

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF VERMONT**

In Re:

**TIMOTHY P. DELANEY and
JANET B. DELANEY,**

Debtors.

**Chapter 7 Case
99-11716**

Appearances:	<i>Raymond J. Obuchowski, Esq. Obuchowski Law Office Bethel, VT Attorney for the Trustee</i>	<i>Gleb Glinka, Esq. Glinka and Schwidde Cabot, VT Attorney for the Debtors</i>
---------------------	--	---

**MEMORANDUM OF DECISION
REGARDING SCOPE OF TRUSTEE'S OBJECTION TO EXEMPTION**

This matter is before the Court on remand from the District Court (Sessions, J.) to determine whether the chapter 7 trustee has preserved his objection to Janet Delaney's exemption of certain non-qualified annuities, claimed pursuant to 12 V.S.A. § 2740(19)(J), on the grounds that the subject annuities are not payable "on account of death, disability, illness, or retirement from or termination of employment." If the objection has been preserved, then the parties will need to address the legal issue of whether the annuities at issue qualify for exemption based upon the circumstances under which they are payable. Depending upon the resolution of that issue, the parties may or may not need to provide evidence concerning the sums that would be reasonably necessary for the support of the debtors or their dependents. This Court has jurisdiction over this proceeding pursuant to 28 U.S.C. §§ 157 and 1334. For the reasons set forth below, this Court holds that the trustee has preserved an objection as to whether the subject annuities are covered by the Vermont exemption statute.

ISSUE

The issue presented is whether the trustee preserved his right to object to the debtor's exemption on the grounds that the subject annuities fail to qualify for exemption under 12 V.S.A. § 2740(19)(J) because they are not payable "on account of death, disability, illness, or retirement from or termination of employment" or whether he has failed to preserve this right by his conduct prior to the appeal herein.

BACKGROUND

The relevant underlying factual issues in this exemption dispute are set forth in this Court's prior Memorandum of Decision Sustaining Trustee's Objection to Exemption [Dkt. # 45-1] dated December 7, 2000, and in the Opinion and Order of the District Court, Docket No. 2:01-CV-26 dated August 22, 2001. Accordingly, only the case background information critical to the instant issue of objection preservation will be addressed here.

On March 30, 2000, the trustee filed Objections to Claim of Exemptions challenging certain exemptions being asserted by the debtors. In pertinent part, the debtors were claiming an exemption of their interest in certain annuities under 12 V.S.A. §2740(19)(J). The Objection reads:

9. The Debtors have claimed an exemption in a 'Pension: Qualified Annuities with Fortis' in the amount of \$58,991.72 under 12 VSA § 2740(19)(J).
10. *The Fortis statement provided to the Trustee shows that at least \$13,235.30 of these funds are labeled 'Non-Qualified.'* Further, 12 VSA §2740(19)(J) refers only to certain 'payments' under a pension or annuity as being exempt, not an entire 'pension' corpus. See e.g. In re Meeham, 162 B.R. 367 (Bkrcty. S.D. Ga. 1993).
11. The Trustee objects to the \$58,991.72 exemption claimed under 12 VSA § 2740 (19)(J).
12. The Debtors have claimed an exemption in a 'Pension: Tax Sheltered Annuity with Equitable Life Assurance Soc. [account number deleted] in the amount of \$2,346.22 under 12 VSA §2740 (19)(J) .
13. *For the latter reason set forth in paragraph 10 above*, the Trustee objects to the \$2,346.22 exemption claimed under 12 VSA § 2740(19)(J).

Trustee's Objections to Claim of Exemptions, at p. 2 [emphasis added].¹

Subsequently, on May 9, 2000, the parties filed a Stipulation on Trustee's Objection to Debtor's Exemptions and agreed as follows:

1. All objections to the Debtors' claimed exemptions, with the exception of the exemption of Janet Delaney's interest in non-qualified annuities under 12 V.S.A. § 2740(19)(J) will be dismissed upon payment to the Trustee of \$4,500.00, subject to approval of the Court; and
2. With the approval of the Court, the hearing scheduled for May 9th on the claimed exemption of Janet Delaney's interest in non-qualified annuities under 12 V.S.A. § 2740(19)(J) will be continued to enable the Trustee to determine whether this exemption protects future payments, as well as present payments, under the annuities. Should the Trustee determine that 12 V.S.A. § 2740(19)(J) does not protect the corpus of the annuities, this question will be presented by the parties to the Court for resolution on stipulated facts; otherwise the Trustee shall withdraw his objection.

Stipulation on Trustee's Objection to Debtor's Exemptions, p. 1. Shortly thereafter, the parties submitted a Motion to Approve Stipulation of Settlement Regarding Trustee's Objections to Claim of Exemptions on June 9, 2000, which was approved by the Court, and states in pertinent part:

8. The Trustee's Objection to Debtors' Claim of Exemptions regarding the Debtors' annuities will remain on the Court calendar until otherwise resolved.

Stipulation on Trustee's Objection to Debtor's (sic) Exemptions, p. 2.

Lastly, on July 17, 2000, the parties filed a Stipulation of Facts which provided that the parties "hereby stipulate to the undisputed facts as follows":

3. The Debtors had originally claimed an exemption in a 'Pension: Qualified Annuities with Fortis' in the amount of \$58,991.72 under 12 VSA § 2740(19)(J).
4. The Fortis statement provided to the Trustee shows that at least \$13,235.30 of these funds are labeled 'Non-Qualified:' contract [account number deleted] in the amount of \$7,436.44; contract [account number deleted] in the amount of \$2,889.76 and contract [account number deleted] in the amount of \$2,882.10. *See* Fortis December 1999 statement of accounts, attached hereto as Exhibit 'A.'

¹ The trustee had also raised various other unrelated objections pertaining to certain tools of the trade, as well as the debtors' joint interest in a bank account and automobile, as constituting exempt property under Vermont Law which are no longer in dispute.

5. The Debtors, on July 6, 2000, amended their objection to claim ‘Qualified’ portion of those annuities as exempt under 12 VSA §2740(16).
6. The Trustee has timely objected to the exemption claimed under 12 VSA § 2740(19)(J).
7. The basis of the Trustee’s objection is that 12 VSA § 2740(19)(J) protects only certain ‘payments’ under a pension or annuity as being exempt, not an entire pension ‘corpus.’
8. The Debtors have claimed an exemption in a ‘Pension: Tax-Sheltered Annuity with Equitable Life Assurance Soc. [account number deleted] in the amount of \$2,346.22 under 12 VSA § 2740(19)(J).
9. For the reasons set forth in paragraph 7 above, the Trustee has also timely objected to the \$2,346.22 exemption claimed under 12 VSA § 2740(19)(J).
10. To assist the Court in its determination as to whether 12 VSA § 2740 (19)(J) applies to the annuity corpora in question, a copy of the policies is attached hereto as Exhibit ‘B.’

Stipulation of Facts, at pp. 1-2.

Pursuant to the Memorandum of Law in Support of Trustee’s Objection to Claim of Exemption filed on August 1, 2000, the trustee states that “[t]he issue presented is whether the debtors may exempt, under 12 VSA § 2740(19)(J), the corpus of several non-qualified annuities and an account they hold with Fortis Investors, Inc. in the amount of \$13,235.30.”² The memorandum specifies the nature of the debtors’ non-qualified funds and indicates that because “the issue to be considered is whether 12 VSA § 2740(19)(J) even applies to the annuities in question” the parties have agreed to reserve the issue of whether the annuities are reasonably necessary for the debtors’ support until the applicability of the exemption statute is resolved.

In addition to arguing that the debtors are only entitled to an exemption limited to any annuity payments presently being received, as opposed to the corpus of the annuities, the trustee also discusses an additional basis for objection, viz., that based upon his review of the annuity contracts these non-qualified funds fail to meet the criteria necessary for protection under 12 V.S.A. § 2740(19)(J). *See* Trustee

² It should be noted that the debtors had amended their schedules to claim the remainder of the Fortis accounts and the Equitable Life tax sheltered annuity as exempt under 12 V.S.A. § 2740(16) and the trustee does not contest that these accounts are deemed qualified under Vermont law.

Memorandum of Law, at pp.4-5. The trustee contends that the requisite limitations on transfer or accessibility are lacking because there are no restrictions placed upon the annuity commencement date or upon the right to withdraw the corpus. In closing, the trustee asserts that in addition to other shortcomings, “because both the payment commencement date and withdrawal of corpus appear to be at debtors’ whim, such future payments are likewise not on account of death, disability, retirement, etc.” and, therefore, the subject annuities fail to qualify for exemption under 12 V.S.A. § 2740(19)(J). Thus, the trustee confines his objections to whether these “non-qualified” accounts meet the criteria for 12 V.S.A. § 2740(19)(J), and does not dispute the applicability of 12 V.S.A. § 2740(16) to the qualified accounts.

In Debtors’ Reply Memorandum Opposing Trustee’s Objection to Exemption dated August 14, 2000, the debtors argue at length that it is the corpus of the accounts, not simply any present right to payment, that warrants exemption under 12 V.S.A. §2740(19)(J). The debtors then describe the trustee’s additional theory that the funds fail to qualify for exemption as not being on account of death, disability, illness or retirement from or termination of employment as a “new objection.” The debtors maintain that because this “additional objection” is not referenced in the Stipulation of Facts filed by the parties, it would be “quite unfair, on the limited record before the Court, to require the debtors to address” this further basis for trustee’s objection. The debtors then proceed to state that “[t]o the extent the trustee wishes to prosecute this additional objection, the debtors should be entitled to present additional documentation before addressing the issue.” *See* Debtors’ Reply Memorandum, at p. 5. In a footnote, the debtors also assert that:

Now that the Debtors are on notice, it may be that the parties can resolve this question through an exchange of documents, including the complete contract for this annuity. Furthermore, it appears that the funds in this annuity were rolled over from and are traceable to a teacher’s retirement account that was fully tax-qualified.”

Debtors’ Reply Memorandum, at p. 5, fn 7.

This Court issued a Memorandum of Decision Sustaining Trustee’s Objection to Exemption on December 7, 2000 holding that the subject exemption statute by its terms only applied to any present right to payment from the subject annuity accounts, and not the corpus. While characterizing this perceived deficiency

as the “gravamen of the Trustee’s Objection,” the Court nonetheless noted:

The Trustee also asserts that the subject annuities fail to satisfy §2740(19)(J) because both the payment commencement date and withdrawal of corpus appears to be at the debtors’ discretion; thus future payments are likewise not on account of the qualifying circumstances in the statute. However, because I find that the claimed exemption is otherwise deficient, the additional grounds asserted need not be addressed.

Memorandum of Decision, at p. 2, fn 1.

On appeal, the District Court reversed the decision of this Court and ruled that §2740(19)(J) can apply to exempt the corpus of annuities that have not ripened to payment status. The District Court declined to address the trustee’s additional objection that the funds fail to qualify for exemption under the statute because they are not on account of death, disability, illness, or retirement from or termination of employment. Rather, because the Bankruptcy Court did not reach this additional basis for objection, the District Court remanded the dispute for this Court to determine, first, whether this objection was preserved, and if so, whether the subject annuities qualify for exemption under the statute based upon the payment circumstances. The District Court noted that based upon debtors’ argument in their brief on appeal, it was unclear whether the trustee had preserved his right to object on this basis. Pursuant to a status hearing on remand held on October 16, 2001, the parties declined an invitation to provide memoranda of law regarding their respective positions on the issue of whether the trustee has preserved this additional basis for objection. Thus, the Court took the matter under advisement and issued a scheduling order.

DISCUSSION

The two touchstones involved in this Court’s determination of whether the trustee has preserved his objection regarding whether these annuities qualify for exemption under the subject Vermont statute based upon their payment circumstances are: first, the language utilized by the parties, especially the trustee, in addressing the objections to exemption and, second, the strong policy in federal courts generally favoring a resolution on the merits, especially in cases where a party has not been derelict in its duties. *See In re Saylor*, 178 B.R. 209, 212 (9th Cir. BAP 1995)(noting strong policy underlying federal rules of civil procedure favoring decision on the merits); *In re Burgner*, 218 B.R. 413, 417 (Bankr. E. D. Tenn. 1998)(acknowledging

general principle that courts favor a decision on the merits); In re Schlosser, 100 B.R. 348, 350 (Bankr. S.D. Ohio 1989)(doubts should be resolved in favor of a decision on the merits of a case); *see also* In re Photo Promotion associates, Inc., 45 B.R. 878, 882 (S.D.N.Y. 1985)(bankruptcy courts, as courts of equity, should look with disfavor on the forfeiture of rights); In re Next Wave Personal Communications, Inc., 244 B.R. 253, 280 (Bankr. S.D.N.Y. 2000)(same); In re Hull, 19 B.R. 501 (Bankr. N.D. Ind. 1982)(generally courts construe language against a waiver of a right and require language to be direct, positive and express).

Section 2740 (19)(J) provides in pertinent part:

The goods or chattels of a debtor may be taken and sold on execution, except the following articles, which shall be exempt from attachment and execution, unless turned out to the officer to be taken on the attachment or execution, by the debtor ... property traceable to or the debtor's right to receive, to the extent reasonably necessary for the support of the debtor and any dependents of the debtor ... *payments under a pension, annuity, profit-sharing, stock bonus, or similar plan or contract on account of death, disability, illness, or retirement from or termination of employment.* (Emphasis added.)

In this instance, the trustee diligently asserted various objections to exemptions being claimed by the debtors, involving items of personal property, bank accounts, and various annuities. The initial objection at issue here was asserted timely and stated that “[t]he Fortis statement provided to the trustee shows that at least \$13,235.30 of these funds are labeled ‘Non-Qualified.’” Trustee’s Objections to Claim of Exemptions, at para. 10. The parties thereafter stipulated to a resolution of all objections to exemptions pertaining to the personal property and joint bank account. In the Stipulation on Trustee’s Objection to Debtor’s Exemptions, the parties agree that “[a]ll objections to the Debtors (sic) claimed exemptions, *with the exception of the exemption of Janet Delaney’s interest in non-qualified annuities under 12 V.S.A. §2740(19)(J)*, will be dismissed.” (Emphasis added). In the Stipulation of Fact, which merely sets forth certain “undisputed facts,” the parties refer to these “Non-Qualified” funds. Moreover, the parties attach as an exhibit to the Stipulation a copy of the subject annuity policies “[t]o assist the Court in its determination as to whether 12 V.S.A. §2740(19)(J) applies to the annuity corpora.” The trustee then addressed the merits of his objection based upon *inter alia* the payment circumstances and commencement date of these policies in his memorandum of law filed thereafter.

In support of their claim that the trustee failed to preserve this objection, the debtors refer to a select portion of the Stipulation of Facts, discounting all the other references to the ongoing exemption objection, as follows: “The basis of the trustee’s objection is that 12 V.S.A. § 2740(19)(J) protects only ‘payments’ under a pension or annuity as being exempt, not an entire pension ‘corpus.’” While this isolated statement may be suggestive of a limited exemption objection, there is nothing in the settlement between the parties that indicates that the settlement encompasses any of the annuity issues raised by the trustee. Moreover, the Stipulation of Facts pertains only to facts that are not disputed; it does not in any way circumscribe the facts in dispute in the universe of the annuity controversy. Furthermore, the fact that the parties attached a copy of the annuity policies to the Stipulation of Facts to assist this Court in determining the applicability of the subject exemption statute is suggestive that the language of the policies might be pertinent to exemption issues other than whether Vermont law limited the exemption to a present right of payment as opposed to the corpus of the account. Indeed, a determination of the merits of the trustee’s primary objection, i.e. that the exemption statute was limited to a present right of payment, would not have involved an analysis of the language of the policies, although the policies would be relevant to an evaluation of the commencement date and payment circumstances.

While the language used by the parties may be a bit less than absolutely clear, this Court cannot find that it represents a direct, positive or express intention on the part of the trustee to abandon what may be a meritorious objection to the exemption status of these annuity accounts. The Court finds that the trustee was not derelict in his duty to notify the debtors of a variety of exemption objections he was asserting on behalf of the bankruptcy estate. The trustee certainly put the debtors on notice that he was challenging the annuities the debtors claimed as being exempt under §2740(19)(J) and addressed the merits of these objections in his initial memorandum of law. This Court feels bound to echo the sentiments expressed by other federal courts that disputes should be resolved on the merits when appropriate, especially when the circumstances are unclear and the target party has acted in a timely and diligent fashion. The debtors were on notice of which funds were being challenged by the trustee under the subject exemption statute, addressed their position in

the papers filed with this Court and have declined this Court's invitation to further brief the matter. In light of all the language used by the parties regarding the exemption objections applicable to these annuities under the circumstances of this case, and in deference to the policy interest of resolving legal issues on the merits, the Court finds that the record does not demonstrate that the trustee failed to preserve his remaining objection as to whether these annuities qualify for exemption under §2740(19)(J) based upon their date of commencement and payment circumstances.

Accordingly, the trustee may proceed with his objection to the subject annuities on both the grounds of the fund's qualification exemption and the debtors' need of the funds for their support. The parties shall submit memoranda of law in support of their respective positions concerning whether the subject annuities qualify as exempt property based upon the circumstances under which they are payable, as directed by the scheduling to be order entered in conjunction with this decision.

October 23, 2001
Rutland, Vermont

/s/ Colleen A. Brown
Colleen A. Brown
United States Bankruptcy Judge