UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF NEW YORK

In re: Rodney Lee Weaver,	Case No. 11-32549
Debtor.	Chapter 13

Order on Chapter 13 Trustee's Motion to Distribute Funds (Docket No. 105) and Setting Further Hearing

By order entered January 4, 2013, the court denied confirmation of Debtor's chapter 13 plan and dismissed the case (Doc. No. 101). On January 9, 2013, Buffalo Welding Company, a subsidiary of Noco Energy Corp. and a judgment creditor of Debtor ("Buffalo Welding"), served the chapter 13 trustee pursuant to Article 52 of New York's CPLR with a restraining notice, demanding that the trustee turn over any of Debtor's funds held by the trustee. Two weeks later, the trustee was served with an execution with notice to garnishee by the Onondaga County Sheriff's Department.

On February 15, 2013, the chapter 13 trustee, recognizing that he is under the general directive of 11 U.S.C. § 1326(a)(2)— to return accumulated plan payments, less the trustee's fees and commissions, to the debtor in a case dismissed prior to plan confirmation— filed a motion which seeks an order permitting him to distribute the funds held on hand to the Onondaga County Sheriff on behalf of Buffalo Welding in compliance with the state court restraining notice and execution (Doc. No. 105, "Motion"). Buffalo Welding, through its attorney, Francis Weimer, Esq., filed an affirmation in support of the Motion. Debtor, through his new counsel, Theodore Araujo, Esq., opposed the motion. A hearing on the Motion was held on March 19, 2013, at which the court heard argument, permitted Debtor to further brief the matter and reserved decision. Debtor filed its supplemental response on March 20, 2013 (Doc. No. 112).

As stated on the record of the initial hearing, there is a split of authority among the cases decided as to whether funds held by a chapter 13 trustee are subject to levy by a creditor before they are remitted to the debtor, with no binding precedent on this court. The cases are collected in *In re Locascio*, 481 B.R. 285 (Bankr. S.D.N.Y. 2012), in which Judge Cecelia Morris found that the plain language of section 1326(a)(2) and the Supremacy Clause required the trustee to return the money directly to the debtor despite a pending state court garnishment, relying principally in her opinion upon the reasoning set forth in *In re Bailey*, 330 B.R. 775, 776 (Bankr. D. Or. 2005) and *In re Davis*, No. 04-30002, 2004 WL 3310531 (Bankr. M.D. Ala. June 16, 2004). Respectfully, this court disagrees.

As noted by the United States Supreme Court in *Altria Group, Inc. v. Good*, 555 U.S. 70, 77 (2008), courts should begin their analysis when considering whether Congress intended to expressly or impliedly preempt a state statute with the premise that "when the text of a pre-emption clause is susceptible of more than one plausible reading, courts ordinarily 'accept the reading that disfavors pre-emption.' " *Id.* (quoting *Bates v. Dow Agrosciences LLC*, 544 U.S. 431, 449 (2005); *see also Interworks Sys., Inc. v. Merchant Fin. Corp.*, 604 F.3d 692 (2d Cir. 2010) ("We will not conclude that a state statute was 'superseded by [a] Federal Act unless that was the clear and manifest purpose of Congress.' " (quoting *Altria Group Inc.*, 555 U.S. at 70)). And, binding precedent instructs this court that "[i]n analyzing any claim of federal preemption, 'the purpose of Congress is the ultimate touchstone.' " *Envtl. Encapsulating Corp. v. The City of New York*, 855 F.2d 48, 53 (2d Cir. 1988) (citations omitted).

In *In re Doherty*, 229 B.R. 461 (Bankr. E.D. Wash. 1999), the bankruptcy court faced with a similar question inquired: "Does the statutory direction to pay to the debtor mean pay exclusively to the debtor or are the funds subject to execution by creditors?" And then noted:

"The language of Section 1326(a)(2) does not directly answer this question." *Id.* at 466. This court's order of dismissal made clear that the automatic stay was no longer in effect and creditors could now pursue their rights against the Debtor and the Debtor's property under state law. As a direct consequence of the dismissal, there was no longer a bankruptcy estate nor "property of the estate" to be protected from the claims of creditors. 11 U.S.C. § 349. In this court's opinion, the directive of section 1326(a)(2) provides a clear statement that the funds on hand, less the trustee's commission and fees, constitutes the debtor's property but does not render those funds insulated from levy under applicable state law.

Debtor would argue that requiring the funds to be returned to the Debtor would encourage the filing of chapter 13 and ensure that debtors who are not successful would not be punished. However, as noted by the court in *Doherty*, this provides more incentive to dismiss a case rather than to work within the structure of the Code by converting the case to another chapter and thereby retain the original filing date for Part V recoveries, a clear benefit to the debtor and to the estate. *In re Doherty*, 229 B.R. at 466. And, while the ability to set aside funds would be a great benefit and, perhaps, incentive to a debtor to file a chapter 13 petition, it is highly unlikely that Congress would seek to provide that incentive to a person who was foregoing the strictures of being a debtor under the Bankruptcy Code. *Id*. Once the bankruptcy estate has terminated, this court can envision no purpose of Congress in the exercise of its bankruptcy power preempting state laws which provide for the enforcement of creditors' remedies. Accordingly, this court concludes that section 1326(a)(2) does not preempt state law and should be interpreted consonant with state law— allowing for levy upon funds to be distributed by a trustee in a dismissed case. *Massachusetts v. Pappalardo (In re Steenstra)*, 307 B.R. 732 (B.A.P. 1st Cir. 2004); *In re Doherty*, 229 B.R. 461.

Since the hearing, the trustee has requested that the court hold a further hearing in light of the subsequent assertion of an existing lien superior to that of Buffalo Welding. The Internal Revenue Service has since joined in that request (Doc. No. 114). Accordingly, it is hereby

ORDERED that the Motion at docket no. 105 is set for further hearing before the United States Bankruptcy Court, James M. Hanley United States Courthouse & Federal Building, 100 S. Clinton Street, Syracuse, New York on April 9, 2013 at 10:00 a.m.

/s/Margaret Cangilos-Ruiz
Margaret Cangilos-Ruiz
United States Bankruptcy Judge

Dated: March 22, 2013
Syracuse, New York