

1 IN THE SUPREME COURT OF THE UNITED STATES

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3 STEPHEN LAW, :

4 Petitioner : No. 12-5196

5 v. :

6 ALFRED H. SIEGEL, CHAPTER 7 :

7 TRUSTEE :

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9 Washington, D.C.

10 Monday, January 13, 2014

11

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

15 APPEARANCES:

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

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

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

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1 P R O C E E D I N G S

2 (11:39 a.m.)

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

6 Mr. Hellman.

7 ORAL ARGUMENT OF MATTHEW S. HELLMAN

8 ON BEHALF OF THE PETITIONER

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

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

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

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

23 The bankruptcy court was not free to
24 override that express and specific prohibition in the
25 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.

17 But our point here is that Congress had made
18 the determination -- we could have -- there could be a
19 policy discussion, of course, about whether exempt
20 property ought to be allowed to go to the administrative
21 costs of the estate or to prepetition creditors in
22 situations in which the -- a court finds litigation
23 misconduct.

24 But that is not the judgment Congress made.

25 JUSTICE ALITO: What was -- what was the

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

8 What should he do?

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

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

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

25 So, again, I think the question is one of

1 policy, and one the policy where Congress has spoken
2 clearly. The text of --

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

5 MR. HELLMAN: Yes, Your Honor.

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

11 MR. HELLMAN: Well, inherent power --

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

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

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

23 This case is about a court saying the
24 property from which that -- that sanction can be
25 satisfied, out of what property can that sanction be

1 paid or forced to be paid. And there --

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

5 MR. HELLMAN: Not --

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

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

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

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

25 There, in Ginsberg, the debtor was a

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

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

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

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

23 This is a case not by implication, but an
24 express prohibition: Exempt property is not liable for
25 the payment of any administrative expense, save in two

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1 situations. It wasn't even as if Congress --

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

11 MR. HELLMAN: Of course, as was the case
12 here, there was a denial of discharge, the classic and
13 serious penalty for debtors who engage in misconduct
14 before a bankruptcy court. Now what that means in almost
15 every case is that there will be debts owed to
16 pre-petition creditors that remain unpaid.

17 It's essentially the bankruptcy death
18 penalty in the sense that it makes the debtor liable for
19 the rest of his days until those debts are paid off.
20 That's a very serious punishment.

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

1 MR. HELLMAN: Two points, Your Honor. One,
2 the question to where you want to draw the line about
3 deterring debtor misconduct and leaving debtors without,
4 literally, their last dollar coming out of bankruptcy is
5 an important question, but a policy question, and one
6 where Congress has spoken with an expressed prohibition.

7 Now, there are other sanctions, not -- none
8 of which were levied here or sought to be levied here,
9 Rule 11 and the like, that might serve to provide an
10 additional source of funds, but not from exempt
11 property, because Congress has walled that off. If one
12 looks --

13 JUSTICE BREYER: The same thing is true of
14 certain retirement funds.

15 MR. HELLMAN: Yes, Your Honor.

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

22 MR. HELLMAN: Congress has amended
23 Section 522 already eight times since 1978, about once
24 every 4-1/2 years, if my math is correct, to fine-tune
25 the extent to which debtors can claim exemptions. As

1 the Court is aware, in 2005 for example, the -- Congress
2 limited the extent to which a debtor could claim an
3 exemption in his homestead, I suppose precisely for
4 analogous reasoning to what Your Honor suggests.

5 It's still nonetheless perfectly clear from
6 Section 522(k) that Congress has not created or allowed
7 some sort of free-floating equitable discretion for
8 bankruptcy courts to reach a different result in cases.
9 And again I would like to point the Court to Section
10 522(c) as well, which is the companion provision to the
11 administrative expenses provision.

12 As the Court, of course, is aware, debtors
13 often have debts arising from all sorts of improper
14 conduct, willful and malicious injury, criminal
15 restitution awards, fraud, embezzlement, there is a
16 whole list of these things in Section 523 and the Code
17 makes these debts non-dischargeable, inherent per se
18 non-dischargeable, meaning that when you go through
19 bankruptcy you're not going to be able to escape paying
20 these debts once the bankruptcy is over.

21 However, in Section 522(c)(1) of the code
22 Congress picked out just two, just two of those
23 categories of debts, alimony and certain tax liability,
24 of these non-dischargeable debts that could be satisfied
25 from exempt property.

1 The debtor who has a wrongful death
2 judgment, the debtor who has a fraud judgment, the
3 debtor who has a criminal restitution award, all of
4 those debts are non-dischargeable, they stay with the
5 debtor until they're paid, but they are expressly not
6 paid from exempt property.

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

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

20 MR. HELLMAN: It's actually even less
21 friendly to the debtor than that, Your Honor. Under
22 California law -- and Federal law takes State law
23 exemptions as it finds it absent a contrary Federal
24 provision -- the debtor if he ever were to receive the
25 \$75,000, by law, California law, would have 6 months to

1 reinvest it in a homestead. That's what California is
2 doing. It's saying, we are going to give you the
3 opportunity to reinvest and have a home.

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

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

13 MR. HELLMAN: Those States that give a
14 homestead exception, and that's 48 of 50, all, with the
15 exception of Pennsylvania and New Jersey, which use the
16 Federal homestead exemption, all of those -- the vast
17 majority of those States have a reinvestment principle.

18 I know Illinois does, I know that several
19 other States do as well, for just the reason Your Honor
20 suggests. This money is not put away in a box such that
21 it can't be touched again. The homestead exemption
22 represents an opportunity for the debtor to have a home.
23 That's what California law protects and California in
24 its judgment decided to award.

25 JUSTICE GINSBURG: Are you saying that he

1 must spend the \$75,000 on a new residence within how
2 many -- what period of time?

3 MR. HELLMAN: 6 months, Your Honor.

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

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

13 The Federal law doesn't have a contrary
14 provision that would --

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

18 MR. HELLMAN: It is available to his
19 creditors.

20 JUSTICE GINSBURG: They have been paid
21 already.

22 MR. HELLMAN: That's right. And the way
23 bankruptcy -- Congress has chosen to make the Bankruptcy
24 Code work is that absent any sort of special award
25 when -- when Congress has made the determination that a

1 debtor is not liable for his administrative expenses
2 once the bankruptcy case closes, even if there has been
3 a denial of discharge.

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

11 JUSTICE GINSBURG: So then what you said
12 before needs to be modified. He does get to keep the
13 \$75,000 because there is no creditors to be paid off
14 from.

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

20 JUSTICE KENNEDY: When you say, "paid off,"
21 do you mean paid off 100 percent?

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

1 CHIEF JUSTICE ROBERTS: So what you started
2 with, oh, this is a terrible sanction, he's denied a
3 discharge and all that, that doesn't mean a thing to
4 him, does it? Because everybody's paid off. He doesn't
5 have any debts.

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

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

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

1 code -- that is the language that controls.

2 CHIEF JUSTICE ROBERTS: I should know this,
3 but who's going to get stuck with the extra couple
4 hundred thousand dollars? Is that the trustee in an
5 individual capacity or someone else?

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

8 CHIEF JUSTICE ROBERTS: They don't recoup
9 that from anywhere else, right? They are on the hook
10 for that?

11 MR. HELLMAN: That is correct, Your Honor.
12 That is correct.

13 Now, the primary authority --

14 JUSTICE KENNEDY: Do they get a thank-you
15 letter from the --

16 (Laughter.)

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

24 In Marrama, the court was -- the Marrama
25 majority was clear to note that no provision of the code

1 expressly forbid the result that the court was going to
2 allow, and that 105 -- Section 105 in that case was
3 being used to accomplish something the code permits and
4 to do it promptly rather than in a delayed fashion.

5 This case is not about prompt versus
6 delayed. This is about doing what the code expressly
7 forbids. This case is not about what Section 105
8 allows. This case is about what section 522 expressly
9 forbids.

10 And, here, Congress has made the judgment,
11 considering all the different deterrent mechanisms and policy
12 interests at play, Congress has made the judgment that
13 administrative expenses are not liable for any
14 administrative -- exempt property is not liable for any
15 administrative expense.

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

21 MR. HELLMAN: We do disagree, Your Honor.
22 The equities in that case, I suppose, are sharper in the
23 sense that the debtor is leaving bankruptcy with more
24 money than he otherwise would be able to have. But it
25 is just as clear in that case that Congress has not made

1 the exception that -- it's more than -- this is not a
2 negative implication case.

3 I want to stress that. It's not just that
4 Congress hasn't put this on the list of things that
5 can't be done. Congress has a flat-out prohibition the
6 structure is not liable for any administrative expense
7 or any prepetition debt, save in the enumerated
8 circumstances.

9 So, yes, with respect, I do think Malley was
10 wrongly decided, and this Court need do nothing more
11 than reaffirm what it has done for 80 years, which is to
12 say that 105 gives bankruptcy courts the power to act.
13 Our position is quite modest. We're only saying they
14 can't do what the code forbids.

15 Whether the code is -- whether they're
16 acting interstitially or they're acting to carry out
17 express provisions of the code, of course that's what
18 105 does.

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

25 JUSTICE KAGAN: But, Mr. Hellman, (k) of

1 course talks about exempt property.

2 MR. HELLMAN: Yes.

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

6 MR. HELLMAN: Yes.

7 JUSTICE KAGAN: -- (1) says, "unless a party
8 in interest objects, the property claimed as exempt is
9 exempt." Now, that suggests that if the party in
10 interest does object, there's a question about whether
11 the party claimed as exempt is exempt.

12 So -- so why isn't it a permissible reading
13 of the statute to essentially say the court gets to
14 decide whether this is exempt property such that (k)
15 comes into effect, and in deciding whether it's exempt
16 property, it can take into account the Petitioner's
17 abuse of process?

18 MR. HELLMAN: Two points. Of course, no
19 objection was ever lodged within the time period that
20 rule --

21 JUSTICE KAGAN: Yes. I completely agree
22 with that, but suppose one were.

23 MR. HELLMAN: That objection -- that
24 objection would not be well founded because it is
25 undisputed that Petitioner is entitled to his homestead

1 exemption under California law. California law says
2 this is his home, he's lived there for the requisite
3 amount of time, he has the equity, all of that.

4 Congress later, in provisions that wouldn't
5 apply to this case either, put some limits on a debtor's
6 ability -- Federal limits on a debtor's ability to claim
7 his homestead exemption; if money is poured into the
8 home before declaring bankruptcy, Congress cut back on
9 that a little bit. And I suppose you could have an
10 objection on that basis.

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

19 JUSTICE ALITO: So you're saying a creditor
20 could not have objected when your client claimed the
21 exemption on the ground that the exemption is going to
22 prevent the discovery -- the disclosure of the
23 fraudulent nature of this mortgage.

24 The creditor could not have objected to the
25 exemption on that basis?

1 MR. HELLMAN: The objection was proper. So
2 the answer to your question is yes, no objection -- no
3 objection would have been proper in that situation
4 because --

5 JUSTICE ALITO: And why is that?

6 MR. HELLMAN: Because Section 522, the way
7 it works is that the question is are you entitled to the
8 exemption under State law. That's what Section 522(b),
9 I believe, asks you to look at. And then there's a
10 question of is an objection going to be interposed
11 within the period provided by Section 522(l).

12 Congress, of course, is free to create other
13 limitations on a debtor's ability to claim exemptions.
14 And as I said, they have done that in Section 522(o),
15 Section 522(p), Section 522(q), which deals
16 specifically, by the way, with situations in which the
17 very filing of the bankruptcy case is a -- is an abuse
18 of the code.

19 And in that case, in Section 522(q),
20 Congress ultimately decided that for debtors whose
21 fraud -- and is convicted of a felony whose filing of
22 the case shows that it's an abuse of the code, Congress
23 decided in those cases that a debtor should not lose all
24 of his exempt property.

25 They put a cap in at \$155,000, which, as

1 Your Honor points out, is quite generous, quite generous
2 given the median income of -- of the American family;
3 and further stated that exemption could be tilted upward
4 where necessary to support the debtor and his
5 dependents. Not downward, no discretion to go downward,
6 but can go upward, if necessary, in the bankruptcy
7 court's view to support the debtor -- reasonably
8 necessary to support the debtor and his dependents.

9 So Congress -- so your question was could
10 there have been an objection? The answer is no. And I
11 would just say in passing that Congress has decided and
12 has amended the statute several times to fine tune
13 exactly when it is -- there ought to be or could be an
14 objection to property validly claimed as exempt under
15 State law.

16 This is not one of those cases; far from it.
17 And, again, I want to stress, this is not an argument
18 from negative implication. This is not an argument from
19 interstices. This is an argument from express and
20 categorical prohibition.

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

23 CHIEF JUSTICE ROBERTS: Thank you, counsel.

24 MR. HELLMAN: Thank you.

25 CHIEF JUSTICE ROBERTS: Mr. Katyal.

1 ORAL ARGUMENT OF NEAL K. KATYAL

2 ON BEHALF OF THE RESPONDENT

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

5 The facts explain why the bankruptcy court
6 exercised its discretion appropriately under both
7 Section 105(a) and the longstanding inherent power of
8 the court. Mr. Law committed a massive fraud on that
9 court with the fake Lily Lee mortgage and fake documents.
10 Petitioner lied repeatedly to the court, and then lied
11 about his lies, all in an attempt to retain nonexempt
12 property and equity in his home in contravention of the
13 code.

14 Section 105(a) was made for a case like
15 this. It provides ample authority for what the
16 bankruptcy court did, both in its first sentence, which
17 uses a sweeping formulation of any order necessary or
18 appropriate and as well as its second sentence which
19 gives bankruptcy courts, quote, "the broad authority to
20 take any action that is necessary or appropriate to
21 prevent an abuse of process."

22 That is the language Marrama used to
23 describe the second sentence, and it fits here
24 perfectly.

25 JUSTICE SOTOMAYOR: My problem is -- my

1 problem is that I read the sentence and it lops off its
2 beginning. What the beginning says is "No provision of
3 this title providing for the raising of an issue by a
4 party of interest can stop a court from doing that." An
5 abusing process, presumably.

6 So how could a party legitimately, whether
7 the trustee or anyone else, make any claims to the
8 exempt property?

9 MR. KATYAL: Justice Soto- --

10 JUSTICE SOTOMAYOR: How can the Court do
11 something neither the Bankruptcy Code nor any of its
12 provisions permit the trustee to do?

13 MR. KATYAL: Justice Sotomayor, for
14 precisely the reasons that both Marrama and Justice
15 Souter in the Malley case suggested, which is at the
16 second sentence fortifies --

17 JUSTICE SOTOMAYOR: That's your strongest
18 argument, that Justice Souter --

19 MR. KATYAL: Well, it's at the second
20 sentence fortifies the first; that is, the way to
21 understand the second -- the power of the court and the
22 orders that are necessarily appropriate. One such power
23 is to remedy fraud upon the court, the abuse of process.
24 That's what Congress used.

25 JUSTICE SOTOMAYOR: My problem is that the

1 code itself doesn't do that. It limits the access to
2 the exemption to specified frauds, to frauds that result
3 in a conviction. To amounts, it doesn't permit the
4 exemption -- it -- it does away with the exemptions for
5 an amount above 155.

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

8 MR. KATYAL: Well, of course, that provision
9 wasn't in effect at the time. That's 522(q) which you
10 are referring to. But we think 522(q) doesn't -- isn't
11 violated here. Absolutely, you're right, Justice
12 Sotomayor, if there were a violation of 522(q), 105(a)
13 couldn't take that back.

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

21 It says nothing about the longstanding power
22 of the court to depart downward and to give up to zero.
23 It's just like a punitive damages cap. So Florida's
24 punitive damages law says that if you have -- if you're
25 the victim of medical malpractice or something, you can

1 get up to \$500,000. You shall -- your award shall not
2 exceed \$500,000.

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

7 Mr. Law tried to invoke the protections of
8 the code while he repeatedly defied the obligations
9 under the code at every turn.

10 JUSTICE SOTOMAYOR: Would you ask -- would
11 you answer Justice Breyer's question? Does this power
12 go to invading the other exempt properties, like an IRS?
13 I'm assuming there are now invasion provisions for an
14 IRS, but would this power permit the court to invade
15 an -- not an IRS --

16 JUSTICE BREYER: An IRA.

17 JUSTICE SOTOMAYOR: Thank you. An IRA.

18 MR. KATYAL: Our argument here is just
19 limited to this type of case in which you're lying about
20 the underlying asset itself and trying to seek an
21 exemption. I know the Solicitor General advances a
22 broader argument, and I suppose that the Court can deal
23 with that in an appropriate case.

24 But here, Mr. Law undervalued his home and
25 put all of these fake mortgages on, and then repeatedly

1 submitted perjured documents to the court about the very
2 exemption. And as Justices -- Justices Ginsburg and
3 Alito said before, what's a Trustee to do in that
4 situation except investigate? That's his duty under
5 Section 704, to try and figure out what has happened.

6 CHIEF JUSTICE ROBERTS: Well, he doesn't have to
7 investigate to the tune of half a million dollars
8 chasing a much smaller amount that is at issue.

9 MR. KATYAL: Well, I think,
10 Mr. Chief Justice, that's the wrong way to look at it,
11 with all respect. For one thing, of course, the -- the
12 trustee's actions allowed title to be cleared and the
13 underlying house to be sold for \$680,000, paying off all
14 the creditors.

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

20 And the second thing is, of course, that
21 when the trustee started his investigation and realized
22 there was a fake mortgage, he would have never thought
23 that this would have become, as you said, a
24 half-million-dollar case. He would have thought, well,
25 look, these documents prove this is a fraud.

1 But what Mr. Law did in response was to take
2 19 separate appeals to -- you know, 14 to the bankruptcy
3 appellate court, five to the Ninth Circuit. I mean --
4 you know, I looked at --

5 JUSTICE BREYER: He behaved very badly, and
6 in view of this, I agree with that. Why wouldn't -- or
7 why didn't the -- or why couldn't the trustee simply
8 sanction? I mean, you have apparently the authority
9 here in 105 to sanction conduct abusive of the judicial
10 process.

11 That includes an order directing payment of
12 expenses. Okay. I guess this is an expense. And that
13 wouldn't be discharged, because it's a postpetition
14 debt.

15 So why not just do that? And even if he
16 doesn't have money now, if he ever gets any he's going
17 to have to pay it. So it looks as if there's an
18 alternative way of paying for this.

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

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

1 MR. KATYAL: Because for --

2 JUSTICE BREYER: -- and you have general
3 language over here saying a general power to sanction,
4 and you have an alternative way that's perhaps almost as
5 good, why read the language that says no to say, well,
6 yes?

7 MR. KATYAL: I want to respond to why there
8 isn't an expressed prohibition in a minute. But just
9 taking your point before, the reason is the facts of
10 this case. That is, the sanction would only be paid out
11 of postpetition debt.

12 And I think there's a pretty good reason why
13 my friend's brief on the other side is willing to
14 entertain sanctions and the like, because he would
15 engage in the same type of conduct that he has now,
16 repeatedly stymying the court in the ability to try and
17 get that \$75,000 sanction, should it ever be imposed.

18 And so that -- so sanctions come from
19 postpetition assets. And that's I think one of the
20 problems.

21 Now, with respect to the bigger question, is
22 there a prohibition somewhere in the code? We don't
23 think there is. We don't think 522(k) says anything
24 like what my friend said in his opening sentence, that
25 this is somehow an express prohibition. We think that

1 the language of 522(k) has to be read against three
2 different things, the first, Section 105(a) and its
3 sweeping language; second, something you never heard a
4 word about in my friend's argument on the other side,
5 which is the longstanding presumption that the
6 protections of the Bankruptcy Code are meant for the
7 honest but unfortunate debtor; and third, language in
8 522 which Justice Kagan alluded to which suggests that
9 someone is not entitled to the right of an exemption,
10 and the court can take it -- the court can refuse to
11 provide it in the first place.

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

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

22 JUSTICE KAGAN: I think that's a little bit
23 backwards, right? Doesn't 105 exist to the extent that
24 there's no prohibition saying otherwise? And then
25 522(k) comes in, and there's your prohibition.

1 MR. KATYAL: No, because I think in order to
2 understand what the prohibition was, you have to -- you
3 have to look to 105(a); that is, what 105(a) does is it
4 says, in general, you have this power. And indeed,
5 522(k), I think it speaks of the general case in which
6 there isn't this type of excessive bad faith, fraud on
7 the court.

8 And so absolutely, I think in general, just
9 as in Marrama itself, there's general language which
10 says administrative expenses normally aren't liable.
11 But in the atypical case, to use Marrama's words, a case
12 like this in which the only way the code would work and
13 functionally work is to incentivize trustees to try and
14 uncover the fraud.

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

19 MR. KATYAL: Your Honor, I think that's what
20 generally both the Hunt prohibition and indeed the first
21 line of Marrama says, which is that the basic idea of
22 the Bankruptcy Code is to provide honest but unfortunate
23 debtors a system of relief. And it misses the forest
24 for the trees to essentially look with tunnel vision
25 just at (k). (K) exists within a larger framework of

1 background duties and obligations that a debtor must
2 comply with.

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

7 And if you adopt Mr. Law's formulation,
8 you're essentially saying that the main architect -- the
9 main safeguard against this type of abuse, the trustee,
10 is left holding the bag at the end of the day. The
11 trustee is the only one here who acted, I think,
12 appropriately, trying to uncover all of this, and he
13 would be stuck with hundreds of thousands of dollars in
14 attorneys' fees.

15 JUSTICE BREYER: But couldn't the --
16 couldn't the bankruptcy judge just deny him, deny him
17 bankruptcy?

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

24 JUSTICE SOTOMAYOR: How do you limit in a
25 principled way -- you say where you differ with the

1 Solicitor General is that if an -- if an IRA had existed
2 here, they would say that could be used. And you're
3 saying, I don't need to go that far. That's on the
4 facts. But on what theory would you limit recovery in
5 those situations?

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

11 And if -- if there is a situation in
12 which -- you know, if some sort of forfeiture was a
13 massive amount compared to the underlying fraud on the
14 court, that wouldn't be appropriate.

15 That would be reviewed under abuse of
16 discretion. All we're suggesting here --

17 JUSTICE KENNEDY: That's hard to enforce.
18 Every lawyer's case is an exceptional case. That's just
19 the way it works.

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

25 This isn't just fraud on the Court, it's

1 fraud on the Court squared. They're lying about the
2 lies themselves. And the bankruptcy court can't work,
3 it can't function if you don't have the trustee
4 incentivized to under -- to undertake the kind of
5 investigation that occurred here.

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

10 And when you have someone like Mr. Law,
11 who's a serial liar to the Court, this isn't just bad
12 faith, Justice Kennedy. This isn't just -- you know,
13 one document that is wrong by 5 or \$10, this is repeated
14 perjury to the Court. And that is the quintessential
15 thing Section 105 is about when it talks about abuse of
16 process.

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

20 JUSTICE BREYER: It made me think of a --
21 think of a bankruptcy petitioner who, in part, has a
22 debt arising towards a creditor that consisted of the
23 most frightful conduct you can think of. I mean,
24 something really awful that he did to somebody. And yet
25 that debtor can be excused, bankrupt, and keeps the

1 \$75,000.

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

7 MR. KATYAL: For two reasons,
8 Justice Breyer, because Section 105(a), as well as the
9 inherent power of the Court deal with specifically this
10 type of situation, abuse of process, fraud on the Court
11 itself, not any type of prepetition conduct or anything
12 like that. It's targeted to this. And, of course, the
13 language in 522(q), which we were talking about earlier,
14 is only about that prepetition conduct.

15 It doesn't have -- so absolutely. Congress
16 is free, if they want, to abrogate 105(a) or the
17 inherent power of the Court and to say, look, if you've
18 engaged in bad faith, fraud on the Court, whatever,
19 you're still entitled to your exemption. That's not
20 what it says.

21 To the contrary, and this picks up on
22 Justice Kagan's point earlier, 522(l) and (v) provide a
23 mechanism to reject an exemption that is being sought.
24 And here, that happened. 522(l) says -- and this is
25 laid out at our brief at pages 38 and 39 -- if someone

1 raises an objection to an exemption that a debtor is
2 seeking, that exemption can be denied.

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

5 MR. KATYAL: It doesn't --

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

9 MR. KATYAL: 522(1) doesn't say that. It
10 refers to a party in interest, which could be a trustee
11 as well. And so here, we think both the trustee
12 objected in filing the motion for -- in 2006 as well as
13 the Court itself. Section 105 has to be read alongside
14 522, and it provides the Court the sua sponte power to
15 do so.

16 There is a time limit, Justice Ginsburg, in
17 Rule 403, but that time limit can itself be extended if,
18 under the terms of the rule, if there's been a
19 subsequent amendment of the underlying schedule. And
20 here we think effectively, there was a subsequent
21 amendment of the underlying schedule; that is, Mr. Law
22 lied.

23 And I think there's a very strong reason why
24 the time limit shouldn't apply here. Imagine that a
25 debtor took a fake set of exemptions and bribed the

1 trustee to look the other way for 30 days. If that were
2 discovered on day 45, I think it would be thoroughly
3 implausible to think that you could -- that the debtor
4 could get the underlying exemption, something that he
5 bribed and lied about just because it didn't meet the
6 30-day requirement.

7 JUSTICE GINSBURG: Maybe you get it from the
8 trustee.

9 MR. KATYAL: I think that --

10 JUSTICE GINSBURG: The faithless trustee.

11 MR. KATYAL: You might be able to go after
12 the trustee as well, but I don't think that the
13 underlying exemption would be given in that
14 circumstance. It's a paradigmatic instance of both the
15 105(a) power as well as the inherent power of the Court.

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

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

1 JUSTICE ALITO: Well, Mr. Hellman said that
2 the creditor and, I guess, any other party could not
3 object to the exemption on the ground that the house was
4 burdened with a fraudulent mortgage. Do you agree with
5 that?

6 MR. KATYAL: I don't. I don't think
7 anything in the language of 522(l) so restricts it.
8 There are other provisions in the Code which say if an
9 objection has been made, for example, to a creditor
10 under Section 502, that the Court's power to deny that
11 relief is circumscribed in 9 different ways. But there
12 is no restriction on the power of the Court here.

13 And that's why I think Justice Kagan's
14 question gets at this point, which is 522(k) assumes
15 that an exemption has been given, and there's a strong
16 reason under the Code the Court is given the power to
17 deny an exemption in the first place.

18 JUSTICE ALITO: Do you have any authority
19 that says that there could be an objection on that
20 basis?

21 MR. KATYAL: I think just the text at 522
22 itself says so.

23 If there are no other questions.

24 CHIEF JUSTICE ROBERTS: Thank you, counsel.
25 Ms. Harrington.

1 ORAL ARGUMENT OF SARAH E. HARRINGTON,
2 FOR UNITED STATES, AS AMICUS CURIAE,
3 SUPPORTING THE RESPONDENT

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

6 I'd like to start, if I could, by taking a
7 little bit of a step back to note that outside of the
8 bankruptcy system, an individual who runs up more debts
9 than they can satisfy with their collective assets has
10 no right to wipe out those debts while retaining some of
11 their property in the face of unpaid assets. That right
12 only comes from the Bankruptcy Code itself. But you
13 only get that right if you follow the rules of
14 bankruptcy.

15 The Petitioner asked this Court to
16 myopically focus on certain provisions of the Code and
17 only provisions of the Code that actually benefit the
18 debtor. But you have to look at any provision of the
19 Code in the context of the whole Code itself because all
20 the provisions are intended to work together.

21 In this case, the surcharge order was
22 necessary and appropriate to enforce provisions such as
23 Section 521 and Section 704 of the Code. Section 521
24 imposes duties on debtors. Those duties include the
25 duty to honestly disclose assets and liabilities, the

1 duty to turn over property to the estate, to the
2 trustee, and the duty to cooperate with the trustee
3 throughout the case.

4 Now, Mr. Law flouted all of those
5 obligations, making it impossible to carry out the
6 provisions of those parts of the Code without
7 surcharging him in some way.

8 Section 704 imposes duties on the trustee.
9 Those duties include the duty to investigate the
10 financial affairs of a debtor and the duty to collect
11 the property of the debtor, reduce it to money and give
12 that money to creditors. And the trustee doggedly
13 pursued his duties under Section 704, but because of Mr.
14 Law's bad faith litigation behavior, he imposed a great
15 cost on the exercise of those duties.

16 And so the Bankruptcy Court exercised its
17 discretion to try to offset some of those costs by
18 imposing a surcharge on what would have otherwise been
19 exempt property of the debtor.

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

1 Now, as I read your brief, you're
2 essentially asking us to put the word "usually" in that
3 provision. Is not usually liable. When is it -- when
4 is it liable? It's -- it's liable when there are
5 special circumstances dealing with debtor dishonesty.
6 And where does that come from?

7 MS. HARRINGTON: What we're asking to do is
8 look at all the provisions of the Code together. And
9 certainly, Section 522(k) expresses Congress's policy
10 judgment that generally honest debtors should not have
11 their exempt property used to pay administrative
12 expenses.

13 But as I've said, 521 and 704 express
14 Congress's policy judgments about what debtors are
15 supposed to do and what trustees are supposed to do.
16 And Section 105 give -- gives Bankruptcy Courts
17 authority to address very unusual circumstances that
18 involve bad faith litigation conduct. So that's bad
19 conduct in the litigation.

20 I think that is an implicit exception to
21 most of the general rules that are laid out in the
22 Bankruptcy Code.

23 In this case, it's really impossible for the
24 Court to have carried out all of the provisions of the
25 Code, but that's directly because of the debtor's

1 behavior in this case, Petitioner's behavior. And so
2 here in this extraordinary circumstance, the Bankruptcy
3 Court addressed that bad faith litigation behavior by
4 exempting what otherwise would have been -- by -- excuse
5 me -- surcharging what otherwise would have been exempt
6 property.

7 CHIEF JUSTICE ROBERTS: What is the -- you
8 do have good facts on your side. But what if the
9 offense is simply the failure to list a particular
10 asset? Does that justify a departure from the usual
11 rule?

12 MS. HARRINGTON: I mean, if it's a
13 negligent -- negligent failure to list the asset, then I
14 don't think --

15 CHIEF JUSTICE ROBERTS: No you know, it's a --
16 it's a bank account that's held in -- you know, a
17 separate name or it's separate real estate. It's fairly
18 common for debtors to leave off some assets they want to
19 conceal. Is that, as a general rule, sufficient to
20 justify this unusual authority?

21 MS. HARRINGTON: I think if they do it in
22 such a way that then they spend the assets -- so the way
23 this issue usually comes up, the way it's come up in
24 most of the courts of appeals is that a debtor tries to
25 hide a nonexempt asset and then wastes the asset in some

1 way, usually by spending it, and then when it's
2 discovered, this is how it came up in the Malley case in
3 the First Circuit, then the Bankruptcy Court surcharges
4 the exempt property to sort of compensate the estate for
5 the wasted nonexempt property.

6 And so I think that -- that's certainly, in
7 our view, an appropriate exercise of authority under
8 Section 105, because there, the debtor is trying to --
9 he doesn't necessarily exit the bankruptcy with more
10 money than he would be entitled to, but he has more
11 money during the bankruptcy and he spends that money --

12 CHIEF JUSTICE ROBERTS: Well, then it --
13 then it becomes a not very unusual exercise of
14 authority. It becomes pretty common since the
15 concealment of nonexempt assets is a fairly -- I don't
16 want to say it happens all the time -- but it's a fairly
17 common situation.

18 MS. HARRINGTON: I don't think it happens
19 terribly often, and when it does happen it isn't very
20 often that the debtor spends the money that he's
21 concealing. He's usually trying to keep the money. And
22 so if it's discovered that he has hidden an asset that
23 he should have turned over, then the Bankruptcy Court
24 can merely order him to turn over the money, to turn
25 over whatever the asset was.

1 It only -- it is only necessary to surcharge
2 what would otherwise be exempt property if that
3 nonexempt asset no longer exists.

4 Here, of course, it's a little bit of a
5 different situation. This Petitioner imposed enormous
6 costs on the estate, radically depleted the value of the
7 estate by requiring the trustee to run up huge
8 attorneys' fees in order to effectuate his duties under
9 the code.

10 JUSTICE BREYER: Is there any case law --
11 because 522 says in (b), it says "The following property
12 may be exempt." It doesn't say it has to be. So is
13 there any case law where the debtor writes down -- you
14 know, a piece of property and a creditor comes in and
15 says: He can't exempt that he has behaved outrageously,
16 and it fits within the category, but he has behaved
17 outrageously.

18 Is there any case law that says under those
19 circumstances the bankruptcy judge can refuse the
20 exemption one way or the other?

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

24 JUSTICE BREYER: I mean, you first have to
25 get to the thing where the -- we are pretending to put

1 the creditor, the bankruptcy judge, as if he were
2 another creditor. The thing, the property, appears on a
3 list that says exempt. And then the trustee or the
4 judge says: No, I'm not going to let you exempt it.
5 And that's basically what he's done.

6 MS. HARRINGTON: Well, the majority of the
7 cases, it's not so much that there's been an objection
8 to the exemption, so much as the exemption has been
9 disallowed at the end of the case or surcharged.

10 But I'm glad -- you know, in the
11 hypothetical you posited, it's the creditor who is
12 expending effort and potentially incurring attorneys'
13 fees in order to expose a debtor's fraud. And in that
14 case, those would not be administrative expenses, and
15 you would think that, at least under the Court's
16 inherent authority -- under --

17 JUSTICE BREYER: You see what I mean? Not
18 only is it administrative expenses, but you have to
19 somehow say, well, the judge is a constructive creditor,
20 and he constructively objected. There are an awful lot
21 of "constructive's" in that sentence that I just gave
22 you.

23 MS. HARRINGTON: Right. And, again, that's
24 not our view. Our view is that the exemption was
25 disallowed, that the debtor is not allowed the benefit

1 of the exemption.

2 But if the creditor had been the one who ran
3 up the attorneys' fees, he could certainly be paid under
4 the court's inherent authority, as in Chambers v. NASCO,
5 and it would be strange to think that the trustee is the
6 only person who couldn't be paid in this sort of
7 circumstance just for doing what the code tells him he
8 has to do.

9 JUSTICE GINSBURG: Ms. Harrington, at the
10 cert stage in this case, the Government suggested the
11 distinction between two situations: One, an action by
12 the debtor to remove property from the estate, leaving
13 the creditors unsatisfied.

14 And that's where you say this power of
15 exemption can be taken away. And then the other side
16 was where the creditors are paid in full and only the
17 trustee's litigation expenses are at issue. Are you
18 dropping that distinction?

19 MS. HARRINGTON: No, Justice Ginsburg, I
20 think -- I think the distinction we were trying to make
21 was more what I was discussing with the Chief Justice,
22 which is when a debtor wastes nonexempt assets and can't
23 turn them over, nonexempt property, can't turn it over to the
24 estate, and so then is forced to turn over exempt
25 property so that the surcharge doesn't pay attorneys'

1 fees; it just compensates the estate, and by extension
2 the creditors, for property that should have been turned
3 over.

4 Our suggestion was that this case, you could
5 decide the case on a narrow grounds and it wouldn't
6 necessarily resolve the issue in those other cases,
7 because in this case the sanction was to pay attorneys'
8 fees, which under a court's traditional inherent
9 authority, a court can order one party to pay another
10 party's attorneys' fees when it's in response to
11 extraordinary bad faith litigation conduct.

12 Now, even in *Chambers v. NASCO*, it's true
13 that the Court was divided in that case, but it was
14 mostly divided about whether the bad faith in that case
15 was in the litigation or before the litigation. Here,
16 there is really no doubt that all of the bad faith
17 conduct in this case is in the litigation. And that's
18 really a very traditional exercise of the court's
19 inherent authority to sanction that type of behavior
20 through attorneys' fees.

21 I think it's important to note also in this
22 case that the available remedies really are insufficient
23 to deal with this debtor's misconduct. He suggests
24 dismissal, discharge, and Rule 11 sanctions. Of course,
25 dismissal wouldn't do anything to punish him because his

1 creditors have been paid and he would just exit the
2 bankruptcy with all of the exempt property he would have
3 gotten if he had been honest.

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

10 It's also not clear that Rule 11 would be
11 sufficient to fully compensate the Trustee for the
12 expenses that have been incurred, because Rule 11
13 sanctions generally aren't available for matters on
14 appeal.

15 And as the record reveals, much of the
16 expenses that were incurred in this place -- in this
17 case resulted from the debtor's more than a dozen
18 appeals to the Bankruptcy Appellate Panel and to the
19 court of appeals.

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

25 MS. HARRINGTON: So our view is that he

1 could have -- the court could have imposed a sanction,
2 and that would not have been a prepetition debt, so it
3 wouldn't have been discharged. And if the court had
4 ordered the debtor to pay the money on pain of contempt,
5 he could have enforced that order notwithstanding any
6 State law provision that would have exempted the
7 property after the bankruptcy.

8 CHIEF JUSTICE ROBERTS: Thank you, counsel.

9 Mr. Hellman, you have 5 minutes remaining.

10 REBUTTAL ARGUMENT OF MATTHEW S. HELLMAN

11 ON BEHALF OF THE PETITIONER

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

14 I think from the litany of punishments that
15 the Government has pointed to in this case, the question
16 here is not whether a Bankruptcy Court can sanction a
17 dishonest debtor. It can. The question is what
18 sanctions has Congress forbidden or allowed. This is a
19 case in which Congress has drawn a line and said exempt
20 property may not be used to satisfy any administrative
21 expense.

22 My second point is that I think there may
23 have been some confusion about what it is to claim an
24 exemption under the Bankruptcy Code. If you look at
25 Section 522(b) of the code, what you'll see is that a

1 debtor is allowed to claim an exemption, may claim an
2 exemption, under State law or Federal law, depending on
3 the scheme that the State has opted into.

4 The right to the exemption is a product of
5 State law unless Federal law says otherwise. And
6 Federal law has started to say otherwise in the
7 Bankruptcy Reform Amendments of 2005. Congress saw a
8 problem in 2005 where debtors were pouring money into
9 their homesteads, then declaring bankruptcy, and then
10 seeking to have all of that property be claimed as
11 exempt.

12 Congress amended Section 522 to deal with
13 that problem, to place limitations on that type of
14 misconduct. Congress has not created a generalized
15 equitable discretion exception to Section 522. And I
16 suggest that the reason it has not done that is because
17 we're talking about exempt property, the core property
18 of the debtor.

19 And it would dramatically shift the power
20 between trustee, as the Chief, as Mr. Chief Justice was
21 suggesting, dramatically shift the power between the
22 trustee and the creditors and the debtor if a debtor's
23 homestead, pension, or wedding ring or other exempt
24 property becomes fair game and at issue if the trustee
25 makes a motion to suggest that the debtor hasn't behaved

1 as forthrightly as the trustee claims he should have.

2 And I want to stress again, at the risk of
3 repeating myself, we are not talking about the
4 traditional, venerable inherent powers of the Court to
5 award attorneys' fees. There's a Rule 9011 in the
6 Bankruptcy Code. It wasn't invoked here, shouldn't have
7 been invoked here. But what we are talking about
8 instead is the property from which that sanction can be
9 satisfied.

10 Congress has determined that exempt property
11 cannot be used to satisfy administrative expenses. The
12 worst prepetition conduct that one could imagine, say,
13 in a couple of narrow circumstances -- Congress has made
14 the choice here as to the status of exempt property.

15 In the RadLAX case, in the Ginsberg case,
16 and I'm not aware of any case to the contrary in
17 between, Congress -- the rule in this Court is the
18 specific provision controls.

19 Here, Congress has spoken specifically,
20 expressly, not by implication, but through prohibitive
21 language saying that exempt property is not available to
22 satisfy administrative expenses.

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

25 CHIEF JUSTICE ROBERTS: Thank you, counsel.

1 The case is submitted.

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

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