This matter came before the Court on August 12, 1992, on objection by the Chapter 7 trustee to the Debtors' claimed exempt property. Brian F. Leonard, the Chapter 7 trustee, (Trustee) represents the bankruptcy estate. Clyde E. Miller (Miller) represents Conrad Edward Wagner and Mary Ann Wagner (Debtors). The Court, having considered the briefs of the parties, and being fully advised in the matter, now makes this ORDER pursuant to the Federal and Local Rules of Bankruptcy Procedure.

I.

The Debtors claim to have employed attorney Ralph E. Sheffey (Sheffey) in 1989 for the purpose of protecting their homestead and, possibly, filing a Chapter 12 bankruptcy petition on their behalf. The Debtors allege that Farmers Home Administration (FmHA) proposed a settlement between the agency and the Debtors concerning their homestead, but Sheffey failed to communicate such a proposal to them. Even though FmHA has foreclosed the mortgage and the redemption period has expired, the Debtors continue to live on the property. The Debtors allege that due to Sheffey's handling of their case they have lost their rights in their homestead. The Debtors retained Miller to commence a legal malpractice action against Sheffey to recover damages resulting from the loss of their homestead. (FN1)

On April 24, 1992, the Debtors filed a Chapter 7 petition. The Debtors listed their legal malpractice action against Sheffey, in an unlimited and undetermined value, as exempt property under Minn.Stat. Section 510.01 and Section 550.37, subd. 9. The Trustee objects to the exemption on the grounds that Debtors' legal malpractice action claim constitutes neither exempt property pursuant to Minn.Stat. Section 510.01 nor "money arising from any claim on account of the destruction of, or damage to, exempt property" pursuant to Minn.Stat. Section 550.37, subd. 9.

II.

Does the Debtors' legal malpractice claim constitute exempt property under Minn.Stat. Section 510.01 and Section 550.37, subd.

III.

Under 11 U.S.C. Section 522 of the Bankruptcy Code, the debtor has the option of choosing either the exemptions pursuant to Section 522 of the Bankruptcy Code or the State law exemptions. In the instant case, the Debtors have chosen to exempt property from the bankruptcy estate under the Minnesota exemption scheme.

(FN1)This Court has not heard and is not deciding the merits of the Debtors' legal malpractice action.

Since the adoption of the Minnesota Constitution in 1857, the Minnesota legislature has been empowered to determine what property of a debtor is to be exempt from creditors.(FN2) In 1858, the legislature created and has subsequently amended the homestead exemption pursuant to that grant of power. In re Haggerty, 448 N.W.2d 363, 364 (Minn. 1989).(FN3)

When determining compliance with the homestead exemption statute, homestead laws are to be liberally construed in order to "carry out the manifest purpose of the Legislature." Jensen v. Christensen, 11 N.W.2d 798, 799 (Minn. 1943) quoting Tomlinson v. Kandiyohi County Bank, 202 N.W. 494, 495. The Minnesota Supreme Court articulated that manifest purpose as a philanthropic one by stating that:

The humane and enlightened purpose of an exemption is to protect a debtor and his family against absolute want by allowing them out of his property some reasonable means of support and education and the maintenance of the decencies and proprieties of life. The legislative purpose was to adapt

(FN2)Minn. Const. art. 1, 12 provides:

A reasonable amount of property shall be exempt from seizure or sale for the payment of any debt or liability. The amount of such exemption shall be determined by law.

(FN3)Minn. Stat. 510.01 HOMESTEAD DEFINED; EXEMPT; EXCEPTION.

The house owned and occupied by a debtor as the debtor's dwelling place, together with the land upon which it is situated to the amount thereafter limited and defined, shall constitute the homestead of such debtor and the debtor's family, and be exempt from seizure or sale under legal process on account of any debt not lawfully charged thereon in writing, except such as are incurred for work or materials furnished in the construction, repair, or improvement of such homestead, or for services performed by laborers or servants.

different classes of debtors.

In re Haggerty, 448 N.W.2d at 367 quoting Poznanovic v. Maki, 296 N.W. 415, 417 (1941). Even with such a benevolent purpose, the burden remains upon the Debtors to establish compliance with the statute. Jensen, 11 N.W.2d at 799. In this case, the Debtors have failed to show that the exempted legal malpractice action complies with the Minnesota exemption statutes.

The Debtors claim that the relationship between the homestead and the legal malpractice action is analogous to the relationship between the homestead and the proceeds from the sale of the homestead pursuant to Minn. Stat. Section 510.07.(FN4) The Debtors have cited no authority for such a comparison.(FN5) The speculative nature of a recovery from such a legal cause of action does not bear any relation to the contractual rights and obligations arising out of a sale or conveyance of real property.

The Debtors additionally claim the legal malpractice action exempt under Minn. Stat. Section 550.37, subd. 9. The Debtors

(FN4)Minn. Stat. 510.07 SALE OR REMOVAL PERMITTED; NOTICE.

The owner may sell and convey the homestead without subjecting it, or the proceeds of such sale for the period of one year after the sale, to any judgment or debt from which it was exempt in the owner's hands . . .

(FN5)No evidence was offered to show the events surrounding the Debtors' loss of their homestead which would establish a relationship between the homestead and the legal malpractice action. The Debtors only claim that Sheffey represented them in 1989; that they only recently lost their homestead due to foreclosure and expiration of the redemption period; and that the one year procedural window of 510.07 has not expired since the Debtors lost their homestead to FmHA.

argue that the legal malpractice action is entitled to exempt status as "[a]ll money arising from any claim on account of the destruction of, or damage to, exempt property." Minn. Stat. Section 550.37, subd. 9. Little authority defines subdivision 9. However, the authority relating to this subdivision points toward a limited construction.

This section was intended to insulate such things as insurance proceeds from the debtor's loss of exempt property due to fire or

some

other unforeseen event.

In re Chastek, 1988 WL 105804 (Bankr.D.Minn 1988)(Bankruptcy Court denied the debtor's exemption of dairy herd termination payments under Minn. Stat. Section 550.37, subd. 9). See Remington v. Sabin, 157 N.W. 504 (1916) (After property was destroyed by fire, the insurance proceeds were exempt from garnishment). County of Nicollet v. Havron, 357 N.W.2d 134 (Minn.App. 1984) (Insurance proceeds arising from the destruction or loss of the homestead was exempt from a Court imposed lien requiring satisfaction of child support arrearages). Joy v. Cooperative Oil Ass'n, 360 N.W.2d 363 (Minn.App. 1984) (Appellate Court decided issue of homestead status while Trial Court's decision, pursuant to Minn. Stat. Section 550.37, subd. 9, exempting insurance proceeds arising due to destruction of homestead by fire was not appealed).

These cases point to a limited construction of subdivision 9; however, the dicta of the Bankruptcy Court further defines subdivision 9. In footnote 9 of In re Ehrich, the Bankruptcy Court states that

MINN. STAT. Section 550.37 subd. 9 . . . is limited by its terms to the cash proceeds of property and casualty insurance claims, or, perhaps, to proceeds of property damage claims against liable third parties.

In re Ehrich, 110 B.R. 424, 429 (Bankr.D.Minn 1990). Even with this broader construction, the Debtors' legal malpractice action could not be construed as a "property-damage" claim. The alleged destruction of the Debtors' homestead by attorney malpractice is not exempt property under Minn. Stat. Section 550.37, subd. 9.

The Debtors argue that under Minn. Stat. Section 550.37, subd. 15(FN6) their legal malpractice action should also be characterized as a wrongful taking through the alleged attorney malpractice. By its plain language, Minn. Stat. Section 550.37, subd. 16, only exempts claims relating to personal property. The Debtors' homestead, the basis for the legal malpractice action, cannot be said to be personal property and cannot be claimed as exempt under Minn. Stat. Section 550.37, subd. 16.

Even with the judicial mandate to liberally construe such statutes in light of the public policy concerns, this Court cannot agree with the Debtors' interpretation of the Minnesota exemption statute.

NOW, THEREFORE, IT IS ORDERED:

(FN6)Minn. Stat. 550.37, subd. 16 provides:

The claim for damages recoverable by any person by reason of a levy upon or sale under execution of the person's exempt personal property, or by reason of the wrongful taking or detention of such property by any person, and any judgment recovered for such damages.

The objection by the Trustee to the claimed exemption by the Debtors is sustained.

Dated: August 25, 1992.

Dennis D. O'Brien
United States Bankruptcy Judge