Report on Public Policy Position

Name of section:
Consumer Law Section

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Regarding:
Amicus Brief Richardson v. Schafer, 6th Cir. BAP, Nos. 10-8030, 10-8031

Date position was adopted:
July 8, 2010

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10 Voted for position
0 Voted against position
0 Abstained from vote
5 Did not vote

Nos. 10-8030, 10-8031

IN THE

UNITED STATES BANKRUPTCY APPELLATE PANEL

FOR THE SIXTH CIRCUIT

In re STEVEN M. SCHAFER AND
In re DOROTHY ANN JONES

THOMAS C. RICHARDSON,
Trustee-Appellant
— v. —
STEVEN M. SCHAFER,
Debtor-Appellee

THOMAS R. TIBBLE,
Trustee-Appellant
— v. —
DOROTHY ANN JONES,
Debtor-Appellee

ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF MICHIGAN NOS. 09-03268, 09-09415

BRIEF *AMICI CURIAE* 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 MICHIGANIN SUPPORT OF DEBTORS' POSITION SEEKING AFFIRMANCE

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RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Richardson v. Schafer, No. 10-8030 and *Tibble v. Jones*, No. 10-8031.

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

1) Is said party a subsidiary or affiliate of a publicly owned corporation? If Yes, list below the identity of the parent corporation or affiliate and the relationship between it and the named party:
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: July 21, 2010
Tara Twomey, Esq.
Attorney for the National Association of Consumer Bankruptcy Attorneys

RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Richardson v. Schafer, No. 10-8030 and *Tibble v. Jones*, No. 10-8031.

Pursuant to 6th Cir. R. 26.1 of the National Consumer Law Center makes the following disclosure:

1) Is said party a subsidiary or affiliate of a publicly owned corporation? If Yes, list below the identity of the parent corporation or affiliate and the relationship between it and the named party:
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/Geoff Walsh Dated: July 21, 2010
Geoff Walsh, Esq.
National Consumer Law Center

RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Richardson v. Schafer, No. 10-8030 and *Tibble v. Jones*, No. 10-8031.

Pursuant to 6th Cir. R. 26.1 Michigan Poverty law Program makes the following disclosure:

1) Is said party a subsidiary or affiliate of a publicly owned corporation? If Yes, list below the identity of the parent corporation or affiliate and the relationship between it and the named party:
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.

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Dated: July 21, 2010

RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Richardson v. Schafer, No. 10-8030 and *Tibble v. Jones*, No. 10-8031.

Pursuant to 6th Cir. R. 26.1 the Legal Services Association of Michigan (LSAM) makes the following disclosure:

1) Is said party a subsidiary or affiliate of a publicly owned corporation? If Yes, list below the identity of the parent corporation or affiliate and the relationship between it and the named party:
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/Ann Routt Dated: July 21, 2010
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RULE 26.1 DISCLOSURE OF CORPORATE AFFILATIONS AND FINANCIAL INTERESTS

Richardson v. Schafer, No. 10-8030 and *Tibble v. Jones*, No. 10-8031.

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

1) Is said party a subsidiary or affiliate of a publicly owned corporation? If Yes, list below the identity of the parent corporation or affiliate and the relationship between it and the named party:
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.

Respectfully Submitted,

By: s/ Adam G. Taub
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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, including fair credit reporting, 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.

ARGUMENT

I. Recognition of Michigan's bankruptcy-specific exemption is consistent with Congress' power to establish uniform bankruptcy laws.

A. Appellant's expansive reading of the *Hood* opinion vitiates the plain text of 11 U.S.C. § 522(b) and ignores the incorporation of state law that pervades the federal bankruptcy system.

The Bankruptcy Code permits a Michigan debtor to 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). The appellee debtors claimed exemptions in their homes under Mich. Comp. Laws § 600.5451(1) (n), their state exemption law in effect when they filed for bankruptcy relief. This law allows bankruptcy debtors who are disabled or over age 65 to exempt up to $51,650 in home equity. Bankruptcy debtors who are not over age 65 or disabled may exempt up to $34,500 in home equity.

The appellant Trustee asserts that Michigan's bankruptcy-specific homestead exemption is unconstitutional. In support of his position he relies on two Michigan bankruptcy court decisions, *In re* Pontius, 421 B.R. 814 (Bankr. W.D. Mich. 2009) and *In re* Wallace, 347 B.R. 626 (Bankr. W.D. Mich. 2006). These courts voided the homestead exemption claims debtors made under MCL § 600.5451(1) (n) as violative of the "Bankruptcy Clause" of the

U.S. Constitution. This 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 two Michigan bankruptcy courts based their holdings on their reading of the Sixth Circuit's opinion in Hood v. Tennessee Student Assistance Corporation, 319 F.3d 755 (6th Cir. 2003), *affirmed on other grounds*, 541 U.S. 440 (2004).

The Bankruptcy Clause applies to Congress, and does not limit legislation by the states. Railway Labor Executives Ass'n v Gibbons, 455 U.S. 457, 469 (1982). Thus, the Trustee's primary challenge does not assert that the Michigan legislature exceeded its authority in enacting MCL § 600.5451(1) (n). Rather, the Trustee contends that *Congress* acted beyond its constitutional authority in authorizing a state law such as Michigan's to be enforced in a bankruptcy case.

In Hood the Sixth Circuit panel addressed the question of whether Congress acted within its Article 1, Section 8 powers in enacting § 106 of the Bankruptcy Code. Section 106 expressly abrogates states' sovereign immunity in certain bankruptcy proceedings. The court concluded that the framers of the constitution intended a full and exclusive grant of authority to Congress to enact bankruptcy laws. This authority included the power to abrogate states' Eleventh Amendment sovereign immunity. Thus, the bankruptcy debtor in

Hood could seek a determination of the dischargeability of her student loan debt in a lawsuit filed in bankruptcy court against a state agency.

The instant case presents a fundamentally different application of the Bankruptcy Clause. Hood involved § 106 of the Bankruptcy Code, a section in which Congress expressly abrogated state's immunity. Here, the Court must consider § 522(b)(3)(A) of the Code, a section in which Congress expressly incorporated a positive rule for the enforcement of state law. Hood had nothing to do with the question of whether Congress can incorporate state law into the bankruptcy laws. The Trustee has fashioned a novel rule that is distinct from any holding of Hood . Applied as a rule of interpretation throughout the Bankruptcy Code, the Trustee's rule would annihilate all references to or incorporations of state law in the Code. A blanket rule mandating federal law exclusivity would preclude any recognition of state exemption laws as authorized by the plain language of § 522(b)(3)(A).

B. **The plain language of § 522(b)(3)(A) incorporates all state exemption laws as potential bankruptcy exemptions.**

By its plain language the text of § 522(b)(3)(A) allows a debtor to claim as exempt "any property" that is exempt under state law. In an effort to get around the unambiguous text of the statute, the Trustee must construct a bifurcation of the state exemption laws referred to in the statute. In his view,

Congress was referring only to "generally applicable" state exemption laws in § 522(b)(3)(A). Trustee-Appellants' Brief pp. 27-28. According to the Trustee, Congress really meant to exclude bankruptcy-specific state exemptions when it referred to "any property" exempt under state law in § 522(b)(3)(A). The Trustee cites to no textual support for his insertion of absent qualifiers into the plain text of the Code. Nor does he cite to any legislative history of § 522(b)(3)(A) to support such a revision. The Trustee's bifurcation of state exemption laws in the context of § 522(b)(3)(A) into "generally applicable" exemption laws and bankruptcy-specific exemption laws is a re-writing of the Code, contrary to its plain meaning and text.

The United States Supreme Court and the Court of Appeals for the Sixth Circuit have interpreted § 522(b)(3)(A) in a manner that directly contradicts the Trustee's gloss on the statute. According to the Supreme Court, nothing in the Code or elsewhere limits a state's power to fashion bankruptcy exemptions that will be recognized and given effect under § 522(b)(3)(A). Owen v. Owen, 500 U.S. 305, 308 (1991). The Supreme Court has concluded that Section 522(b) "allows the States to define what property a debtor may exempt from the bankruptcy estate that will be distributed among his creditors."). *Id* at 306. In construing § 522(b)(3)(A) the Sixth Circuit 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).

In its opinion in Hood the Sixth Circuit appropriately examined the constitutional authority for Congress to abrogate state sovereign immunity through the express terms of § 106 of the Code. However, it is a very different matter to extend that constitutional analysis to nullify a clear Congressional directive to incorporate state law into the scheme of exemptions applicable in bankruptcy. Such an interpretation runs afoul of the long-standing and substantial reliance of the Bankruptcy Code upon state law in countless aspects. *See e.g.* 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.").

The Trustee's Bankruptcy Clause argument, based on his idiosyncratic reading of Hood, creates another distinction that is completely unsupported by any text in the Constitution or the Bankruptcy Code. The Trustee's interpretation of the Bankruptcy Clause is premised on a non-existent limit to the Constitution's grant of power to Congress. The Trustee sees the Bankruptcy Clause as granting Congress the power to negate state laws, but not the power to treat state laws positively. Under this view, Congress could enact

a federal law, such as § 106 of the Code, abrogating traditional state immunities. However, under this restrictive grant of power, Congress could not enact a bankruptcy law that recognized or incorporated state laws, such as state property or exemption laws. If the Framers of the Constitution intended a plenary grant of power to Congress to enact bankruptcy laws, which is certainly the Trustee's position, then this deliberate hamstringing of the Congressional power could not have been something the Framers intended. As discussed in the following section, the courts' interpretations of the uniformity requirement of the Bankruptcy Clause have always been consistent with the view of a full and complete grant of legislative power to Congress.

C. The Trustee's view of the "uniformity" required by the Bankruptcy Clause is contrary to current Supreme Court precedent.

According to the Trustee, Congress could not authorize enforcement of MCL § 600.5451(1) (n) under § 522(b)(3)(A) because to do so would give effect to a bankruptcy law that was not "uniform." Thus, the Trustee's argument hinges on what is meant by a "uniform" bankruptcy law under Article I § 8 of the Constitution. To support his view of the requisite uniformity standard the Trustee relies heavily upon the 1902 U.S. Supreme Court decision in Hanover National Bank v. Moyses, 186 U.S. 181 (1902). The Hanover court upheld the Bankruptcy Act's reliance on state exemption laws, certainly a holding that undercuts the Trustee's position in this appeal. 186 U.S. at 189-90. In validating

the use of state exemptions in federal bankruptcy cases, the Hanover court rejected the contention that this practice violated the uniformity requirement of the Bankruptcy Clause. *Id.* State exemption laws had a uniform statewide application. In the court's view, the federal law's reliance on state laws having uniform geographic application within a state satisfied the constitutional uniformity requirement.

While ignoring the basic holding of Hanover, the Trustee has seized upon one sentence in the opinion as an endorsement of his position in this appeal. In approving the use of state exemptions, the Hanover court stated, "We concur in this view and hold that the system is, in a constitutional sense, uniform throughout the United States, when the trustee takes in each state whatever would have been available to the creditor if the bankrupt[cy] law had not been passed." Hanover, 186 U.S. at 190. In refusing to enforce MCL § 600.5451(1)(n), the Pontius court also considered this sentence from Hanover to express the controlling interpretation of the Bankruptcy Clause's uniformity requirement. *In re* Pontius, *supra,* 421 B.R. at 821. According to the Pontius court, in interpreting federal bankruptcy laws the "concept of geographical uniformity has been applied consistently." *Id.* The same sentence from Hanover regarding the bankruptcy trustee taking in each state whatever would have been available to creditors absent the bankruptcy filing appears quoted

four times in the Trustee's Brief. Trustee-Appellant's Brief on Appeal, pp.16, 32, 33, 34.

Contrary to the Pontius court's assurance of the "continuing validity" of a geographic uniformity requirement under the Bankruptcy Clause, the Hanover court's characterization does not reflect the current law. In 1982 the Supreme Court substantially modified Hanover's formulation of the Bankruptcy Clause's uniformity standard. Railway Labor Executives Ass'n v Gibbons, 455 U.S. 457, 469 (1982). The Trustee does not mention Gibbons in his Brief. Rather than mandating a strict geographical uniformity test, the Gibbons court held that, "[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. Instead of mandating geographical uniformity, the Supreme Court adopted a standard requiring a classification of affected parties that is general and does not benefit only one entity or person. This classification-based standard, and not the location-based standard the court approved in Hanover, is now the operative test for Bankruptcy Clause uniformity. *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."); *In re* Urban, 375 B.R. 882, 891 (B.A.P. 9th Cir. 2007) ("Because the uniformity clause is flexible and encompasses the concept of class, as well as geographic

uniformity, Congress may enact bankruptcy laws that treat defined classes of debtors or creditors differently, so long as the classification scheme applies in the same manner to all similarly situated parties."); *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 Hanover the Supreme Court approved an existing practice under federal law in which debtors could claim the exemptions applicable under the law of the state where they had lived for the greater portion of the preceding six months. Hanover, 186 U.S. at 189. In approving the exemption scheme then in effect, the court was not declaring all other exemption systems unconstitutional under the Bankruptcy Clause. The question of uniformity based on a class definition rather than geography was not before the Hanover court. Thus, Hanover does not preclude enforcement of bankruptcy specific exemptions at issue here. In any case, the contemporary uniformity standard, unlike the geographical uniformity scheme approved in Hanover , *does* allow for disparate treatment under an exemption scheme of debtors residing in the same geographical area. Under this rule a trustee will not always take the same property in bankruptcy that a creditor in the same state would take absent the bankruptcy.

As the bankruptcy court noted below in this matter, Congress' enactment of amendments to the Code in 2005 to control the "mansion loophole" indicates that when Congress wishes to do so, it will limit use of particular state exemptions. *In re* Jones, 428 B.R. 720, 729 n. 8 (Bankr. W.D. Mich. 2010); *See also In re* Applebaum, 422 B.R. 684, 690 (B.A.P. 9th Cir. 2009). The 2005 amendment to § 522(b)(3)(A) established an extended domiciliary requirement that must be satisfied before a debtor may claim the exemptions of his or her current state of residence. In order to claim the state law exemptions of the state of residence 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 debtors moving to a state such as Florida, with an unlimited homestead exemption, for the purpose of converting assets to exempt 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 jurisdiction. *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 exemptions under Ohio state 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 holding as characterized by the Trustee. 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, *supra*, 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 MCL § 600.5451(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.

The reach of the federal exclusivity doctrine espoused by the Trustee and the bankruptcy courts in Wallace and Pontius is extraordinary. If followed consistently, it would disrupt the interplay between state and federal law that has always been a cornerstone of American bankruptcy practice. The attempt to interject this doctrine into the sphere of bankruptcy exemptions is particularly inappropriate. The Trustee's arguments, as well as those of the bankruptcy courts in Wallace and Pontius, depend on faulty reasoning that does not stand up under scrutiny. For example, the Wallace court devised the following analysis, which both the Pontius court and the Trustee quote with approval and in full:

> [I]t is within Congress' discretion under the Bankruptcy Clause to decide what is to be the set of exemptions available to debtors seeking bankruptcy relief. Congress can create its own scheme. It can establish more than one scheme. It can reference state law for purposes of defining the scheme it has chosen. For that matter, Congress could reference the laws of Kazakstan to define the bankruptcy exemption scheme if it were to so choose. What Congress cannot do under the Constitution is delegate to Kazakstan, to the states, or to any other entity the power to actually decide what is to be the appropriate scheme. That power is reserved under the Constitution for the exclusive exercise of Congress.

Wallace, 347 B.R. at 635; Pontius, 427 B.R. at 820; Trustee's Brief at 27. This little dissertation is colorful and pithy. But what does it really say? It says that Congress can "reference" state law for purposes of defining a bankruptcy exemption scheme. Yet, it goes on to say that Congress cannot delegate to the states the "power to decide what is to be the appropriate scheme." Putting Kazakstan aside, the court's logic becomes derailed as it moves along. 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? States can either create their own sets of exemptions, which federal bankruptcy law will recognize, or the states cannot do this. The court's explication creates an unresolved contradiction.

Section 522(b)(3)(A) is either a valid exercise of Congressional power under the Bankruptcy Clause or it is not. Arguments such as those offered by the Trustee and the court in Wallace offer inconsistent and illogical views of the Congressional power exercised in § 522(b)(3)(A). They avoid the question of the validity of this exercise by writing new text into the Bankruptcy Code. The appellee debtors are correct in asserting that that Congress acted well within its constitutional authority in enacting § 522(b)(3)(A) and that application of MCL § 600.5451(1)(n) is perfectly consistent with the existing text of the Code.

II. The Trustee cannot show a conflict between MCL § 600.5451(1)(n) and the Bankruptcy Code because the Code expressly authorizes recognition of state-created exemptions in bankruptcy.

In order to prevail in a Supremacy Clause challenge the trustee must show that MCL § 600.5451(1)(n) "frustrates the full effectiveness of the federal law." Perez v. Campbell, 402 U.S. 637, 652 (1971); *In re* Vasko, 6 B.R. 317, 323 (Bankr D. Ohio 1980) ("The state law must in its effect, obstruct the basic objectives of the federal law.") Given the role that Congress expressly allocated to state-created exemption laws in bankruptcy, the Trustee cannot pass the threshold to begin a Supremacy Clause challenge. Significantly, Congress placed no limits on the content of state law exemptions to be recognized in bankruptcy cases. Owen v. Owen, 500 U.S. 305, 308 (1991); Sheehan v. Peveich, 574 F.3d 248, 252 (4th Cir. 2009); Storer v. French, 58 F.3d 1125, 1128-29 (6th Cir. 1995).

In view of § 522(b)(3)(A)'s plain language, there can be no conflict between use of state-created exemptions and the federal law. Rhodes v. Stewart, 705 F.2d 159, 163 (6th Cir. 1983) ("It is equally axiomatic, however, that Congress has not preempted an area wherein it has legislated when it expressly and concurrently authorizes the state legislatures to disregard or opt-out of such federal legislative area. In such instance, rather than preempting the area, Congress expressly authorizes the states to 'preempt' the *federal* legislation."(emphasis in original)); *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 Code "is simply inaccurate"); *In re* Applebaum, 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.")

Given the Code's clear language, the Trustee can only struggle to create the appearance of a conflict between the operation of the federal and state exemption provisions. One of the Trustee's tactics is to characterize the Michigan law as something other than an exemption law. For example, in his Brief the Trustee endorses a distinction drawn by the Indiana bankruptcy court in *In re* Cross, 255 B.R. 25 (Bankr. N.D. Ind. 2000), a decision striking down a bankruptcy-specific state exemption. The Trustee provides the following quote from the court:

> Recognizing otherwise applicable state exemptions in bankruptcy proceedings is not the same as allowing states to create exemptions just for those proceedings. The first situation simply recognizes non-bankruptcy entitlements. It allows debtors to protect the same property in bankruptcy that they could keep from creditors outside of bankruptcy. *The second directly controls the distribution of assets between debtors and creditors and, thus, how the consequences of bankruptcy are allocated between them.*

Cross, 255 B.R. at 34 (emphasis added) (quoted at Trustee's Brief p. 28). This purported distinction between "otherwise applicable state exemptions" and state bankruptcy- specific exemptions does not withstand scrutiny. In fact, all exemptions applied in bankruptcy, whether bankruptcy-specific or not, directly control the distribution of assets between debtors and creditors. The Trustee and the Cross court describe a distinction without a difference and call it a "conflict."

In another attempt to conjure up a conflict scenario the Trustee again quotes extensively from Cross. Trustee's Brief p. 39, referring to Cross, 255 B.R. at 34-35. Here, the argument focuses on a parade of horribles that could possibly ensue if states were allowed to create bankruptcy-specific exemptions. According to the Cross court, this would make it possible for states to pass extreme laws, allowing either no exemptions at all in bankruptcy or exempting all of a debtor's property from the bankruptcy estate. Yet, on the same page of his Brief, the Trustee again refers to Cross, quoting that court's conclusion: "Indiana can create any exemptions it wants or no exemptions whatsoever. What it may not do, however, is create (or deny) exemptions solely because of bankruptcy." Cross at p. 36, Trustee's Brief. p. 39. This quote displays a fundamental flaw in the Cross court's analysis and in the arguments of the Trustee. Namely, states do not need bankruptcy-specific exemptions in order to bring about the dire consequence of all-or-nothing exemptions in

bankruptcy cases. As the Cross court recognized, states, as a matter of their general law, can create any exemptions they want, or none at all, and these can be applied in bankruptcy cases. The focus on bankruptcy-specific exemptions as having the potential in and of themselves to undermine the bankruptcy system is a red herring. The bankruptcy court below correctly noted that it is the effect of state exemption statutes, not their appearance in the form of bankruptcy-specific exemptions, that in a myriad of ways creates incentives or disincentives for debtors or creditors to get involved in a bankruptcy proceeding. *In re* Jones, *supra*, 428 B.R. at 729.

Finally, to support his Supremacy Clause argument the Trustee relies heavily upon the pre-Code decision in International Shoe Co. v. Pinkus, 278 U.S. 261 (1929). Pinkus involved a debtor who filed for relief under an Arkansas insolvency law. The state statute in question purported to operate as a full-service bankruptcy law, setting out a scheme for liquidation of assets, distribution to creditors, and discharge of debts. The debtor in question was barred from obtaining a discharge of debts under the federal Bankruptcy Act in effect at the time because he had obtained a federal bankruptcy discharge within the past six years. Therefore, he filed for relief under the state law and obtained a discharge of his debts. The state law in question clearly conflicted with the federal Bankruptcy Act by discharging debts that could not be

discharged under the federal law. The Supreme Court held that the state law discharge was invalid as contrary to the controlling federal law.

At one point in its Supremacy Clause analysis the Pinkus court stated, "States may not pass or enforce laws to interfere with or complement the Bankruptcy Act or to provide additional or auxiliary regulations." 278 U.S. at 265. The state "laws" the court was addressing here were entire insolvency systems that operated tangentially to the federal system, paying out creditors and granting discharges in contravention of federal law. The Trustee in the instant case never discusses the nature of the comprehensive state law at issue in Pinkus. Instead he seizes upon the court's language to the effect that states cannot pass laws that "complement" the federal bankruptcy law. Trustee-Appellant's Brief, pp. 19, 23 n. 1.

As he did with his frequent references to a sentence expressing an outdated legal rule from the Hanover decision, the Trustee refers repeatedly to this sentence from Pinkus, despite its outdated characterization of the relevant constitutional test, its vastly different context, and its appearance decades before the enactment of Bankruptcy Code § 522(b)(3)(A). Section 522(b)(3)(A) invites states to "complement" federal bankruptcy law. They are invited to do so by formulating their own bankruptcy exemptions. States that accept this invitation are not obstructing the basic objectives of the federal law; they are furthering those objectives.

CONCLUSION

For the foregoing reasons, the judgment of the Bankruptcy Court should be affirmed.

Respectfully Submitted,

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CERTIFICATE OF COMPLIANCE

Compliance with Type-Volume Limitations, Typeface Requirements, and Type Style Requirements

1. The brief complies with the type-volume limitations of FED. R. BANK. P. Bankruptcy Procedure 8010, 6th Cir. BAP LBR 8010-1(d) and FED. R. APP. P. 32(a)(5) and 32(a)(7)(B) because:

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