

NORTH,SOUTH, EAST OR WEST: ARE IRAs EXEMPT ASSETS UNDER THE BANKRUPTCY CODE?

By Attorney Raynor D. Zillgitt, Jr.

Recently, Bankruptcy Judge Jeffrey R. Hughes issued an opinion that will impact the decision of many prospective debtors to file a Chapter 7 bankruptcy petition in the Western District of Michigan. In *In re Dale*, 252 B.R. 430 (Bankr. W.D. Mich. 2000), the court ruled that the debtor's IRA's are only exempt from a bankruptcy estate to the extent the debtor is eligible at the time of the bankruptcy petition to draw benefits from the IRA on account of illness, disability, death, age or length of service. *Id.* at 432. Although there was no controlling authority, the opinion was contrary to three decisions in the Western District, two of which were reported. *Jurgensen v Chalmers* (*In re Chalmers*), 248 B.R. 94 (W.D. Mich. 2000); *Brucher v Dettman* (*In re Brucher*), No. 2:99-CV-184 (W.D. Mich. Nov. 22, 1999) (unpublished); and *In re Hall*, 151 B.R. 412 (Bankr. W.D. Mich. 1993).

The debtors in *Dale* filed a Chapter 7 proceeding and as part of their petition scheduled five IRAs as assets of the estate. The IRAs totaled approximately \$33,000 and were the extent of the debtors' retirement planning. On the date the bankruptcy was filed, the debtors were 48 and 52 years old. As part of their petition, the debtors elected to exempt the IRAs pursuant to 11 USC § 522(d)(10)(E). The Chapter 7 trustee objected, oral argument was subsequently held, and the court issued its opinion on August 25, 2000.

Section 522 (d) of the Bankruptcy Code provides that the following property may be exempt:

(10) The debtor's right to receive –

(E) a payment under a stock bonus, pension, profit-sharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor, unless –

(i) such plan or contract was established by or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose;

(ii) such payment is on account of age or length of service; and

(iii) such plan or contract does not qualify under section 401(a), 403(a), 403(b), or 408 of the Internal Revenue Code of 1986.

In 1992, Judge Stevenson published her opinion in *In re Moss*, 143 B.R. 465 (Bankr. W.D. Mich. 1992), which indicated that the debtor's interest in an IRA was not exempt under § 522(d)(10)(E) of the Bankruptcy Code. A year later, Judge Gregg ruled in *In re Hall*, 151 BR at 412, that the debtor's interest in his IRA was exempt. Recently, Judge McKeague in *Jurgensen* reversed the *Moss* decision. 248 B.R. at 99.

In *Hall*, the debtor had exempted an IRA pursuant to § 522(d)(10)(E) and the Trustee objected. Judge Gregg denied the Trustee's objection. In reaching his conclusion to allow the debtor to exempt his IRA, Judge Gregg analyzed the statute in its entirety. The court took issue with the *Moss* decision and the cases following it by stating that it was superfluous for the *Moss* court to go beyond the statute and analyze the clauses, "benefit akin to future earnings," "control over the investment" and "present right to payment." *Id.* at 425. Instead the *Moss* court needed only to look at the entire statute according to Judge Gregg. *Id.*

Judge Gregg then examined the third prong of the exception to § 522(d)(10)(E)(iii) and indicated that "[i]ndividual retirement plans, are without question, included in the class of plans or contracts" described in that exception. *Id.* at 426.

The court continued:

If a court holds an individual retirement plan is not a 'similar plan or contract' under § 522(d)(10)(E), it is impossible to reconcile the specific language in § 522(d)(10)(E)(iii) with the rest of the subsection. Because every word or phrase of § 522(d)(10)(E) must be given effect, this court cannot ignore Congress's inclusion of individual retirement plans in § 522(d)(10)(E)(iii). *Sutherland, supra*, §46.06. Similarly, because the same words or phrases used more than once must have the same meaning, the only rational conclusion is the 'similar plan or contract' language in § 522(d)(10)(E) includes individual retirement plans.

Id.

Thus, the court ruled in favor of the debtor's scheduled exemptions. *Id.* at 427. Judge McKeague also ruled in a similar vein in *Jurgensen*. There he held:

Although the language of § 522(d)(10)(E) is unambiguous, the issue at hand requires the Court to reconcile two sections of text whose plain meaning seemingly lies in conflict. The common understanding of the terms 'on account of' works to exclude virtually all IRAs, while the implication of subsection (iii) warrants their inclusion. Rather than relying on policy arguments or legislative history, the Court reads the statute as a whole to reach a reasonable result that gives effect to both the statute's text and its scheme. Accordingly, the Court concludes that although the 'on account of' factors may serve as exclusive triggers, with regard to age, they cannot work to

exclude those qualified IRAs permissibility exempted by the negative implication of § 522(d)(10)(E)(iii).

248 B.R. at 99.

Judge Hughes acknowledged this contrary authority by stating in his opinion:

I acknowledge that my decision adds yet another compass point from which future courts may select as they confront this issue. I also recognize that my decision runs counter to the decisions of three of the four judges in this district who have addressed this issue and that two of those three judges have appellate authority over my decisions. I value consistency within the district. However, as I read and reread the Hall, Jurgensen, Brucher and Moss decisions, I could not escape the conclusion that each court struggled as it attempted to decipher Section 522(d)(10)(E). Moreover, I could not find anything within these decisions or the multitude of other decisions concerning Section 522(d)(10)(E) which analyzed this subsection in the context of the four other subsections of Section 522(d)(10).

The appellate courts may not accord the same significance to these other subsections as I have. If not, then my decision will be overturned and I will follow their direction. However, I could not in good conscience ignore what I believe is a very compelling argument, particularly when it appears that that argument has not been considered by any previous court which has addressed this issue.

Dale, 252 B.R. at 432 (n 3).

The direction that the court added to the IRA compass was to focus not on the body of subsection (E), but instead to analyze the language of subsection (10) which states “the debtor’s right to receive a payment . . .” (Emphasis added.) The court determined that to give effect to the entire provision, it must not focus on whether the debtor’s “interest” in the IRA was exempt, but whether the debtor’s “right to receive a payment” under the IRA was exempt. *Id.*

Noting the paucity of legislative history of the section, the court included that Congress did not intend a broad retirement plan exemption by the statute. If so, they would have done so by clearly stating that “all interest” in a stock bonus, pension, profit-sharing, annuity or similar plan would be exempt. *Id.* at 433.

Consequently, Judge Hughes determined that for the IRAs to be exempt, the debtor must be currently eligible to receive a payment on account of illness, disability, death, age or length of service under the IRA. *Id.* at 440. Since the debtors did not qualify to currently receive a payment for any of the above reasons, the IRAs were deemed not exempt.

Judge Hughes undertook a thorough and lengthy discussion to support his conclusions. In doing so, the court attempted to reconcile the numerous inconsistencies in the statute and harmonize the other subsections included in Section 522 (d)(10). *Id.*

In summary, the result of this decision is that unless the debtor is currently receiving a payment under an IRA, and the payment is reasonably necessary for his or her support or for the support of a dependant, then the IRA is not exempt under the Bankruptcy Code. However, assets under a traditional ERISA-qualified pension plan, such as a 401K plan, are still exempt under the Bankruptcy Code. See, e.g., *Patterson v Shumate*, 504 U.S. 753; 112 S. Ct. 2242 (1992). Furthermore, outside of the Bankruptcy Court, IRAs are still exempt from creditors under Michigan law. MCLA § 600.6023(a)(11).

Judge Hughes' decision also impacts other retirement vehicles including pensions established by governmental entities and churches. Therefore, retirement plans through the State of Michigan, or its public universities fall under the ambit of the Dale decision, and would only be exempt if there was a present right to receive a payment. Consequently, Judge Hughes' decision will undoubtedly cause disparate treatment between similar debtors based upon where they work and what type of retirement plans they participate in.

It should be noted that the Dale decision is currently on appeal to the United States District Court for the Western District of Michigan. A decision is expected shortly.

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