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***In Re Reilly, Revamping Taylor in Contravention of the Code***

by  
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## INTRODUCTION

Plagued by an ever growing mountain of debt, an individual may find himself with no other choice than to file a petition with the bankruptcy court. Filing a petition starts the process by which a debtor may receive a discharge from certain debts that arose before the petition was filed, subject to certain exceptions.<sup>1</sup> In order to receive a discharge a debtor must comply with various provisions of the Bankruptcy Code including filing a schedule of assets and liabilities.<sup>2</sup> Some of the assets listed may be exempted and retained by the debtor to help start anew.<sup>3</sup> Others will be sold by the trustee and the proceeds used to pay off creditors.<sup>4</sup> Specific substantive rules govern the process through which assets are either sold or exempted under the Bankruptcy Code.<sup>5</sup> Procedural rules, defined in the Bankruptcy Code and supplemented by the Federal Rules of Bankruptcy Procedure provide additional guidance to debtors and trustees regarding the time frame for claiming and objecting to property claimed as exempt.<sup>6</sup> The Bankruptcy rules are promulgated by the Supreme Court rather than Congress. “Such rules shall not abridge, enlarge, or modify any substantive right.”<sup>7</sup>

Courts have generally looked to the Supreme Court’s decision in *Taylor v. Freeland & Kronz*, to determine whether a debtor may retain assets listed as exempt if the trustee fails to follow these specific procedural rules, which are designed to effectuate efficiency in the bankruptcy process.<sup>8</sup> In *Taylor*, the Court held the trustee’s failure to object within FRBR 4003(b)’s 30-day requirement rendered the property fully exempt even though the debtor had no

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<sup>1</sup> See 11 U.S.C. § 727(b).

<sup>2</sup> See 11 U.S.C. § 521(B)(i).

<sup>3</sup> See discussion *infra* Part I.B.

<sup>4</sup> See discussion *infra* Part I.B.

<sup>5</sup> See discussion *infra* Part I.B.

<sup>6</sup> See discussion *infra* Part I.B.

<sup>7</sup> 28 U.S.C. § 2075.

<sup>8</sup> See generally *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992).

colorable basis for claiming the proceeds of the lawsuit as exempt.<sup>9</sup> In the 18 years since this decision was announced, bankruptcy and appellate courts have differed as to its holding, meaning, context and application.<sup>10</sup> For example, the Eighth Circuit has held that *Taylor* does not apply where the debtor intends to only partially exempt an asset claimed as exempt, but only where the debtor claims the full amount as exempt.<sup>11</sup> In contrast, the Third Circuit has held that *Taylor* requires the trustee to object where a debtor lists an identical entry for the property's value and the amount of the exemption, otherwise the property is fully exempt.<sup>12</sup> The Supreme Court has granted certiorari in *In re Reilly* to clarify ambiguities that have developed in applying *Taylor*.<sup>13</sup> Implementation of the Eighth Circuit's decision in *In re Wick* is consistent with the plain meaning of the exemption provisions, accounts for the specific monetary limitations as well as the standard for valuation of exemptions imposed by Congress and better effectuates the purposes and policies of the Bankruptcy Code

This Comment examines the Bankruptcy Code's exemption statute, Section 522, specifically whether a debtor may exempt property in its entirety merely by indicating that the value of the property is identical to the claimed exemption. Part I of this Comment provides a brief overview of the policies underlying the Bankruptcy Code. This Part also provides an overview of the Bankruptcy Code's exemption statute, its procedure and application. Part II.A analyzes *Taylor v. Freeland & Kronz*, a Supreme Court decision interpreting the exemption provision and FRPB 4003(b). Part II.B discusses the Eighth Circuit's decision in *In re Wick*, which rejects the proposition that one exempts an asset in its entirety by listing both the value of the property and the value of the exemption as unknown. Part II.C discusses the Third Circuit's

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<sup>9</sup> *Id.* at 642-44. See also discussion *infra* Part II.A.

<sup>10</sup> See discussion *infra* Part II.

<sup>11</sup> See *In re Wick*, 276 F.3d 412 (8th Cir. 2002).

<sup>12</sup> See *In re Reilly*, 534 F.3d 173 (3d Cir. 2008).

<sup>13</sup> See *In re Reilly*, 534 F.3d 173 (3d Cir. 2008), *cert. granted*, 77 U.S.L.W. 3267 (U.S. Apr. 27, 2009) (No. 08-538).

decision in *In re Reilly*, which holds that a debtor signals her intention to exempt property “in kind” by listing identical entries for the value of the property and the amount of the claimed exemption. Part III argues that the Supreme Court should resolve the circuit split in accordance with *In re Wick* because this standard is more consistent with the plain language of the Bankruptcy Code, its policies and procedure.

## I. THE BANKRUPTCY CODE: POLICIES AND PROCEDURES

### A. Policy

Article I § 8 grants Congress the power to establish uniform Laws on the subject of Bankruptcies throughout the United States.<sup>14</sup> Bankruptcy laws were believed by the Framers to be incorporated in the Constitution because of problems that varying state laws caused for creditors and interstate commerce.<sup>15</sup> The central focus of this Comment is a Chapter 7 bankruptcy case, which allows a debtor to discharge all of his or her debts that arose before the commencement of the case.<sup>16</sup> In exchange for a general discharge, the debtor is required to turn over all nonexempt property to the trustee for sale and distribution according to a structured priority scheme.<sup>17</sup> The Bankruptcy Code attempts to balance two competing objectives in a Chapter 7 case: fair distribution of the debtor’s assets for the benefit of creditors and to provide debtor’s a “fresh start.”<sup>18</sup> The Code effectuates these policies through its various provisions.

In order to provide debtors a “fresh start” the Bankruptcy Code entitles a debtor to exempt certain property so that it will not be available to his or her creditors.<sup>19</sup> “The purpose of exemptions is to make possible the debtor’s fresh start by allowing him or her to keep those

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<sup>14</sup> U.S. CONST. art. I, § 8, cl. 4.

<sup>15</sup> Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 AM. BANKR. INST. L. LEV. 5, 13 (1995).

<sup>16</sup> See generally 11 U.S.C. § 727.

<sup>17</sup> See 11 U.S.C. §§ 507, 522, 541, 542.

<sup>18</sup>

<sup>19</sup> See generally, 11 U.S.C. § 522(d). See also discussion *infra* Part I.B.

items of property deemed reasonably necessary to daily life. They preserve the debtor’s dignity and give the debtor some basis upon which to build a new life.”<sup>20</sup> The Code balances the need for providing a debtor with a “fresh start” against the equally important principle of equal treatment of creditors. For example, Section 522 places certain monetary amounts on claimed exemptions that a debtor may take.<sup>21</sup> Additionally, to provide equal distribution to creditors, the Bankruptcy Code allows remaining property of the estate to be sold and divided among creditors.<sup>22</sup> Creditors are not necessarily treated “equally” across the board; rather, certain creditors such as secured creditors are given priority treatment over all unsecured creditors as to their secured collateral.<sup>23</sup> As for unsecured creditors, the Code provides a priority scheme that allows specific unsecured creditors, such as domestic support obligations, to be paid in full before general unsecured creditors.<sup>24</sup> As the Supreme Court stated in *Williams v. U.S. Fid. & Guar. Co.*, “[i]t is the purpose of the bankrupt[cy] act to convert the assets of the bankrupt into cash for distribution among creditors, and then to relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon . . . misfortunes. And nothing is better settled than that statutes should be sensibly construed with a view to effectuating the legislative intent.”<sup>25</sup>

## B. Procedure

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<sup>20</sup> 2 Collier on Bankruptcy ¶ 2.05.

<sup>21</sup> See generally, 11 U.S.C. § 522(d)(1).

<sup>22</sup> See generally, 11 U.S.C. § 726.

<sup>23</sup> See 11 U.S.C. § 506(a)(1). If a secured creditor’s claim exceeds the value of the collateral, they are allowed an unsecured claim and gave no priority over other unsecured claims. *Id.* However, if the value of the property exceeds the amount of a secured creditor’s claim, the secured creditor is entitled to interest, reasonable fees, costs, or other charges provided in their security agreement. 11 U.S.C. § 506(a)(2).

<sup>24</sup> See 11 U.S.C. §§ 726(b), 507(a).

<sup>25</sup> See 236 U.S. 549, 555 (1915) (citations omitted).

A debtor commences a case by filing a petition for relief with the bankruptcy court.<sup>26</sup> Once a petition is filed a bankruptcy estate arises by operation of law comprised of “all legal or equitable interests of the debtor in property as of the commencement of the case.”<sup>27</sup> Property of the estate is then subject to sale and distribution for the benefit of creditors.<sup>28</sup> To effectuate the Bankruptcy Code’s policy of a fresh start, the Code provides that debtors may exempt certain property from sale and distribution for the benefit of creditors.<sup>29</sup> Section 522 allows a debtor to choose between the federal exemption statute, Section 522(d), or their states’ exemption statute. Additionally, Section 522(b)(2) allows a state to “opt out” of the federal exemption provisions by statute.<sup>30</sup> A majority of states have chosen to “opt out” of the federal exemption scheme, thereby denying their citizens the right to elect the federal exemptions.<sup>31</sup> In fact, many states exemption statutes reduce the amount of applicable exemptions compared to the federal statute.<sup>32</sup> For purposes of this Comment, references will be made to the federal exemption statute.

The federal exemption statute lists classes of property that a debtor may exempt. For example, the statute allows a debtor to exempt, among other things, real or personal property that the debtor uses as a residence (homestead exemption), an interest in one motor vehicle,

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<sup>26</sup> 11 U.S.C. § 301(a).

<sup>27</sup> 11 U.S.C. § 541(a)(1).

<sup>28</sup> See 11 U.S.C. §§ 363(b)(1), 726(a).

<sup>29</sup> See generally 11 U.S.C. § 522. See also Richard E. Flint, *Bankruptcy Policy: Toward a Moral Justification for Financial Rehabilitation of the Consumer Debtor*, 48 WASH. & LEE L. REV. 515, 543 (1991) (“Under principles of distributive justice, each individual in our society is entitled to a level of human dignity. In order to achieve that dignity the individual must be provided with a minimum level of subsistence and the opportunity to provide himself and his family without the burden of overwhelming debt.”)

<sup>30</sup> See 11 U.S.C. § 522(b)(1). § 522 provides that a state may “opt-out” of the federal exemption statute by specifically enacting a statute that does not authorize debtors domiciled in the state to use the federal exemptions. § 522(b)(2).

<sup>31</sup> See 4 Collier on Bankruptcy ¶ 522.05. The following states have elected under 11 U.S.C. § 522(b)(2) “opt out” of the federal exemption scheme: Alabama, Arizona, California, Colorado, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Louisiana, Maine, Maryland, Mississippi, Missouri, Montana, Nebraska, Nevada, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, South Carolina, South Dakota, Tennessee, Utah, Virginia, West Virginia and Wyoming. *Id.* at note 5.

<sup>32</sup> *Id.* But cf. *infra* note 34.

household goods, jewelry, tools of the trade, health aids and life insurance policies.<sup>33</sup> On its face the exemption statute seems quite generous, but for certain types of exempt property a maximum amount is stated capping the allowable exemption.<sup>34</sup> For instance, a debtor's homestead exemption is limited to \$20,200 in value and her interest in a motor vehicle may not exceed \$3,225.<sup>35</sup> Subject to limited exceptions, property exempted under Section 522 is not liable during or after the case for any debt that arose before the commencement of the case.<sup>36</sup>

In order to claim an applicable exemption a debtor must file a list of property claiming to be exempt.<sup>37</sup> Federal Rule of Bankruptcy Procedure 1007 directs the debtor to file a schedule of assets on Official Form 6C, titled "Schedule C – Property Claimed as Exempt" (hereinafter "Schedule C").<sup>38</sup> Schedule C requires the debtor to describe the property, specify the law providing each exemption, state the value of the claimed exemption and the current value of the property without deducting the exemption.<sup>39</sup> Because exemption provisions are often limited according to the nature of the property (or its value) the information provided by Schedule C is essential to evaluate the propriety of the claimed exemption.<sup>40</sup> Section 522 provides that unless a

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<sup>33</sup> See generally 11 U.S.C. § 522(d).

<sup>34</sup> See *id.* § 522(d). If a married couple is filing jointly, § 522(m) permits them to double their allowable exemptions.

<sup>35</sup> *Id.* § 522(d)(1)-(2). In some regards, it may prove advantageous to choose a state's exemption statute over the federal exemptions. For example, § 522(d)(1) limits the homestead exemption to \$20,200, while Texas allows a homestead, consisting of not more than 10 acres of land, to be exempted in full. See TEX. PROP. CODE ANN. § 41.001 (Vernon 2005). To combat potential problems associated with conversion of non-exempt assets into exempt assets, particularly with regard to unlimited homestead exemptions, Congress enacted § 522(o) (reducing the value of an interest in real property "to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10-year period ending on the date of the filing of the petition with the intent to hinder, delay, or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the debtor had held the property so disposed of,") and § 522(p) (limiting the debtor's interest in homestead to \$136,875 if the debtor acquired the homestead within 1,215 days of the date of filing the petition).

<sup>36</sup> See 11 U.S.C. § 522(c).

<sup>37</sup> 11 U.S.C. § 522(l).

<sup>38</sup> See generally FED. R. BANKR. P. 1007. In a voluntary case, Schedule C must be filed with the petition or within 14 days thereafter. In an involuntary case Schedule C is required to be filed by the debtor within 14 days of the entry of the order for relief. *Id.*

<sup>39</sup> See Official Form 6C.

<sup>40</sup> See 5 Collier on Bankruptcy ¶ 522.05.



party in interest objects, the property claimed as exempt on the list is exempt.<sup>41</sup> Bankruptcy Rule 4003(b) provides that a “party in interest may file an objection to the list of property claimed as exempt within 30-days after the meeting of creditors held under § 341(a) is concluded or within 30-days after any amendment to the list or supplemental schedules is filed, whichever is later.”<sup>42</sup> If the debtor has fraudulently asserted an exemption, the rule allows the trustee to file an objection at any time prior to one year after the closing of the case.<sup>43</sup> As discussed *infra* Part II, the bankruptcy courts have divided about the proper interpretation of Section 522 and the FRBP 4003.

## II. *TAYLOR V. FREELAND & KRONZ* AND ITS PROGENY

In order to more fully understand the circuit split discussed *infra*, an examination of the Supreme Court’s jurisprudence on the interplay between Section 522 and FRBP 4003 is necessary. In *Taylor*, the Supreme Court granted certiorari to decide whether a trustee may contest the validity of an exemption after the 30-day period provided by FRBP 4003, even if the debtor has no colorable basis for claiming the exemption.<sup>44</sup> Under a plain meaning approach the Court held that a trustee may not contest the validity of the exemption after the 30-day period.<sup>45</sup> Slightly modified factual variations have led to different interpretations of this decision among bankruptcy courts.<sup>46</sup>

### A. *Taylor v. Freeland & Kronz*

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<sup>41</sup> 11 U.S.C. § 522(l).

<sup>42</sup> See FED. R. BANKR. P. 4003(b)(1).

<sup>43</sup> See FED. R. BANKR. P. 4003(b)(2). This section was added to the rules in 2008. The Advisory Committee notes that “[e]xtending the deadline for trustees to object to an exemption when the exemption claim has been fraudulently made will permit the court to review and, in proper circumstances, deny improperly claimed exemptions, thereby protecting the legitimate interests of creditors and the bankruptcy estate. See FED. R. BANKR. P. 4003(b)(2) advisory committee’s notes.

<sup>44</sup> *Taylor v. Freeland & Kronz*, 503 U.S. 638 (1992).

<sup>45</sup> *Id.*

<sup>46</sup> See discussion *infra* Parts II.B and C.

In *Taylor*, the debtor, Emily Davis, filed a Chapter 7 bankruptcy petition in October of 1984.<sup>47</sup> At this time the debtor was also engaged in protracted state court litigation with her former employer, Trans World Airlines (TWA), for employment discrimination on the basis of race and sex.<sup>48</sup> On her exemption schedules, Davis listed the expected proceeds from the lawsuit against TWA as exempt, listing its value as “unknown.”<sup>49</sup> The trustee did not object to the claimed exemption.<sup>50</sup> Davis received a discharge on October 16, 1985.<sup>51</sup> Subsequently, TWA settled with Davis on the issue of damages, agreeing to pay her \$110,000.<sup>52</sup> A portion of this payment was made to her attorneys for their fees.<sup>53</sup> After learning of the settlement, the trustee instituted an action against the debtor and her attorneys to turn the money over to the bankruptcy estate; the debtor in turn argued that the money was exempt as she had previously indicated on her schedules.<sup>54</sup>

The bankruptcy court construed the language of § 522(l) as containing an additional requirement that there be a statutory basis for a claimed exemption before the failure of any party in interest to timely object has any legal effect.<sup>55</sup> After ruling that the basis of the suit was in tort, rather than for lost wages, the bankruptcy court held that because there was no statutory basis for

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<sup>47</sup> *Id.* at 640.

<sup>48</sup> *Id.* In 1980, Davis secured a ruling in her favor on the issue of liability from the Pittsburgh Human Relations Commission, a damage award was pending. On appeal to the Court of Common Pleas of Allegheny County, the Commission’s decision was reversed. However, the decision of the Commission was reinstated after a favorable ruling for Davis in the Commonwealth Court of Pennsylvania. After Davis filed her Chapter 7 petition, the Pennsylvania Supreme Court affirmed. *In re Davis*, 105 B.R. 288, 290-91 (Bkrcty. W.D. Pa. (1989).

<sup>49</sup> *See Taylor*, 503 U.S. at 640. At the Section 341 meeting of creditors, Davis’ lawyers informed the trustee that they estimated Davis may win \$90,000 in her lawsuit against TWA. The trustee opined that the proceeds of the lawsuit were property of the estate under Section 541, but doubted that the lawsuit had any value. *Id.* at 640-41.

<sup>50</sup> *Id.*

<sup>51</sup> *In re Davis*, 105 B.R. at 291.

<sup>52</sup> *See Taylor*, 503 U.S. at 641.

<sup>53</sup> *Id.*

<sup>54</sup> *Id.* The trustee brought this proceeding 11 U.S.C. § 549(a), which allows the trustee to avoid a transfer of property of the estate that occurs after the commencement of the case, and 11 U.S.C. § 550(a), which allows recovery by the trustee, after avoidance under § 549, for the benefit of the estate, the property transferred from the initial transferee or any immediate or mediate transferee of such initial transferee. *In re Davis*, 105 B.R. at 292.

<sup>55</sup> *In re Davis*, 105 B.R. at 292.

permitting an exemption for tort recovery, the money was ordered to be returned to the trustee.<sup>56</sup> This decision was affirmed by the district court.<sup>57</sup> On appeal, the Third Circuit reversed holding that “in the absence of an objection filed within thirty days after the section 341(a) creditor’s [*sic*] meeting or the filing of an amendment to the exemption list, property claimed as exempt by the debtor is exempt.”<sup>58</sup> Because no party in interest objected to the claimed exemption, the proceeds of the lawsuit were exempt.<sup>59</sup>

Interpreting section 522(l) and FRBP 4003(b) the Supreme Court ruled even though the debtor had no colorable basis for claiming the proceeds of her lawsuit as exempt, the trustee’s failure to object within the time prescribed by FRBP 4003(b) is determinative, and he may not thereafter challenge the validity of the exemption.<sup>60</sup> The Court’s opinion was a pragmatic one. According to the Court, “[d]eadlines may lead to unwelcome results, but they prompt parties to act and they produce finality.”<sup>61</sup> The Court said that if the trustee is unaware of the potential value of the claimed exemption he could have asked for a hearing on the issue, or asked for an extension of time.<sup>62</sup> The trustee argued that such a rule will create improper incentives and encourage debtors to claim improper exemptions on the chance that a party in interest will fail to

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<sup>56</sup> *Id.* at 294. If the debtor’s lawsuit had been considered one for lost wages, § 522(d)(11) provides that the debtor may exempt her right to receive “a payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor. 11 U.S.C. § 522(d)(11)(E).

<sup>57</sup> *In re Davis* 118 B.R. 272 (WD Pa. 1990).

<sup>58</sup> *Taylor v. Freeland & Kronz*, 938 F.2d 420, 424 (3d Cir. 1991). The Third Circuit surveyed and examined three approaches taken by courts in ruling on the matter. The first, a literal approach that strictly enforces the 30 day requirement; second, a requirement that a claimed exemption must have a statutory basis in order to be exempt if no party in interest objects within the 30 day period (adopted by the bankruptcy court in this matter); and third, a good faith statutory basis standard, which allows a court to uphold the claimed exemption if there is a good faith basis for it (the standard previously adopted by the 6th and 8th Circuits). *Id.* at 423-24 (citations omitted).

<sup>59</sup> *Id.* at 426.

<sup>60</sup> *See Taylor*, 503 U.S. at 642-44.

<sup>61</sup> *Id.* at 644.

<sup>62</sup> *Id.* Rule 4003(b) permits a party in interest to ask the bankruptcy court for an extension of time. *See* FED. R. BANKR. P. 4003(b).

object.<sup>63</sup> However, the Court found that the Bankruptcy Code adequately covered improper conduct. For example, § 727(a)(4)(B) authorizes a denial of discharge if the debtor knowingly and fraudulently presented or used a false claim and 18 U.S.C. § 152, which imposes criminal penalties for fraud in bankruptcy cases.<sup>64</sup>

In the end, the Court's ruling in *Taylor* led to a split among the Circuits and paved the way to allow some unscrupulous conduct and gamesmanship by debtors depending on the jurisdiction in which they reside.

#### B. *In Re Wick*

In *In re Wick*, the debtor filed a Chapter 7 bankruptcy petition in July of 1997.<sup>65</sup> On Schedule C, the debtor described the property as stock options, exempt under the wildcard provision of Section 522(d)(5).<sup>66</sup> The debtor listed the current value of the property as “unknown” and the value of the claimed exemption as “unknown.”<sup>67</sup> At the meeting of creditors, the trustee received copies of the employment agreement that detailed the aforementioned stock options, but did not object at that time.<sup>68</sup> The debtor received a discharge in November of 1997.<sup>69</sup> In October of 1998, the debtor filed suit against her former company requesting a court-ordered buyout of the stock.<sup>70</sup> The state court granted the buyout and valued the options at

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<sup>63</sup> See *Taylor*, 503 U.S. at 644.

<sup>64</sup> *Id.*

<sup>65</sup> See, *In Re Wick*, 276 F.3d 412, 413 (8th Cir. 2002).

<sup>66</sup> *Id.* at 414.

<sup>67</sup> *Id.* The stock options stemmed from the sale of the debtor's company and required her to remain employed by the company for one year. At issue in this case, not pertinent to our discussion, was what portion of the stock options became part of the bankruptcy estate under Section 541(a)(1), which includes in the estate all legal and equitable interest of the debtor in property as of the commencement of the case, and what portion would be assigned to the debtor as earnings from services performed by an individual debtor after the commencement of the case under Section 541(a)(6). The court held that the bankruptcy estate's interest was limited to the pro rata portion of the proceeds, from the liquidation sale of the stock options that are related to the debtor's pre-petition services. The court further determined that one third represented the pro rata portion that the estate was entitled to as pre-petition earnings. *Id.* at 415-17.

<sup>68</sup> *Id.* at 414.

<sup>69</sup> *Id.*

<sup>70</sup> *Id.*

\$97,200.<sup>71</sup> The trustee then petitioned to re-open the debtor’s bankruptcy case, demanding turnover of the \$97,200 less the \$3,925 exemption to which she was entitled.<sup>72</sup>

In a well-reasoned opinion the bankruptcy court held that *Taylor* was not applicable.<sup>73</sup> Because the debtor listed a valid statutory basis for the exemption claimed (unlike the debtor in *Taylor*) she “indicated that she did not intend to claim an exemption any greater than the dollar value allowed by that particular statute [§ 522(d)(5)].”<sup>74</sup> As such, the trustee’s failure to object did not turn the exemption into one for the entire asset rather than the specified dollar limit.<sup>75</sup> The district court reversed finding *Taylor* to be directly applicable.<sup>76</sup> According to the district court, because the trustee made no objection to the exemption claimed within the 30-day time period, the stock options became exempt in full.<sup>77</sup>

Reversing the decision of the district court, the Eighth Circuit rejected the contention that listing the current value of the property as “unknown” is sufficient to make an asset fully exempt.<sup>78</sup> Instead, the court reasoned that it “may signal nothing more than that the asset has not been valued or that the debtor is unsure of how to come up with an accurate market value.”<sup>79</sup> The court went on to explain that “when a specific dollar figure given by statute limited the amount of the exemption, and the trustee did not forsake an interest in the options, either through inadvertence or misjudgment, listing “unknown” does not, by itself, render the options fully

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<sup>71</sup> *Id.*

<sup>72</sup> *See, In re Wick*, 276 F.3d at 414. The \$3,925 amount represents the amount that the debtor had remaining under Section 522(d)(5) that she could have used to exempt “any property” under the wildcard provision “[g]iven the dollar limitations then applicable and the other items claimed as exempt under § 522(d)(5).” *See In re Wick*, 249 B.R. 900, 905 (Bkrcty. D. Minn. 2000). Each dollar amount listed in Section 522 is subject to change every three years to reflect the change in the Consumer Price Index for All Urban Consumers, published by the Department of Labor. 11 U.S.C. § 104.

<sup>73</sup> *See, In re Wick*, 276 F.3d at 418.

<sup>74</sup> *See In re Wick*, 249 B.R. at 913.

<sup>75</sup> *Id.* The bankruptcy court went on to posit that the trustee had no basis for objecting to the claimed exemption because it was valid and within the allowed dollar amount.

<sup>76</sup> *See In re Wick*, 256 B.R. 618, 625 (D. Minn. 2001).

<sup>77</sup> *Id.*

<sup>78</sup> *See In re Wick*, 276 F.3d at 416.

<sup>79</sup> *Id.*

exempt.”<sup>80</sup> The Court reasoned that *Taylor* did not apply because Wick intended to only partially exempt the claimed asset, in contrast to Taylor who, in fact, claimed the full amount as exempt.<sup>81</sup> Consequently, the stock options were partially exempt up to \$3,925 and the resulting proceeds were property of the estate.<sup>82</sup>

### C. *In Re Reilly* and Exemptions “In Kind”

The Third Circuit also had the opportunity to interpret *Taylor* after a trustee failed to object to a claimed exemption within the 30-day period. In *Reilly*, the debtor filed a Chapter 7 bankruptcy petition in April of 2005.<sup>83</sup> The debtor claimed an exemption in certain business equipment used for her catering business.<sup>84</sup> On Schedule C, the debtor indicated the current value of the property as \$10,718.<sup>85</sup> She listed the value of the claimed exemption also as \$10,718, “asserting \$1,850 of it under 11 U.S.C. § 522(d)(6) and \$8,868 under 11 U.S.C. § 522(d)(5).”<sup>86</sup> No objection was made by the trustee or a party in interest within the 30-day time period of Rule 4003(b).<sup>87</sup>

Subsequently, the trustee had the business equipment appraised for \$17,200.<sup>88</sup> On August 10, 2005, the trustee moved to sell the business equipment, subject to the debtor’s partial

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<sup>80</sup> *Id.* See also *In re Cormier*, 382 B.R. 377, 405 (W.D. Mich. 2008) (interpreting *Wick* as standing “for the proposition that when there exists a specific dollar limit in the statute, listing the current market value [in column 4 of Schedule C] does not result in the asset become fully exempt.” *Id.*

<sup>81</sup> See *In re Wick*, 276 F.3d at 417-18.

<sup>82</sup> *Id.* See also note 60, *supra*.

<sup>83</sup> *In re Reilly*, 534 F.3d 173, 174.

<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

<sup>86</sup> *Id.* Section 522(d)(6) allows a debtor to exempt up to \$2,025 in value, in any implements, professional books, or tools, of the trade of the debtor. Section 522(d)(5), commonly known as the “wildcard provision”, allows a debtor to exempt her interest in any property, not to exceed in value \$1,075 plus up to \$10,125 of any unused amount of the exemption under Section 522(d)(1) (the homestead exemption). These figures indicated in this footnote reflect the dollar amounts allowed as of April 2007, not the relevant 2005 figures applicable when this debtor filed. Dollar amounts are adjusted periodically and will change again in March 2010. See 11 U.S.C. § 522(d)(1) note 1.

<sup>87</sup> *In re Reilly*, 534 F.3d at 174.

<sup>88</sup> *Id.*

exemption.<sup>89</sup> The debtor, citing *Taylor*, argued that the business equipment was fully exempt because the trustee failed to object, and thus was not subject to liquidation and distribution. The bankruptcy court agreed with the debtor, and determined that the property was fully exempt.<sup>90</sup> The district court for the middle district of Pennsylvania denied the appeal.<sup>91</sup> The trustee appealed to the Third Circuit.

On appeal, the Third Circuit framed the issue as follows: “whether a Chapter 7 trustee who does not lodge a timely objection to a debtor’s exemption of personal property may nevertheless move to sell the property if he later learns that the property value exceeds the amount of the claimed exemption.”<sup>92</sup> The trustee argued that *Taylor* was not controlling because it did not address whether a debtor’s valuation of property claimed as exempt becomes conclusive in the absence of a timely objection.<sup>93</sup> After recognizing a split of authority, the Third Circuit disagreed, reasoning that *Taylor* stands for the proposition that “where the debtor signals her intention to exempt certain property in its entirety by listing an identical entry for the property’s value and the amount of the exemption, the trustee must object pursuant to Rule 4003 lest the property be rendered fully exempt.”<sup>94</sup> According to the court, because the debtor listed the value of the business equipment as \$10,718, and the amount of the claimed exemption as \$10,718, the trustee was on notice that the debtor intended to exempt the property in full.<sup>95</sup> Having notice of the debtor’s intention, the trustee should have had the business equipment

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<sup>89</sup> *In re Reilly*, 403 B.R. 336, 337 (M.D. Pa. 2006).

<sup>90</sup> *Id.*

<sup>91</sup> *See generally*, *In Re Reilly*, 403 B.R. 336 (M.D. Pa. 2006).

<sup>92</sup> *In re Reilly*, 534 F.3d at 174.

<sup>93</sup> *Id.* at 178.

<sup>94</sup> *Id.* at 179.

<sup>95</sup> *Id.* at 178.

appraised, sought a hearing under 4003(c)<sup>96</sup> or requested an extension of time.<sup>97</sup> The trustee's failure to object rendered the property fully exempt, regardless of the property's ultimate market value.<sup>98</sup>

The Third Circuit does not stand alone in its interpretation of *Taylor*. The Eleventh Circuit and a Sixth Circuit Bankruptcy Appellate Panel also share this interpretation. In contrast, the Eighth Circuit's interpretation is in accordance with the First and Ninth Circuits.<sup>99</sup> The circuit split along with the gamesmanship invited by the Third Circuits holding and the practical implications makes this issue ripe for determination. Indeed, the Supreme Court agrees and has granted the trustee's petition for writ of certiorari.<sup>100</sup>

### III. THE DECISION

*Taylor* has been universally recognized and applied by bankruptcy courts. On appeal to the Supreme Court, neither party in *In re Reilly* argues that *Taylor* should be overruled; rather, they disagree as to the application of the decision.<sup>101</sup> The Court's decision will depend significantly on interpreting the Bankruptcy Code's provisions and distinguishing its decision in *Taylor*. The issue presented must be decided by the Court in accordance with the plain meaning of the text. In addition, each section must not be read in isolation, rather the statute's full text, language and structure must be accounted for to properly implement the intent of Congress.

#### A. *In re Reilly* Fails to Give Effect to the Language of the Statute

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<sup>96</sup> This subsection governs any objection made by a party in interest under FRBP 4003. A party objecting to an exemption bears the burden of proof to show that the exemption is not properly claimed. See FED. R. BANKR. P. 4003(c).

<sup>97</sup> *In re Reilly*, 534 F.3d at 178.

<sup>98</sup> *Id.*

<sup>99</sup> See generally, *In re Green*, 31 F.3d 1098 (11th Cir. 1994); *In re Anderson*, 377 B.R. 865 (B.A.P. 6th Cir. 2007); *In re Hyman*, 967 F.2d 1316 (9th Cir. 1992); *In re Barroso-Herrans*, 524 F.3d 341 (1st Cir. 2008).

<sup>100</sup> See *In re Reilly*, 534 F.3d 173 (3d Cir. 2008), *cert. granted*, 77 U.S.L.W. 3267 (U.S. Apr. 27, 2009) (No. 08-538).

<sup>101</sup> Brief of Petitioner at 26, *Schwab v. Reilly*, No. 08-538 (July 10, 2009) (arguing that *Taylor* is distinguishable from the case at hand and the court of appeals' holding that *Taylor* controls the disposition of this matter misunderstands the facts and reasoning of that decision); Brief for Respondent, at 2-3, *Schwab v. Reilly*, No. 08-538 (Sept. 18, 2009) (arguing that this case is a nearly identical issue and presents an "even more compelling candidate for the same result.").



In order to resolve the dispute over the meaning of Section 522(l), the language of the statute must be first examined.<sup>102</sup> Where the meaning of the statute is unambiguous, then the inquiry has ended and the sole function of the court is to enforce the statute according to its terms.<sup>103</sup> Every word of the statute shall be given effect.<sup>104</sup> “The plain meaning of legislation should be conclusive, except in the ‘rare cases in which the literal application of a statute’ will produce a result demonstrably at odds with the intentions of its drafters.”<sup>105</sup>

The relevant language at issue is Section 522(l), which reads as follows: “The debtor shall file a list of *property* that the debtor claims as exempt under subsection (b) of this section. If the debtor does not file such a list, a dependent of the debtor may file such a list, or may claim property as exempt from property of the estate on behalf of the debtor. Unless a party in interest objects, the property claimed as exempt on such list is exempt.”<sup>106</sup> Bankruptcy Rule 4003 gives an interested party, specifically the trustee, 30-days from the Section 341(a) meeting of creditors to object to the list of property claimed as exempt.<sup>107</sup> The language of Section 522(l) is unambiguous and should be interpreted according to its plain meaning. *Taylor v. Freeland & Kronz* determined this statute and its clarifying rule to be unambiguous and therefore, applied its plain meaning.

In *Taylor*, the debtor claimed certain *property* as exempt, to wit, the expected proceeds from an employment discrimination claim against her former employer.<sup>108</sup> The trustee failed to object within the time prescribed by Bankruptcy Rule 4003(b).<sup>109</sup> Consequently, the Court ruled

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<sup>102</sup> See *U.S. v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 241 (1989).

<sup>103</sup> *Id.* (interpreting § 506(b) to authorize payment of post petition interest on allowed nonconsensual oversecured claims).

<sup>104</sup> See *Rake v. Wade*, 508 U.S. 464, 471 (1993).

<sup>105</sup> *Id.* at 242 (quoting *Griffin v. Oceanic Contractors, Inc.*, 458 U.S. 564, 571 (1982)).

<sup>106</sup> See 11 U.S.C. § 522(l) (italics supplied).

<sup>107</sup> See FED. R. BANKR. P. 4003.

<sup>108</sup> See *Taylor*, 503 U.S. at 640.

<sup>109</sup> *Id.*

that by operation of Section 522(l) (in conjunction with Rule 4003(b)), the property claimed as exempt was exempt, even though the debtor had no colorable basis for claiming the exemption.<sup>110</sup> This is the holding of *Taylor*, as it was the only issue addressed by the Court.<sup>111</sup>

Applying the foregoing to the facts of *In re Reilly*, the Court should come to a similar conclusion. In *In re Reilly*, the debtor claimed certain property as exempt, to wit, business equipment.<sup>112</sup> Just as the trustee in *Taylor*, the trustee failed to object within the time prescribed by Bankruptcy Rule 4003(b). However, the difference between *Taylor* and *In re Reilly* is the consequence of the trustee's failure to object.<sup>113</sup> In *Taylor*, the trustee lodged an untimely objection to the property, because the debtor had no colorable basis for claiming it.<sup>114</sup> Under a plain meaning approach to Section 522(l), the trustee's failure to object to the property rendered the property exempt.<sup>115</sup> Thus the Court performed its proper function enforcing the statute according to its terms.<sup>116</sup> In contrast, the debtor's claimed exemption in *In re Reilly* was proper under Section 522(d)(5)'s wildcard provision and Section 522(d)(6)'s professional tools exemption.<sup>117</sup> In *In Re Reilly* the trustee did not object to the property, but rather to the valuation of the property as claimed by the debtor.<sup>118</sup> Accordingly, no objection under Section 522(l) was proper or even required as the Third Circuit held.<sup>119</sup> Any other reading fails to give effect to the language of the statute.

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<sup>110</sup> *Id.* at 643-44.

<sup>111</sup> *Id.* at 641 (As stated by the Court, the only issue was "whether the trustee may contest the validity of an exemption after the 30-day period if the debtor had no colorable basis for claiming the exemption."). *Id.*

<sup>112</sup> *In re Reilly*, 534 F.3d at 176.

<sup>113</sup> See discussion *supra*, Part II.A. [possible discussion in this footnote as to why *Taylor* is factually wrong]

<sup>114</sup> *Taylor*, 503 U.S. at 644.

<sup>115</sup> See 11 U.S.C. § 522(l)

<sup>116</sup> See *supra* note 85.

<sup>117</sup> See generally 11 U.S.C. § 522(d)(5)-(6).

<sup>118</sup> See discussion *supra* Part II.C.

<sup>119</sup> See discussion *supra* Part II.C.

The trustee in *In re Reilly* (or for that matter any trustee in a similar situation where the debtor properly claims an exemption) had no basis to object under Section 522(l). The bankruptcy court in *In re Wick* made this same point. “The issue at hand is the valuation of the property claimed exempt, not the validity of the exemption. The Trustee does not have and could not have, an objection to the validity of Wick’s exemption because [§ 522(d)(5)] allows her to exempt any type of property.”<sup>120</sup> The Third Circuit’s interpretation of Section 522(l) expands the scope of the statute beyond its plain meaning. According to the Third Circuit, not only does Section 522(l) require the debtor to file a list of property claimed as exempt, it also requires the debtor to file a list of the value of such property. Section 522(l) simply does not require this result.

While it may be true that Schedule C requires the debtor to describe the property as well as the value of the claimed exemption and the current value of the property without deducting the exemption, the statute, Section 522(l), does not require the debtor to do so.<sup>121</sup> Bankruptcy Rule 9009 provides that Official Forms prescribed by the Judicial Conference of the United States shall be observed and used.<sup>122</sup> However, these rules and forms shall not abridge, enlarge, or modify any substantive right.<sup>123</sup> The Third Circuit’s transformed the language of Section 522(l) as follows: if a party in interest objects to anything listed on Schedule C, including the value of the claimed exemption, he or she must object or the property and its attendant value figures are determinative and controlling. In *In re Reilly*, the debtor interprets Section 522(l) one step

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<sup>120</sup> *In re Wick*, 249 B.R. 900, 913 (Bkrcty. D. Minn. 2000). *See also* *In re Hyman*, 967 F.2d 1316, 1319 (9th Cir. 1992) (indicating on similar facts that the trustee had no basis for objection, and if he had objected the trustee may have suffered the judge’s “ire” because the debtor’s were clearly entitled to the exemption); Brief of the National Association of Bankruptcy Trustees as Amicus Curiae in Support of the Petitioner, at 11-13, *Schwab v. Reilly*, No. 08-538 (Sept. 18, 2009) (arguing that requiring a trustee to object to a properly claimed exemption simply because the exemption claimed equals the listed value would make a mockery out of any notion of efficiency that the official forms strive to achieve).

<sup>121</sup> *See generally* Official Form 6C.

<sup>122</sup> FED. R. BANKR. P. 9009.

<sup>123</sup> 28 U.S.C. § 2075.

further, stating that “[a] trustee who wishes to preserve any potential right to deprive a debtor of an asset claimed as exempt must object where, as here, the debtor does not concede in his or her schedules that the value of the relevant assets exceeds the amount claimed as exempt.”<sup>124</sup> Such a reading is prohibited by the language of Section 522(l) itself and surely would abridge, enlarge or modify substantive rights of both parties in interest and debtors in contravention of 28 U.S.C. § 2075.<sup>125</sup> Under the Third Circuit’s interpretation, a debtor’s substantive right to exempt property would be enlarged, beyond what Section 522(d) allows. Substantive rights of creditors to have property sold and proceeds distributed to them would also be diminished. This interpretation is not sanctioned by the Bankruptcy Code, the Bankruptcy Rules or Schedule C for that matter.

The information provided by Schedule C may be nothing more than an administrative convenience to the trustee, helping him or her evaluate the propriety of the claimed exemption.<sup>126</sup>

At least one court has agreed:

The fourth column requires the debtor to state “Current Value of Property Without Deducting Exemption.” This information is *not* required by § 522. This court believes the total value of the property in Column 4, as contrasted to the value (amount) claimed as exempt in Column 3, is likely included for the administrative convenience of the parties in interest. By comparing the figures in Column 3 and Column 4, one can easily see whether (according to the debtor’s value estimation) the property may be administered for the benefit of the estate. . . . The current value “bonus information in Column 4 of Schedule C may not be used, and should not be used, to determine “the property claimed as exempt” for purposes of § 522(l).<sup>127</sup>

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<sup>124</sup> Brief for Respondent at 38, Schwab v. Reilly, No. 08-538 (Sept. 18, 2009). It should be noted that assets are property of the estate under Section 541(a) as of commencement of the case, they no longer property belonging to the debtor. The trustee does not have merely a potential right to the property, he has an absolute right to the property that is property of the estate.

<sup>125</sup> See discussion *supra*, Part I.B.

<sup>126</sup> See 5 Collier on Bankruptcy ¶ 522.05. See also Brief of the National Association of Bankruptcy Trustees as Amicus Curiae in Support of the Petitioner, at 11, Schwab v. Reilly, No. 08-538 (Sept. 18, 2009) (arguing that the forms used in bankruptcy proceedings produce efficiency, minimize costs and expenses and speeds up the decision making process).

<sup>127</sup> In re Cormier, 382 B.R. 377, 395 (W.D. Mich. 2008).

Other courts have wrongly extended *Taylor*. The Ninth Circuit BAP’s decision is representative. “Given *Taylor*, a distinction can no longer be drawn between objecting to an exemption itself and objecting to the value of the property subject to an exemption. All objections to exemptions are subject to Rule 4003(b). *Taylor* made it clear that the purpose for the short objection period in Rule 4003(b) is to encourage finality. Allowing a trustee to distinguish between an objection to an exemption itself and the value of the property subject to that exemption does not promote finality.”<sup>128</sup> Such a broad reading is inconsistent with general principles of statutory interpretation. “Where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.”<sup>129</sup> Section 522(l) requires a party in interest to object to the property claimed as exempt.<sup>130</sup> Conspicuously absent in the statute is the requirement that a party in interest object to the value of the property claimed as exempt. A cursory review of the statute reveals that Congress knows how to use the word “value.” In fact, the word “value” is used nine times in Section 522(d) alone.<sup>131</sup> In addition, Congress also combined the words “property” and “value” in this statute on more than one occasion. For example, Section 522(d)(5) the debtor may exempt his or her “aggregate interest in any property, not to exceed in value \$1,075 plus up to \$10,125 of any unused amount of the exemption provide under paragraph (1) of this subsection.”<sup>132</sup> Congress specifically chose to include the words value and property in one section of the same statute and chose to omit the combination in Section 522(l). It is therefore presumed that Congress acted intentionally and

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<sup>128</sup> In re Morgan-Busby, 272 B.R. 257, 265 (9th Cir. BAP 2002) (citations omitted).

<sup>129</sup> Russello v. U.S., 463 U.S. 16, 23 (1983).

<sup>130</sup> See 11 U.S.C. § 522(l).

<sup>131</sup> See generally 11 U.S.C. § 522(d).

<sup>132</sup> 11 U.S.C. § 522(d)(5).

purposely in the inclusion of the word “property” in Section 522(l) and the exclusion of the word “value”.<sup>133</sup>

The often cited canon of construction *expressio unius est exclusio alterius*, meaning expression of the one is the exclusion of the other, is helpful to interpret Section 522(l). “What it means is this: If you see a sign that says children under twelve may enter free, you should have no need to ask whether your thirteen-year-old must pay. The inclusion of one class is an explicit exclusion of the other.”<sup>134</sup> Congress spoke clearly when it included the word property and excluded the word value from Section 522(l). Indeed the two objections, one to the property claimed as exempt and the other to the value, are separate and distinct; they each serve competing interests.<sup>135</sup> The objection to property claimed as exempt gives the debtor a prompt determination as to his rights in property.<sup>136</sup> In contrast, the objection to valuation allows creditors to obtain a fair valuation of the property for payment of their allowed claims.<sup>137</sup> Accordingly, because the intent of Congress is clear from the statutory text this is the end of the matter and the trustee does not waive an objection to the value of property if he or she fails to object within 30-days of the Section 341(a) meeting of creditors.<sup>138</sup>

#### B. Monetary Limitations and the Standard for Valuation of Exempt Property Preclude Application of *Taylor* in this Context.

Simply stated *Taylor* does not control the outcome of *In re Reilly*. The Third Circuit understood *Taylor* to stand for the proposition that “where a debtor signals her intention to

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<sup>133</sup> See *supra* note 102.

<sup>134</sup> ANTONIN SCALIA, A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW 25 (Amy Gutmann ed., Princeton University Press) (1997).

<sup>135</sup> *In re Hyman*, 123 B.R. 342, 348 (B.A.P. 9th Cir. 1991).

<sup>136</sup> *Id.* See also *Taylor*, 503 U.S. at 644 (reasoning that strictly enforcing Rule 4003’s 30-day provision may lead to unwelcome results, but it produces finality).

<sup>137</sup> *Id.*

<sup>138</sup> See generally, *Chevron U.S.A. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842 (1984). See also *Addison v. Reavis*, 158 B.R. 53, 60-61 (E.D. Va. 1993) (recognizing a distinction between objecting to property claimed as exempt and the value of such property claimed as exempt. Holding that only an objection to property claimed as exempt must be made within Rule 4003(b)’s 30 day period).

exempt certain property in its entirety by listing an identical entry for the property's value and the amount of the exemption, the trustee must object pursuant to Rule 4003 lest the property be rendered fully exempt."<sup>139</sup> Even assuming that a debtor signals her intention to exempt property in its entirety by listing an identical value for the property and the amount of the exemption, it does not follow that the property becomes fully exempt. Such an interpretation not only fails to give effect to the language of Section 522(l), as discussed *supra* Part IV.A, but also fails to give effect to other provisions of the Bankruptcy Code limiting the amount of exemptions and the standard for valuation. Moreover, such an interpretation is incompatible with the policy underlying the Bankruptcy Code.

*1. Specific Limits Established by Congress in Section 522(d) preclude the Application of Taylor as Interpreted by the Third Circuit*

According to the Supreme Court, statutory construction is a holistic endeavor and must account for the statute's full text, language, structure and subject matter.<sup>140</sup> It has been stressed that "in expounding a statute, we must not be guided by a single sentence or member of a sentence, but look to the provisions of the whole law, and to its object and policy."<sup>141</sup> The Third Circuit's interpretation of *Taylor* fails to account for the statute's full text, its object and policy, specifically by ignoring the monetary limitations imposed by Section 522(d).

Section 522(d) places monetary limitations on certain categories of property that the debtor may exempt.<sup>142</sup> For example, a debtor may exempt his or her aggregate interest, not to exceed \$20,200 in value, in real or personal property that the debtor uses as a residence; up to \$3,225 in one motor vehicle, \$10,775 in consumer goods such as household furnishings<sup>143</sup>, and

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<sup>139</sup> In re Reilly, 534 F.3d at 179.

<sup>140</sup> See U.S. Nat. Bank of Oregon v. Independent Ins. Agents of America, Inc. 508 U.S. 439, 455 (1993).

<sup>141</sup> *Id.* See also United States v. Heirs of Boisdore, 49 U.S. 113, 122 (1849).

<sup>142</sup> See generally 11 U.S.C. § 522(d).

<sup>143</sup> But the particular item may not individually exceed \$525. 11 U.S.C. § 522(d)(3).

\$2,025 in tools of the trade<sup>144</sup> On the other hand, Congress chose to allow a debtor to exempt certain classes of property in full, regardless of value. Items such as professionally prescribed health aids, social security benefits, unemployment compensation, alimony and support payments, and certain retirement funds are entirely exempt.<sup>145</sup> The fact that Congress chose to include monetary limitations on certain categories of property and not others, in the same statute, must mean something.<sup>146</sup> Section 522(l) should not be read to limit the application of Section 522(d). If Section 522(l) is interpreted to allow a debtor to exceed these monetary limitations, we fail to give effect to the statute's full text, its object and policy.

The debtor in *In re Reilly* argues that if Congress had intended to limit the property claimed as exempt on a debtor's schedules to the amount stated in Section 522(d), it could have done so expressly.<sup>147</sup> The debtor believes that Congress' failure to include similar limitations in Section 522(l) is determinative and a court should not infer that limitations exist.<sup>148</sup> This argument reads Section 522(l) in isolation and fails to account for the full text of the statute, including Section 522(d). "A standard principle of statutory construction provides that identical words and phrases within the same statute should normally be given the same meaning."<sup>149</sup> The Bankruptcy Code should not be read as a series of unrelated and isolated provisions; identical words used in different parts of the Bankruptcy Code should be interpreted to have the same meaning.<sup>150</sup> This principle applies here.

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<sup>144</sup> See 11 U.S.C. § 522(d)(1)-(6). Other property also contains monetary limitations on property to be exemption such as the debtors interest in the cash value of a life insurance policy or payment on account of personal bodily injury not including pain and suffering or compensation for actual pecuniary loss. See 11 U.S.C. § 522(d)(8)-(11).

<sup>145</sup> See 11 U.S.C. § 522(d)(10)-(11).

<sup>146</sup> See generally *Russello v. U.S.*, 463 U.S. 16, 23 (1983).

<sup>147</sup> Brief for Respondent at 39, *Schwab v. Reilly*, No. 08-538 (Sept. 18, 2009).

<sup>148</sup> *Id.* at 40.

<sup>149</sup> *Powerex Corp. v. Reliant Energy Services, Inc.*, 551 U.S. 224, 232 (2007).

<sup>150</sup> See generally *Gustafson v. Alloyd Co. Inc.*, 513 U.S. 561, 570 (1995).



Section 522(d) lists property that may be exempted by a debtor under Section 522(b)(2), the federal exemptions.<sup>151</sup> Monetary limitations are placed on certain classes of property and not others.<sup>152</sup> Section 522(l) qualifies this provision and requires a debtor to submit a list of the property that a debtor claims as exempt under subsection (b).<sup>153</sup> In order to file a list of property in accordance with Section 522(l), the debtor must first reference Section 522(b), which explains that a debtor may exempt from property of the estate property listed under subsection (d). The debtor's argument in *In re Reilly* that if Congress had intended to limit the effect of Section 522(l) in accordance with a value limit set forth elsewhere in the statute (i.e. Section 522(d)), they would have done so expressly<sup>154</sup>, is simply without merit. Unlike debtor's contention Congress did limit the effect of Section 522(l) to actual or stated values by specifically requiring a debtor to file a list of property claimed as exempt under subsection (b). Subsection (b) specifically incorporates Section 522(d).<sup>155</sup> Requiring Section 522(l) to expressly duplicate the limitations provided for in Section 522(d) would be unnecessary and cumulative. The term property must be defined by reference to Section 522(d) and its attendant monetary limitations, otherwise identical words and phrases within Section 522 are given different meanings. *Taylor* does not change this result.

*Taylor* must be read "as referring in context to circumstances similar to the circumstances then before the Court and not referring to quite different circumstances that the Court was not then considering."<sup>156</sup> The issue, as framed by the Court, was whether the trustee may contest a claimed exemption after the 30-day objection period has run if the debtor had no colorable basis

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<sup>151</sup> 11 U.S.C. § 522(d).

<sup>152</sup> *Id.*

<sup>153</sup> 11 U.S.C § 522(l).

<sup>154</sup> *See supra* note 147-48.

<sup>155</sup> 11 U.S.C. § 522(b)(2).

<sup>156</sup> *Illinois v. Lidster*, 540 U.S. 419, 424 (2004).

for claiming the exemption.<sup>157</sup> The debtor had no colorable basis for the exemption because the basis of the claimed exemption was a tort suit, for which no exemption exists under Section 522(d).<sup>158</sup> Under *Taylor*, it would not have mattered if the debtor listed the value of the claimed exemption as unknown or for one million dollars. Regardless of the amount claimed or the fact that the amount claimed matched the exemption claim, the property claimed as exempt was improper. There was no discussion, nor did the Court's holding rest on the fact that a debtor signaled some sort of intention to exempt the property in full by listing an identical entry for the property's value and amount of exemption.<sup>159</sup>

In *In re Reilly*, the debtor filed a list of property that she claimed as exempt under subsection (b). In order to determine what property that she was entitled to exempt under the statute, she referenced subsection (d), which enabled her to claim an exemption in specific business equipment.<sup>160</sup> Unlike the debtor in *Taylor*, the exemption listed was valid and the trustee had no basis for objecting. In order for the statute's full text to be accounted for, we must give effect to the monetary limitations provided for in Section 522(d). Accordingly, the debtor should be limited to the amount of the claimed exemption to which she was entitled, \$10,718.<sup>161</sup>

## 2. Fair Market Value as the Standard for Valuation

The Bankruptcy Code defines value as “fair market value as of the date of the filing of the petition or, with respect to property that becomes property of the estate after such date, as of

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<sup>157</sup> See *Taylor*, 503 U.S. at 639.

<sup>158</sup> See discussion *supra* Part II.A.

<sup>159</sup> See generally *Taylor*, 503 U.S. at 640-44. See also *In re Cormier*, 382 B.R. 377, 405 (W.D. Mich. 2008) (“The unstated premise in *Taylor* is limited: when a debtor claims property as fully exempt, and no objection is timely filed, the property is exempt. However, other than this remise, the Supreme court was not called upon to interpret the exemption statute, included § 522(d), nor did it even discuss it, except perhaps in passing. In *Taylor* there is no statutory analysis, much less any holding, about what property is “claimed exempt” and *how* a debtor may claim an “in kind” exemption to assert the entire property as exempt.”).

<sup>160</sup> See *In re Reilly*, 534 F.3d at 174. The debtor also claimed part of the business equipment as exempt under Section 522(d)(5)'s wild card provision in the amount of \$8,868, an amount accounting for the value of any unused amount of the exemption provided under Section 522(d)(1)'s homestead exemption. *Id.*

<sup>161</sup> *In re Reilly*, 534 F.3d at 174.

the date such property becomes property of the estate.”<sup>162</sup> Fair market value is defined as the price that a buyer is willing to pay and a seller willing to accept on the open market and in an arms length transaction.<sup>163</sup> Because fair market value will not be determined until there is a sale of the property, allowing an exemption “in kind” based on the debtor’s estimated valuation of the property matching the claimed exemption is inconsistent with the notion that value is to be determined by a property’s fair market value.

After notice and hearing, the trustee may use, sell, or lease property of the estate.<sup>164</sup> The primary role of the trustee is to liquidate the debtor’s assets in a manner that maximizes return for creditors.<sup>165</sup> In order to conduct a sale a trustee must first obtain a written appraisal of the property, unless there is an established market for the property.<sup>166</sup> With the court’s approval a trustee may employ an appraiser to assist the trustee in determining value.<sup>167</sup> After notice and hearing to all interested parties the trustee may then conduct a sale through public auction or private sale.<sup>168</sup> To prevent collusive bidding courts may require that the sale be publicly advertised.<sup>169</sup> After sale of property, the trustee is required to file a report with the Bankruptcy Court that includes an itemized statement of the property sold; list of bidders; the name of the purchaser; the price received for each item; the date, time and place of sale; compensation paid

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<sup>162</sup> 11 U.S.C. § 522(a)(2).

<sup>163</sup> BLACK’S LAW DICTIONARY 754 (3rd pocket ed., 2006). However, some courts have determined that fair market value must take into account the liquidation context of a Chapter 7 liquidation case and hold that fair market value is equivalent to liquidation value. *See generally*, In re Walsh, 5 B.R. 239 (Bankr. D.D.C. 1980). *Cf.* In re Mitchell, 103 B.R. 819 (Bankr. W.D. Tex. 1989) (holding that the appropriate valuation standard is fair market value, in accordance with the plain meaning of the statute).

<sup>164</sup> 11 U.S.C. § 363(b)(1).

<sup>165</sup> [www.uscourts.gov/bankruptcycourts/bankruptcybasics/chapter7.html#trustee](http://www.uscourts.gov/bankruptcycourts/bankruptcybasics/chapter7.html#trustee) (last visited Feb. 20, 2010).

<sup>166</sup> 1 BANKRUPTCY PRACTICE HANDBOOK § 7.47 (2d ed.).

<sup>167</sup> *Id.* *See also* 11 U.S.C. § 327(a).

<sup>168</sup> 1 BANKRUPTCY PRACTICE HANDBOOK § 7.47 (2d ed.).

<sup>169</sup> *Id.*

to professional person conducting sale (i.e. auctioneer); copies of sale advertisements; and a list of all sale expenses.<sup>170</sup>

Surely this procedure was not intended by Congress or the courts to be circumvented by a debtor's mere listing of property and estimation of value on Schedule C. In order to determine the value of the property to be exempted under Section 522(d), which is the fair market value, the trustee must conduct a sale or at a minimum an appraisal of the property. Only then will creditors receive the process to which they are entitled for payment of their claims. "Although objections to the exemptions themselves should be made as quickly as possible, the 'objections to valuation, on the other hand, need not be completed with such expediency, nor should the creditor be required to rush out and value the debtor's property in order to protect his interests in that property.'"<sup>171</sup>

Returning to the facts of *In re Reilly*, the absurdity that would result if a debtor's estimate of the property's value were to become conclusive proof of its fair market value is obvious. In *In re Reilly*, the debtor listed her business equipment with a value of \$10,718.<sup>172</sup> The business equipment consisted of catering utensils and instruments.<sup>173</sup> Unlike other types of property, such as stock, whose value may be determined by the stock market, or cars whose value may be reliably determined by reference to a website such as Kelly Blue Book, there is no readily established market for catering utensils and instruments. In order to determine the true value of this property with no established market, it becomes increasingly important to have the equipment appraised by a professional or sold in a private or public auction. Indeed, the trustee sought an appraisal of the business equipment in this case. The business equipment appraised for

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<sup>170</sup> See Local Rule (Bankr. W.D. Mich.) 6004.

<sup>171</sup> See *In re Hyman*, 123 B.R. 342, 348 (B.A.P. 9th Cir. 1991) (quoting *In re Allen*, 44 B.R. 38, 40 (Bkrtcy. N.M. 1984).

<sup>172</sup> *In re Reilly*, 534 F.3d at 174.

<sup>173</sup> *Id.*

\$17,200, 60% more than the value the debtor had listed for the property.<sup>174</sup> This conclusively shows the fallibility of relying on a debtor's estimation of the property, especially in undefined markets. Accordingly, Congress chose to equate the value of property by reference to the fair market value, rather than the value estimated by the debtor.<sup>175</sup> While a court may, in its discretion, accept an estimate of fair market value from the debtor, a sale or appraisal in excess of an estimate is significantly more reliable evidence of value as defined by Section 522(a)(2).<sup>176</sup>

#### CONCLUSION

In 2008, there were 744,424 Chapter 7 filings.<sup>177</sup> 714,389 of those were individual filings.<sup>178</sup> In the midst of a recession, unemployment rates at staggering numbers and an accompanying housing market crash we can only expect that more individuals will seek protection under the Bankruptcy Code. The American Bankruptcy Institute estimates that filings will surpass 1.4 millions in 2009 alone.<sup>179</sup> As more and more cases are filed each month it becomes imperative that a trustee is able to rely on properly submitted forms and schedules of the debtor. The practical reality is that not all debtors will be entirely truthful, honest or candid. Requiring that a trustee objects in every instance where a debtor may have undervalued his or her property would bring the system to a slow crawl.<sup>180</sup> Implementation the Eighth Circuit's

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<sup>174</sup> *Id.*

<sup>175</sup> *See* 11 U.S.C. § 522(a)(2).

<sup>176</sup> *See generally*, *Fitzgerald v. Davis*, 729 F.2d 306, 308 (4th Cir. 1984).

<sup>177</sup> *See* USCourts.gov, BUSINESS AND NONBUSINESS BANKRUPTCY CASES COMMENCED, BY CHAPTER OF THE BANKRUPTCY CODE, DURING THE TWELVE MONTH PERIOD ENDED DEC. 31, 2008, *available at* <http://uscourts.gov/bnkrpctystats/statistic.htm#calendar> (last visited Feb. 20, 2010).

<sup>178</sup> *Id.*

<sup>179</sup> John Hartgen, *November Consumer Bankruptcy Filings Drop 18 Percent from Previous Month*, Dec. 2, 2009, <http://www.abiworld.org/AM/Template.cfm?Section=Home&TEMPLATE=/CM/ContentDisplay.cfm&CONTENTID=59380>

<sup>180</sup> *See also In re Wick*, 276 F.3d at 417 (noting that “[s]ince exemptions are routinely smaller than the assets they are designed to protect (for example, with homes), objections would multiply greatly if *Taylor* were read so broadly.”).

decision in *In re Wick* will ensure that debtors and creditors are treated fairly in the system, and will not reward those who try and take advantage of its perceived technicalities.

In *In re Reilly*, the Supreme Court should hold that if the value of the property claimed as exempt exceeds the monetary limitations of Section 522(d), only to the extent of the monetary limitations is the property exempt, regardless if the trustee has objected within the 30-days provided for by Rule 4003(b). This holding is consistent with the plain meaning of Section 522(l), which only requires a party in interest to object to the property claimed as exempt and not to the valuation of that property. In addition, this holding accounts for the Bankruptcy Code's full text rather than reading provisions in isolation. A contrary holding would disregard the specific monetary limitations imposed by Congress as well as the fair market value standard used to determine the value of exempt property. In the end, bankruptcy is a privilege and not a right. A debtor's fresh start must yield to the countervailing principle of fair distribution to creditors for the obligations and responsibilities incurred by a debtor.