

**UNITED STATES BANKRUPTCY COURT  
NORTHERN DISTRICT OF FLORIDA  
TALLAHASSEE DIVISION**

IN RE:

WILLIAM ARTHUR THOMAS, III,  
  
Debtor.

CASE NO.: 09-41174-KKS

CHAPTER: 7

**ORDER DENYING CHAPTER 7 TRUSTEE'S  
MOTION TO SURCHARGE DEBTOR'S EXEMPT PROPERTY  
AND FOR TURNOVER OF DEBTOR'S EXEMPT PROPERTY (DOC. 63)**

This matter came before the Court on the Chapter 7 Trustee's Motion to Surcharge Debtor's Exempt Property and for Turnover of Debtor's Exempt Property (Doc. 63; the "Surcharge motion"). The Debtor filed a Response to the Trustee's Motion (Doc. 67) and the Court held a duly noticed hearing on July 18, 2013. Upon due consideration of the pleadings, applicable case law, undisputed facts and argument of counsel, and for the reasons set forth below, the Court finds that the Trustee's Motion to Surcharge Debtor's Exempt Property and for Turnover of Debtor's Exempt Property should be denied.

**FINDINGS OF FACT**

1. On December 18, 2009 the Debtor, William Arthur Thomas, III, filed a voluntary petition for Chapter 7 relief. Along with his petition, the Debtor filed his Schedules and Statement of Financial Affairs ("SOFA"). In the Debtor's Schedules he listed a Farmers & Merchants Bank IRA (the "FMB IRA") worth \$19,000.00, which he claimed as fully exempt.

2. Sometime after the Debtor filed his petition, the Trustee discovered that the Debtor was party to pre-petition contracts that were not disclosed in the Debtor's Schedules or SOFA. One of the omitted pre-petition contracts was an agreement between the Debtor and Craig Mobley entered on September 24, 2009 that gave the Debtor the right to purchase real property from Mr. Mobley (the "Mobley contract") and, essentially, "flip" the property for a profit.

3. In April of 2011, as a result of contracts entered into post-petition for the purchase and sale of the Mobley property, the Debtor made a net profit on the Mobley contract of \$30,839.13 (the “Mobley profit”). The Chapter 7 Trustee filed Adversary Proceeding No. 10-04018 against the Debtor on December 23, 2010 requesting that the Mobley profit be deemed property of the estate, requesting turnover to the Trustee pursuant to Section 542 of the Bankruptcy Code, and demanding judgment against the Debtor for the Mobley profit.

4. On March 13, 2012 this Court granted the Trustee’s Motion for Summary Judgment in A.P. 10-04018, finding that the Mobley profit was property of the estate (the “Order,” Doc. 84, 10-04018). The Debtor appealed. On July 13, 2012 the United States District Court for the Northern District of Florida affirmed, and the debtor again appealed.

5. On April 16, 2013 the Eleventh Circuit affirmed the District Court’s ruling and found that this Court’s Order was proper (Doc. 99, 10-04018), after which this Court entered a Final Judgment on May 9, 2013, awarding the Trustee an amount equal to the Mobley profit plus post-judgment interest (Doc. 96, 10-04018). The Trustee filed the Surcharge motion on May 13, 2013.

## **CONCLUSIONS OF LAW**

### Surcharge of the Debtor’s Exempt Property

6. The Trustee asserts that the facts of the case and the Debtor’s conduct warrant a surcharge on the Debtor’s FMB IRA, and demands an order requiring the Debtor to turn over the FMB IRA. The Trustee acknowledges that the Debtor has been cooperative in providing documentation relating to his business affairs, specifically including the omitted contracts and the Mobley profit in particular, but points out that the Debtor only began doing so after the Trustee found out about and began inquiring into the omitted contracts.

7. The Debtor argues, *inter alia*, that he truly believed that these contracts were not assets of this estate because any income from the contracts depended on events orchestrated by him post-petition. The Debtor urges that the facts in the cases cited by the Trustee, in which courts have surcharged exempt assets, are distinguishable because of his good faith belief that the Mobley profit was not property of the estate, and because he did not participate in a similar degree of obfuscation, concealment, or general bad faith as displayed by the debtors in the cases cited by the Trustee.

8. Bankruptcy courts have the authority pursuant to 11 U.S.C. § 105(a) to surcharge a debtor's exemption if exceptional circumstances are present. *In re Onubah*, 375 B.R. 549, 553 (B.A.P. 9th Cir. 2007) (quoting *Latman v. Burdette*, 366 F.3d 774 (9th Cir. 2004)). "Exceptional circumstances are present when a debtor engages in inequitable conduct, that when left unchallenged, denies 'creditors access to property in excess of that which is properly exempted under the Bankruptcy Code.'" *Id.*

9. The Trustee contends that the Debtor's omission of pre-petition contracts from the Debtor's Schedules and SOFA constitutes sufficient exceptional circumstances on which to order a surcharge of the Debtor's exemption in the FMB IRA. Although the Debtor's original omissions were in violation of the disclosure obligation imposed on the Debtor pursuant to 11 U.S.C. § 521, the Court does not agree that those omissions alone, under the facts of this case, warrant a surcharge. The cases cited by the Trustee support such a conclusion. In those cases, the courts did not find that non-disclosure of interests alone rose to the level of wrongful misconduct or exceptional circumstances necessary for the Court to allow a surcharge on otherwise exempt assets. *See Malley v. Agin*, 693 F.3d 28 (1st Cir. 2012); *In re Hamblen*, 354 B.R. 322 (Bankr. N.D. Ga. 2006).

10. In *Malley*, the court surcharged the debtor's exempt assets because the debtor repeatedly declared and swore under oath that he received nothing from a pre-petition sale, even though he had actually received \$25,000.00. *Malley*, 693 F.3d 28. The *Malley* court concluded that the combination of the debtor's willful concealment of received funds, the funds having been completely spent, and the continuing misrepresentation of the debtor "amounted to fraud on the court, the trustee, and general creditors." *Id.* at 29. Similarly, the court in *Hamblen* ruled that the debtors' concealment and false statements with respect to undisclosed funds, which the debtors had dissipated, were enough to justify surcharge. *In re Hamblen*, 354 B.R. at 327. The *Hamblen* court noted that the joint-debtor wife provided false testimony regarding undisclosed funds during a Rule 2004 examination and that both debtors were uncooperative and evasive when being inquired about the use of such funds. *Id.*

11. In this case, the Debtor did not engage in the type of actions amounting to fraud or exceptional misconduct exhibited by the debtors in *Malley* and *Hamblen*. In contrast to the debtor in *Malley*, who repeatedly lied under oath, and the debtor in *Hamblen* who gave false testimony and was evasive when questioned about estate property, at the July 18 hearing the Trustee acknowledged that the Debtor in this case has made substantial efforts to be forthright and honest in his dealings with the Trustee since the Trustee originally requested information about the unlisted contracts.

12. The Trustee contends that the Debtor's exemption should be surcharged because the Debtor has not yet turned over the Mobley profit. Even under the cases cited by the Trustee, there must be something more than just the combination of failing to disclose interests and turn over property of the estate before the Court should order a surcharge on the Debtor's exempt property. See *In re Onubah*, 375 B.R. 549 (B.A.P. 9th Cir. 2007); *In re Karl*, 313 B.R. 827 (Bankr. W.D. Mo. 2004).

13. In *Karl*, the court surcharged the debtor's exemption not merely on account of the debtor having failed to comply with the court's order to turn over property, but also because the debtor failed to adequately cooperate with the trustee, acted directly in contravention to the trustee's instructions regarding estate property, and did not offer any acceptable explanation as to why property had not been turned over to the trustee. *In re Karl*, 313 B.R. 827. The *Karl* court ruled that "when a debtor's contemptuous conduct involves the suppression of estate property, or when a debtor fails to adequately explain its loss, a court may surcharge the debtor's exemption in an effort to prevent a fraud on the bankruptcy court and to protect creditors by preventing the debtor from sheltering more assets than permitted by the Bankruptcy Code." *Id.* at 831 (citing *Latman*, 366 F.3d at 784-785). Likewise, in *Onubah*, it was not just the debtor's failure to turn over property alone that warranted a surcharge; rather, it was the debtor's "unjustified refusal to turn over property of the estate to the trustee ...." *Id.* at 554 (citing *Latman*, 366 F.3d at 785). The debtor in *Onubah* twice used Chapter 11 filings for the purpose of obstructing the Chapter 7 trustee's attempts to sell Chapter 7 estate property, in spite of the debtor's obvious inability to fund a Chapter 11 plan. *Id.* at 553. The *Onubah* court noted that the debtor used the Bankruptcy Code in a disingenuous manner and that the debtor's efforts to obstruct the Chapter 7 trustee's administration of the estate "were not litigation tactics undertaken in good faith." *Id.* at 554.

14. Without question the Debtor in this case has yet to turn over the Mobley profit to the Trustee, but here the Debtor and the Trustee have been awaiting a final ruling on whether the property is even property of the estate, which was not issued until May 9 and June 11, 2013 (Doc. 96 & 100; AP 10-04018). The Record is devoid of any motion filed by the Trustee during the pendency of the appeals seeking turnover of the Mobley profit, nor is there any evidence that the Debtor has the Mobley profit and has willfully refused to turn it over to the Trustee since the Eleventh Circuit rendered its opinion. This Court did not enter a Final Judgment in favor of the

Trustee as to the Mobley profit until May 9, 2013 (Doc. 96; AP 10-04018). Clearly, the determination as to whether the Mobley profit was an asset of this estate entailed a lengthy appeals process, and it was not until the end of the appeals process that the Debtor's obligation to turn over the Mobley profit to the Trustee became final.<sup>1</sup>

15. While it was the Debtor who prompted the protracted appeals process, which in turn delayed the final judgment requiring the Debtor to turn over the Mobley profit, the fact that the Debtor did so in good faith is evidenced by the appellate courts' treatment of the issues on appeal; issuing opinions rather than *per curiam* affirming or denying. This is in stark contrast to the debtor in *Onubah* who resorted to litigation tactics such as colluding with creditors to file an involuntary Chapter 11 petition for no reason other than to thwart the trustee's administration of the estate.

16. The Debtor has not engaged in the sort of inequitable conduct that other courts have used as a basis for surcharging exempt property. Since the Trustee first requested that the Debtor provide her information about his unlisted contracts he has been cooperative and has made significant efforts to provide documentation about the interests previously undisclosed. Because the deferment of the Debtor's obligation to turn over the Mobley profit was a result of the Debtor's good faith appeals, the Debtor's failure to pay the Mobley profit to the Trustee is justified and should not be treated as wrongful misconduct. *See In re Onubah*, 375 B.R. at 556 ("remedy of surcharge may not be used to shift costs to a debtor who has unsuccessfully, but in good faith . . . challenged the trustee's administration of the estate.").

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<sup>1</sup> The Debtor did not post a bond or obtain a stay of this Court's ruling in A.P 10-04018 pending appeal. The Eleventh Circuit's judgment and mandate were filed in the adversary proceeding on June 11, 2013. The Eleventh Circuit's Memorandum Opinion was issued on April 16, 2013 (Doc. 99, AP 10-04018), after which this Court entered final judgment for the Trustee and against the Debtor. The Trustee did not file anything in the adversary proceeding or this administrative bankruptcy case in an effort to enforce this Court's order on turnover until the Trustee filed her motion for Turnover and for Surcharge on May 13, 2013 (Doc. 63). There is no evidence, nor was there any argument, that the Trustee had made any effort to demand or try to collect from the Debtor the Mobley profit until she filed the Surcharge motion.

17. There is no evidence or even allegation that the FMB IRA contains funds traceable to the Mobley profit. The Record appears to show the opposite: The FMB IRA existed pre-petition and has not increased in amount since the Debtor received the Mobley profit post-petition.

#### Turnover of the Debtor's FMB IRA

18. The Trustee requests that the Debtor's FMB IRA be turned over pursuant to 11 U.S.C. § 542(a). "Section 542(a) requires turnover to the trustee of property of the estate." *In re Challenge Air Int'l, Inc.*, 952 F.2d 384, 386 (11th Cir. 1992). Property of the estate "is comprised of . . . all legal or equitable interest of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). Although "property of the estate" as defined in § 541(a)(1) broadly encompasses much of a debtor's interests, a debtor may exempt property from being part of the estate by claiming exemptions allowed under § 522(b). *See Matter of Wilson*, 694 F.2d 236, 238 (11th Cir. 1982). The Bankruptcy Code does provide for federal exemptions; however, states have the opportunity to opt out of federal exemptions of § 522(d) and limit a debtor's exemptions to those authorized under state law. 11 U.S.C. § 522(b). Pursuant to Florida Statute § 222.20, Florida has chosen to "opt out" of the federal exemptions.

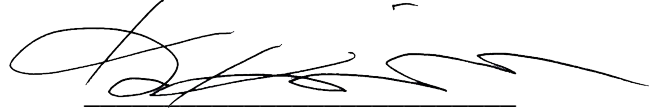
19. Here, the Debtor claimed his FMB IRA as exempt under Florida Statute § 222.21(2). No party in interest filed an objection to this exemption. Section 522(l) of the Bankruptcy Code provides that "[u]nless a party in interest objects, the property claimed as exempt on such list is exempt." The Debtor's FMB IRA is exempt and not subject to turnover under 11 U.S.C § 542.

Exceptional circumstances do not exist in this case that warrant a surcharge on or turnover of the Debtor's FMB IRA.

For the reasons stated, it is:

ORDERED: that the Trustee's Motion to Surcharge Debtor's Exempt Property and for Turn-over of Debtor's Exempt Property is DENIED.

DONE AND ORDERED at Tallahassee, Florida this 8th day of August, 2013.



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Karen K. Specie  
United States Bankruptcy Judge