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IN THE SUPREME COURT OF THE UNITED STATES

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 STEPHEN LAW, :
 Petitioner : No. 12-5196
 v. :
 ALFRED H. SIEGEL, CHAPTER 7 :
 TRUSTEE :

- - - - - x

Washington, D.C.
Monday, January 13, 2014

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 11:39 a.m.

APPEARANCES:

MATTHEW S. HELLMAN, ESQ., Washington, D.C.; on behalf of Petitioner.

NEAL K. KATYAL, ESQ., Washington, D.C.; on behalf of Respondent.

SARAH E. HARRINGTON, ESQ., Assistant to the Solicitor General, Department of Justice, Washington, D.C.; for United States, as amicus curiae, supporting Respondent.

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P R O C E E D I N G S

(11:39 a.m.)

CHIEF JUSTICE ROBERTS: We will hear argument next in Case 12-5196, Law v. Alfred H. Siegel, Chapter 7 Trustee.

Mr. Hellman.

ORAL ARGUMENT OF MATTHEW S. HELLMAN

ON BEHALF OF THE PETITIONER

MR. HELLMAN: Thank you, Mr. Chief Justice, and may it please the Court:

Congress expressly prohibited what the bankruptcy court did here. Under Section 522(k) of the Code, Congress specified that a debtor's exempt property, his homestead, his pension, his wedding ring, is not liable for the payment of, quote, "any administrative expense."

JUSTICE SCALIA: Excuse me. Will you crank up your -- your thing? I can't you hear well enough. That's good.

MR. HELLMAN: Congress, in Section 522(k), specified specifically that a debtor's exempt property is not liable for any administrative expense.

The bankruptcy court was not free to override that express and specific prohibition in the name of equity, a point that has been clear for at least

1 80 years, since this Court's case in *Ginsberg & Sons*,
2 and said Congress made the judgment that debtors and
3 their dependents, even dishonest debtors, ought not be
4 deprived of their exempt property such that they would
5 emerge from bankruptcy as wards of the State.

6 Instead, Congress authorized other serious
7 punishments for debtor misconduct. But arguments for
8 punishment that the Code forbids must be addressed to
9 Congress and not the supposed equitable discretion of
10 the bankruptcy court.

11 Now, if I could, I'd like to --

12 JUSTICE ALITO: I am somewhat taken aback by
13 your constant reference -- your repeated references to
14 "wards of the State."

15 What we're talking about is whether your
16 client gets \$75,000. Do you think everybody who doesn't
17 have \$75,000 is a ward of the State?

18 MR. HELLMAN: This is his last \$75,000, Your
19 Honor.

20 JUSTICE ALITO: Yes. Well, do you -- do you
21 know what the -- the median net worth of a household in
22 the United States is?

23 MR. HELLMAN: It's -- it's about -- I'm not
24 sure what the median net worth --

25 JUSTICE ALITO: It's less than \$70,000. So

1 the question here is not whether he's going to be a ward
2 of the State. The question is whether he's going to be
3 above the median in his assets.

4 MR. HELLMAN: Well, I think what's going on
5 here, Your Honor, is actually a federalism principle.
6 Congress recognized, in 522, that States, in effect,
7 would be the ones who would have to take care of those
8 who do not have a home, do not have tools of trade, do
9 not have a pension.

10 And so what 522 does is it says that the
11 State authorizes you an exemption, and you claim it, and
12 it becomes exempt, then you get to keep it through the
13 bankruptcy law, because otherwise, in effect, it is the
14 State that ends up being required to house or support
15 or -- or help those and their dependents who are
16 deprived of, essentially, their last dollar, which is
17 what is exactly the case here.

18 Here every penny -- all of Mr. Law's
19 creditors in this case have been paid off. The trustee
20 has already received approximately \$280,000. We're just
21 talking about literally, literally, the last \$75,000,
22 and all of it, that would be going to the trustee.

23 JUSTICE GINSBURG: I don't follow that,
24 because I thought that \$75,000 would go to satisfy part
25 of the claim, that there would still be the legal fees

1 unpaid.

2 MR. HELLMAN: All his creditors -- the debts
3 that existed beforehand --

4 JUSTICE GINSBURG: Yes. But now the -- the
5 trustee, who is obliged to try to find what assets he or
6 she can, spends a huge amount of money in order to -- to
7 prove that this claim of a second mortgage was false.

8 And -- and there should be -- so what
9 happens then, on your theory, that all that money was
10 spent and the result is that the second mortgage is
11 canceled; the creditors are satisfied? Nobody pays the
12 legal expenses. Is that --

13 MR. HELLMAN: Well, the first 280,000 have
14 been satisfied, and the trustee was not obligated by any
15 law to pursue the administration of the estate in a way
16 that would be cost-ineffective. But our point here is
17 that Congress had made the determination -- we could
18 have -- there could be a policy discussion, of course,
19 about whether exempt property ought to be allowed to go
20 to the administrative costs of the estate or to
21 prepetition creditors in situations in which the -- a
22 court finds litigation misconduct.

23 But that is not the judgment Congress made.

24 JUSTICE ALITO: What was -- what was the
25 trustee supposed to do? Suppose the trustee has a meter

1 running on -- on his desk, and he's hot in pursuit of
2 this phantom Lily Lin of China, but we get -- we get to
3 the point where he's down to the -- he says, well, if I
4 do any more work, the only way I'm going to get paid is
5 out of the \$75,000. I better stop, because otherwise,
6 I'm going to be working free.

7 What should he do?

8 MR. HELLMAN: Well, the trustee, in that
9 situation -- and the trustee handbook, pages 4-3, 4-4 of
10 the trustee handbook that the United States Office of
11 Trustee puts out, notes that administrators on the
12 estate ought to assess whether or not pursuing a claim
13 will be an effective -- will yield an effective return
14 for the estate.

15 And, again, Congress, made the judgment
16 that, when a debtor lies to a court, he loses his
17 discharge. And that has an effect on the debtor's
18 obligations going forward. It means that the debtor's
19 prepetition debts, to the extent they're unsatisfied,
20 stay with him for the rest of his life.

21 But Congress did not say the denial of
22 discharge allows the trustee to recover anything more
23 than it otherwise would.

24 So, again, I think the question is one of
25 policy, and one the policy where Congress has spoken

1 clearly. The text of --

2 JUSTICE SOTOMAYOR: Can we talk about that
3 policy?

4 MR. HELLMAN: Yes, Your Honor.

5 JUSTICE SOTOMAYOR: I mean, it would seem to
6 me that a court's sanctioning power is among one of the
7 most respected and longstanding powers. So putting
8 aside the government's reliance on the statutory scheme,
9 I don't see it. But how about the inherent power?

10 MR. HELLMAN: Well, inherent power --

11 JUSTICE SOTOMAYOR: Meaning, you want to
12 read a preclusion of the inherent power out of -- not
13 from an express term, but implicitly.

14 MR. HELLMAN: No, Your Honor. Just -- I
15 should note, of course, inherent power was never argued
16 below, nor presented in the bio. But I think the more
17 important response to your question is the following:
18 We are not talking in this case about the inherent power
19 to sanction a litigant.

20 This -- we don't dispute that Rule 11 exists
21 and other punishments exist under the Code.

22 This case is about a court saying the
23 property from which that -- that sanction can be
24 satisfied, out of what property can that sanction be
25 paid or forced to be paid. And there --

1 JUSTICE SOTOMAYOR: But you are talking
2 about the inherent power. You're saying a court, in
3 its --

4 MR. HELLMAN: Not --

5 JUSTICE SOTOMAYOR: -- inherent power, can't
6 use that property. That's what you're saying.

7 MR. HELLMAN: My point is that there is no
8 longstanding tradition of the same vein of a court being
9 able to sanction, to be able to say, you owe attorneys'
10 fees for this bad conduct. That's not what this case is
11 about. This case is about the property out of which
12 that sanction can be paid.

13 And Congress spoke specifically. And when
14 Congress speaks specifically, this Court recognized in
15 NASCO, in Nova Scotia, and in a long line of cases
16 beforehand, in the Article III context no less, in the
17 Article III court, this Court recognized that where
18 Congress speaks expressly, a court does not have the
19 inherent power or otherwise to reach the contrary
20 result.

21 And I think the Ginsberg case is quite on
22 point here because the facts of that case were striking
23 even today.

24 There, in Ginsberg, the debtor was a
25 corporation, and an officer of that corporation was

1 seeking to flee the jurisdiction with corporate cash,
2 funds of the corporation. A creditor went to the
3 bankruptcy court and said, we need to detain this
4 person, arrest him. He's fleeing with property of the
5 estate.

6 This Court said the arrest writ was not
7 valid. Why? Because the Bankruptcy Code specified the
8 situations in which arrest was authorized.

9 Conditions A, B, and C needed to be
10 satisfied. This was situation D, and the creditor
11 adverted to the general equitable powers of the
12 bankruptcy court, which are codified then, as now, in
13 their provision. And this Court said, no, the specific
14 provision that's at stake here, at issue here, means
15 that the equitable provision, the general equity cannot
16 overcome that.

17 And in fact, Ginsberg was a less clear case
18 than this one. The arrest provision in Ginsberg was
19 framed affirmatively. You may arrest if situations A, B
20 and C are here. And the Court said you can't add
21 situation D to that.

22 This is a case not by implication, but an
23 express prohibition: Exempt property is not liable for
24 the payment of any administrative expense, save in two
25 situations. It wasn't even as if Congress --

1 JUSTICE KENNEDY: Your position is that the
2 trustee can take no action to make the estate whole in
3 the event of, say, Justice Alito's type of hypothetical,
4 the bank -- the estate bankruptcy trustee spends
5 \$125,000 in legal fees to bring property back to the
6 estate that had been concealed by wrongful conduct of
7 the debtor and the debtor still gets \$75,000 of that?
8 There is nothing the bankruptcy trustee can do to make
9 that bankruptcy estate whole?

10 MR. HELLMAN: Of course, as was the case
11 here, there was a denial of discharge, the classic and
12 serious penalty for debtors who engage in misconduct
13 before a bankruptcy court. What that means in almost
14 every case is that there will be debts owed to
15 pre-petition creditors that remain unpaid. It's
16 essentially the bankruptcy death penalty in the sense
17 that it makes the debtor liable for the rest of his days
18 until those debts are paid off. That's a very serious
19 punishment.

20 JUSTICE KENNEDY: What about the house? The
21 house was still exempt because if they levy on the
22 house, you go back to bankruptcy and it's still exempt.
23 So there's nothing you can do to make the trustee -- the
24 estate whole.

25 MR. HELLMAN: Two points, Your Honor. One,

1 the question to where you want to draw the line about
2 deterring debtor misconduct and leaving debtors without,
3 literally, their last dollar coming out of bankruptcy is
4 an important question, but a policy question, and one
5 where Congress has spoken with an expressed prohibition.
6 Now, there are other sanctions, not -- none of which
7 were levied here or sought to be levied here, Rule 11
8 and the like, that might serve to provide an additional
9 source of funds, but not from exempt property, because
10 Congress has walled that off. If one looks --

11 JUSTICE BREYER: The same thing is true of
12 certain retirement funds.

13 MR. HELLMAN: Yes, Your Honor.

14 JUSTICE BREYER: So if, in fact, the person
15 has \$4 million in this special retirement fund account
16 and he's behaved in the most extraordinarily dishonest
17 way, the trustee has no power to impose a sanction on
18 those funds, even if he'll earn a big income, he's lied
19 nonstop, etcetera.

20 MR. HELLMAN: Congress has amended
21 Section 522 already eight times since 1978, about once
22 every 4-1/2 years, if my math is correct, to fine-tune
23 the extent to which debtors can claim exemptions. As
24 the Court is aware, in 2005 for example, the -- Congress
25 limited the extent to which a debtor could claim an

1 exemption in his homestead, I suppose precisely for
2 analogous reasoning to what Your Honor suggests.

3 It's still nonetheless perfectly clear from
4 Section 522(k) that Congress has not created or allowed
5 some sort of free-floating equitable discretion for
6 bankruptcy courts to reach a different result in cases.
7 And again I would like to point the Court to Section
8 522(c) as well, which is the companion provision to the
9 administrative expenses provision. As the Court, of
10 course, is aware, debtors often have debts arising from
11 all sorts of improper conduct, willful and malicious
12 injury, criminal restitution awards, fraud,
13 embezzlement, there is a whole list of these things in
14 Section 523 and the Code makes these debts
15 non-dischargeable, inherent per se non-dischargeable,
16 meaning that when you go through bankruptcy you are not
17 going to be able to escape paying these debts once the
18 bankruptcy is over.

19 However, in Section 522(c)(1) of the code
20 Congress picked out just two, just two of those
21 categories of debts, alimony and certain tax liability,
22 of these non-dischargeable debts that could be satisfied
23 from exempt property. The debtor who has a wrongful
24 death judgment, the debtor who has a fraud judgment, the
25 debtor who has a criminal restitution award, all of

1 those debts are non-dischargeable, they stay with the
2 debtor until they're paid, but they are expressly not
3 paid from exempt property.

4 That is a quintessential policy judgment of
5 Congress's to decide where to draw the line between
6 deterring, not making bankruptcy a haven for those who
7 seek to avoid their misconduct or engage in misconduct,
8 but at the same time recognizing that taking someone's
9 homestead -- taking someone's homestead in effect, with
10 respect, does leave them without a home, and
11 essentially --

12 JUSTICE SOTOMAYOR: When he takes that
13 \$75,000 and assuming he doesn't pay debts with it and he
14 invests it, what happens to the income on that
15 investment? Is that exempt, too, from paying off his
16 creditors?

17 MR. HELLMAN: It's actually even less
18 friendly to the debtor than that, Your Honor. Under
19 California law -- and Federal law takes State law
20 exemptions as it finds it absent a contrary Federal
21 provision -- the debtor if he ever were to receive the
22 \$75,000, by law, California law, would have 6 months to
23 reinvest it in a homestead. That's what California is
24 doing. It's saying: We are going to give you the
25 opportunity to reinvest and have a home.

1 If it's not reinvested, it's not exempt, at
2 least not for purposes of the Federal scheme going
3 forward. If it doesn't retain its exempt character,
4 then if he puts it in a bank account, that's not exempt;
5 the interest and principal, both of those are available
6 to satisfy any creditor who might -- who might be out
7 there to whom he owes funds.

8 JUSTICE SOTOMAYOR: That's California, but
9 that's not necessarily every other State.

10 MR. HELLMAN: Those States that give a
11 homestead exception, and that's 48 of 50, all, with the
12 exception of Pennsylvania and New Jersey, which use the
13 Federal homestead exemption, all of those -- the vast
14 majority of those States have a reinvestment principle.
15 I know Illinois does, I know that several other States
16 do as well, for just the reason Your Honor suggests.
17 This money is not put away in a box such that it can't
18 be touched again. The homestead exemption represents an
19 opportunity for the debtor to have a home. That's what
20 California law protects and California in its judgment
21 decided to award.

22 JUSTICE GINSBURG: Are you saying that he
23 must spend the \$75,000 on a new residence within how
24 many -- what period of time?

25 MR. HELLMAN: 6 months, Your Honor.

1 JUSTICE GINSBURG: 6 months. And if at the
2 end of 6 months he can't find a home at that price, then
3 what happens?

4 MR. HELLMAN: California law says it needs
5 to be reinvested within 6 months in a homestead.
6 Otherwise it loses its exempt character. I'm not sure
7 if there is any sort of waiver law that could be -- my
8 understanding is 6 months is the time that he has. And
9 that's California's decision. The Federal law doesn't
10 have a contrary provision that would --

11 JUSTICE GINSBURG: Then if 6 months runs,
12 and he hasn't purchased a new home, then the \$75,000
13 goes where?

14 MR. HELLMAN: It is available to his
15 creditors.

16 JUSTICE GINSBURG: They have been paid
17 already.

18 MR. HELLMAN: That's right. And the way
19 bankruptcy -- Congress has chosen to make the Bankruptcy
20 Code work is that absent any sort of special award
21 when -- when Congress has made the determination that a
22 debtor is not liable for his administrative expenses
23 once the bankruptcy case closes, even if there has been
24 a denial of discharge. Congress has determined that,
25 although a debtor will be on the hook for the debts that

1 he brought into bankruptcy, he will not be on the hook
2 for debts arising from the administrative expenses going
3 forward, because I think Congress understood that those
4 expenses might be out of the debtor's control and that a
5 debtor ought not leave bankruptcy in a worse
6 condition --

7 JUSTICE GINSBURG: So then what you said
8 before needs to be modified. He does get to keep the
9 \$75,000 because there is no creditors to be paid off
10 from.

11 MR. HELLMAN: The \$75,000 is not protected
12 from any creditor who might have a claim to it. That's
13 all I meant to suggest, Your Honor. In this case his
14 creditors have in fact been paid off and there is no
15 sanctions award or other award that would --

16 JUSTICE KENNEDY: When you say "paid off,"
17 do you mean paid off 100 percent?

18 MR. HELLMAN: The -- his primary creditor
19 was a judgment creditor who had a debt of \$160,000;
20 negotiated it down to \$120,000 in exchange for being
21 paid first. And I do mean 100 percent, yes.

22 CHIEF JUSTICE ROBERTS: So what you started
23 with, oh, this is a terrible sanction, he's denied a
24 discharge and all that, that doesn't mean a thing to
25 him, does it? Because everybody's paid off. He doesn't

1 have any debts.

2 MR. HELLMAN: This debtor does not have any
3 remaining debts. Most debtors, however, because of the
4 way the priority scheme works in bankruptcy, will be
5 paying their administrative expenses first and have
6 their obligations come second. And, of course, if there
7 is a non-dischargeable debt, as I said, then even
8 without a finding of non-dischargeability, those stay
9 going forward.

10 And I want to emphasize again that we are
11 not talking here -- my friends on the other side suggest
12 that this is sort of from a deep tradition of the
13 inherent power of a court to sanction. This is not
14 about that power. This is about the property from which
15 a sanction award can be paid. There is no tradition
16 supporting that award.

17 And, of course, as this Court said in
18 Owen v. Owen, where the code is clear -- and I don't
19 think, with respect, it could be much clearer than
20 saying not liable for any administrative expense, save
21 in two situations not present here -- that is the
22 code -- that is the language that controls.

23 CHIEF JUSTICE ROBERTS: I should know this,
24 but who's going to get stuck with the extra couple
25 hundred thousand dollars? Is that the trustee in an

1 individual capacity or someone else?

2 MR. HELLMAN: It's really the trustee's law
3 firm, which is an arm of the trustee.

4 CHIEF JUSTICE ROBERTS: They don't recoup
5 that from anywhere else, right? They are on the hook
6 for that?

7 MR. HELLMAN: That is correct, Your Honor.
8 That is correct.

9 Now, the primary authority --

10 JUSTICE KENNEDY: Do they get a thank-you
11 letter from the --

12 (Laughter.)

13 MR. HELLMAN: The primary authority that my
14 friends on the other side used to support their reading
15 of the statute is the Marrama case. And I want to
16 emphasize, that case does not support the proposition
17 that bankruptcy courts can violate specific provisions
18 of the code if they believe equity warrants another
19 result.

20 In Marrama, the court was -- the Marrama
21 majority was clear to note that no provision of the code
22 expressly forbid the result that the court was going to
23 allow, and that 105 -- Section 105 in that case was
24 being used to accomplish something the code permits and
25 to do it promptly rather than in a delayed fashion.

1 This case is not about prompt versus
2 delayed. This is about doing what the code expressly
3 forbids. This case is not about what Section 105
4 allows. This case is about what section 522 expressly
5 forbids.

6 And, here, Congress has made the judgment,
7 considering all the different turn mechanisms and policy
8 interests at play, Congress has made the judgment that
9 administrative expenses are not liable for any
10 administrative -- exempt property is not liable for any
11 administrative expense.

12 JUSTICE ALITO: In the Malley case, Justice
13 Souter said that if this is not what Section 105(a) was
14 intended for, it's hard to see what Section 501(a) was
15 intended for. I take it you just think he's flatly
16 wrong.

17 MR. HELLMAN: We do disagree, Your Honor.
18 The equities in that case, I suppose, are sharper in the
19 sense that the debtor is leaving bankruptcy with more
20 money than he otherwise would be able to have. But it
21 is just as clear in that case that Congress has not made
22 the exception that -- it's more than -- this is not a
23 negative implication case. I want to stress that. It's
24 not just that Congress hasn't put this on the list of
25 things that can't be done. Congress has a flat-out

1 prohibition the structure is not liable for any
2 administrative expense or any prepetition debt, save in
3 the enumerated circumstances.

4 So, yes, with respect, I do think Malley was
5 wrongly decided, and this Court need do nothing more
6 than reaffirm what it has done for 80 years, which is to
7 say that 105 gives bankruptcy courts the power to act.
8 Our position is quite modest. We're only saying they
9 can't do what the code forbids. Whether the code is --
10 whether they're acting interstitially or they're acting
11 to carry out express provisions of the code, of course
12 that's what 105 does.

13 The scholars brief that is submitted on our
14 side on pages 21 to 26 lists a bevy of practices that
15 will -- that should and will continue unabated because
16 they -- under Section 105 by bankruptcy courts to carry
17 out the administration of justice, because there are
18 things that the code does not expressly forbid.

19 JUSTICE KAGAN: But, Mr. Hellman, (k) of
20 course talks about exempt property.

21 MR. HELLMAN: Yes.

22 JUSTICE KAGAN: Is there a possibility of
23 reading the statute such that the exemption just never
24 comes into effect? If you look at 522(1) --

25 MR. HELLMAN: Yes.

1 JUSTICE KAGAN: -- (1) says, "unless a party
2 in interest objects, the property claimed as exempt is
3 exempt." Now, that suggests that if the party in
4 interest does object, there's a question about whether
5 the party claimed as exempt is exempt.

6 So -- so why isn't it a permissible reading
7 of the statute to essentially say the court gets to
8 decide whether this is exempt property such that (k)
9 comes into effect, and in deciding whether it's exempt
10 property, it can take into account the Petitioner's
11 abuse of process?

12 MR. HELLMAN: Two points. Of course, no
13 objection was ever lodged within the time period that
14 rule --

15 JUSTICE KAGAN: Yes. I completely agree
16 with that, but suppose one were.

17 MR. HELLMAN: That objection -- that
18 objection would not be well founded because it is
19 undisputed that Petitioner is entitled to his homestead
20 exemption under California law. California law says
21 this is his home, he's lived there for the requisite
22 amount of time, he has the equity, all of that.

23 Congress later, in provisions that wouldn't
24 apply to this case either, put some limits on a debtor's
25 ability -- Federal limits on a debtor's ability to claim

1 his homestead exemption; if money is poured into the
2 home before declaring bankruptcy, Congress cut back on
3 that a little bit. And I suppose you could have an
4 objection on that basis.

5 But this was not a case in which the
6 Petitioner lost his exemption because he wasn't entitled
7 to it. To the contrary, at page 69a of the appendix,
8 the court observes this is the exemption to which he's
9 otherwise entitled, but it's his -- the court found that
10 his litigation misconduct warranted taking away what he
11 was otherwise entitled to under Section 522(1) and
12 protected by (k) and (c).

13 JUSTICE ALITO: So you're saying a creditor
14 could not have objected when your client claimed the
15 exemption on the ground that the exemption is going to
16 prevent the discovery -- the disclosure of the
17 fraudulent nature of this mortgage. The creditor could
18 not have objected to the exemption on that basis?

19 MR. HELLMAN: The objection was proper. So
20 the answer to your question is yes, no objection -- no
21 objection would have been proper in that situation
22 because --

23 JUSTICE ALITO: And why is that?

24 MR. HELLMAN: Because Section 522, the way
25 it works is that the question is are you entitled to the

1 exemption under State law. That's what Section 522(b),
2 I believe, asks you to look at. And then there's a
3 question of is an objection going to be interposed
4 within the period provided by Section 522(l).

5 Congress, of course, is free to create other
6 limitations on a debtor's ability to claim exemptions.
7 And as I said, they have done that in Section 522(o),
8 Section 522(p), Section 522(q), which deals
9 specifically, by the way, with situations in which the
10 very filing of the bankruptcy case is a -- is an abuse
11 of the code. And in that case, in Section 522(q),
12 Congress ultimately decided that for debtors whose
13 fraud -- and is convicted of a felony whose filing of
14 the case shows that it's an abuse of the code, Congress
15 decided in those cases that a debtor should not lose all
16 of his exempt property.

17 They put a cap in at \$155,000, which, as
18 Your Honor points out, is quite generous, quite generous
19 given the median income of -- of the American family;
20 and further stated that exemption could be tilted upward
21 where necessary to support the debtor and his
22 dependents. Not downward, no discretion to go downward,
23 but can go upward, if necessary, in the bankruptcy
24 court's view to support the debtor -- reasonably
25 necessary to support the debtor and his dependents.

1 So Congress -- so your question was could
2 there have been an objection? The answer is no. And I
3 would just say in passing that Congress has decided and
4 has amended the statute several times to fine tune
5 exactly when it is -- there ought to be or could be an
6 objection to property validly claimed as exempt under
7 State law.

8 This is not one of those cases; far from it.
9 And, again, I want to stress, this is not an argument
10 from negative implication. This is not an argument from
11 interstices. This is an argument from express and
12 categorical prohibition.

13 And if there are no further questions, I'll
14 reserve the balance of my time.

15 CHIEF JUSTICE ROBERTS: Thank you, counsel.

16 MR. HELLMAN: Thank you.

17 CHIEF JUSTICE ROBERTS: Mr. Katyal.

18 ORAL ARGUMENT OF NEAL K. KATYAL

19 ON BEHALF OF THE RESPONDENT

20 MR. KATYAL: Thank you, Mr. Chief Justice,
21 and may it please the Court:

22 The facts explain why the bankruptcy court
23 exercised its discretion appropriately under both
24 Section 105(a) and the longstanding inherent power of
25 the court. Mr. Law committed a massive fraud on that

1 court with the fake mortgage and fake documents.
2 Petitioner lied repeatedly to the court, and then lied
3 about his lies, all in an attempt to retain nonexempt
4 property and equity in his home in contravention of the
5 code.

6 Section 105(a) was made for a case like
7 this. It provides ample authority for what the
8 bankruptcy court did, both in its first sentence, which
9 uses a sweeping formulation of any order necessary or
10 appropriate and as well as its second sentence which
11 gives bankruptcy courts, quote, "the broad authority to
12 take any action that is necessary or appropriate to
13 prevent an abuse of process." That is the language
14 Marrama used to describe the second sentence, and it
15 fits here perfectly.

16 JUSTICE SOTOMAYOR: My problem is -- my
17 problem is that I read the sentence and it lops off its
18 beginning. What the beginning says is "No provision of
19 this title providing for the raising of an issue by a
20 party of interest can stop a court from doing that." An
21 abusing process, presumably.

22 So how could a party legitimately, whether
23 the trustee or anyone else, make any claims to the
24 exempt property?

25 MR. KATYAL: Justice Soto- --

1 JUSTICE SOTOMAYOR: How can the Court do
2 something neither the Bankruptcy Code nor any of its
3 provisions permit the trustee to do?

4 MR. KATYAL: Justice Sotomayor, for
5 precisely the reasons that both Marrama and Justice
6 Souter in the Malley case suggested, which is at the
7 second sentence fortifies --

8 JUSTICE SOTOMAYOR: That's your strongest
9 argument, that Justice Souter --

10 MR. KATYAL: Well, it's at the second
11 sentence fortifies the first; that is, the way to
12 understand the second -- the power of the court and the
13 orders that are necessarily appropriate. One such power
14 is to remedy fraud upon the court, the abuse of process.
15 That's what Congress used.

16 JUSTICE SOTOMAYOR: My problem is that the
17 code itself doesn't do that. It limits the access to
18 the exemption to specified frauds, to frauds that result
19 in a conviction. To amounts, it doesn't permit the
20 exemption -- it -- it does away with the exemptions for
21 an amount above 155.

22 So if the code doesn't permit full recovery
23 for fraud, why should a court be permitted to do it?

24 MR. KATYAL: Well, of course, that provision
25 wasn't in effect at the time. That's 522(q) which you

1 are referring to. But we think 522(q) doesn't -- isn't
2 violated here. Absolutely, you're right, Justice
3 Sotomayor, if there were a violation of 522(q), 105(a)
4 couldn't take that back.

5 But the language of 522(q), which is found
6 in the blue brief at page 19a of the appendix, just says
7 that if there is a circumstance of a felony -- it
8 doesn't even mention fraud -- but if there is a felony
9 that occurs and -- in the filing of the petition, then
10 it says that -- that you can't get more than -- you
11 shall not exceed \$156,000.

12 It says nothing about the longstanding power
13 of the court to depart downward and to give up to zero.
14 It's just like a punitive damages cap. So Florida's
15 punitive damages law says that if you have -- if you're
16 the victim of medical malpractice or something, you can
17 get up to \$500,000. You shall -- your award shall not
18 exceed \$500,000.

19 But of course, that doesn't take back the
20 power of the factfinder to say you shall get nothing in
21 a particular case. And this is a perfect illustration
22 of a case in which a debtor should get nothing.

23 Mr. Law tried to invoke the protections of
24 the code while he repeatedly defied the obligations
25 under the code at every turn.

1 JUSTICE SOTOMAYOR: Would you ask -- would
2 you answer Justice Breyer's question? Does this power
3 go to invading the other exempt properties, like an IRS?
4 I'm assuming there are now invasion provisions for an
5 IRS, but would this power permit the court to invade an
6 -- not an IRS --

7 JUSTICE BREYER: An IRA.

8 JUSTICE SOTOMAYOR: Thank you. An IRA.

9 MR. KATYAL: Our argument here is just
10 limited to this type of case in which you're lying about
11 the underlying asset itself and trying to seek an
12 exemption. I know the Solicitor General advances a
13 broader argument, and I suppose that the Court can deal
14 with that in an appropriate case.

15 But here, Mr. Law undervalued his home and
16 put all of these fake mortgages on, and then repeatedly
17 submitted perjured documents to the court about the very
18 exemption. And as Justices -- Justices Ginsburg and
19 Alito said before, what's a Trustee to do in that
20 situation except investigate? That's his duty under
21 Section 704, to try and figure out what has happened.

22 CHIEF JUSTICE ROBERTS: Well, he'd have to
23 investigate to the tune of half a million dollars
24 chasing a much smaller amount that is at issue.

25 MR. KATYAL: Well, I think,

1 Mr. Chief Justice, that's the wrong way to look at it,
2 with all respect. For one thing, of course, the -- the
3 trustee's actions allowed title to be cleared and the
4 underlying house to be sold for \$680,000, paying off all
5 the creditors.

6 If Mr. Law's representations were accepted
7 -- and this is something the Bankruptcy Court found at
8 page 77 -- the trustee would have had to abandon the
9 property altogether. That's \$680,000 that nobody would
10 have gotten. So that's the first thing.

11 And the second thing is, of course, that
12 when the trustee started his investigation and realized
13 there was a fake mortgage, he would have never thought
14 that this would have become, as you said, a
15 half-million-dollar case. He would have thought, well,
16 look, these documents prove this is a fraud.

17 But what Mr. Law did in response was to take
18 19 separate appeals to -- you know, 14 to the bankruptcy
19 appellate court, five to the Ninth Circuit. I mean, you
20 know, I looked at --

21 JUSTICE BREYER: He behaved very badly, and
22 in view of this, I agree with that. Why wouldn't -- or
23 why didn't the -- or why couldn't the trustee simply
24 sanction? I mean, you have apparently the authority
25 here in 105 to sanction conduct abusive of the judicial

1 process. That includes an order directing payment of
2 expenses. Okay. I guess this is an expense. And that
3 wouldn't be discharged, because it's a postpetition
4 debt.

5 So why not just do that? And even if he
6 doesn't have money now, if he ever gets any he's going
7 to have to pay it. So it looks as if there's an
8 alternative way of payment.

9 MR. KATYAL: So two responses. First of
10 all, as to the existence of an alternative sanction, I
11 think this Court in Chambers was very clear in saying
12 that doesn't displace other powers of the court.

13 JUSTICE BREYER: No, it doesn't. But why,
14 when you have pretty clear language saying this shall
15 not be used for administrative expense --

16 MR. KATYAL: Because for --

17 JUSTICE BREYER: -- and you have general
18 language over here saying a general power to sanction,
19 and you have an alternative way that's perhaps almost as
20 good, why read the language that says no to say, well,
21 yes?

22 MR. KATYAL: I want to respond to why there
23 isn't an expressed prohibition in a minute. But just
24 taking your point before, the reason is the facts of
25 this case. That is, the sanction would only be paid out

1 of postpetition debt. And I think there's a pretty good
2 reason why my friend's brief on the other side is
3 willing to entertain sanctions and the like, because he
4 would engage in the same type of conduct that he has
5 now, repeatedly stymying the court in the ability to try
6 and get that \$75,000 sanction, should it ever be
7 imposed.

8 And so that -- so sanctions come from
9 postpetition assets. And that's I think one of the
10 problems.

11 Now, with respect to the bigger question, is
12 there a prohibition somewhere in the code? We don't
13 think there is. We don't think 522(k) says anything
14 like what my friend said in his opening sentence, that
15 this is somehow an express prohibition. We think that
16 the language of 522(k) has to be read against three
17 different things: The first, Section 105(a) and its
18 sweeping language; second, something you never heard a
19 word about in my friend's argument on the other side,
20 which is the longstanding presumption that the
21 protections of the Bankruptcy Code are meant for the
22 honest but unfortunate debtor; and third, language in
23 522 which Justice Kagan alluded to which suggests that
24 someone is not entitled to the right of an exemption,
25 and the court can take it -- the court can refuse to

1 provide it in the first place.

2 JUSTICE BREYER: If he has the exemption,
3 (k) says: "Property that the debtor exempts under this
4 section is not liable for payment of any administrative
5 expense." That's why I thought it seemed a fairly
6 definite no, unless you read the general knowledge and
7 tradition to mean yes.

8 MR. KATYAL: I think you have to read the
9 language of 522(k), which was enacted in 1978, against
10 the fact that Section 105(a) was on the books and indeed
11 enhanced in 1978.

12 JUSTICE KAGAN: I think that's a little bit
13 backwards, right? Doesn't 105 exist to the extent that
14 there's no prohibition saying otherwise? And then
15 522(k) comes in, and there's your prohibition.

16 MR. KATYAL: No, because I think in order to
17 understand what the prohibition was, you have to -- you
18 have to look to 105(a); that is, what 105(a) does is it
19 says, in general, you have this power. And indeed,
20 522(k), I think it speaks of the general case in which
21 there isn't this type of excessive bad faith, fraud on
22 the court.

23 And so absolutely, I think in general, just
24 as in Marrama itself, there's general language which
25 says administrative expenses normally aren't liable.

1 But in the atypical case, to use Marrama's words, a case
2 like this in which the only way the code would work and
3 functionally work is to incentivize trustees to try and
4 uncover the fraud.

5 JUSTICE KAGAN: So but then you're saying
6 essentially that every provision in the Bankruptcy Code
7 ought to be read with an addendum that says, "Except if
8 there's an abuse of process."

9 MR. KATYAL: Your Honor, I think that's what
10 generally both the Hunt prohibition and indeed the first
11 line of Marrama says, which is that the basic idea of
12 the Bankruptcy Code is to provide honest but unfortunate
13 debtors a system of relief. And it misses the forest
14 for the trees to essentially look with tunnel vision
15 just at (k). (K) exists within a larger framework of
16 background duties and obligations that a debtor must
17 comply with.

18 A debtor can't come in and say, oh, I've
19 just met 522. It presupposes they've already met, for
20 example, 5 -- Section 521, which is a truthful
21 disclosure of assets and liabilities.

22 And if you adopt Mr. Law's formulation,
23 you're essentially saying that the main architect -- the
24 main safeguard against this type of abuse, the trustee,
25 is left holding the bag at the end of the day. The

1 trustee is the only one here who acted, I think,
2 appropriately, trying to uncover all of this, and he
3 would be stuck with hundreds of thousands of dollars in
4 attorneys' fees.

5 JUSTICE BREYER: But couldn't the --
6 couldn't the bankruptcy judge just deny him, deny him
7 bankruptcy?

8 MR. KATYAL: Yes, he can deny him
9 bankruptcy, but that doesn't solve the underlying
10 problem that Mr. Law would still have \$75,000 in assets
11 that he is trying to seek under his exemption and the
12 trustee has spent hundreds of thousands of dollars
13 trying to unravel that scheme.

14 JUSTICE SOTOMAYOR: How do you limit in a
15 principled way -- you say where you differ with the
16 Solicitor General is that if an -- if an IRA had existed
17 here, they would say that could be used. And you're
18 saying, I don't need to go that far. That's on the
19 facts. But on what theory would you limit recovery in
20 those situations?

21 MR. KATYAL: Well, we're not advocating for
22 a limit, but I suppose if one -- if the Court wanted to
23 find one, they'd find it in Chambers itself, which said
24 that the inherent power of the court is something that
25 could be exercised sparingly and only in extreme cases.

1 And if -- if there is a situation in which, you know, if
2 some sort of forfeiture was a massive amount compared to
3 the underlying fraud on the court, that wouldn't be
4 appropriate. That would be reviewed under abuse of
5 discretion. All we are suggesting here --

6 JUSTICE KENNEDY: That's hard to enforce.
7 Every lawyer's case is an exceptional case. That's just
8 the way it works.

9 MR. KATYAL: Well, but I think that's a
10 problem that -- with Chambers itself, Justice Kennedy,
11 and I think the courts have figured out ways to deal
12 with that problem, by saying it's only reserved for the
13 exceptional case and this is really truly that case.

14 This is not just fraud on the Court, it's
15 fraud on the Court squared. They're lying about the
16 lies themselves. And the bankruptcy court can't work,
17 it can't function if you don't have the trustee
18 incentivized to under -- to undertake the kind of
19 investigation that occurred here.

20 My friend talks about denial of discharge or
21 criminal penalties being ways to try and deal with this,
22 but all of those sanctions depend on the action of the
23 trustee to uncover the fraud in the first place.

24 And when you have someone like Mr. Law,
25 who's a serial liar to the Court, this isn't just bad

1 faith, Justice Kennedy. This isn't just, you know, one
2 document that is wrong by 5 or \$10, this is repeated
3 perjury to the Court. And that is the quintessential
4 thing Section 105 is about when it talks about abuse of
5 process.

6 If you don't permit equitable forfeiture
7 here, you are essentially giving effect to Mr. Law's
8 abuse of process. With respect to the underlying --

9 JUSTICE BREYER: It made me think of a --
10 think of a bankruptcy petitioner who, in part, has a
11 debt arising towards a creditor that consisted of the
12 most frightful conduct you can think of. I mean,
13 something really awful that he did to somebody. And yet
14 that debtor can be excused, bankrupt, and keeps the
15 \$75,000.

16 Now, while lying to a bankruptcy trustee is
17 bad, it's not hard for us to think of conduct that's far
18 worse. And yet, he can keep the \$75,000. Why should --
19 why should this particular form of bad conduct allow the
20 invasion of the homestead?

21 MR. KATYAL: For two reasons,
22 Justice Breyer, because Section 105(a), as well as the
23 inherent power of the Court deal with specifically this
24 type of situation, abuse of process, fraud on the Court
25 itself, not any type of prepetition conduct or anything

1 like that. It's targeted to this. And, of course, the
2 language in 522(q), which we were talking about earlier,
3 is only about that prepetition conduct. It doesn't
4 have -- so absolutely. Congress is free, if they want,
5 to abrogate 105(a) or the inherent power of the Court
6 and to say, look, if you've engaged in bad faith, fraud
7 on the Court, whatever, you're still entitled to your
8 exemption. That's not what it says.

9 To the contrary, and this picks up on
10 Justice Kagan's point earlier, 522(l) and (v) provide a
11 mechanism to reject an exemption that is being sought.
12 And here, that happened. 522(l) says -- and this is
13 laid out at our brief at pages 38 and 39 -- if someone
14 raises an objection to an exemption that a debtor is
15 seeking, that exemption can be denied.

16 JUSTICE GINSBURG: I thought the objection
17 had to be raised by a creditor within a certain time.

18 MR. KATYAL: It doesn't --

19 JUSTICE GINSBURG: I thought -- isn't there
20 a provision that says, and if there's no objection, the
21 exemption is what is claimed?

22 MR. KATYAL: 522(l) doesn't say that. It
23 refers to a party in interest, which could be a trustee
24 as well. And so here, we think both the trustee
25 objected in filing the motion for -- in 2006 as well as

1 the Court itself. Section 105 has to be read alongside
2 522, and it provides the Court the sua sponte power to
3 do so.

4 There is a time limit, Justice Ginsburg, in
5 Rule 403, but that time limit can itself be extended if,
6 under the terms of the rule, if there's been a
7 subsequent amendment of the underlying schedule. And
8 here we think effectively, there was a subsequent
9 amendment of the underlying schedule; that is, Mr. Law
10 lied.

11 And I think there's a very strong reason why
12 the time limit shouldn't apply here. Imagine that a
13 debtor took a fake set of exemptions and bribed the
14 trustee to look the other way for 30 days. If that were
15 discovered on day 45, I think it would be thoroughly
16 implausible to think that you could -- that the debtor
17 could get the underlying exemption, something that he
18 bribed and lied about just because it didn't meet the
19 30-day requirement.

20 JUSTICE GINSBURG: Maybe you get it from the
21 trustee.

22 MR. KATYAL: I think that --

23 JUSTICE GINSBURG: The faithless trustee.

24 MR. KATYAL: You might be able to go after
25 the trustee as well, but I don't think that the

1 underlying exemption would be given in that
2 circumstance. It's a paradigmatic instance of both the
3 105(a) power as well as the inherent power of the Court.

4 JUSTICE KENNEDY: I recognize the problem
5 that if you have sanctions, that he can't pay the
6 sanctions and you're right back where you started. But
7 are there cases in which there are sanctions imposed of
8 an amount such as \$75,000, \$100,000?

9 MR. KATYAL: Sure. There's been a -- there
10 have been a number of cases, the red brief talks about
11 them at page 32 going all the way back, in which the
12 exemptions have been denied altogether for purposes of
13 bad conduct. And we think this case falls within that.

14 JUSTICE ALITO: Well, Mr. Hellman said that
15 the creditor and, I guess, any other party could not
16 object to the exemption on the ground that the house was
17 burdened with a fraudulent mortgage. Do you agree with
18 that?

19 MR. KATYAL: I don't. I don't think
20 anything in the language of 522(1) so restricts it.
21 There are other provisions in the Code which say if an
22 objection has been made, for example, to a creditor
23 under Section 502, that the Court's power to deny that
24 relief is circumscribed in 9 different ways. But there
25 is no restriction on the power of the Court here. And

1 that's why I think Justice Kagan's question gets at this
2 point, which is 522(k) assumes that an exemption has
3 been given, and there's a strong reason under the Code
4 the Court is given the power to deny an exemption in the
5 first place.

6 JUSTICE ALITO: Do you have any authority
7 that says that there could be an objection on that
8 basis?

9 MR. KATYAL: I think just the text at 522
10 itself says so.

11 If there are no other questions.

12 CHIEF JUSTICE ROBERTS: Thank you, counsel.

13 Ms. Harrington.

14 ORAL ARGUMENT OF SARAH E. HARRINGTON,

15 FOR UNITED STATES, AS AMICUS CURIAE,

16 SUPPORTING THE RESPONDENT

17 MS. HARRINGTON: Thank you,
18 Mr. Chief Justice, and may it please the Court:

19 I'd like to start, if I could, by taking a
20 little bit of a step back to note that outside of the
21 bankruptcy system, an individual who runs up more debts
22 than they can satisfy with their collective assets has
23 no right to wipe out those debts while retaining some of
24 their property in the face of unpaid assets. That right
25 only comes from the Bankruptcy Code itself. But you

1 only get that right if you follow the rules of
2 bankruptcy.

3 The Petitioner asked this Court to
4 myopically focus on certain provisions of the Code and
5 only provisions of the Code that actually benefit the
6 debtor. But you have to look at any provision of the
7 Code in the context of the whole Code itself because all
8 the provisions are intended to work together.

9 In this case, the surcharge order was
10 necessary and appropriate to enforce provisions such as
11 Section 521 and Section 704 of the Code. Section 521
12 imposes duties on debtors. Those duties include the
13 duty to honestly disclose assets and liabilities, the
14 duty to turn over property to the estate, to the
15 trustee, and the duty to cooperate with the trustee
16 throughout the case.

17 Now, Mr. Law flouted all of those
18 obligations, making it impossible to carry out the
19 provisions of those parts of the Code without
20 surcharging him in some way.

21 Section 704 imposes duties on the trustee.
22 Those duties include the duty to investigate the
23 financial affairs of a debtor and the duty to collect
24 the property of the debtor, reduce it to money and give
25 that money to creditors. And the trustee doggedly

1 pursued his duties under Section 704, but because of Mr.
2 Law's bad faith litigation behavior, he imposed a great
3 cost on the exercise of those duties. And so the
4 Bankruptcy Court exercised its discretion to try to
5 offset some of those costs by imposing a surcharge on
6 what would have otherwise been exempt property of the
7 debtor.

8 JUSTICE KAGAN: Ms. Harrington, you clearly
9 have the facts on your side. The question is whether
10 you have the law. And -- and 522(k) says, as
11 Justice Breyer said, "Property that the debtor exempts
12 under this section is not liable for payment of any
13 administrative expense."

14 Now, as I read your brief, you're
15 essentially asking us to put the word "usually" in that
16 provision. Is not usually liable. When is it -- when
17 is it liable? It's -- it's liable when there are
18 special circumstances dealing with debtor dishonesty.
19 And where does that come from?

20 MS. HARRINGTON: What we're asking to do is
21 look at all the provisions of the Code together. And
22 certainly, Section 522(k) expresses Congress's policy
23 judgment that generally honest debtors should not have
24 their exempt property used to pay administrative
25 expenses. But as I've said, 521 and 704 express

1 Congress's policy judgments about what debtors are
2 supposed to do and what trustees are supposed to do.
3 And Section 105 give -- gives Bankruptcy Courts
4 authority to address very unusual circumstances that
5 involve bad faith litigation conduct. So that's bad
6 conduct in the litigation.

7 I think that is an implicit exception to
8 most of the general rules that are laid out in the
9 Bankruptcy Code.

10 In this case, it's really impossible for the
11 Court to have carried out all of the provisions of the
12 Code, but that's directly because of the debtor's
13 behavior in this case, Petitioner's behavior. And so
14 here in this extraordinary circumstance, the Bankruptcy
15 Court addressed that bad faith litigation behavior by
16 exempting what otherwise would have been -- by -- excuse
17 me -- surcharging what otherwise would have been exempt
18 property.

19 CHIEF JUSTICE ROBERTS: What is the -- you
20 do have good facts on your side. But what if the
21 offense is simply the failure to list a particular
22 asset? Does that justify a departure from the usual
23 rule?

24 MS. HARRINGTON: I mean, if it's a
25 negligent -- negligent failure to list the asset, then I

1 don't think --

2 CHIEF JUSTICE ROBERTS: You know, it's a --
3 it's a bank account that's held in, you know, a separate
4 name or it's separate real estate. It's fairly common
5 for debtors to leave off some assets they want to
6 conceal. Is that, as a general rule, sufficient to
7 justify this unusual authority?

8 MS. HARRINGTON: I think if they do it in
9 such a way that then they spend the assets -- so the way
10 this issue usually comes up, the way it's come up in
11 most of the courts of appeals is that a debtor tries to
12 hide a nonexempt asset and then wastes the asset in some
13 way, usually by spending it, and then when it's
14 discovered, this is how it came up in the Malley case in
15 the First Circuit, then the Bankruptcy Court surcharges
16 the exempt property to sort of compensate the estate for
17 the wasted nonexempt property.

18 And so I think that -- that's certainly, in
19 our view, an appropriate exercise of authority under
20 Section 105, because there, the debtor is trying to --
21 he doesn't necessarily exit the bankruptcy with more
22 money than he would be entitled to, but he has more
23 money during the bankruptcy and he spends that money --

24 CHIEF JUSTICE ROBERTS: Well, then it --
25 then it becomes a not very unusual exercise of

1 authority. It becomes pretty common since the
2 concealment of nonexempt assets is a fairly -- I don't
3 want to say it happens all the time -- but it's a fairly
4 common situation.

5 MS. HARRINGTON: I don't think it happens
6 terribly often, and when it does happen it isn't very
7 often that the debtor spends the money that he's
8 concealing. He's usually trying to keep the money. And
9 so if it's discovered that he has hidden an asset that
10 he should have turned over, then the Bankruptcy Court
11 can merely order him to turn over the money, to turn
12 over whatever the asset was. It only -- it is only
13 necessary to surcharge what would otherwise be exempt
14 property if that nonexempt asset no longer exists.

15 Here, of course, it's a little bit of a
16 different situation. This Petitioner imposed enormous
17 costs on the estate, radically depleted the value of the
18 estate by requiring the trustee to run up huge
19 attorneys' fees in order to effectuate his duties under
20 the code.

21 JUSTICE BREYER: Is there any case law --
22 because 522 says in (b), it says "The following property
23 may be exempt." It doesn't say it has to be. So is
24 there any case law where the debtor writes down, you
25 know, a piece of property and a creditor comes in and

1 says: He can't exempt that he has behaved outrageously,
2 and it fits within the category, but he has behaved
3 outrageously. Is there any case law that says under
4 those circumstances the bankruptcy judge can refuse the
5 exemption one way or the other?

6 MS. HARRINGTON: None that I am aware of.
7 And our view of the case is not so much that the
8 exemption was denied in this case, but that the --

9 JUSTICE BREYER: I mean, you first have to
10 get to the thing where the -- we are pretending to put
11 the creditor, the bankruptcy judge, as if he were
12 another creditor. The thing, the property, appears on a
13 list that says exempt. And then the trustee or the
14 judge says: No, I'm not going to let you exempt it.
15 And that's basically what he's done.

16 MS. HARRINGTON: Well, the majority of the
17 cases, it's not so much that there's been an objection
18 to the exemption, so much as the exemption has been
19 disallowed at the end of the case or surcharged.

20 But I'm glad -- you know, in the
21 hypothetical you posited, it's the creditor who is
22 expending effort and potentially incurring attorneys'
23 fees in order to expose a debtor's fraud. And in that
24 case, those would not be administrative expenses, and
25 you would think that, at least under the Court's

1 inherent authority -- under --

2 JUSTICE BREYER: You see what I mean? Not
3 only is it administrative expenses, but you have to
4 somehow say, well, the judge is a constructive creditor,
5 and he constructively objected. There are an awful lot
6 of "constructive's" in that sentence that I just gave
7 you.

8 MS. HARRINGTON: Right. And, again, that's
9 not our view. Our view is that the exemption was
10 disallowed, that the debtor is not allowed the benefit
11 of the exemption.

12 But if the creditor had been the one who ran
13 up the attorneys' fees, he could certainly be paid under
14 the court's inherent authority, as in *Chambers v. NASCO*,
15 and it would be strange to think that the trustee is the
16 only person who couldn't be paid in this sort of
17 circumstance just for doing what the code tells him he
18 has to do.

19 JUSTICE GINSBURG: Ms. Harrington, at the
20 cert stage in this case, the Government suggested the
21 distinction between two situations: One, an action by
22 the debtor to remove property from the estate, leaving
23 the creditors unsatisfied. And that's where you say
24 this power of exemption can be taken away. And then the
25 other side was where the creditors are paid in full and

1 only the trustee's litigation expenses are at issue.

2 Are you dropping that distinction?

3 MS. HARRINGTON: No, Justice Ginsburg, I
4 think -- I think the distinction we were trying to make
5 was more what I was discussing with the Chief Justice,
6 which is when a debtor wastes nonexempt assets and can't
7 turn over, nonexempt property, can't turn it over to the
8 estate, and so then is forced to turn over exempt
9 property so that the surcharge doesn't pay attorneys'
10 fees; it just compensates the estate, and by extension
11 the creditors, for property that should have been turned
12 over.

13 Our suggestion was that this case, you could
14 decide the case on a narrow grounds and it wouldn't
15 necessarily resolve the issue in those other cases,
16 because in this case the sanction was to pay attorneys'
17 fees, which under a court's traditional inherent
18 authority, a court can order one party to pay another
19 party's attorneys' fees when it's in response to
20 extraordinary bad faith litigation conduct.

21 Now, even in *Chambers v. NASCO*, it's true
22 that the Court was divided in that case, but it was
23 mostly divided about whether the bad faith in that case
24 was in the litigation or before the litigation. Here,
25 there is really no doubt that all of the bad faith

1 conduct in this case is in the litigation. And that's
2 really a very traditional exercise of the court's
3 inherent authority to sanction that type of behavior
4 through attorneys' fees.

5 I think it's important to note also in this
6 case that the available remedies really are insufficient
7 to deal with this debtor's misconduct. He suggests
8 dismissal, discharge, and Rule 11 sanctions. Of course,
9 dismissal wouldn't do anything to punish him because his
10 creditors have been paid and he would just exit the
11 bankruptcy with all of the exempt property he would have
12 gotten if he had been honest.

13 The same thing with discharge. He was
14 denied a discharge of his debts, but then after that the
15 trustee sold his house, and it sold for \$300,000 more
16 than he had represented it was worth. And so all the
17 creditors were paid. And so that really had no
18 practical effect in this case.

19 It's also not clear that Rule 11 would be
20 sufficient to fully compensate the Trustee for the
21 expenses that have been incurred, because Rule 11
22 sanctions generally aren't available for matters on
23 appeal. And as the record reveals, much of the expenses
24 that were incurred in this place -- in this case
25 resulted from the debtor's more than a dozen appeals to

1 the Bankruptcy Appellate Panel and to the court of
2 appeals.

3 JUSTICE KAGAN: I'm not sure I understand
4 that. Are you saying that the court could not just have
5 fined him, let's say, \$100,000 or however much he
6 wanted, however -- whatever the costs were, and that he
7 could get that out of the debtor's future earnings?

8 MS. HARRINGTON: So our view is that he
9 could have -- the court could have imposed a sanction,
10 and that would not have been a prepetition debt, so it
11 wouldn't have been discharged. And if the court had
12 ordered the debtor to pay the money on pain of contempt,
13 he could have enforced that order notwithstanding any
14 State law provision that would have exempted the
15 property after the bankruptcy.

16 CHIEF JUSTICE ROBERTS: Thank you, counsel.

17 Mr. Hellman, you have 5 minutes remaining.

18 REBUTTAL ARGUMENT OF MATTHEW S. HELLMAN

19 ON BEHALF OF THE PETITIONER

20 MR. HELLMAN: Thank you, Your Honor. Just a
21 few brief points in rebuttal.

22 I think from the litany of punishments that
23 the Government has pointed to in this case, the question
24 here is not whether a Bankruptcy Court can sanction a
25 dishonest debtor. It can. The question is what

1 sanctions has Congress forbidden or allowed. This is a
2 case in which Congress has drawn a line and said exempt
3 property may not be used to satisfy any administrative
4 expense.

5 My second point is that I think there may
6 have been some confusion about what it is to claim an
7 exemption under the Bankruptcy Code. If you look at
8 Section 522(b) of the code, what you'll see is that a
9 debtor is allowed to claim an exemption, may claim an
10 exemption, under State law or Federal law, depending on
11 the scheme that the State has opted into.

12 The right to the exemption is a product of
13 State law unless Federal law says otherwise. And
14 Federal law has started to say otherwise in the
15 Bankruptcy Reform Amendments of 2005. Congress saw a
16 problem in 2005 where debtors were pouring money into
17 their homesteads, then declaring bankruptcy, and then
18 seeking to have all of that property be claimed as
19 exempt.

20 Congress amended Section 522 to deal with
21 that problem, to place limitations on that type of
22 misconduct. Congress has not created a generalized
23 equitable discretion exception to Section 522. And I
24 suggest that the reason it has not done that is because
25 we're talking about exempt property, the core property

1 of the debtor.

2 And it would dramatically shift the power
3 between trustee, as the Chief, as Mr. Chief Justice was
4 suggesting, dramatically shift the power between the
5 trustee and the creditors and the debtor if a debtor's
6 homestead, pension, or wedding ring or other exempt
7 property becomes fair game and at issue if the trustee
8 makes a motion to suggest that the debtor hasn't behaved
9 as forthrightly as the trustee claims he should have.

10 And I want to stress again, at the risk of
11 repeating myself, we are not talking about the
12 traditional, venerable inherent powers of the Court to
13 award attorneys' fees. There's a Rule 9011 in the
14 Bankruptcy Code. It wasn't invoked here, shouldn't have
15 been invoked here. But what we are talking about
16 instead is the property from which that sanction can be
17 satisfied.

18 Congress has determined that exempt property
19 cannot be used to satisfy administrative expenses. The
20 worst prepetition conduct that one could imagine, say,
21 in a couple of narrow circumstances -- Congress has made
22 the choice here as to the status of exempt property. In
23 the RadLAX case, in the Ginsberg case, and I'm not aware
24 of any case to the contrary in between, Congress -- the
25 rule in this Court is the specific provision controls.

1 Here, Congress has spoken specifically,
2 expressly, not by implication, but through prohibitive
3 language saying that exempt property is not available to
4 satisfy administrative expenses.

5 For those reasons, we would ask the Court to
6 reverse the surcharge order. Thank you.

7 CHIEF JUSTICE ROBERTS: Thank you, counsel.
8 The case is submitted.

9 (Whereupon, at 12:36 p.m., the case in the
10 above-entitled matter was submitted.)

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