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# RETIREMENT PLAN ASSETS: THE RETENTION RIGHTS OF AN OKLAHOMA DEBTOR IN BANKRUPTCY

## I. INTRODUCTION

Participation in retirement and pension plans has grown at a tremendous rate in recent years.<sup>1</sup> This growth has been due, in large part, to the enactment of the Employer Retirement Income Security Act of 1974 (ERISA)<sup>2</sup> which, coordinated with the Internal Revenue Code of 1954, provide favorable tax treatment for qualified plans.<sup>3</sup> At the same time ERISA plans were gaining in popularity, personal bankruptcy petitions were being filed in record numbers.<sup>4</sup>

A question has developed in several jurisdictions regarding the treatment of a debtor's interest in these plans under the Bankruptcy Reform Act of 1978.<sup>5</sup> This Comment will discuss whether, under the Bankruptcy Code and Oklahoma law,<sup>6</sup> a debtor's interest in ERISA plans may be used to satisfy the claims of creditors in a bankruptcy proceeding. Due to the organizational structure of the Bankruptcy Code,<sup>7</sup> this ques-

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1. Assets held in private pension funds have grown from 176 billion dollars in 1974 to 573 billion dollars in 1982. UNITED STATES DEP'T OF COMMERCE, STATISTICAL ABSTRACT OF THE U.S. 384 (104th ed. 1984).

2. Pub. L. No. 93-406, 88 Stat. 898 (1974) (codified at 29 U.S.C. §§ 1001-1144 (1982) and in scattered sections of 26 U.S.C.).

3. Retirement plans qualified under I.R.C. § 401 (1982) are exempt from taxation under the provisions of I.R.C. § 501 (1982). The Internal Revenue Code also allows for deductions for contributions made by employers and establishes minimum vesting standards which make it easier for an employee to take accumulated benefits when changing jobs. *See id.* §§ 404, 411.

4. The number of bankruptcy petitions filed in 1982 reached almost 500,000. This figure is three times the 1972 rate. UNITED STATES DEP'T OF COMMERCE, *supra* note 1, at 563.

5. 11 U.S.C. §§ 101-151326 (1982) (referred to herein as the Bankruptcy Code or Code).

6. Oklahoma law (discussed *infra* notes 75-113 and accompanying text) is involved by virtue of Bankruptcy Code provisions allowing for the exclusion of certain assets from the estate based on applicable nonbankruptcy law and exemption from the estate based on state law. *Id.* §§ 522(b)(1), 541(c)(2).

7. A voluntary bankruptcy proceeding is commenced upon the filing of a petition. *Id.* § 301. Commencement of the case acts as an automatic stay preventing creditors from initiating or continuing most actions against the debtor in satisfaction of claims. *Id.* § 362. When the action is initiated under section 301, an estate is formed and is generally comprised of all property interests of the debtor at the time the case was commenced. *Id.* § 541. From the estate, a debtor is allowed to retain certain items of property in order to permit the debtor a fresh start in life following the termination of the bankruptcy proceeding. *See id.* § 522. The balance of the estate is paid to creditors on the basis of a priority system set forth in section 507. *Id.* § 726. After the distribution of assets has occurred, the court discharges the unsatisfied debts. *Id.* § 727.

Other forms of bankruptcy, for example, reorganization under Chapter 11 or the wage earner

tion must be answered in two parts. First, whether funds held in ERISA qualified plans are excluded from the estate of a debtor in bankruptcy.<sup>8</sup> Second, whether such funds, if included in the bankruptcy estate, are exempt from attachment, execution, or other forced sale under applicable bankruptcy or nonbankruptcy law.<sup>9</sup> To date, these questions have not been specifically addressed in Oklahoma.<sup>10</sup>

Since no case law exists in Oklahoma, judicial decisions from other jurisdictions will be explored. The interpretation of the Bankruptcy Code, as developed in these decisions, will be discussed in light of relevant Oklahoma statutes. Through this process, a suggestion will be made for the treatment of a debtor's interest in an ERISA plan in bankruptcy proceedings applying Oklahoma law.

## II. TREATMENT IN OTHER JURISDICTIONS

The issue of whether a debtor's interest in ERISA plans may be protected from creditors in a bankruptcy proceeding has not been treated consistently by courts confronted with the problem. One line of cases, represented by *Samore v. Graham (In re Graham)*<sup>11</sup> and *Goff v. Taylor (In re Goff)*,<sup>12</sup> holds that ERISA qualified plans are both a part of the estate and are not exempted by either federal bankruptcy or non-bankruptcy law.<sup>13</sup> In direct conflict with this position are the cases fol-

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plan under Chapter 13, have different provisions for administration, distribution, and discharge. This short overview pertains to a bankruptcy liquidation under Chapter 7 of the Code. This Comment is limited to the formation of the estate and whether, under sections 541 and 522, the retirement plan assets may be retained by a debtor in bankruptcy. See generally Vukowich, *Reforming the Bankruptcy Reform Act of 1978: An Alternative Approach*, 71 GEO. L.J. 1129 (1983) (discussing the Bankruptcy Reform Act of 1978).

8. Exclusion relates to the formation of the estate under the provisions of section 541 of the Bankruptcy Code. 11 U.S.C. § 541. Funds which are excluded from the estate do not become subject to the authority of the trustee and are never considered during the bankruptcy proceeding to be property of the debtor. Federal law controls the formation of the bankruptcy estate and the definition of what property will be brought into the estate upon its creation. See *id.*

9. *Id.* § 522. Exemption refers to the right of a debtor to retain property of the estate free from the claims of creditors. The difference between exemption and exclusion is that an exemption is granted *from* property of the estate, while an exclusion operates to prevent property from ever *becoming* property of the estate. Exemptions may be granted on the basis of either state or federal law. See *Pickens v. Pickens*, 125 Tex. 410, 414, 83 S.W.2d 951, 954 (1935).

10. No case has been reported in which the issue of an Oklahoma debtor's right to retain assets held in ERISA plans was decided by a bankruptcy court or a federal district court in a bankruptcy proceeding.

11. 24 Bankr. 305 (Bankr. N.D. Iowa 1982).

12. 706 F.2d 574 (5th Cir. 1983).

13. See, e.g., *Goff*, 706 F.2d at 579-80 (ERISA qualified Keogh plans, other than spendthrift trusts, are not exempt under applicable nonbankruptcy law); *Graham*, 24 Bankr. at 308 (including the ERISA fund in the bankruptcy estate); *In re Howerton*, 21 Bankr. 621, 622-23 (Bankr. N.D. Tex. 1982) (retirement account was not exempt under Bankruptcy Code).

lowing *Clotfelter v. Ciba-Geigy Corp. (In re Threewitt)*<sup>14</sup> and *Barr v. Hinshaw (In re Hinshaw)*<sup>15</sup> which hold, respectively, that ERISA plans are not included in the assets of the bankruptcy estate, or if included, are exempt under federal bankruptcy and nonbankruptcy law.<sup>16</sup>

#### A. Exclusion From The Estate

The first issue to be discussed in determining whether ERISA plan assets may be retained by a debtor in bankruptcy is whether such assets become property of the estate upon the filing of a bankruptcy petition. The bankruptcy estate, as defined under section 541 of the Bankruptcy Code, is generally comprised of all legal and equitable interests in property held by the debtor at the commencement of the case.<sup>17</sup> While each state has the authority to determine the extent and nature of a debtor's property rights, whether those interests become an asset of the bankruptcy estate is a question governed by the provisions of the Bankruptcy Code.<sup>18</sup> Section 541, often referred to as the automatic inclusion provision of the Bankruptcy Code, has been broadly interpreted by courts. The general rule is that all property or interests in property held by the debtor upon filing of the bankruptcy petition automatically become part of the bankruptcy estate.<sup>19</sup>

Only one exception to the general rule is applicable to this analysis. Section 541(c)(2) excludes from the assets of the estate any interest the debtor has in a trust in which transferability is effectively restricted by nonbankruptcy law.<sup>20</sup> This exception and the disagreement over its interpretation have resulted in conflicting conclusions as to whether the exemption provided in section 541(c)(2) is limited to spendthrift trusts.

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14. 24 Bankr. 927 (D. Kan. 1982).

15. 23 Bankr. 233 (Bankr. D. Kan. 1982).

16. *Threewitt*, 24 Bankr. at 930 (pension plan qualifying under ERISA is excluded from the bankruptcy estate); *Warren v. G.M. Scott & Sons (In re Phillips)*, 34 Bankr. 543, 546 (Bankr. S.D. Ohio 1983) (debtor's interest in pension plan which qualified under ERISA is not part of debtor's estate); *In re Pruitt*, 30 Bankr. 330, 332 (Bankr. D. Colo. 1983) (interest of a thrift plan which qualified under ERISA was not part of the estate); *Hinshaw*, 23 Bankr. at 236 (tax qualified ERISA plans provide debtor with an exemption under the Code).

17. 11 U.S.C. § 541(a) (1982); *Threewitt*, 24 Bankr. at 930; *Hinshaw*, 23 Bankr. at 236; *Avery Fed. Sav. & Loan Ass'n v. Klayer (In re Klayer)*, 20 Bankr. 270, 272 (Bankr. W.D. Ky. 1981).

18. See *Graham*, 24 Bankr. at 309 ("Non-bankruptcy law defines what the debtor's interest in property is, while bankruptcy law determines whether that interest passes to the bankruptcy trustee as property of the bankrupt's estate.").

19. *Id.*; *Klayer*, 20 Bankr. at 272.

20. See 11 U.S.C. § 541(c)(2) ("A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.").

The two views are best illustrated by the following case which produced two published opinions.

*In re Threewitt*<sup>21</sup> involved the issue of whether the debtor's interest in an ERISA qualified pension plan was property of the estate under section 541 of the Bankruptcy Code. The trustee in bankruptcy sought a court order requiring the defendant (the debtor's employer) to turn over to the estate the debtor's interest in an ERISA fund.<sup>22</sup> The defendant argued that restrictions on alienation of a beneficiary's interest, which were contained in the plan, are required by ERISA in order to qualify the plan as tax exempt.<sup>23</sup> Since ERISA plans are required to contain restrictions on transferability, and since ERISA is applicable nonbankruptcy law within the meaning of section 541(c)(2), the defendant argued that assets held in ERISA plans do not become property of the estate by virtue of section 541(c)(2)'s exception to the automatic inclusion provision.<sup>24</sup> The bankruptcy court rejected the defendant's argument and limited the effect of the section 541(c)(2) exception to spendthrift trusts.<sup>25</sup> The court held that the ERISA fund was not a traditional spendthrift trust and therefore was not exempt from the debtor's estate.<sup>26</sup> The court's conclusion was based on the legislative history of section 541<sup>27</sup> and has been followed by other courts addressing the same issue.<sup>28</sup> The bankruptcy court also noted that section 522(d)(10)(E)<sup>29</sup> offers a limited exemption for pension plan payments. The court then reasoned that it would be unlikely for Congress to provide for the exemption of an asset that had already been excluded from the bankruptcy estate.<sup>30</sup>

Under the bankruptcy court's decision in *Threewitt* and the cases that follow its analysis,<sup>31</sup> assets held in an ERISA plan become a part of the estate unless the plan meets the requirements of applicable state law

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21. *Clotfelter v. Ciba-Geigy Corp. (In re Threewitt)*, 20 Bankr. 434 (Bankr. D. Kan. 1982), *rev'd*, 24 Bankr. 927 (D. Kan. 1982).

22. 20 Bankr. at 435.

23. *Id.* at 436.

24. *Id.* at 438.

25. *Id.* The Congressional committee reports relied on by the court in *Threewitt* state: "Paragraph (2) of subsection (c) . . . preserves restrictions on transfer of a spendthrift trust to the extent that the restriction is enforceable under applicable nonbankruptcy law." H.R. REP. NO. 95-595, 95th Cong., 1st Sess. 369 (1977), *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 6325.

26. 20 Bankr. at 438.

27. *Id.*

28. *See Goff*, 706 F.2d at 580; *Strasma*, 26 Bankr. at 450; *Graham*, 24 Bankr. at 310; *Howerton*, 21 Bankr. at 622.

29. 11 U.S.C. § 522(d)(10)(E).

30. *Threewitt*, 20 Bankr. at 438-39.

31. *See cases cited supra* note 28.

governing the creation of spendthrift trusts. One requirement generally recognized is that a person may not restrict a creditor's access to a trust he has created for his own benefit.<sup>32</sup> A spendthrift clause<sup>33</sup> inserted by the settlor of a self-settled trust<sup>34</sup> is void as to then existing or future creditors.<sup>35</sup> If an ERISA qualified pension plan is created in the form of a self-settled trust, the anti-alienation clause would be ineffective and the ERISA plan would not qualify for exclusion under section 541(c)(2).

The bankruptcy court's decision in *Threewitt* was appealed to the district court.<sup>36</sup> In reversing the bankruptcy court, the district court stated that to view section 541(c)(2) as applying only to spendthrift trusts was an "unnecessarily narrow" interpretation of congressional intent.<sup>37</sup> The district court held that under section 541(c)(2), the proper question to be decided was whether an anti-alienation clause in an ERISA plan would be enforceable against creditors in a nonbankruptcy action.<sup>38</sup> Relying on a long line of cases holding that such restrictions are enforceable against general creditors, the district court concluded "by virtue of section 541(c)(2), that the bankruptcy trustee may not reach Mr. Threewitt's interest in the Plan."<sup>39</sup>

In reaching this conclusion, the district court also rejected the bankruptcy court's inference of legislative intent. The bankruptcy court had reasoned that since pension plan payments were exempt to a limited degree under section 522, Congress would not have exempted an asset already excluded from the estate.<sup>40</sup> The district court stated that this

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32. RESTATEMENT (SECOND) OF TRUSTS § 156(1) (1959).

33. See *Avery Fed. Sav. & Loan Ass'n v. Klayer* (*In re Klayer*), 20 Bankr. 270, 273 (Bankr. W.D. Ky. 1981). A spendthrift clause is one which purports to restrict the ability of a trust beneficiary to transfer or encumber his interest either by voluntary or involuntary action. This type of clause is most often used by the relative or guardian of a person unable to manage his affairs. Public policy supports this use and will enforce the clause thus protecting the settlor's intent to provide a continuous income for the beneficiary or to protect the assets of the beneficiary despite his incapacity or poor judgment. Under this reasoning, when the identity of the settlor and beneficiary are merged, the justification for enforcing such a clause against creditors is destroyed. See generally 76 AM. JUR. 2D *Trusts* § 168 (1969) (discussing the law of spendthrift trusts).

34. The term *self-settled trust* is used to define a trust in which the beneficiary (the person to whom the beneficial interest in a trust belongs) and the settlor (the person creating the trust) are the same person. See BLACK'S LAW DICTIONARY 142-43, 1231 (5th ed. 1979); see also G. BOGERT, HANDBOOK ON THE LAW OF TRUSTS 154 (5th ed. 1973) (discussing the effect of a spendthrift clause in a trust created by a settlor for his own benefit).

35. See *Graham*, 24 Bankr. at 310; see also *Arizona Bank v. Morris*, 7 Ariz. App. 107, 436 P.2d 499 (1968) (discussing attempts to restrict alienation of interests in a self-settled trust).

36. *Clotfelter v. Ciba-Geigy Corp.* (*In re Threewitt*), 24 Bankr. 927 (D. Kan. 1982).

37. *Id.* at 929.

38. *Id.*

39. *Id.*

40. *Id.*

conclusion might have been persuasive if section 522(d)(10)(E) only applied to ERISA plans.<sup>41</sup> Because this Code provision also embraces a number of plans not qualified under ERISA,<sup>42</sup> the district court did not "consider it remarkable that Congress did not bother to further complicate an already complex code by taking pains to insure that there was no overlap between Section 522(d)(10)(E) and Section 541(c)(2)."<sup>43</sup>

Other courts have criticized the bankruptcy court's interpretation of section 541(c)(2) as being based upon improper rules of statutory interpretation.<sup>44</sup> The court in *In re Pruitt*<sup>45</sup> stated: "When a statute is clear on its face there is no need to resort to legislative history."<sup>46</sup> According to *In re Pruitt*, section 541(c)(2) is "clear on its face and does not limit itself to spendthrift trusts."<sup>47</sup>

Based on a review of the different courts' reasoning, the more persuasive view is that ERISA plan assets are excluded from the estate by virtue of section 541(c)(2) of the Bankruptcy Code. The ambiguity found by several courts in the language of the provision only becomes apparent after reading the legislative history of the section. The language of the section itself is clear; it is the language used in the history of the section that is vague and which casts doubt on the meaning of the provision. Therefore, it is inappropriate to resort to legislative history and the clear meaning of the statute should control. ERISA plan assets should be excluded from the estate.

## B. *Exemptions Under the Bankruptcy Code*

Upon commencement of a bankruptcy action, property of the debtor not qualified for exclusion will be brought into the bankruptcy estate by operation of the automatic inclusion provision of section 541.<sup>48</sup> This does not mean, however, that all property of the estate will be used to satisfy the claims of creditors. In order to allow a debtor to make a fresh start following the termination of the bankruptcy proceeding,<sup>49</sup> the

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41. *Id.* at 930.

42. *Id.* The court noted that section 522(d)(10)(E) exempted the right to receive payments from such plans as Christmas stock bonuses paid upon twenty-five years of service or profit sharing plans restricted to senior employees.

43. *Id.*

44. *See, e.g., Warren v. G.M. Scott & Sons (In re Phillips)*, 34 Bankr. 543 (Bankr. S.D. Ohio 1983).

45. 30 Bankr. 330 (Bankr. D. Colo. 1983).

46. *Id.* at 331.

47. *Id.*

48. *See supra* notes 17-20 and accompanying text.

49. One goal of the uniform exemption provisions of the Bankruptcy Code, and of exemptions

Bankruptcy Code allows a debtor to retain certain types of property free from the claims of creditors. Section 522 of the Bankruptcy Code authorizes these exemptions and defines the property which may be claimed by a debtor in bankruptcy.

Unless forbidden by state statute, a debtor may choose between the exemption system contained in section 522(d) and those exemptions allowed under other federal, state, or local law.<sup>50</sup> The exemption for retirement plans is contained in section 522(d)(10)(E).<sup>51</sup> This provision limits the amount entitled to be exempted to that amount "reasonably necessary for the support of the debtor and any dependent of the debtor."<sup>52</sup> This provision has been interpreted in a conservative manner and generally will not result in an exemption for the full value of the retirement plan.

Due to the limitations of section 522(d)(10)(E), debtors in many instances attempt to claim an exemption for the full value of the plan under section 522(b)(2)(A). Section 522(b)(2)(A) recognizes that certain exemptions may be granted by federal nonbankruptcy law. Among the exemptions listed representatively in the legislative history of section 522<sup>53</sup> are Foreign Service Retirement and Disability payments,<sup>54</sup> Social Security payments,<sup>55</sup> civil service retirement benefits,<sup>56</sup> and Railroad Retirement

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in general, is to allow a debtor a fresh start in life following the termination of a bankruptcy proceeding. "[T]here is a Federal interest in seeing that a debtor that goes through bankruptcy comes out with adequate possessions to begin his fresh start." H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 126, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5963, 6087.

50. The authority to elect between alternative exemption systems is given in section 522(b) which provides:

(b) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate either—

(1) property that is specified under subsection (d) of this section, unless the State law that is applicable to the debtor . . . specifically does not so authorize; or, in the alternative,

(2)(A) any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition . . . .

11 U.S.C. §§ 522(b)(1)-(2)(A).

51. *Id.* § 522(d)(10)(E).

52. *Id.* A court will limit the exemption allowed to that amount "reasonably necessary for support." *Id.* Factors considered by a court in making the determination of what amount, if any, is necessary for support include the debtor's health, income, age, and employment status. See *In re Clark*, 18 Bankr. 824, 828 (Bankr. E.D. Tenn. 1982) (application of these factors to the exemption granted under section 522(d)(10)(E)).

53. See H.R. REP. NO. 95-595, 95th Cong., 2d Sess. 360, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5963, 6316; S. REP. NO. 95-989, 95th Cong., 2d Sess. 75, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5861.

54. 22 U.S.C. § 1104 (repealed 1981).

55. 42 U.S.C. § 407 (1982).

56. 5 U.S.C. § 8346 (1982).



ment Act annuities and pensions.<sup>57</sup> The common element in each of these federal statutes as they relate to the exemption question under section 522(b)(2)(A) is the requirement that the beneficiary's rights or interest must be restricted from voluntary or involuntary transfer in some way.<sup>58</sup> The statutes requiring that ERISA qualified plans contain restrictions on alienation are similarly phrased.<sup>59</sup>

The court in *Barr v. Hinshaw (In re Hinshaw)*<sup>60</sup> compared the language of those statutes provided by Congress in the legislative history<sup>61</sup> of section 522(b)(2)(A) with the language restricting alienation required of all ERISA qualified plans.<sup>62</sup> *Hinshaw* ruled that since the provisions were substantially similar, ERISA qualified plans were included in the estate but exempt from creditors under section 522(b)(2)(A).<sup>63</sup>

Taking the opposite position from the court in *Hinshaw*, the court in *Samore v. Graham (In re Graham)*<sup>64</sup> held that Congress did not intend to include ERISA qualified plans in the provision for exemptions under "other federal law."<sup>65</sup> The court noted that Congress did not include ERISA in the list of examples provided in the legislative history even though ERISA had been enacted prior to the enactment of the Bankruptcy Code.<sup>66</sup> *Graham* also compared the language of the restrictions contained in ERISA plans with the language contained in the example statutes listed in the legislative history.<sup>67</sup> *Graham* held that the provisions were significantly distinguishable in that no absolute prohibition on creditor process was required of ERISA plans.<sup>68</sup> The court interpreted the ERISA requirements to place only *some* restriction on the ability of

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57. 45 U.S.C. § 231m (1982).

58. Compare Foreign Service Act, 22 U.S.C. § 4060 (1982) (replacing 22 U.S.C. § 1104 (1976)) ("None of the moneys mentioned in this subchapter shall be assignable either in law or equity . . . or be subject to execution, levy, attachment, garnishment, or other legal process . . .") with Social Security Act, 42 U.S.C. § 407 (1982) ("The right of any person to any future payment under this subchapter shall not be transferable or assignable, at law or in equity, and none of the moneys . . . shall be subject to execution, levy, attachment, garnishment, or other legal process, or to the operation of any bankruptcy or insolvency law.").

59. Compare 22 U.S.C. § 4060 and 42 U.S.C. § 407 (1982) (*supra* note 58) with 29 U.S.C. § 1056(d)(1) (1982) (ERISA plans must "provide that benefits provided under the plan may not be assigned or alienated") and 26 U.S.C. § 401(a)(13) (1982) ("A trust shall not constitute a qualified trust under this section unless the plan . . . may not be assigned or alienated.").

60. 23 Bankr. 233 (Bankr. D. Kan. 1982).

61. See *supra* notes 53-57.

62. See *supra* note 59.

63. *Hinshaw*, 23 Bankr. at 235.

64. 24 Bankr. 305 (Bankr. N.D. Iowa 1982).

65. *Id.* at 312. The *Graham* court included the plan in the estate.

66. *Id.*

67. *Id.*

68. *Id.*

the beneficiary to transfer an interest.<sup>69</sup> According to *Graham*, if Congress had intended for ERISA plans to receive the benefit of exemption under section 522(b)(2)(A), then language prohibiting *execution* or *involuntary* alienation of interests would have been required in ERISA plans.<sup>70</sup>

In determining whether a debtor may exempt the assets held in ERISA qualified plans under section 522(b)(2)(A), one must look to the language contained in the plan's clause restricting transfer or alienation of a beneficiary's interest. If the language is reasonably similar to the language contained in the legislative history examples, it is appropriate to conclude that ERISA plans are exempt as federal law other than section 522(d).<sup>71</sup> The differences do not appear to be so great as to prevent an individual from taking advantage of the exemption.<sup>72</sup>

### C. Conflict in Existing Case Law

The split of authority over the two central issues discussed in this Comment cannot be satisfactorily reconciled. The division between the two schools of thought in this matter is due in part to inconsistent methods of statutory interpretation. Those cases following the *Graham* decision (ERISA plans neither excluded nor exempt from the bankruptcy estate) interpret the relevant Code provisions by placing a great deal of emphasis on the intent of Congress as expressed in legislative history.<sup>73</sup> The line of cases following *Threewitt* and *Hinshaw* (ERISA plans are excluded from the bankruptcy estate or, if included, are exempt) follow a stricter approach and look more closely to the language contained in the Code provisions themselves.<sup>74</sup>

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69. *Id.*

70. *Id.* Such language was contained in the restrictions on alienation found in those plans used as examples in the legislative history.

71. See 11 U.S.C. § 522(b); *supra* notes 53-57.

72. This position is further supported by case law holding that exemption statutes are to be liberally construed in favor of the debtor. See *Phelan v. Lacey*, 51 Okla. 393, 394, 151 P. 1070, 1071 (1915) ("[W]here there is a doubt as to whether certain property is exempt . . . , the doubt should be resolved in favor of the exemption."); *Nelson v. Fightmaster*, 4 Okla. 38, 38, 44 P. 213, 213 (1896) ("Exemption laws . . . will be liberally construed; . . . the debtor will generally be allowed the benefit of the doubt . . .").

73. *Graham*, 24 Bankr. at 312. For cases following the *Graham* analysis, see *Goff v. Taylor* (*In re Goff*), 706 F.2d 574, 580-86 (5th Cir. 1983); *In re Strasma*, 26 Bankr. 449, 451 (Bankr. W.D. Wis. 1983); *Avery Fed. Sav. & Loan Ass'n v. Klayer* (*In re Klayer*), 20 Bankr. 270, 272 (Bankr. W.D. Ky. 1981).

74. For cases following the analysis of *Threewitt* and *Hinshaw*, see *Warren v. G.M. Scott & Sons* (*In re Phillips*), 34 Bankr. 543, 544 (Bankr. S.D. Ohio 1983); *In re Pruitt*, 30 Bankr. 330, 331 (Bankr. D. Colo. 1983).

It is possible that a disagreement more basic than statutory interpretation exists concerning fundamental policy considerations which permeate the entire Bankruptcy Code. These considerations involve a choice between conservative and liberal interpretations of exemption statutes which will favor either the debtor or the creditor and cannot help but touch on issues of fairness, equity, and compassion. Every decision allowing the debtor to retain property places a hardship on the creditor. In fact, the creditor funds the debtor's fresh start. Principles of equity require that a balance be reached between these competing values—fairness to the creditor and the public interest in protecting a debtor's recovery.

Oklahoma courts, when faced with these issues, will not be limited to a choice between the two schools of thought which have developed in other jurisdictions. The ambiguity, if any, present in the Code provisions has been greatly clarified by legislative enactment. Furthermore, Oklahoma case law has clearly resolved the relevant policy considerations. With these guides, a uniform treatment of ERISA plans will be possible in Oklahoma.

### III. OKLAHOMA TREATMENT OF RETIREMENT PLANS

In 1953, the Oklahoma legislature passed a series of statutes guaranteeing the validity and enforcement of restrictions on the alienation or encumbrance of any interest in a tax exempt retirement, pension, or profit sharing plan.<sup>75</sup> This guarantee is codified in title 60, sections 326-328 of the Oklahoma Statutes.<sup>76</sup>

Section 326 defines property which may contain effective restrictions on alienation.<sup>77</sup> Under section 326, restrictions will be enforced when contained in any "retirement, pension or profit sharing plan, qualified for tax exemption purposes under present or future Acts of Congress, or any trusts, insurance and annuity contracts constituting a part thereof . . . ."<sup>78</sup> Restrictions on alienation contained in these plans are valid regardless of "any rule or law against restraints on alienation . . . ."<sup>79</sup> The scope of the provisions in these statutes clearly includes a retirement plan qualified for tax exemption under ERISA. Furthermore, the analysis of rules pertaining to spendthrift trusts is not relevant since section

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75. See Act of June 6, 1953, ch. 21a, § 1, 1953 Okla. Sess. Laws, 344, 344.

76. (Supp. 1984).

77. OKLA. STAT. tit. 60, § 326 (Supp. 1984).

78. *Id.*

79. *Id.*

326 acts to supersede *any* rule against restraints on alienation.<sup>80</sup> Section 327 authorizes any plan defined under section 326 to restrict or prohibit alienation or encumbrance of a person's interest and to prevent creditors from affecting garnishment, attachment, or execution against the assets of the plan.<sup>81</sup> Incorporating the provisions of sections 326 and 327, section 328 provides that "[a]ny person having an interest in any such plan . . . containing the provisions set forth . . . shall have no right to alienate or encumber [the] interest . . . and the interest . . . shall be exempt from garnishment, attachment, execution or the claims of creditors."<sup>82</sup>

The balance of this Comment will discuss the impact of this legislation on the issues presented—whether assets held by a debtor in ERISA qualified retirement plans are excluded from the bankruptcy estate, or if not excluded, whether they are exempt under the Bankruptcy Code from creditor process.

### A. *Exclusion From The Bankruptcy Estate*

As previously discussed, section 541(c)(2) provides an exception to the automatic inclusion provision of the Bankruptcy Code.<sup>83</sup> This exception applies to property held in a trust containing a restriction on alienation which is "enforceable under applicable nonbankruptcy law."<sup>84</sup> Since title 60, sections 326-328 of the Oklahoma Statutes is "applicable nonbankruptcy law,"<sup>85</sup> a restriction on alienation which would be enforceable under section 328 would be enforceable in a bankruptcy proceeding.<sup>86</sup> By operation of section 541(c)(2) of the Bankruptcy Code, the result of enforcing section 328 would be the exclusion of assets held in an ERISA plan from the estate in bankruptcy of the debtor.

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80. The *Graham* court held that section 541(c)(2) of the Bankruptcy Code applied to spendthrift trusts and that restrictions on alienation which would be valid under state law applicable to spendthrift trusts would be valid against the trustee in a bankruptcy proceeding. *Graham*, 24 Bankr. at 310-11. Section 326 provides that no tax exempt "retirement, pension or profit sharing plan . . . shall be construed as violating *any* rule against restraints on alienation . . ." OKLA. STAT. tit. 60, § 326 (Supp. 1984) (emphasis added). This language acts to supersede Oklahoma law relating to spendthrift trusts where retirement plans are concerned.

81. OKLA. STAT. tit. 60, § 327 (Supp. 1984).

82. *Id.* § 328.

83. *See supra* notes 20-47 and accompanying text.

84. 11 U.S.C. § 541(c)(2).

85. *Id.*; *see also Goff*, 706 F.2d at 580 (acknowledging that a state's nonbankruptcy law affecting spendthrift trusts may provide an exception to automatic inclusion provisions).

86. "[T]he relevant question is whether [the debtor's] interest in the Plan would be protected from creditors in an ordinary state court action in which nonbankruptcy law would apply. . . . [I]f the . . . provisions are enforceable against general creditors, they are enforceable against the bankruptcy trustee." *Threewitt*, 24 Bankr. at 929.

There are two tests which must be met by a retirement plan in order to qualify for enforcement under section 328. First, the plan must qualify for tax exempt status.<sup>87</sup> Second, the plan must provide against both voluntary and involuntary alienation of any interest in the account.<sup>88</sup> By using the term ERISA qualified plan, the author has assumed that the various requirements for tax exemption under the Internal Revenue Code have been met.<sup>89</sup> The remaining test is whether the restrictions on alienation authorized by section 327 are included in the plan.

Only one reported case in Oklahoma has addressed the adequacy of language contained in restrictions on alienation under section 327. The Supreme Court in *Patee v. Patee (In re Patee)*<sup>90</sup> held that the plan's provision was within the meaning of section 327.<sup>91</sup> While the court did not reprint the exact language, a copy of the plan provided by the bank states:

[N]o benefits or beneficial interests provided for hereunder shall be subject in any manner to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance or charge, either voluntary or involuntary, and any attempt . . . shall be null and void, and neither shall such benefits or beneficial interests be liable for or subject to the debts, contracts, liabilities, engagements or torts of any person to whom such benefits or funds are payable.<sup>92</sup>

In a unanimous opinion, the court held that a plan with a provision "containing the proscriptions authorized by section 327" effectively protects the debtor's interest or any other interest in a tax exempt retirement plan from claims of creditors filed against the decedent debtor's estate in probate proceedings.<sup>93</sup>

The language held to be sufficient under section 327 in *Patee* is similar to language used in other ERISA plans.<sup>94</sup> Therefore, since section

87. See *supra* notes 77-79 and accompanying text.

88. See *supra* note 81 and accompanying text.

89. Qualifications for tax exemption under the Internal Revenue Code are established in I.R.C. §§ 401, 501 (1982). The qualifications are numerous and their analysis would not add to the discussion of the issues in this Comment. Furthermore, some courts have held that the issue of tax exempt status should properly be resolved by the Commissioner of Internal Revenue and that ruling on the matter prior to IRS determination would be inappropriate. See, e.g., *Goff*, 706 F.2d at 580 n.16; *Warren v. G.M. Scott & Sons (In re Phillips)*, 34 Bankr. 543, 544 n.2 (Bankr. S.D. Ohio 1983) (citing *In re Baviello*, 12 Bankr. 412, 416 n.5 (Bankr. E.D.N.Y. 1981)).

90. 664 P.2d 1035 (Okla. 1983).

91. *Id.* at 1036.

92. Central National Bank of Oklahoma City, Oklahoma, Profit Sharing Plan, Article IX, § 9.2 *Spendthrift Trust* (referenced in *Patee*) (reprinted by permission of Central National Bank, Oklahoma City, Oklahoma).

93. *Patee*, 664 P.2d at 1036.

94. Compare *supra* note 92 and accompanying text with Universal Pensions Incorporated, Pension Plan § 12.04 ("A Participant's interest in this Plan may not be assigned or alienated, either

327 prescribes no mandatory language,<sup>95</sup> it is reasonable to conclude that ERISA plans will receive the benefit of section 328 protection against creditors in a nonbankruptcy action in state courts. A restriction on transferability enforceable against creditors in a nonbankruptcy action is enforceable against the bankruptcy trustee.<sup>96</sup>

In Oklahoma, any retirement plan meeting ERISA requirements will be excluded from the bankruptcy estate. This conclusion is reached on the basis of the statutory language contained in both section 541(c)(2) of the Bankruptcy Code and sections 326-328 of title 60 of the Oklahoma Statutes.

### B. *Exemption for Property of the Estate*

Section 522(b)(1) of the Bankruptcy Code allows a debtor to choose between the exemptions found in section 522(d) and exemptions granted in other federal, state, or local law;<sup>97</sup> however, states are given the option of prohibiting this choice by enacting legislation specifically forbidding exemption under section 522(d).<sup>98</sup> Oklahoma, like a number of other states,<sup>99</sup> has opted out of the exemption provisions found in section 522(d), thereby removing the right of its citizens to choose between exemption systems.<sup>100</sup> The opt out provision of the Bankruptcy Code has been upheld against constitutional challenges<sup>101</sup> that such provisions vio-

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voluntarily or involuntarily. This shall not preclude the Trustee from complying with a court order requiring deduction from the benefits of a Participant in pay status for alimony or support payments.") (reprinted by permission of Universal Pensions Incorporated, Brainerd, Minnesota). Universal Pensions provides services to banks and savings and loans in connection with the administration of IRA and Keogh accounts. The spendthrift clause quoted here is a part of one plan available nationally to subscribers.

95. OKLA. STAT. tit. 60, § 328 will enforce restrictions on alienation in retirement plans containing the provisions set forth in section 327 or provisions of substantially the same force and effect.

96. *Threewitt*, 24 Bankr. at 929.

97. 11 U.S.C. § 522(b)(1) (1982) (quoted *supra* note 50).

98. *Id.*

99. See 9 AM. JUR. 2D *Bankruptcy* § 324 (1980 & Supp. 1984) (partial listing of states exercising the option to establish their own exemptions in lieu of section 522(d) as authorized by section 522(b)(1) and examples of the type of legislation the states have enacted). This action is often referred to as "opting out" of the federal exemption provisions.

100. Under 11 U.S.C. § 522(b)(1), a state may specifically prevent a debtor from electing exemptions provided under section 522(d). Oklahoma has prohibited the debtor's selection of exemptions:

No natural person residing in this state may exempt from the property of the estate in any bankruptcy proceeding the property specified in subsection (d) of Section 522 of the Bankruptcy Reform Act of 1978 . . . except as many otherwise be expressly permitted under this title or other statutes of this state.

OKLA. STAT. tit. 31, § 1(B) (Supp. 1984).

101. See *In re Sullivan*, 680 F.2d 1131, 1133 (7th Cir. 1982); *In re Reynolds*, 24 Bankr. 334, 347 (Bankr. S.D. Ohio 1982); *In re Parrish*, 19 Bankr. 331, 334 (Bankr. D. Colo. 1982); *Foster v. City Loan & Sav. Co.* (*In re Foster*), 16 Bankr. 467, 468 (Bankr. N.D. Ohio 1981).

late both the uniformity requirement<sup>102</sup> and the supremacy clause of the United States Constitution.<sup>103</sup> Therefore, in Oklahoma, a debtor may exempt from property of the bankruptcy estate only that property listed in the Oklahoma exemption statute<sup>104</sup> or in other federal<sup>105</sup> and state law.<sup>106</sup>

Although more generous than section 522(d) of the Bankruptcy Code,<sup>107</sup> the Oklahoma exemption provisions contained in title 31 of the Oklahoma Statutes do not contain an exemption for retirement plan assets. This omission, in light of the previous discussion concerning title 60, sections 326-328 of the Oklahoma Statutes, is not surprising. When the Oklahoma exemption statute became effective,<sup>108</sup> retirement plan assets had been protected from creditor process under sections 326-328 for over twenty-five years.<sup>109</sup>

Sections 326-328 are referred to as exemption statutes<sup>110</sup> and only have an exclusionary effect when applied to the provisions of section 541(c)(2) of the Bankruptcy Code. If the two part test for application of section 328 is met (the retirement plan must qualify for tax exempt status and contain restrictions on alienation), the assets of the retirement plan will be protected from the claims of creditors under state law.

Since Oklahoma has exercised the option to substitute the exemptions provided for under section 522(b)(2)(A) for those found under section 522(d),<sup>111</sup> any exemption granted by state law is valid under the

102. The uniformity clause provides that Congress shall have the power "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States . . ." U.S. CONST. art. I, § 8, cl. 4.

103. The provision referred to as the supremacy clause states that "This Constitution, and the Laws of the United States which shall be made in Pursuance thereof . . . shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding." U.S. CONST. art. VI, cl. 2.

104. OKLA. STAT. tit. 31, § 1(A) (Supp. 1984).

105. See, e.g., 42 U.S.C. § 407 (1982) (social security benefits); 45 U.S.C. § 228(L) (Railroad Retirement Act annuities and pensions); 45 U.S.C. § 352(E) (veterans' benefits).

106. See, e.g., OKLA. STAT. tit. 60, §§ 326-328.

107. Compare 11 U.S.C. § 522(d) (1982) (limiting the debtor to \$7,500 equity in his residence, \$1,200 interest in a motor vehicle, and \$750 interest in tools, apparatus, and books of his business or profession) with OKLA. STAT. tit. 31, § 1(A) (Supp. 1984) (allowing the debtor to retain the full value of his principal place of residence, \$1,500 equity in a motor vehicle, and all tools, apparatus, and books used in any trade or professions of the debtor or his dependent).

108. The effective date was October 1, 1981. See Act of Apr. 28, 1981, ch. 118, § 2, 1981 Okla. Sess. Laws 196, 199-200 (codified at OKLA. STAT. tit. 31, § 1 (Supp. 1984)).

109. The statutes exempting retirement plan assets first became effective on June 6, 1953. See Act of June 6, 1953, ch. 21a, §§ 1-3, 1951 Okla. Sess. Laws 344, 344.

110. See 7 COLLIER ON BANKRUPTCY 529-30, 541 (15th ed. 1984).

111. The opt out provision in section 522(b)(1) of the Bankruptcy Code was exercised in OKLA. STAT. tit. 31, § 1(B) (Supp. 1984). See *supra* notes 97-107 and accompanying text.

Bankruptcy Code.<sup>112</sup> Therefore, the exemption provided for ERISA plans under Oklahoma statutes will be enforced in a bankruptcy proceeding involving an Oklahoma debtor.<sup>113</sup>

#### IV. CONCLUSION

Although no uniform treatment exists under federal law on the issue of whether a debtor may retain assets held in ERISA plans, Oklahoma statutes provide a reliable basis for the opinion that such plans are, in Oklahoma, protected from creditor process even in a bankruptcy proceeding. This Comment discussed two theories which support such a conclusion.

First, by applying sections 326-328 to the exception granted in the automatic inclusion provisions of the Bankruptcy Code, ERISA funds may properly be excluded from the bankruptcy estate. Sections 326-328 will act to enforce any restriction on alienation contained in an ERISA plan. Section 541(c)(2) of the Bankruptcy Code states that restrictions enforceable under nonbankruptcy law are enforceable in bankruptcy proceedings. Under this analytical approach, a debtor's interest in an ERISA plan does not become property of the bankruptcy estate and is not, therefore, subject to liquidation in satisfaction of creditors' claims.

The second theory is that sections 326-328 create an exemption under state law which is enforceable under section 522(b)(2)(A) of the Bankruptcy Code. Since states are granted the option of defining the bankruptcy exemptions to be allowed in their own jurisdictions, and since Oklahoma has exercised that option, the exemption granted under sections 326-328 must be considered in determining what property an Oklahoma debtor may exempt from the bankruptcy estate. Section 328 states that any tax exempt retirement plan containing restrictions on the voluntary or involuntary alienation of an interest will be exempt from garnishment, attachment, execution, or the claims of creditors. Therefore, a clear exemption applies in Oklahoma for assets held in ERISA qualified plans. This exemption must be allowed in an Oklahoma bankruptcy proceeding and will be given the force of federal law under the Bankruptcy Code.

The result, under either theory, is that an Oklahoma debtor may

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112. A debtor may exempt from property of the estate "any property that is exempt under Federal law, other than subsection (d) of [section 522], or State or local law that is applicable on the date of filing of the petition . . ." 11 U.S.C. § 522(b)(2)(A) (emphasis added).

113. See *id.*; *supra* notes 75-96 and accompanying text.



retain, subsequent to the filing of a petition in bankruptcy, any interest held in a tax exempt retirement plan which contains restrictions on the voluntary or involuntary alienation of a beneficial interest.

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