Nos. 11-1340, 11-1387

IN THE
UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

In re STEVEN M. SCHAFER

THE STATE OF MICHIGAN
Intervenor-Appellant
And

STEVEN M. SCHAFER,
Debtor-Appellant

— v. —

THOMAS C. RICHARDSON,
Trustee-Appellee

ON APPEAL FROM THE UNITED STATES BANKRUPTCY APPLELLATE PANEL FOR THE SIXTH CIRCUIT, NO. 10-8030, 10-8031

BRIEF *AMICI CURIAE* OF THE NATIONAL ASSOCIATION OF CONSUMER BANKRUPTCY ATTORNEYS, NATIONAL CONSUMER LAW CENTER, LEGAL SERVICES ASSOCIATION OF MICHIGAN, THE MICHIGAN POVERTY LAW PROGRAM, AND THE COUNCIL OF THE CONSUMER LAW SECTION OF THE STATE BAR OF MICHIGAN IN SUPPORT OF DEBTOR'S POSITION SEEKING REVERSAL OF THE BANKRUPTCY APPELLATE PANEL

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June 27, 2011 (*Amici* continued inside)

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RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Schafer v. Richardson, No. 11-1340, 11-1387

Pursuant to 6th Cir. R. 26.1 of the National Association of Consumer Bankruptcy Attorneys makes the following disclosure:

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NO.

2) Is there a publicly owned corporation, not a party to the appeal, that has a financial interest in the outcome? If yes, list the identity of such corporation and the nature of the financial interest:
NO.

/s/Tara Twomey Dated: June 27, 2011
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RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Schafer v. Richardson,, No. 11-1340, 11-1387

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NO.

/s/Geoff Walsh Dated: June 27, 2011
Geoff Walsh, Esq.
National Consumer Law Center

RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Schafer v. Richardson, No. 11-1340, 11-1387

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NO.

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Dated: June 27, 2011

RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Schafer v. Richardson, No. 11-1340, 11-1387

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2) Is there a publicly owned corporation, not a party to the appeal, that has a financial interest in the outcome? If yes, list the identity of such corporation and the nature of the financial interest:
NO.

/s/Ann Routt Dated: June 27, 2011

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RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Schafer v. Richardson, No. 11-1340, 11-1387

Pursuant to 6th Cir. R. 26.1 the Council of the Consumer Law Section of the State Bar of Michigan makes the following disclosure:

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2) Is there a publicly owned corporation, not a party to the appeal, that has a financial interest in the outcome? If yes, list the identity of such corporation and the nature of the financial interest:
NO.

Respectfully Submitted,

By: s/ Karen Merrill Tjapkes
Karen Merrill Tjapkes (P58467)
Chairperson 2010-2011
Consumer Law Council

The Section Council is organized under the bylaws of the State Bar of Michigan. The Section Council does not represent the State Bar of Michigan, which takes no position on issues in this case.

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STATEMENT OF INTEREST OF *AMICI CURIAE*

Incorporated in 1992, the National Association of Consumer Bankruptcy Attorneys ("NACBA") is a non-profit organization of more than 4800 consumer bankruptcy attorneys nationwide. NACBA's corporate purposes include education of the bankruptcy bar and the community at large on the uses and misuses of the consumer bankruptcy process. Additionally, NACBA advocates nationally on issues that cannot adequately be addressed by individual member attorneys. It is the only national association of attorneys organized for the specific purpose of protecting the rights of consumer bankruptcy debtors. NACBA has filed *amicus curiae* briefs in various courts seeking to protect the rights of consumer bankruptcy debtors.

The National Consumer Law Center, Inc. (NCLC) is a non-profit Massachusetts corporation specializing in consumer law, with historical emphasis on consumer credit. NCLC is recognized nationally as an expert in consumer credit issues and has drawn on this expertise to provide information, legal research, policy analyses, and market insights to federal and state legislatures, administrative agencies, and the courts for over 38 years. NCLC is the author of the Consumer Credit and Sales Legal Practice Series, consisting of eighteen practice treatises and annual supplements.

The Legal Services Association of Michigan (LSAM) is a Michigan nonprofit organization incorporated in 1982. LSAM's members are the thirteen largest civil legal services organizations in Michigan that collectively

provide legal services to low-income individuals and families in over 50,000 cases per year.[1] LSAM members have extensive experience with all aspects of preservation of homeownership – public and private housing – for low-income families. Most LSAM members directly represent low-income families in debt collection and bankruptcy cases. All LSAM members work daily—*e.g.,* in consumer law, elder law, public benefits, family law, and housing cases—with seniors and disabled clients whose only major asset is their homes.

The Michigan Poverty Law Program (MPLP) is a cooperative effort of Legal Services of South Central Michigan and the University of Michigan Law School. MPLP provides state support services to local legal services programs and other poverty law advocates. MPLP's goals are: to support the advocacy of field programs; to coordinate advocacy for the poor among the local programs; and to assure that a full range of advocacy continues on behalf of the poor. MPLP also advocates and represents individuals in areas such as low-income housing, consumer protections, consumer bankruptcy, debt collection, predatory lending and foreclosure prevention.

[1] LSAM's members are: the Center for Civil Justice, Elder Law of Michigan, Lakeshore Legal Aid, Legal Aid and Defender, Legal Aid of Western Michigan, Legal Services of Eastern Michigan, Legal Services of Northern Michigan, Legal Services of South Central Michigan, Michigan Indian Legal Services, Michigan Migrant Legal Assistance Program, Michigan Legal Services, Neighborhood Legal Services, and the University of Michigan Clinical Law Program.

The Council of the Consumer Law Section of the State Bar of Michigan is organized under the bylaws of the State Bar. The Council is the elected governing body of the Section. The goals of the Section, as expressed in its bylaws, include educating the bench and bar about consumer law issues. This brief is submitted pursuant to a vote of the governing Section Council. The Section Council does not represent the State Bar of Michigan, which takes no position on issues in this case.

Amici have a vital interest in the outcome of this case. The Bankruptcy Code permits individual debtors to exempt certain property from the bankruptcy estate pursuant to state law, thereby putting that property beyond the reach of the trustee and creditors. In the bankruptcy context, exemptions serve the overriding purpose of helping the debtor to obtain a fresh start. The Trustees argument strikes at the heart of debtors' fresh start by seeking to deny them the benefit of exemptions properly enacted by the State of Michigan and made applicable to debtors by Congress through section 522(b)(3)(A).

This case bears on the fundamental purpose of the Bankruptcy Code, and the ability of Congress to incorporate state law into the bankruptcy laws. *Amici* believe that they bring an important perspective to this case that will be helpful to the court in deciding this matter.

SUMMARY OF ARGUMENT

State laws related to bankruptcies are presumed valid as long as they meet two constitutional standards. First, under the Supremacy Clause the state law must not conflict with federal law. Second, any bankruptcy law must apply uniformly to defined groups of debtors and creditors. The latter is a requirement of the Bankruptcy Clause. The Michigan bankruptcy specific homestead exemptions pass both tests.

Michigan's law does not conflict with federal law. Congress expressly authorized states to supply the exemptions to be allowed in bankruptcy cases. The Sixth Circuit has held, and the B.A.P. agreed, that the federal government and the states have concurrent jurisdiction in the area of bankruptcy exemptions. Because of the clear Congressional directive for state involvement in the area of bankruptcy exemptions, there is no express or implied federal preemption.

State homestead exemption laws set a wide variety of monetary limits on homestead exemptions. These range from a few thousand dollars to unlimited amounts. For purposes of their homestead exemptions, state laws categorize debtors under an unlimited variety of classifications. They classify debtors based on factors such as age, physical condition, income, county of residence, rural or urban residence, and the type of debts they have incurred. The fact

that state homestead laws vary greatly, classifying debtors in multiple ways, does not conflict with or impede in any way the operation of federal bankruptcy laws.

The B.A.P held that Michigan's law violated the Bankruptcy Clause's uniformity requirement. Many aspects of the B.A.P.'s Bankruptcy Clause ruling were actually based on a "field preemption" analysis. This preemption analysis was inconsistent with the B.A.P's own acknowledgement that Congress directed states to act in the area of bankruptcy exemptions. *See* 11 U.S.C. § 522(b)(3)(A).

Assuming for the sake of argument that the Bankruptcy Clause applies to state legislation, Michigan's law passes muster under the appropriate contemporary standard for determining what the Clause requires. Michigan's bankruptcy specific homestead exemption law applies uniformly to defined classes of debtors. The classifications are not directed to only one debtor (the law is not private legislation) and the classifications are not arbitrary. This is all the uniformity that the Bankruptcy Clause requires.

ARGUMENT

I. Michigan's Bankruptcy-Specific Exemptions Function Consistently with Congress's Power to Establish Uniform Bankruptcy Laws.

A. Introduction

When he filed for bankruptcy relief, debtor Steven Schafer claimed an exemption in his home under Mich. Comp. Laws § 6000.5451(1)(n), a Michigan exemption law in effect at the time he filed his bankruptcy petition. Michigan law allows debtors who are disabled or over age 65 and who file for bankruptcy relief to exempt up to $51,650 in home equity. Michigan homeowners who are not over age 65 or disabled and file for bankruptcy relief may exempt up to $34,500 in home equity. Mr. Schafer is disabled and therefore claimed the $51,650 exemption amount.

The Chapter 7 Trustee objected to Mr. Schafer's homestead exemption claim, asserting that Michigan's bankruptcy-specific homestead exemption was unconstitutional. The trustee argued that Mich. Comp. Laws § 6000.5451(1)(n) contravened the "Bankruptcy Clause" of the U.S. Constitution. The Bankruptcy Clause grants to Congress the power "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. Art. I, sec. 8, cl. 4. The Bankruptcy Court denied the trustee's objection, holding that Michigan's bankruptcy-specific exemption did not

suffer from any constitutional infirmities. In re *Jones*, 428 B.R. 720 (Bankr. W.D. Mich. 2010).[2] The Bankruptcy Appellate Panel ("B.A.P.") reversed, ruling that the Michigan statute was invalid as contrary the Bankruptcy Clause. In re *Schafer*, -- B.R. --, 2011 WL 650545 (B.A.P. 6th Cir. Feb. 24, 2011).

B. The Plain Language of 11 U.S.C. § 522(b)(3)(A) Incorporates All State Exemption Laws as Potential Bankruptcy Exemptions.

Congress provided in the Bankruptcy Code that a debtor may exempt from the bankruptcy estate "any property that is exempt under federal law . . . or State or local law that is applicable on the date of the filing of the petition." 11 U.S.C. § 522(b)(3)(A). A provision expressly authorizing use of state exemption laws in bankruptcy cases has been an integral feature of federal bankruptcy law since the nineteenth century. *See Schafer*, 2011 WL 650545 at *4-5 (discussing prior federal bankruptcy statutes and their exemption schemes).

By its plain language the text of § 522(b)(3)(A) allows a Michigan bankruptcy debtor to claim as exempt "any property" that is exempt under Michigan law. There is no textual support for an insertion of absent qualifiers into this plain text of the Code. With § 522(b)(3)(A) Congress did not limit its grant of authority to the states to fashion the exemption laws to be recognized in bankruptcy cases.

[2] The cases of two similarly situated Michigan bankruptcy debtors, Mr. Schafer and Ms. Jones were consolidated for purposes of appeals and briefing. Ms. Jones was dismissed from this appeal on April 21, 2011.

Case law has consistently acknowledged that Congress chose deliberately not to preempt state law in the area of defining the exemptions to be allowed in bankruptcy cases. Section 522(b)(3)(A) "allows the States to define what property a debtor may exempt from the bankruptcy estate that will be distributed among his creditors." *Owen v. Owen*, 500 U.S. 305, 306 (1991). In construing § 522(b)(3)(A) this Court held that, with respect to exemptions, Congress expressly authorized states to "preempt" federal law. *Rhodes v. Stewart*, 705 F.2d 159, 163 (6th Cir. 1983), *cert. denied* 464 U.S. 983 (1983). The *Rhodes* court emphasized that through § 522(b) Congress "vested in the states the ultimate authority to determine their own bankruptcy exemptions." *Id. Accord Storer v. French*, 58 F.3d 1125, 1128 (6th Cir. 1995). *See also Sheehan v. Peveich*, 574 F.3d 248 (4th Cir. 2009) *cert. denied sub nom Sheehan v. Jackson*, 130 S. Ct. 1066 (2010) (with respect to bankruptcy exemptions, "[t]here can be no preemption, however, where Congress 'expressly and concurrently authorizes' state legislation on the subject . . . . 'In such instance, rather than preempting the area, Congress expressly authorizes the states to 'preempt' the *federal* legislation.' " quoting *Rhodes,* 705. F.2d at 163); In re *Sullivan*, 680 F.2d 1131, 1137 (7th Cir. 1982) (to say that state exemption provisions are in conflict with the language of the [Bankruptcy] Code "is simply inaccurate").

Section 522(b)(3)(A) operates consistently with the Bankruptcy Code's general approach of allowing state law to determine property rights in

bankruptcy cases. *Butner v. United States*, 440 U.S. 48, 54 (1979) ("Congress has generally left the determination of property rights in the assets of a bankruptcy estate to state law."). Courts have repeatedly rejected arguments asserting that Congress somehow violated the Bankruptcy Clause's uniformity requirement by incorporating state law into the Bankruptcy Code. *See, e.g.*, *Herrin v. GreenTree-AL, L..LC.*, 376 B.R. 316, 321 (S.D. Ala. 2007) (applying state law to determine real property interests subject to modification under 11 U.S.C. § 1322(b)(2) does not violate the Bankruptcy Clause); In re *Simon*, 311 B.R. 641 (Bankr. S. D. Fla. 2004) (construing fine and penalty discharge exception under state laws not contrary to Bankruptcy Clause).

C. State Homestead Laws Routinely Recognized in Bankruptcy Cases Set a Wide Range of Monetary Limits and Employ a Variety of Classifications Based on the Status of Debtors and Their Properties

The B.A.P. did not find or even suggest that Michigan's bankruptcy-only homestead exemption conflicted with federal bankruptcy law. The court did not point to any aspect of Michigan's law that frustrates or interferes with the operation of the Bankruptcy Code. In terms of the dollar amounts exempted and its special treatment of disabled and elderly debtors, Michigan's bankruptcy-specific exemption law is not unusual. It fits well within the range of homestead exemptions recognized in bankruptcy cases every day around the country.

State homestead exemptions come in all sizes and forms. Florida and Texas, for example, do not place dollar limits on their homestead exemptions.[3] Debtors residing in these states for the appropriate periods of time may file for bankruptcy relief and, consistently with 11 U.S.C. § 522(b)(3)(A), exempt millions of dollars in home equity from the reach of the bankruptcy trustee and creditors. Other states have set relatively high homestead exemption limits. These include Nevada ($550,000), Massachusetts ($500,000), and Minnesota ($750,000 for an agricultural homestead).[4] At the other end of the spectrum, Alabama, Tennessee, and Virginia do not allow bankruptcy debtors to claim federal bankruptcy exemptions and in most circumstances limit the homestead exemption to $5,000.[5]

Many state homestead exemption laws do more than simply set a dollar cap on home equity that may be claimed as exempt from creditors. Certain state exemption laws take into account personal characteristics of the debtor or the nature of the underlying debts. Hawaii, for example, allows a higher homestead exemption to debtors who are over the age of 65.[6] California debtors who are over age 55 and have gross annual incomes under $15,000 may

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[3] Fla. Const. art X, § 4; Fla. Stat. Ann. §§ 222.01, .02; Tex. Const. art. 16 §§ 50, 51; Tex Prop. Code § 41.001 and § 41.002.
[4] Nev. Rev. Stat. Ann. § 21.090; Mass. Ann. Laws ch. 188, §§ 1 and 1A; Minn. Stat. § 510.02.
[5] Ala. Code § 6-10-2; Tenn. Code Ann. § 26-2-301; Va. Code Ann. § 34-4.
[6] Hawaii Rev. Stat. § 651-92.

claim a homestead exemption of $150,000, as opposed to younger, higher income debtors who are limited to a $50,000 homestead exemption.[7]

Still other states vary their homestead exemptions based upon the nature of the debts at issue. For example, homeowners in Louisiana can claim an unlimited homestead exemption "in the case of an obligation arising directly as a result of a catastrophic or terminal illness or injury."[8] Otherwise, Louisiana homeowners are limited to a $35,000 homestead exemption.[9] Connecticut raises its otherwise applicable $75,000 homestead exemption limit to $125,000 when payment of a debt for hospital costs is at issue.[10] Florida, Texas, and Kansas set acreage limitations to their homestead exemptions that vary depending on the property location, differing by county or based upon urban versus rural distinctions.[11]

In determining the amount of home equity that a debtor may exempt from creditors, state laws classify debtors by a myriad of factors, including age, income, physical condition, and the types of debts they have accumulated. State exemption laws allow for variations depending on property location within the state and how land is used. No court rulings have questioned Congress's intent

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[7] *See e.g. In re* Bush, 346 B.R. 207 (Bankr. S.D. Cal. 2006) (discussing Cal. Code Civ. P. 704.730(a)(2))
[8] La. Rev. Stat. Ann. § 20:1.
[9] *See id.*
[10] Conn. Gen. Stat. § 52-352b(t).
[11] Fla. Const. art. X, § 4; Tex. Const. art. 16, § 51; Kan. Stat. Ann. § 60-2301.

or its authority in permitting the enforcement of this wide range of state exemption laws in bankruptcy proceedings pursuant to § 522(b)(3)(A).

As the B.A.P noted, eight states in addition to Michigan have adopted a form of homestead exemption that applies specifically to bankruptcy debtors. [12] Michigan's bankruptcy specific exemptions set limits ($51,650 and $34,500) that are well within the range of those routinely recognized as applicable in bankruptcy cases under § 522(b)(3)(A).

II. Michigan's Bankruptcy-Specific Exemption Does Not Conflict With Federal Bankruptcy Law.

The Supremacy Clause clearly applies to state legislation and sets the appropriate standard for resolving conflicts between federal and state laws, mandating that the federal law predominates. The B.A.P did not find that the Michigan law conflicted with any provision of federal bankruptcy laws or otherwise impeded the enforcement of federal bankruptcy law. As discussed above, this Court's recognition in *Rhodes v. Stewart* that Congress expressly authorized states to preempt federal law in the area of bankruptcy exemptions precludes a finding that federal law preempts state law in the area of bankruptcy exemptions.

Given the range of exemptions that are routinely enforced in bankruptcy cases nationally, it cannot be seriously argued that Michigan's law conflicts with or interferes with the operation of federal bankruptcy laws. In re *Applebaum*,

[12] *Schafer*, 2011 WL 650545 at *7 n.10 (naming California, Colorado, Georgia, Indiana, Montana, New York, Ohio, and West Virginia).

422 B.R. 684, 691(B.A.P. 9th Cir. 2009) ("There is no conflict between the purposes and goals of the Bankruptcy Code and the California bankruptcy-only exemption statute. Simply because the exemptions differ from the federal exemptions (or from its non-bankruptcy counterpart), does not mean that such differences create a conflict that impedes the accomplishment and execution of the Bankruptcy Code.")

III. Michigan's Bankruptcy-Specific Exemptions Satisfy the Bankruptcy Clause's Uniformity Requirement.

A. *Hood* did not Displace the Supreme Court Precedent Setting Standards for What is a Uniform Law under the Bankruptcy Clause.

The B.A.P. and the bankruptcy court below agreed that states and the federal government have concurrent jurisdiction in the area of defining exemptions that are to be applied in bankruptcy cases. *Schafer*, 2011 WL 650545 at *11. However, the B.A.P and the bankruptcy court disagreed over the question of whether the Bankruptcy Clause applies to state legislation. By its express language the Clause refers only to Congress's authority to enact uniform bankruptcy laws. The bankruptcy court below, as have other courts, considered the Bankruptcy Clause inapplicable to state legislation. *Jones*, 428 B.R. at 729 n.9.

In determining that the Bankruptcy Clause could be a basis for striking down a state statute, the B.A.P. looked to this Court's opinion in *Hood v. Tennessee Student Assistance Corp.,* 319 F.3d 755 (6th Cir. 2003), *aff'd on other grounds*

541 U.S. 440 (2004). According to the B.A.P., "Hood established that the exercise of state power, whether it is to legislate or to assert immunity from suit, is limited by the uniformity requirement set forth in the Bankruptcy Clause." *Schafer*, 2011 WL 650545 at *10. Concluding that it was appropriate to review the Michigan statute for compliance with the Bankruptcy Clause, the B.A.P went on to find that the state law did not pass muster under judicial interpretations of what constitutes a uniform bankruptcy law. *Id.* at *13-14.

There are three problems with the B.A.P.'s analysis of the Bankruptcy Clause and its relation to state laws. First, the panel in *Hood* did not expressly say that the Bankruptcy Clause could serve as the basis to strike down a state statute. In affirming this Court's decision the Supreme Court clearly did not so hold. Second, the question of state/federal relations presented in this appeal is the reverse of the situation presented by *Hood*.

Hood addressed the question of whether Congress could exercise its bankruptcy powers to enact § 106(a) of the Bankruptcy Code, a provision that overrides the Eleventh Amendment immunity protection that otherwise shields the states from actions brought in federal courts. The gist of this Court's ruling in *Hood* was that, unless Congress says otherwise, its authority to legislate in the area of bankruptcy is virtually unlimited *vis a vis* the states. In the instant appeal the Court must consider the impact of § 522(b)(3)(A) of the Code. Here, Congress expressly created a positive rule that the exemption laws of the states will be

enforced in bankruptcy cases. The instant case does not require that the Court probe the outer limits of Congressional authority over an inconsistent state law. Nor does this appeal present a situation where federal law has preempted the specific field. Congress has expressly said that it is not preempting the field of bankruptcy exemptions. *Hood* is simply irrelevant. Third, assuming for the sake of argument that the Bankruptcy Clause applies to state legislation, Michigan's bankruptcy specific homestead exemption statute does not violate the Bankruptcy Clause's uniformity standard. On the contrary, Michigan's law is an appropriate uniform law that easily passes muster under current judicial interpretations of what the Bankruptcy Clause requires.

This Brief will proceed to address the third point first. The Michigan statute is consistent with the requirements of the Bankruptcy Clause. The Court need not decide whether in some other scenario the Bankruptcy Clause can serve as the basis to invalidate a state statute. Similarly, it is not necessary in this appeal to address issues related to the outer limits of federal bankruptcy powers as suggested by the B.A.P.'s reference to this Court's *Hood* opinion.

B. In Construing the Bankruptcy Clause the B.A.P Applied a Rule of "Geographic Uniformity" that Later Supreme Court Rulings Supplemented with a Test Requiring Only That a Bankruptcy Law Apply Uniformly to a Class of Debtors.

In striking down the Michigan statute the B.A.P. held that the state law violated a requirement under the Bankruptcy Clause that any law related to bankruptcy must operate with "geographic uniformity." *Schafer*, 2011 WL 650545 at *13-14. The B.A.P. applied a "geographic uniformity" standard that had been mentioned in a Supreme Court opinion over a century ago. *See Hanover National Bank of the City of New York v. Moyse,* 186 U.S. 181 (1902). The B.A.P.'s analysis focused upon language in the *Hanover* decision stating that in bankruptcy cases the bankruptcy trustee in each state should take "whatever would have been available to the creditor if the bankrupt[cy] law had not been passed." *Hanover*, 186 U.S. at 190, *quoted* at *Schafer*, 2011 WL 650545 at *5, 13-14.

The creditor in *Hanover* challenged the 1898 Bankruptcy Act on a number of grounds. The Supreme Court rejected arguments that the Act improperly allowed non-merchants to file voluntary bankruptcy petitions and provided inadequate notice to affected creditors. The Court's treatment of the exemption issue was less clear. The opinion does not specify the nature of the creditor's claims regarding exemptions. The objecting creditor had obtained a judgment against the debtor in Mississippi. The debtor later moved to

Tennessee, sought bankruptcy relief in that state, and claimed the protection of Tennessee exemption laws. The Bankruptcy Act of 1898, in effect at the time, allowed the debtor to claim the exemptions in force in Tennessee, the state where the debtor was domiciled. The creditor challenged this provision of the 1898 Act, claiming that it violated the uniformity requirement of the Bankruptcy Clause. Presumably the creditor would have received a more favorable distribution from the bankruptcy estate if non-Tennessee exemptions were applied. Disagreeing with the creditor's challenge to the 1898 Act's exemption scheme, the Supreme Court held that the Act's exemption provisions were in fact "uniform." The uniformity was "geographical, and not personal." *Hanover*, 186 U.S. at 188. The creditor would receive whatever he would get if the debtor's property were liquidated through "judicial process" in a "general execution" outside of bankruptcy in Tennessee. *Id.* at 190-91. This result amounted to "geographic uniformity" in the treatment of debtors and creditors under the Bankruptcy Act, and was consistent with the Bankruptcy Clause's uniformity requirement. *Hanover* did not involve any question of a state's bankruptcy-only exemption law

Applying Michigan's bankruptcy-specific homestead exemption law in Mr. Schafer's chapter 7 case, the trustee does not take from Mr. Schafer's home equity whatever would have been available to creditors in a collection

proceeding applying only state law.[13] Applying the *Hanover* language literally, the Michigan bankruptcy-only homestead exemption does not apply "uniformly" to all debtors living within the state's borders. It classifies debtors who have filed for bankruptcy relief differently from debtors who have not done so. Therefore, according to the B.A.P, the law violates the "geographic uniformity" standard quoted from the *Hanover* opinion.

C. The Supreme Court's Interpretations of the Bankruptcy Clause after *Hanover*

In two later decisions the Supreme Court supplemented the *Hanover* Court's "geographic uniformity" standard for determining uniformity under the Bankruptcy Clause. *Railway Labor Executive Ass'n v. Gibbons*, 455 U.S. 457 (1982); *Blanchette v. Connecticut Gen. Ins. Corp.*, 419 U.S. 102 (1974). In these cases the Court recognized an alternative basis for assessing whether a law complied with the Bankruptcy Clause's

[13] In a non-bankruptcy debt collection context Michigan debtors may claim a homestead exemption of $3,500. Mich. Comp. Laws § 600.6023(1)(h). Michigan has not opted out of the federal bankruptcy exemption scheme found in 11 U.S.C. § 522(d). Therefore a Michigan debtor in bankruptcy may elect to claim the higher federal bankruptcy homestead exemption of $21,625. 11 U.S.C. § 522(d)(1) (for cases filed before April 1, 2010 the amount was $20,200). After deducting secured claims and sale costs against the $160,000 value of his home, Mr. Schafer listed $44,695 in home equity as an asset in his bankruptcy schedules. Allowing only the non-bankruptcy state law exemption or only the federal bankruptcy homestead exemption would leave sufficient non exempt equity to permit the bankruptcy trustee to liquidate Mr. Schafer's residence and distribute the value of non-exempt equity to creditors. Claiming the Michigan bankruptcy-specific exemption for a disabled bankruptcy debtor ($51,650) permits Mr. Schafer to exempt all his home equity and keep his home.

uniformity requirement. If the bankruptcy law in question applied to debtors differently over a common geographic area, it could nevertheless withstand Constitutional challenge if it treated the debtors differently based on a reasonable classification. In the words of the *Gibbons* Court, "[t]o survive scrutiny under the Bankruptcy Clause, a law must at least apply uniformly to a defined class of debtors." 455 U.S. at 473.

Blanchette v. Connecticut General Insurance Corp., 419 U.S. 102 (1974), involved a challenge to legislation creating a special insolvency reorganization system for regional railroads. Certain railroads challenged the statute as violating the Bankruptcy Clause's uniformity requirement. The railroads argued that the federal legislation violated the standard articulated in the *Hanover* opinion because it treated debtors differently based on geographic location (the railroads subject to the law operated in the East and Midwest). The Supreme Court rejected this contention. The Court noted that a similar uniformity standard applied to the Congressional power to levy duties and excise taxes.[14] After considering prior precedent construing the uniformity clause for duties and excise taxes, the court concluded that the bankruptcy laws, like laws pertaining to duties and excise taxes, need not be geographically uniform. According to the *Blanchette* Court, a law is uniform when it operates with the same force and effect wherever the subject of regulation is found. Legislation may designate an "evil

[14] Congress is empowered to lay and collect "all Duties and Excises (which) shall be uniform throughout the United States." U.S. Const. Art. 1, sec. 8 cl. 1),

to be remedied" and adopt classifications for addressing the problem. *Blanchette*, 419 U.S. at 160-61 (*quoting The Head Money Cases*, 112 U.S. 580, 594-95 (1884)). Despite disparate geographical impact, legislation may be uniform if the classifications apply to defined parties as necessary to address a particular government objective.

The Constitutional provision applicable to laws establishing duties and excise taxes sets a higher standard for uniformity than the Bankruptcy Clause. *See Schultz v. U.S.*, 529 F.3d 343, 355 (6th Cir. 2008). Nevertheless, even under this stricter standard, the Supreme Court has recognized alternatives to the geographic uniformity standard. *See U.S. v. Ptasynski*, 462 U.S. 74 (1983). In *Ptasynski* the court upheld a federal statute creating an oil production excise tax exemption that clearly preferred one geographic area over all others. The Court deferred to Congress's finding that that there was a reasonable basis for the classification. According to the Court, the uniformity clause at issue "encompasses some notion of equality" and "does not prevent Congress from defining the subject of a tax by drawing distinctions between similar classes." *Ptasynski*, 462 U.S. at 82.

Railway Labor Executives Ass'n v. Gibbons, 455 U.S. 457 (1982), is the only case in which the Supreme Court struck down a bankruptcy statute because it did not comply with the Bankruptcy Clause. Congress enacted the statute in question in *Gibbons* in order to regulate labor relations of one insolvent railroad, the Rock Island Railroad. Because the statute applied to only one entity it was "nothing more than a private bill." *Gibbons*, 455 U.S. at 471. A private bill could not possibly apply uniformly to a

class of similarly situated entities. In striking down the law the Court again summarized the limited situations in which it was appropriate to invalidate a statute under the Bankruptcy Clause:

> Prior to today, the Court has never invalidated a bankruptcy law for lack of uniformity. The uniformity requirement is not a straightjacket that forbids Congress to distinguish among classes of debtors, nor does it prohibit Congress from recognizing that state laws do not treat commercial transactions in a uniform manner.

455 U.S. at 469. Supreme Court jurisprudence now recognizes that lack of geographic uniformity is not fatal to a bankruptcy law. It is sufficient that the law apply uniformly to a distinct class of affected parties.

More recently, after reviewing these same Supreme Court decisions construing the Bankruptcy Clause, the Seventh Circuit concluded that "the clause forbids only two things: The first is arbitrary regional differences in the provisions of the Bankruptcy Code. The second is private bankruptcy bills – that is, bankruptcy laws limited to a single debtor – or the equivalent." *Matter of Reese*, 91 F.3d 37, 39 (7th Cir. 1996). *Gibbons* was a clear example of private legislation, a law designed to apply to only one entity. A rare case involving the other scenario, a fundamentally arbitrary regional classification under the bankruptcy laws appeared in *St. Angelo v. Victoria Farms, Inc.,* 38 F.3d 1525 (9th Cir. 1994). The *Victoria Farms* court struck down a provision of federal

bankruptcy legislation that delayed implementation of various aspects of the U.S. Trustee program in only two states. No rationale could be proffered as to why these two states had been singled out for different treatment, leading the court to conclude that the classifications were completely arbitrary and therefore not uniform.

Neither the "private bill" nor the arbitrary classification defects apply to the Michigan statute in question here. This is not private legislation applicable to one party. The Michigan law applies to a clearly defined class of debtors – all Michigan homeowners who file for bankruptcy relief. A state has a legitimate interest in preserving homeownership for its residents who seek a fresh start in bankruptcy. Debtors who obtain a fresh start after discharge of burdensome debts and remain in their homes are more likely to contribute to stable communities than those forced to give up their homes in bankruptcy, as the trustee seeks to force Mr. Schafer to do in this case.

D. This Court and Other Courts Have Recognized that Laws Pass Scrutiny Under The Bankruptcy Clause When They Apply to Uniform Classes of Debtors

In *Schultz v. U.S.*, 529 F.3d 343 (6th Cir. 2008), this Court had occasion to review the development of the "geographic uniformity" standard under the Bankruptcy Clause. *Schultz* involved a challenge to the means-testing standards enacted in 2005. These amendments applied a federally mandated set of standards to determine chapter 13 debtors' disposable income. These standards vary from state to

state based on federal data. As a result, debtors fare differently under the test, facing greater or lesser debt repayment burdens in obtaining chapter 13 relief, depending upon the state where they live. Debtors in *Schultz* contended that this means testing system with varying state standards violated the uniformity requirement of the Bankruptcy Clause. In particular, the debtors claimed that the system failed the "geographic uniformity" test.

In construing the "geographic uniformity" standard, the *Schultz* court reviewed the Supreme Court's decisions in *Hanover*, *Blanchette*, and *Gibbons*, discussed above. *Schultz*, 529 F.3d at 350-53. The court recognized *Blanchette*'s modification of the *Hanover* standard. Sixty years after *Hanover*, the *Blanchette* Court held that a bankruptcy law could withstand constitutional challenge despite lack of geographic uniformity in its application "as long as the law operates uniformly upon a given class of creditors and debtors." *Schultz*, 529 F.3d at 351. Concluding that the BAPCPA means testing provisions functioned as a uniform law the *Schultz* Court concluded, "Congress is allowed to distinguish among classes of debtors, and to treat categories of debtors differently, whether it be through the incorporation of varying state laws 'affecting dower, exemptions, the validity of mortgages, priorities of payment and the like.' " *Id.* at 352 (*quoting Stellwagen v. Clum*, 245 U.S. 605, 613 (1918)). Thus, this Court has recognized that federal bankruptcy laws may incorporate state exemption laws that are not geographically uniform so long as the laws distinguish among defined classes of debtors in the same geographic area.

Other courts have analyzed the post-*Hanover* Supreme Court decisions in the same way. In construing the Bankruptcy Clause, a bankruptcy appellate panel for the Ninth Circuit rejected an argument for geographic uniformity that relied heavily on *Hanover*. In re *Urban*, 375 B.R. 882, 890 (B.A.P. 9th Cir. 2007). As the *Schultz* court did, the *Urban* court traced the evolution of the "geographical uniformity" standard from *Hanover* through the Supreme Court's *Blanchette* and *Gibbons* rulings. The *Urban* court found that the *Hanover* Court's "bright line" rule requiring identical distribution to creditors inside and outside of bankruptcy within the same geographic area had been modified substantially by the addition of different and more flexible standards based on classification of debtors along non- geographic terms. *Urban*, 375 B.R. at 889-91. *See also* In re *Applebaum*, 422 B.R. 684, 692 (B.A.P. 9th Cir. 2009) ("The concept of uniformity requires that federal bankruptcy laws apply equally in form (but not necessarily in effect) to all creditors and debtors, or to 'defined classes' of debtors and creditors", *quoting Gibbons*, 455 U.S. at 473); In re *Chandler,* 362 B.R. 723, 728-29 (Bankr. N.D. W.Va. 2007) ("Geographical uniformity and class uniformity are separate concepts, and when a law is applied to a specified class of debtors, the uniformity requirement is met, so long as the law applies uniformly to that defined class of debtors.").

In focusing upon one excerpt from the 1902 *Hanover* opinion and allowing it to serve as the foundation for its decision in this case, the B.A.P. failed to consider one hundred years of court rulings construing the Bankruptcy Clause since *Hanover*. The

Amici do not concede that the Bankruptcy Clause applies to state legislation. But even if it did, the Michigan bankruptcy-only exemption law passes muster under the appropriate judicial interpretation of what the Bankruptcy Clause requires.

E. The B.A.P's Interpretation of the Bankruptcy Clause's Uniformity Requirement Invalidates the 2005 "Mansion Loophole" Amendments and Critical Code Provisions.

The 2005 amendment to § 522(b)(3)(A) established an extended domiciliary requirement that must be satisfied before a bankruptcy debtor may claim the homestead exemption of his or her current state of residence. Today, in order to claim the state law homestead exemptions of the state of residence in a bankruptcy case the debtor must have lived in the state for two years or more as of the petition date. The intent of the amendment was to deter a perceived practice of potential bankruptcy debtors moving to a state such as Florida, with an unlimited homestead exemption, for the purpose of converting assets to exempt real property in anticipation of filing for bankruptcy relief in the new state. One obvious consequence of the 2005 amendment has been that debtors claiming exemptions in a single geographic area are not treated the same inside and outside of bankruptcy.

A recent decision applying the "mansion loophole" amendment shows how using permissible classifications of bankruptcy exemptions can have a sharply disparate impact on debtors filing for bankruptcy relief within the same state. *See* In re *Varanasi*, 394 B.R. 430 (Bankr. S.D. Ohio 2008). Mr. Varanasi

owned a house, valued at $50,000, free and clear in Cambridge, Ohio. Ohio has opted out of the federal exemptions and has a state law homestead exemption of $5,000. Mr. Varasani had not lived in Ohio for two years prior to filing his bankruptcy petition in Ohio. For several years before returning to his residence in Ohio, he had lived and worked in New Hampshire. Applying the amended provisions of § 522(b)(3)(A), Mr. Varasani could not claim a homestead exemption under Ohio law. Instead, he was required to use New Hampshire exemptions. Because New Hampshire has a $100,000 homestead exemption, Mr. Varasani could claim his full $50,000 interest in his home as exempt. Had his next-door neighbor filed for bankruptcy relief at the same time, the neighbor would likely have been limited to the Ohio $5,000 homestead exemption. This disparate treatment of neighbors would clearly not conform to the *Hanover* language on geographic uniformity adopted by the B.A.P. The bankruptcy trustee in Mr. Varasani's case did not recover whatever a creditor would have received in an execution against Mr. Varasani outside of bankruptcy.

In an opinion addressing various challenges to Mr. Varasani's exemption claims, the Ohio bankruptcy court rejected a challenge asserting that this outcome violated the bankruptcy uniformity clause. In re *Varasani,* 394 B.R. at 439. The court noted that in amending § 522(b)(3) Congress created "a specific class of debtors based on whether they have relocated from one state

to another within a defined period of time." *Id.* The bankruptcy-specific exemptions, such as Mich. Comp. Laws § 6000.5451(1)(n), similarly create specific classes of debtors, those who have filed for bankruptcy relief, those who have not filed for bankruptcy relief, as well as those who are over 65 years old or disabled. Debtors within each class are treated consistently. *See also* In re *Urban*, 375 B.R. 882, 889-91 (B.A.P. 9th Cir. 2007) (holding that the "mansion loophole" amendment is a uniform law based on classifications, despite lack of geographic uniformity; and noting effect of subsequent court rulings on the *Hanover* language regarding trustees taking whatever non-bankruptcy creditors would take).

The B.A.P's reliance on *Hanover* calls into question the very existence of concurrent federal and state exemption in bankruptcy. Because Michigan has not opted out of the federal bankruptcy exemptions under 11 U.S.C. § 522(d), Michigan debtors may choose either the state or federal exemptions in their bankruptcy cases. Putting aside the question of the bankruptcy-specific homestead exemption, any Michigan debtor can choose the federal exemptions in a bankruptcy case and exempt $21,625[15] in home equity or chose the state exemptions in bankruptcy and exempt only $3,500 in home equity.[16] Debtors needing to preserve home equity invariably choose the federal exemptions with

[15] 11 U.S.C. § 522(d)(1).
[16] Mich. Comp. Laws § 600.6023(1)(h).

the higher homestead limit. However, in cases in which Michigan debtors choose the higher federal exemption, the bankruptcy trustee does not take "whatever would have been available to the creditor if the bankrupt[cy] law had not been passed." *Hanover*, 186 U.S. at 190. The B.A.P.'s strict adherence to the *Hanover* language calls into question the entire federal/state treatment of exemptions in bankruptcy authorized in 11 U.S.C. § 522(b) and (d).[17]

F. Regardless of the Labels Used, Congress has Authorized States to Provide the Exemption Schemes to be Used in Bankruptcy Cases

The B.A.P quotes an analysis from a different Michigan bankruptcy court which held that the state's bankruptcy-specific exemption was unconstitutional. *Schafer*, 2011 WL 650545 at *13, quoting from In re *Wallace,* 347 B.R. 626 (Bankr. W.D. Mich. 2006). In discussing bankruptcy exemptions the *Wallace* court acknowledged that Congress "can reference state law for purposes of defining the scheme it has chosen." The court went on to state that what Congress could not do under the Constitution was "delegate . . . to the states . . . the power to actually decide what is to be the appropriate scheme." *Wallace*, 347 B.R. at 635. The B.A.P. quoted this explication in support of its interpretation of how the Bankruptcy Clause functions.

[17] Elsewhere in its decision the *Schafer* court notes that the 1898 Bankruptcy Act did not contain a set of uniform federal exemption. *Schafer*, 2011 WL 650545 at *5. However, the court apparently failed to note the impact of this fact on the application of the *Hanover* language in the context of the 1978 Bankruptcy Code, which does provide a uniform set of federal exemptions.

Like many aspects of the B.A.P. decision, the quote from the *Wallace* court uses terms that are unclear. The B.A.P. and the *Wallace* courts agree that Congress can "reference" state law for purposes of defining a bankruptcy exemption scheme. At the same time they say that Congress cannot "delegate" to the states the "power to decide what is to be the appropriate scheme." The statement begs several the question: How can Congress "reference" a scheme of state exemptions unless a state has first decided what the scheme of state exemptions to be referenced will be? Obviously, states have the power to enact and amend their own exemptions, and under § 522(b)(3)(A) Congress unquestionably authorized states to supply the exemption scheme that will be recognized in bankruptcy cases.

CONCLUSION

For the foregoing reasons, the judgment of the Bankruptcy Appellate Panel should be reversed.

Respectfully Submitted,

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CERTIFICATE OF SERVICE

I certify that on June 27, 2011 the foregoing Brief *Amici Curiae* in Support of Reversal was filed with the U.S. Court of Appeals for the Sixth Circuit and served on the counsel listed below through the ECF system.

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