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## Feature

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### Reasonable Search and Seizure

#### Balancing a Trustee's Duties Against the Fourth Amendment



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The Bankruptcy Code delivers immense relief to the “honest but unfortunate debtor” by way of the discharge. The entire bankruptcy system works on the presumption that debtors enter the process in good faith, honestly represent their assets and liabilities, and will fulfill the requisite duties of a debtor under the Bankruptcy Code. However, fraud and concealment have been concerns of bankruptcy laws for hundreds of years.<sup>1</sup> Indeed, the orderly distribution of the debtor's assets under chapter 7 would be impossible if the system countenanced concealment of assets or outright fraud by debtors.

The Bankruptcy Code contains various safeguards to mitigate the potential for fraud and provide remedies if fraud has occurred, most notably with a denial of discharge. The chapter 7 trustee serves a paramount role in ensuring that the system remains honest and open, and is statutorily mandated to investigate the debtor's financial affairs.<sup>2</sup> In a perfect world, the debtor would disclose all assets in full candor to assist the trustee in the performance of his/her duties.

Unfortunately, the world is not perfect. This becomes all too clear in cases involving property that is easily concealable or moveable like jewelry, precious metals, cash, art and vehicles. Many debtors may make inadvertent omissions in their petitions and later cooperate with the trustee in correcting oversights. However, some debtors enter the process intent on concealing assets and information from the trustee and creditors. What is the trustee to do if he/she has reason to believe that the debtor has concealed potentially valuable undisclosed

property? Indeed, what if the property is believed to be concealed in the most constitutionally sensitive place of all: the debtor's home?

This raises some interesting Fourth Amendment issues that are rarely considered by the bankruptcy bar. While a bankruptcy trustee generally has broad discretion in executing his/her duties,<sup>3</sup> the Fourth Amendment creates a tricky situation when faced with an obstreperous debtor. Case law addressing how a trustee must balance his/her duties to investigate a debtor's financial affairs with the Fourth Amendment's privacy protections is sparse. However, in two reported cases, *Taunt v. Barman*<sup>4</sup> and *Youngman v. Bursztyn*,<sup>5</sup> bankruptcy courts have issued *ex parte* orders providing for a trustee to perform an inspection of a debtor's residence, and in doing so have created some standards to show when and how seeking such an order might be appropriate.

#### *In re Barman*

Norman Barman disclosed only one asset when he filed for chapter 7 relief on March 20, 1999: wearing apparel valued at \$500.<sup>6</sup> The trustee's investigation uncovered a litany of undisclosed assets and fraudulent activities. For example, Barman had disposed of records pertaining to his vending and video machine business, and he was not forthright about the location of any of the remaining video poker machines.<sup>7</sup> In addition, the debtor purchased properties in others' names, including his parents, where he stored \$40,000 worth of fur-

<sup>1</sup> Michael D. Sousa, “A Delicate Balancing Act,” *Yale Journal on Regulation*, Vol. 28 (2011): “England promulgated the first Anglo-bankruptcy law in 1542 during the reign of King Henry VIII, and its primary purpose was not the rehabilitation of debtors, but the prevention of fraud by debtors upon their creditors.” Prof. Sousa's work on this article's topic is highly recommended for anyone seeking a deeper and more scholarly examination of the issues.

<sup>2</sup> 11 U.S.C. § 704(a)(4).

<sup>3</sup> See *Commodity Futures Trading Comm'n v. Weintraub*, 471 U.S. 343, 352, 105 S. Ct. 1986 (1985) (“[T]he Bankruptcy Code gives the trustee wide-ranging managing authority over the debtor.”); see also *In re Allou Distribs. Inc.*, 392 B.R. 24, 30 (Bankr. E.D.N.Y. 2008) (“A Chapter 7 trustee's powers to act on behalf of the bankruptcy estate are broad in scope.”).

<sup>4</sup> *In re Barman*, 252 B.R. 403 (Bankr. E.D. Mich. 2000).

<sup>5</sup> *In re Bursztyn*, 366 B.R. 353 (Bankr. D.N.J. 2007).

<sup>6</sup> *Barman* at 407.

<sup>7</sup> *Id.*

niture. The debtor also had a business in bankruptcy in South Carolina and was held in contempt for willfully violating a court order there. Barman's wife bought and sold homes in her name during the relevant time frames, despite having a modest income that came only from the debtor's business. Lastly, the trustee received information that there were 15-20 video poker machines at one of the homes purchased by Barman's wife, and that the couple stored a trailer there with personal property packed inside in preparation of a move.<sup>8</sup> In all, the trustee's investigation and the bankruptcy proceeding in South Carolina had established facts showing that Barman was (1) attempting to conceal or move assets, and (2) uncooperative with court orders.

The trustee initiated an adversary proceeding against Barman and his wife alleging fraudulent transfers and concealment of assets. At the same time, he filed an *ex parte* motion for an order authorizing him to enter the debtor's residence to inspect, inventory and appraise personal property, which the court granted. In a subsequent motion to suppress evidence, Barman contended, among other things, that the search of his residence was a violation of his Fourth Amendment rights to be free from unreasonable search and seizure.<sup>9</sup>

This was a case of first impression. As the Fourth Amendment only applies to government action, the threshold question is whether the trustee is a state actor or a private person. While panel trustees are private persons, the court nonetheless found that a trustee carrying out his/her duties during a case was enough to be considered a "government action." First, the trustee acted under the authority of law in carrying out his/her duties pursuant to § 704 and Bankruptcy Rule 2015(a)(1). Second, the trustee is appointed to a case through the office of a Department of Justice official, the U.S. Trustee.<sup>10</sup> In addition, trustees' actions are subject to court approval and they are under the discipline and authority of the bankruptcy court with jurisdiction over the case in which they are appointed.<sup>11</sup> The court also noted that there is a long-recognized derivative judicial immunity for actions that the trustee, as an officer of the court, enjoys from liability for actions within the scope of his/her official duties.<sup>12</sup> Accordingly, these factors led the court to find that the trustee's actions were subject to the Fourth Amendment.

The court next addressed the standards to apply to the search. As the Fourth Amendment only protects against unreasonable searches and seizures, the court had to decide whether this was a reasonable search. To do so, the court balanced the public interest between the need for a trustee to inspect a debtor's home when there is probable cause to search for secreted assets, and the effects that the inspection would have on the debtor's privacy interests. For the public interest, there is a statutory duty of a trustee to investigate the debtor's financial affairs and marshal property of the estate, as well as the strong interest in an effective and open disclosure regime. On the other hand, since all of the debtor's personal property is property of the estate, thereby creating a broad realm, there is the possibility that a trustee

will search places that will not have anything to do with the search's target, seriously treading on a debtor's intimate and personal items.

The court found that to balance all of these interests, the first procedure that the trustee would have to follow would be to make a reasonable request for an inspection order. To be reasonable, the request would have to be a written motion in compliance with federal and local rules, and the trustee would have to present detailed facts establishing that there is property of the estate on the premises. If the motion was *ex parte*, the trustee would need to set forth detailed facts as to why such relief was necessary without notice to the debtor. The request would also have to be reasonable in its proposed execution, with the inspection occurring during regular business hours, in the debtor's presence and without forcible entry. The court raised the possibility that there might be facts that the trustee could present to warrant deviation from these general principles, but for the most part, these would be the standards for a reasonable request and a reasonable search.

### **In re Bursztyn**

In *Bursztyn*, the debtor's original petition showed a modest estate with assets of just over \$200,000 (almost all of which was a contingent claim against her ex-husband) and liabilities of almost \$195,000.<sup>13</sup> In several sections of the petition, the debtor disclosed a small household with very few assets, listing costume jewelry worth \$135, ordinary household goods worth \$1,000, ordinary clothing worth \$300, and no art or collectibles.<sup>14</sup>

The debtor was a party to an acrimonious divorce that produced multiple judicial decisions that the trustee was able to rely on to challenge the petition.<sup>15</sup> In one decision, a New Jersey Superior Court judge found that the debtor had retained artwork and jewelry worth \$125,000 during her divorce proceedings.<sup>16</sup> In that same decision, the judge took notice of the fact that the debtor had "constantly violated Court Orders, changed counsel, retained needless experts, and generally obstructed the litigation process on numerous occasions."<sup>17</sup> The divorce case led to an appeal, and the appellate division handed down a decision that included an observation that the couple spent \$134,000 to purchase fine jewelry during a two-year period.<sup>18</sup>

The appellate division's decision also referred to the debtor's "disregard for the authority of the Court."<sup>19</sup> These two judicial decisions made or affirmed findings that the debtor (1) retained assets and attempted to keep them out of her divorce proceedings, and (2) was not cooperative or compliant with court orders.

Based on the state court decision, the trustee sought turnover of the debtor's undisclosed jewelry and art. The bankruptcy court entered orders directing the debtor to turn over the property, but the debtor was uncooperative. The trustee then applied *ex parte* for an order and preliminary injunction to enter the debtor's residence with the assistance of the U.S. Marshals Service and her professionals to search for,

8 *Id.* at 409-10.

9 *Id.* at 410.

10 *Id.* at 413 (citing statutory authority in Titles 11 and 28).

11 *Id.* (citing §§ 324, 327 and 327 as examples).

12 *Id.* at 410 (citing *Kashani v. Fulton (In re Kashani)*, 190 B.R. 875, 883 (B.A.P. 9th Cir. 1995)).

13 *Bursztyn* at 356.

14 *Id.*

15 *Id.*

16 *Id.* at 357.

17 *Id.* (internal citation omitted).

18 *Id.*

19 *Id.* at 358.

seize and appraise specific estate property, namely the jewelry and art contemplated in the state court decisions.<sup>20</sup> The resulting order required that the search be performed within 10 days and during business hours. In executing the search, the trustee personally served the order upon the debtor, who was home at the time. The search uncovered art and jewelry appraised at \$242,767, almost double what the state court decisions had estimated the value of the property to be.<sup>21</sup> After the search and seizure of the items, the debtor filed an opposition to the order as violating the Fourth Amendment.<sup>22</sup> Inevitably, this led the court to begin an analysis of the Fourth Amendment in the bankruptcy context.

Like in *Barman*, the *Bursztyn* court examined the threshold matter of government action. If the trustee is not a government actor, then the debtor's objections would be immaterial. The court began by conceding that the duties and characteristics of a chapter 7 trustee puts her in a gray area for purposes of determining state action.<sup>23</sup> However, citing *Barman*, the *Bursztyn* court found that the trustee's actions during a case present a sufficiently close nexus to governmental action to apply the Fourth Amendment.<sup>24</sup>

Next, the court examined whether the Fourth Amendment was in fact violated. The court balanced the debtor's privacy interests against the public's interest in a sound bankruptcy system to determine whether the search was reasonable. Sound administration and statute require a trustee to investigate a debtor's financial affairs, which sometimes requires an inspection of a debtor's residence in a search for assets. In weighing these interests, the court said it would not lead to an inevitable victory for the trustee; "[r]ather, this remedy is reserved only for the rare situations where a bankruptcy trustee presents the Court with specific, concrete, and compelling reasons to justify such a procedure as well as convince[s] the Court that doing so is a matter of substantial need."<sup>25</sup>

The court concluded that the trustee's application and search were reasonable under the circumstances. The trustee had established a lengthy record that described assets in particularity (a stash of jewelry and art) that were easily movable by a debtor whose "overall deceitfulness and disdain for the judicial system cannot be minimized."<sup>26</sup> The court felt the trustee was "abundantly justified in believing a substantial need existed to search the Debtor's residence."<sup>27</sup> The court seemed satisfied with the application due to three factors: (1) the scope of the application was to find specific items that were identified by reliable sources as being held by the debtor (here, two judicial decisions); (2) the items had the potential to be moved and were undisclosed; and (3) the debtor had a record of scorn for the judicial process. In light of this, the search of the debtor's residence was reasonable and did not violate the Fourth Amendment.

## Conclusion

These two cases are examples of how a trustee who wishes to search for assets in a debtor's home can satisfy Fourth

Amendment concerns. As a threshold matter, a chapter 7 trustee's action will be subject to the Fourth Amendment. While not as stringent as in a criminal context, the trustee should still set forth the strong government interest in the search. The search should also request an inspection that is reasonable in its request and execution, with detailed supporting facts demonstrating why the extraordinary relief is necessary. The inspection should also be reasonable in execution, occurring in a reasonable amount of time from the entry of the order (10 days in *Bursztyn*), during business hours and with the debtor's knowledge or presence.

These two cases also show the types of debtors that create the circumstances where the courts may find that the facts warrant such relief. The debtors in both cases were shown to have concealed assets and misrepresented their affairs in their petitions. Both had been uncooperative with the trustees, and adversary proceedings had been filed. In addition, both debtors were found to have been disobedient and contemptuous of courts and their authority. Perhaps more than anything, this last detail provided the basis to tip the scales toward reasonableness and in the trustees' favor. The results of these two cases, in which the trustee uncovered significant undisclosed assets, suggest that at least in those instances, the ends justified the means. **abi**

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<sup>20</sup> *Id.* at 360.

<sup>21</sup> *Id.* at 362.

<sup>22</sup> *Id.*

<sup>23</sup> *Id.* at 364.

<sup>24</sup> *Id.* at 368.

<sup>25</sup> *Id.* at 372.

<sup>26</sup> *Id.* at 373.

<sup>27</sup> *Id.*