

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

**FOR PUBLICATION ON THE
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In re :
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JAY A. SMITH, :
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Debtor. :
-----X

Chapter 7
Case No. 00-35244 (CGM)

**DECISION ON TRUSTEE'S OBJECTION TO
DEBTOR'S CLAIMED EXEMPTION**

APPEARANCES:

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CECELIA G. MORRIS, UNITED STATES BANKRUPTCY JUDGE

This matter is before the Court on the motion of the former Chapter 7 trustee, Michael O’Leary, Esq., (hereinafter “former Trustee” or “Trustee” or “O’Leary”), seeking to strike the debtor’s claimed exemption in the reopened bankruptcy case¹ of Jay A. Smith (“Debtor”). For the reasons set forth herein, the Court finds that Trustee’s motion is untimely and that Debtor is entitled to his claimed exemption.

The Court considers whether the trustee’s motion objecting to Debtor’s claimed exemption is timely where the debtor supplemented his original petition and claimed an exemption as provided in Federal Rules of Bankruptcy Procedure (hereinafter “Rule” or “Bankruptcy Rule”) 1007(h).²

Jurisdiction

The Court has jurisdiction over this proceeding pursuant to 28 U.S.C. § 1334(b) and the “Standing Order of Referral of Cases to Bankruptcy Judges” of the United States District Court for the Southern District of New York, dated July 10, 1984 (Ward, Acting C.J.). This is a core matter under 28 U.S.C. § 157(b)(2)(B).

Background

The legally significant facts are not disputed. On February 8, 2000, Debtor filed for voluntary

¹ The former Trustee’s motion to reopen the debtor’s case was returnable on the same day set for the hearing to consider the instant motion. Debtor’s case was reopened to administer estate assets on October 31, 2000. Michael O’Leary was reappointed trustee of Debtor’s bankruptcy case on November 6, 2000.

² Federal Rule of Bankruptcy Procedure 1007(h), provides in pertinent part:

If, as provided by § 541(a)(5) of the Code, the debtor acquires or becomes entitled to acquire any interest in property, the debtor shall within 10 days after the information comes to the debtor's knowledge or within such further time the court may allow, file a supplemental schedule in the chapter 7 liquidation case If any of the property required to be reported under this subdivision is claimed by the debtor as exempt, the debtor shall claim the exemptions in the supplemental schedule. *The duty to file a supplemental schedule in accordance with this subdivision continues notwithstanding the closing of the case*

FED. R. BANKR. P. 1007(h) (emphasis added).

chapter 7 relief under Title 11 of the United States Code (hereinafter “Bankruptcy Code” or “Code”). On March 28, 2000, Trustee filed a no-asset/no-distribution report indicating that Debtor’s estate lacked non-exempt assets for Trustee to distribute. Accordingly, after the issuance of an Order of Final Decree discharging the trustee, the Clerk of Court closed Debtor’s case on May 15, 2000.³

During the pendency of Debtor’s bankruptcy case, on April 4, 2000, Debtor’s mother died intestate (“Decedent”) in New York State.⁴ On April 24, 2000, the debtor advised his attorney that he was entitled to an indeterminate intestate distribution from Decedent’s estate. Trustee acknowledges receiving a letter from Debtor’s counsel dated April 24, 2000, advising Trustee that Debtor’s intestate distribution was subject to § 541(a)(5)(A) of the Code and was therefore property of Debtor’s bankruptcy estate.⁵ The trustee however did not take any immediate steps to prevent Debtor’s case from closing. Instead, on May 16, 2000, one day after Debtor’s case closed, the former Trustee unsuccessfully attempted to withdraw the no-asset/no-distribution report filed on March 28, 2000.

In early June and at the former Trustee’s request, Debtor’s counsel forwarded to O’Leary the materials germane to the administration of Decedent’s estate. On July 16, 2000, Debtor

³ See 11 U.S.C. § 350(a); FED. R. BANKR. P. 5009.

⁴ See N.Y. EST. POWERS & TRUSTS LAW §§ 4-1.1 to -1.6 (McKinney 1998).

⁵ Bankruptcy Code section 541(a) provides, in relevant part:

The commencement of a case under §301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(5) Any 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)(A).

supplemented schedules A, B, and C of his petition pursuant to Rule 1007(h). Debtor's supplemental schedules were filed on notice to all parties in interest and more than 2 months after Debtor's case closed. The supplemental schedules listed Debtor's share in the intestate distribution received from Decedent's estate. Debtor's share of the intestate distribution was one-seventh of \$225,000.⁶ Debtor's Amended Schedule C asserts a cash exemption of \$2,270 pursuant to the New York exemption scheme.⁷ In the instant motion filed by Trustee 79 days after Debtor amended his schedules, O'Leary objects to Debtor's claimed exemption.

Section 541(a)(5) and Rule 1007(h)

Upon the filing of a bankruptcy petition, all of a debtor's property interests become property of a bankruptcy estate. 11 U.S.C. § 541(a)(1). This estate includes property "that the debtor acquires or becomes entitled to acquire within 180 days after [the date of the petition]-- (A) by bequest, devise, or inheritance." 11 U.S.C. § 541(a)(5)(A). Section 541(a)(5) is implemented by Rule 1007(h) which provides, in part:

If . . . the debtor acquires or becomes entitled to acquire any interest in property, the debtor shall within 10 days after the information comes to the debtor's knowledge or within such further time the court may allow, file a supplemental schedule in the chapter 7 liquidation case If any of the property required to be reported under this subdivision is claimed by the debtor as exempt, the debtor shall claim the exemptions in the supplemental schedule. The duty to file a supplemental schedule in accordance with this subdivision continues notwithstanding the closing of the case

FED. R. BANKR. P. 1007(h).

Bankruptcy Rule 1007 is the exclusive procedural mechanism to inform trustees of a debtor's post-petition acquisition of estate property. 9 L. King, COLLIER ON BANKRUPTCY ¶ 1007.08 at 1007-15 (15th ed. rev. 1996). Absent a court ordered extension, the debtor ordinarily has 10 days to discharge Rule 1007(h) duties. FED. R. BANKR. P. 1007(h); *cf.* FED R. BANKR. P. 9006(b)(1)

⁶ Without factoring Debtor's claimed exemption, Trustee will administer assets approximating \$32,152.50.

⁷ *See* N.Y. DEBT. & CRED. LAW § 283(2) (McKinney 2001).

(requiring a showing of excusable neglect for untimely acts); *Pioneer Inv. Servs. Co. v. Brunswick Assoc. Ltd. P'ship*, 507 U.S. 380, 113 S. Ct. 1489, 123 L. Ed. 2d 74 (1993) (examining “excusable neglect”). The debtor’s duty to file supplemental schedules continues notwithstanding the prior closing of the debtor’s case. *See* FED. R. BANKR. P. 1007(h).

If the debtor claims any portion of the property from the supplemental schedule as exempt, Rule 1007(h) requires that the debtor claim the exemption in the supplemental schedule. *Id.* As one court has described the proper Rule 1007(h) procedure, once a debtor becomes entitled and does receive a § 541(a)(5) asset, Rule 1007(h) requires the debtor to file a supplemental schedule. *See Mertz v. Rott (In re Mertz)*, 955 F.2d 596, 598 (8th Cir. 1992).

As a preliminary matter, the Court notes that the litigants have already conceded various points of possible contention. Debtor concedes that his intestate distribution is property of the bankruptcy estate pursuant to § 541(a)(5).⁸ Trustee does not challenge the timeliness of Debtor’s supplemental schedules and, *a fortiori*, the timeliness of Debtor’s claimed exemption.⁹ The Court, therefore, will confine its analysis to the propriety of Trustee’s motion to Debtor’s claimed exemption.

⁸ The Court is cognizant that although the rights of distributees in a decedent’s estate are determined as of the date of the decedent’s death, the amounts to which the beneficiaries are actually entitled to receive are incapable of ascertainment until the period of administration has been completed. 38 N.Y. JUR. 2D, DECEDENTS’ ESTATES § 100 (1984) (citing *In re Williams’ Estate*, 162 Misc. 507, 510, 295 N.Y.S. 56, 59 (Surr. Ct. Kings Co. 1937), *aff’d*, 254 A.D. 741, 4 N.Y.S.2d 467 (2d Dep’t 1938)). Consequently, a time lag between when a party first learns of a possible intestate distribution and when a party learns of the actual sums to be distributed, if any, is expected.

⁹ Trustee, to his credit, has openly acknowledged the impeccable comportment of the Debtor and Debtor’s attorney throughout the course of this case. In contrast, the few reported cases examining Rule 1007(h) have involved patent debtor misconduct. *See, e.g., Mertz*, 955 F.2d at 598-99 (approving of bankruptcy court’s finding that debtor’s intentional failure to report asset supported denial of discharge); *Woodson v. Fireman’s Fund Insur. Co., (In re Woodson)*, 839 F.2d 610, 614-15 (9th Cir. 1988) (refusing to allow debtor in possession that violated fiduciary obligations under the Code to benefit from failure to discharge 1007(h) duties); *In re Euerle*, 70 B.R. 72, 73-4 (Bankr. N.H. 1987) (ordering a hearing to examine the propriety of imposing sanctions for debtor’s total failure to supplement schedules).

Objections to Exemptions- § 522(l) and Rule 4003(b)

The procedure for claiming and objecting to claimed exemptions is controlled by 11 U.S.C. § 522(l) and Rule 4003(b). Section 522(l) of the Code provides, in part, that: “[t]he debtor shall file a list of property that the debtor claims as exempt [and] . . . [u]nless a party in interest objects, the property claimed as exempt on such list is exempt.” 11 U.S.C. § 522(l). Bankruptcy Rule 4003(b)¹⁰ provides that the trustee or any creditor may file objections to a claimed exemption within 30 days of the filing of Rule 1007(h) supplemental schedules. *See* FED. R. BANKR. P. 4003(b); *Bell v. Bell (In re Bell)*, 225 F.3d 203, 218 n.21 (2d Cir. 2000) (noting that Rule 4003(b) provides a thirty-day time period to object, running from the date a debtor files amended or supplemental schedules).

As a general proposition, the deadlines provided for in the Federal Rules of Bankruptcy Procedure are to be interpreted strictly and in a manner consistent with the Code’s policies in favor of providing a fresh start for the debtor and the prompt administration of the case. *Dombroff, M.D. v. Greene (In re Dombroff)*, 192 B.R. 615, 621 (S.D.N.Y. 1996) (examining Rule 4004) (citing *Taylor v. Freeland & Kronz*, 938 F.2d 420 (3d Cir. 1991), *aff’d*, 503 U.S. 638, 112 S. Ct. 1644, 118 L. Ed. 2d 280 (1992)) (citation omitted). The exemption scheme was designed to permit individual debtors to retain property so that they will be able to enjoy a fresh start after bankruptcy. *U.S. v.*

¹⁰ Federal Rules of Bankruptcy Procedure 4003(b) provides, in part:

The trustee or any creditor may file objections to the list of property claimed as exempt within 30 days after the conclusion of the meeting of creditors held pursuant to Rule 2003(a) or the filing of any amendment to the list or supplemental schedules unless, within such period, further time is granted by the court. . . .

FED. R. BANKR. P. 4003(b) (amended 2000). As of December 1, 2000, Rule 4003(b) has been amended, in part, as follows:

A party in interest may file an objection to the list of property claimed as exempt only 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. . . .

FED. R. BANKR. P. 4003(b) (emphasis added). The Advisory Committee Note clarifies that the amendment conforms the rule to § 522(l) of the Code by recognizing that any party in interest may file an objection or request an extension of time to do so.

Security Indus. Bank, 459 U.S. 70, 72, 103 S. Ct. 407, 409, 74 L. Ed. 2d 235 n.1 (1982).

The Supreme Court in *Taylor v. Freeland & Kronz* addressed whether a trustee may contest the validity of an exemption after the 30-day period contemplated by Rule 4003(b) has expired. *Taylor v. Freeland & Kronz*, 503 U.S. 638, 639, 112 S. Ct. 1644, 1646, 118 L. Ed. 2d 280 (1992). Despite no colorable basis for the claimed exemption, the debtor in *Taylor* claimed an exemption for an anticipated monetary award from a discrimination lawsuit. *Taylor*, 503 U.S. at 642, 112 S.Ct. 1644. The Chapter 7 trustee did not file an objection within the 30 days allowed by Rule 4003(b). *See Taylor*, 503 U.S. at 641-42, 112 S.Ct. 1644. The Court held that the trustee's failure to do so barred him from challenging the validity of debtor's claimed exemption. *Taylor*, 503 U.S. at 642, 112 S.Ct. 1644. In determining that the exemption was valid by default under § 522(l), the Court noted that "[d]eadlines may lead to unwelcome results, but they prompt parties to act and they produce finality." *Taylor*, 503 U.S. at 644, 112 S. Ct. 1644. The Court's ruling follows directly from § 522(l) which provides that property claimed as exempt is exempt in the absence of an objection. 4 L. King, COLLIER ON BANKRUPTCY ¶ 522.05[2][b] at 522-29 (15th ed. rev. 1998); *see also Bell*, 225 F.3d at 209 (characterizing *Taylor* as having strictly interpreted § 522(l) and Rule 4003(b)).

Applying these principles here, Debtor's claimed exemption is properly exempt. On July 16, 2000, Debtor's supplemental schedule claimed \$2,270 as exempt from Debtor's bankruptcy estate. None of Debtor's creditors objected, and O'Leary's objection was filed on October 3, 2000, well outside the 30-day period prescribed by Rule 4003(b). In the absence of a timely objection, § 522(l) dictates that the property claimed as exempt is exempt. Trustee's instant objection is untimely and Debtor is entitled to his claimed exemption.

The arguments raised by Trustee require this Court to consider whether the facts of this case justify changing this unassailable result. The Court finds that none of Trustee's arguments warrant deviating from the general rule.

“Tolling” Argument

O’Leary acknowledges that Rule 4003(b) imposes a 30-day time-limit for objecting to Debtor’s claimed exemption. O’Leary argues nonetheless that his instant objection is timely. O’Leary claims that his motion is timely because at the time Debtor filed his supplemental schedules O’Leary was not yet reappointed to serve as trustee in Debtor’s case. As O’Leary reads Rule 4003(b), the 30-day deadline to object is tolled until a former trustee is reappointed in the debtor’s case. Hence, O’Leary argues he should have had 30 days from his reappointment as case Trustee, or until December 6, 2000, to object to Debtor’s claimed exemption that was filed on July 16, 2000.

The Court rejects Trustee’s argument because § 522(l), and Rules 1007(h) and 4003(b) negate O’Leary’s theory. The Court finds no reason to conclude that the property Debtor claimed as exempt is still property of the bankruptcy estate. Hence, O’Leary’s motion is untimely. Two points demonstrate this proposition:

First, the 30-day deadline to object under Rule 4003(b) is triggered by a debtor’s claimed exemption under Rule 1007(h) and not the reappointment of a case trustee. Even in a closed case a debtor may file a supplemental schedule that includes a claimed exemption. *See* FED. R. BANKR. P. 1007(h). Bankruptcy Rule 4003(b) gives a trustee and creditors 30 days from the filing of a supplemental schedule to object. *See* FED. R. BANKR. P. 4003(b). Read together both Rules clearly contemplate that a debtor may file an exemption claim in a closed case with 30 days for parties in interest to object. *See generally In re 20/20 Sport, Inc.*, 200 B.R. 972, 977 (Bankr. S.D.N.Y. 1996) (Lifland, J.) (“As with a statute, a court’s inquiry is complete if it finds the text of a federal rule to be clear and unambiguous.”). Here, Debtor filed his supplemental schedules on July 16, 2000, after his case had closed. Parties in interest had 30 days or until August 16, 2000, to object to the claimed exemption. It is undisputed that no party in interest objected before August 16, 2000.

Second, § 522(l) is self-executing, meaning that unless a party in interest objects to a debtor’s claim, the property claimed as exempt is exempt. *See Bell*, 225 F.3d at 215. Once property becomes exempt it is withdrawn from the estate and the creditors for the benefit of the debtor. *See Id.* This

observation is important because it is well-settled that the allowance of a claim of exemption due to the expiration of the 30-day period is to revest the property in the debtor and to end its status as property of the bankruptcy estate. *See Redfield v. Peat, Marwick, Mitchell & Co. (In re Robertson)*, 105 B.R. 440, 446 (Bankr. N.D. Ill. 1989); *accord Bell*, 225 F.3d at 215-16. Indeed, once the deadline for objections to exemptions has passed, exempted property is beyond the jurisdiction of the bankruptcy court. *See Bell*, 225 F.3d at 216; *see also Turner v. Ermiger (In re Turner)*, 724 F.2d 338, 341 (2d Cir. 1983) (Friendly, J.) (finding that where a debtor has already “reclaimed” exempted property from the estate, a dispute over such property is not sufficiently “related to” the bankruptcy case to sustain federal jurisdiction under the identical predecessor to 28 U.S.C. § 1334(b)). Here, Debtor’s property revested 30 days after Debtor’s creditors failed to object to the claimed exemption in the supplemental schedule. O’Leary’s argument does nothing to reverse the effects of Debtor’s exemption. The property Debtor claimed as exempt is no longer part of the bankruptcy estate. Hence, O’Leary’s objection is untimely.

This Court can find no reason to conclude that the property Debtor claimed as exempt is still property of the bankruptcy estate. Were the right to object vested in a case trustee alone, the Court’s finding that Trustee’s objection is untimely would remove Debtor’s claimed exemption from any scrutiny. But this is not the case here. Trustee does not question that Debtor’s creditors had a full opportunity to object to Debtor’s claimed exemption. Nor does Trustee suggest that Debtor attempted anything untoward with the timing of the supplemental schedules. Instead, O’Leary suggests that a Debtor’s claimed exemption and hence a part of Debtor’s fresh start should remain undetermined until a trustee is reappointed in the case. Crediting this theory would permit Trustee to extend the right to object to Debtor’s claimed exemption until 146 days after Debtor filed his supplemental schedule. In this Court’s estimation and on the facts presented, the dual aims of certainty and finality preclude adopting O’Leary’s theory. *See Taylor*, 503 U.S. at 644, 112 S. Ct. 1644. Consequently, O’Leary’s tolling argument is rejected.

Trustee’s Policy Argument

Trustee underpins his theory by arguing that although Debtor was not motivated by a desire

to impede the trustee's duties, *see* 11 U.S.C. § 704(1), other less well-intentioned debtors could subvert a trustee's opportunity to participate in the exemption-objection process by simply filing a supplemental schedule after the case trustee has been discharged. Stated another way, Trustee questions whether the debtor's pattern of conduct, although not Debtor's conduct per se, presents an opportunity for others similarly situated to abuse the bankruptcy process.

The Court rejects O'Leary's policy argument based on the Supreme Court's reasoning in *Taylor*. To the extent the debtor's pattern of conduct could impede a trustee from discharging statutory duties, improper conduct in bankruptcy proceedings is punishable under various provisions of the Bankruptcy Code, Bankruptcy Rules and United States Code:

See, e.g., 11 U.S.C. § 727(a)(4)(B) (authorizing denial of discharge for presenting fraudulent claims); Rule 1008 (requiring filings to "be verified or contain an unsworn declaration" of truthfulness under penalty of perjury); Rule 9011 (authorizing sanctions for signing certain documents not "well grounded in fact and . . . warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law"); 18 U.S.C. § 152 (imposing criminal penalties for fraud in bankruptcy cases).

Taylor, 503 U.S. at 644, 112 S. Ct. 1644.

If these provisions do not deal with Trustee's concerns, *Taylor* is quite clear that Congress may enact provisions to address any perceived difficulties. *Id.*, at 644-45, 112 S. Ct. 1644; *see also Union Bank v. Wolas (In re ZZZ Best Co., Inc.)*, 502 U.S. 151, 158, 112 S. Ct. 527, 531, 116 L. Ed. 2d 514 (1991) ("The fact that Congress may not have foreseen all of the consequences of a statutory enactment is not a sufficient reason for refusing to give effect to its plain meaning."). Consequently, the Court also rejects Trustee's policy argument.

Amended Rule 4003(b)

Even if the result the Court reaches may seem harsh, amended Rule 4003(b), which became effective December 1, 2000, states in relevant part:

A party in interest may file an objection to the list of property claimed as exempt only 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.
FED. R. BANKR. P. 4003(b) (emphasis added).

The Advisory Committee Note clarifies that the amendment conforms the rule to § 522(l) of the Code by recognizing that any party in interest may file an objection or request an extension of time to do so. *See* FED. R. BANKR. P. 4003 advisory committee note; 11 U.S.C. § 522(l) (“Unless a party in interest objects, the property claimed as exempt . . . is exempt.”). It is debatable, based on 28 U.S.C. § 2075¹¹ and the Advisory Committee’s Note, that no substantive change has been effected by the amendment. The Court’s ruling however would not change even if amended Rule 4003(b) were applicable.¹² The Court notes that despite the text of § 522(l), Trustee presupposed that a former trustee may not object to a Debtor’s claimed exemption under former Rule 4003(b). The Court did not reach this consideration to address Trustee’s motion. Instead, the Court relies on the authority of *Taylor* in finding that absent an objection within 30 days of a debtor’s claimed exemption, the property claimed as exempt is exempt. *See Taylor*, 503 U.S. at 643, 112 S. Ct. 1644.

Conclusion

Although the Court appreciates that the timing of the various deadlines was unusual, it is inescapable that Trustee would not have been in this unenviable position had Debtor’s case remained open and/or Trustee taken more decisive action in response to Debtor’s supplemental schedules. The Court finds that none of Trustee’s arguments compel deviating from the general rule as espoused in *Taylor* that absent an objection within 30 days, the property claimed as exempt is exempt.

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28 U.S.C. § 2075 provides, in relevant part, that “[t]he Supreme Court shall have the power to prescribe . . . the practice and procedure in cases under title 11. Such rules shall not abridge, enlarge, or modify any substantive right. . . .”

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28 U.S.C. § 2074(a) provides, in pertinent part, that “[t]he Supreme Court may fix the extent [that a new rule or amendment] shall apply to proceedings then pending, except that the Supreme Court shall not require the application of such rule to further proceedings then pending to the extent that, in the opinion of the court in which such proceedings are pending, the application of such rule in such proceedings would not be feasible or would work injustice, in which event the former rule applies.”

Having finally moved to object to Debtor's claimed exemption 79 days after Debtor filed his supplemental schedules, Trustee has necessarily foreclosed his right to object to Debtor's claimed exemption. Trustee's objection has been foreclosed because the consequence of Debtor's creditors failing to object within 30 days of Debtor's claimed exemption is to re-vest the claimed-exempt property in the debtor. Debtor's claimed-exempt property vested before Trustee's motion filed on October 3, 2000. Trustee's objection is therefore untimely.

On the record of this case and for the reasons stated above, the Court finds that Trustee's motion is untimely and that the Debtor is entitled to his claimed exemption. Debtor's counsel SETTLE ORDER pursuant to S.D.N.Y. LBR 9074-1.

Dated: Poughkeepsie, New York

August 10 , 2001

/S/ Cecelia Morris
Cecelia G. Morris
U.S. Bankruptcy Judge