

(Cite as: 1996 WL 69702 (Bankr.D.Vt.))

In re Sharron FREESE, Debtor.

Raymond J. OBUCHOWSKI, Trustee of the Bankruptcy Estate of Sharron Freese,

Plaintiff,

v.

Sharron and James FREESE, Defendants.

Bankruptcy No. 94-10316 (FGC).

Adv. No. 95-1060.

United States Bankruptcy Court. D. Vermont.

Feb. 8, 1996.

R. Obuchowski, Obuchowski & Reis, Bethel, Vermont, Trustee pro se for the Bankruptcy Estate (Trustee).

R. Rice, Cohen & Rice, Rutland, Vermont, for James and Sharron Freese (Defendants).

**MEMORANDUM OF DECISION ON POST-CONVERSION OBJECTION TO PRE-CONVERSION
EXEMPTION**

FRANCIS G. CONRAD, Bankruptcy Judge.

***1** Before us, [FN1] on cross-motions for summary judgment, is the Chapter 7 Trustee's attempt to snag for the benefit of Estate creditors an inheritance received by Debtor's husband from his mother. Debtor, without objection, exempted her entireties interest in the inheritance during a failed Chapter 13. Her husband, prior to conversion to Chapter 7, transferred the funds from a joint account with Debtor into an annuity in his sole name. Based on this set of facts, we deny Trustee's motion and grant summary judgment to Debtor.

FACTS

Debtor's spouse, a former Vermont state police officer, was advised to put \$63,000 that he inherited into a tenancy by the entirety account with Debtor so that, in the event of his sudden death, she could avoid probate and have immediate access to his funds. The inheritance, received by the non-debtor husband about six months after he married Debtor, was held for about six years in an investment account with Dean Witter. It is undisputed that he directed all investment activity and used his social security number to report all income generated from the fund. Debtor never withdrew money from or exercised any control over the funds in the Dean Witter account.

When Debtor filed a Chapter 13 bankruptcy petition on May 19, 1994, she included in her list of assets the investment account at Dean Witter held with her spouse as tenants by the entirety. Debtor claimed an exemption for her interest in the investment account in the Chapter 13 case. No objections were filed to the exemption during that case.

The Chapter 13 plan, confirmed by this Court on August 1, 1994, states, as § 1327(b) [FN2] provides, that Debtor's property reverted in Debtor upon confirmation. In March of 1995, after confirmation of the Chapter 13 Plan, and on the advice of his accountant, Debtor's spouse closed the Dean Witter account and purchased an annuity in his sole name. He had a legal right to do this. There is no evidence that Debtor participated in this transaction. On April 18, 1995, Debtor's Chapter 13 case was voluntarily converted to a case under Chapter 7.

Following the May 1995 §341(a) meeting of Chapter 7 creditors, Trustee initiated this adversary proceeding against Debtor and her spouse under § 549(a), [FN3] claiming that an avoidable transfer occurred when Debtor's spouse withdrew the funds from the joint account and put them in his own name. We grant summary judgment to Defendants and deny Trustee's motion because we are unable to find in this sequence of events any legal log for Trustee to set his avoidance grappling hook into. Transfers of non-estate property are not avoidable by a trustee under §549 and the property at issue in this case was not property of the estate at the time of transfer.

DISCUSSION

Under §522(b)(2)(B), Debtor "may exempt from property of the estate"

any interest or property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law.

***2** Debtor claimed an exemption under Vermont law, 15 VSA §67, which states:

Real estate and tangible personal property ...held and owned by husband and wife by the entirety, are made chargeable during the lifetime of the husband for the debts contracted by him for the necessary upkeep of such property, in the same manner and to the same extent as if owned and held by him in his sole name.

While the statute, at first glance, does not appear to be an exemption statute, later cases have interpreted it to mean that entires are reachable by the sole creditors of only one spouse only if those debts were incurred for the necessary upkeep of such property. In any other case, properties held by the entirety simply cannot be attached for the sole debt of one spouse. See *Pettingill v. United States*, 205 F.Supp. 10 (D.Vt. 1962); *In Re Estate of Elliot*, 149 Vt. 248 (1988).

Only two joint creditors were listed on the Debtor's petition; payments to both were current at the time of filing and continued to be current thereafter. The remaining debts were solely Debtor's, and were not incurred for the upkeep of her husband's inheritance, over which she exercised no control. The exemption was thus proper when made.

No objections to Debtor's claim of exemption were made during the pendency of the Chapter 13 case. The Bankruptcy Code makes it pellucidly clear what happens when no one objects to a debtor's claim of exemption: "unless a party in interest objects, the property claimed as exempt on such list is exempt." § 522(1). The Supreme Court resolved any doubt about the statute's clear import in *Taylor v. Freeland & Kronz*, 503 U.S. 638, 112 S.Ct. 1644, 118 L. Ed.2d 280 (1992), when it held that a trustee's failure to timely object to a debtor's claimed exemption prevented challenge to an exemption regardless of whether the debtor had a colorable statutory basis for claiming the exemption.

Trustee argues, however, that his objection is in fact timely, because it was made within 30 days of the May 1995 §341 meeting of creditors, as required by Fed.R.Bkrtcy.P. 4003(b). [FN4] That Trustee did in fact timely object after conversion is not disputed. The issue we must decide is whether exemptions exempted pre-conversion are subject to a new objection period after conversion. The circuits are split on whether the time period mentioned in Rule 4003(b) closes once and for all 30 days after the first meeting of creditors, or whether a second 30-day period for filing objections to exemptions begins when a case is converted to Chapter 7 and another meeting of creditors is held. Debtor cites *In re Robert L. Brown*, 178 B.R. 722 (Bkrtcy.E.D.Tenn.1995), which held that conversion does not subject exemptions lawfully taken while the case was in Chapter 11 to a second period for objections after conversion to Chapter 7. Trustee cites *In re Jerry Weissman*, 173 B.R. 235 (M.D.Fla. 1994), which held that a Chapter 7 Trustee, in a converted case, had another 30 days to object to a debtor's claim of exemption made during the Chapter 13 case and to which no objection was raised.

***3** Weissman gives the Chapter 7 Trustee a second bite of the apple on policy grounds:

To construe Rule 4003(b) to mean that the original §341 meeting triggers the thirty (30) day time frame in which to file objections would deprive Chapter 7 trustees of the opportunity to challenge the debtor's claims of exempted property. This interpretation would allow debtors to immunize certain property merely because the Chapter 13 trustee failed to file a timely objection following the original §341 meeting. With the procedural advantage afforded by this narrow interpretation of Rule 4003(b), debtors could routinely file under Chapter 13, list the bare minimum of property on Schedule C to qualify for Chapter 13 status, and once the time limit for objections expires, claim the same exemptions after converting to Chapter 7, thereby protecting certain assets even if the law clearly would otherwise prohibit such claims. Certainly, when considering the policies underlying the Bankruptcy Code, this cannot be the intent of the legislators in devising distinct plans and schedules for debt payment.

Weissman, *supra*, 173 B.R. at 236-37.

The policy arguments made by Weissman are undeniably strong. We do not believe, however, that we have the power to make policy pronouncements about property that is not property of the estate. Accordingly, we believe that the better argument is to be found in *Brown*, which involved a case converted from Chapter 11.

There is widespread agreement that the effect of an exemption is to remove property from the bankruptcy estate and to vest it in the debtor. Section 522(b) of the Code directly states that the "debtor may exempt from property of the estate the property listed ..." on his schedule of exemptions (emphasis added) Therefore, unless there is some mechanism for the debtor's property to reenter the bankruptcy estate upon conversion, it would seem that exemptions in the Chapter 11, once considered final and unobjectionable under the rule in *Taylor*, must be considered final and unobjectionable in the converted case as well.

Brown, *supra*, 178 B.R. at 726-27.

The 1994 Amendments to the Bankruptcy Code now supply "a mechanism for the debtor's property to reenter the bankruptcy estate upon conversion" from Chapter 13. New §348(f)(1) (A) now defines property of the estate upon a conversion from Chapter 13 to "consist of the property of the estate, as of the date of the filing of the petition, that remains in the possession of or is under the control of the debtor on the date of conversion...." The 1994 Amendment, however, does not apply here because it was enacted after commencement of this case. Norton Bkrcty. Code Pamphlet 1995-1996 ed., 229. Even if it did apply, Trustee would lose because, though the inheritance was a part of Debtor's estate "as of the date of the filing of the petition," it was not "in the possession of or ... under the control of the debtor on the date of conversion." §348(f)(1)(A).

***4** Finally, we cannot accept Trustee's rationale that an apparent unfairness would result by allowing this Debtor to transfer joint funds exempted from her unsuccessful Chapter 13 and

make them unavailable to creditors in the resulting Chapter 7. There is not even a hint that the transfer was made with any intent to hinder, delay or defraud any creditor. Eight months after confirmation, Debtor's husband, on the advice of his accountant, transferred the jointly held account into an annuity in his sole name, as he had every legal right to do. The transfer was lawful because the funds were not property of the estate. In light of the specific facts here, it would be irrational to punish the spouse of a Debtor whose reorganization failed. That would defeat the State's purpose in enacting 15 VSA §67 to protect entireties interests from the sole debts of one spouse. Finally, what could be more unfair than allowing Debtor's creditors to attach the inheritance of her spouse, whose only mistake was to try to protect her in the event of his untimely death?

Debtor's motion for summary judgment is granted. Trustee's motion is denied. Debtor is to settle an order on five days' notice to Trustee.

FN1. Our subject matter jurisdiction over this controversy arises under 28 USC §1334 (b) and the General Reference to this Court under Part V of the Local District Court Rules for the District of Vermont. This is a core matter under 28 USC §§157(b)(2)(A), (B), and (O). This Memorandum of Decision constitutes findings of fact and conclusions of law under F.R.Civ.P. 52, as made applicable by F.R.Bkrtcy.P. 7052.

FN2. Hereafter, all statutory references are to Title 11 of the United States Code unless otherwise specifically noted.

FN3. §549(a) provides in pertinent part:

[T]he trustee may avoid a transfer of property of the estate--

(1) that occurs after the commencement of the case; and

(2)(A) that is authorized only under section 303(f) of 542(c) of this title; or

(B) that is not authorized under this title or by the court.

FN4. Rule 4003(b) provides, in pertinent part:

The trustee or any creditor may file objections to the list of property claimed as exempt within 30 days after the conclusion of the meeting of creditors held pursuant to Rule 2003(a) or the filing of any amendment to the list or supplemental schedules unless, within such period, further time is granted by the court. Copies of the objections shall be delivered or mailed to the trustee and to the person filing the list and the attorney for such person.

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