Study D-353 June 16, 1995

Memorandum 95-31

Debtor-Creditor Relations: Retirement Account Exemption

At the April 1995 meeting, the Commission discussed Memorandum 95-23 concerning the retirement account exemption issues raised by Bankruptcy Judge Alan M. Ahart. (Judge Ahart's letter was attached to Memorandum 94-25, Exhibit pp. 53-54, considered at the May 1994 meeting.) The Commission requested additional information relating to limits under federal law on contributions to qualified retirement plans. There was also some discussion concerning whether a broader revision of the retirement account exemption might be appropriate, instead of focusing on one-person or closely-held corporations, which is the issue raised by Judge Ahart.

This memorandum provides additional background on the retirement account exemption, discusses related federal law, and considers several approaches to the small corporate plan issue as well as retirement exemptions in general.

Basic statutory material from California, several other states, and federal law is included in the attached Exhibit.

Context of Exemption Discussion

The Commission has enjoyed a lengthy and significant involvement in debtor-creditor law. The claim and delivery statute, Attachment Law, Enforcement of Judgments Law (including exemptions), Wage Garnishment Law, and other related legislation (including the repeal of civil arrest) have been enacted on recommendation of the Commission during the last 25 years. The Commission is charged with reviewing the amount of exemptions in the Enforcement of Judgments Law every 10 years by Code of Civil Procedure Section 703.120. The statute also authorizes the Commission "to maintain a continuing review of and submit recommendations concerning enforcement of judgments."

Much of the law in this area is determined under or influenced by the federal Bankruptcy Code and interpreted in the bankruptcy courts. Section 522(d) of the Bankruptcy Code provides a set of exemptions applicable in bankruptcy throughout the country, unless a state opts out pursuant to Section 522(b)(1) — almost all the states have opted out. California has technically opted out of the federal bankruptcy exemptions (Code Civ. Proc. § 703.130), but the federal exemptions have been enacted into state law in Section 704.140 in nearly identical language. (See Exhibit pp. 1-3, setting out the language of the Commission's current recommendation in SB 832, which conforms the amounts in the state alternative exemption to the recently doubled federal exemptions.) Thus, in a bankruptcy filed in California, the debtor may choose either the state money judgment exemptions in Sections 704.010 *et seq.* or the state restatement of the federal bankruptcy exemptions in Section 703.140. This scheme is beneficial to debtors in bankruptcy, since a debtor without a homestead can benefit from the federal wildcard exemption (see Section 703.140(b)(1), (5)), whereas a debtor with a homestead will use the state money judgment exemptions with as much as a $100,000 homestead exemption (see Section 704.730). This scheme is intended to prevent spouses from getting the benefit of both exemption sets which would happen if one claims the state set and the other claims the federal set. (See Section 703.140(a), in Exhibit pp. 1-2.)

Policy decisions concerning money judgment enforcement proceedings under the state statutes need to consider the interplay of bankruptcy law. The level of an important exemption can be a major factor in deciding whether to petition in bankruptcy and in deciding which set of exemptions to claim. Remember, though, that the alternative bankruptcy exemptions in Section 703.140 are not available to debtors in money judgment enforcement proceedings. In this respect, the statute is one-way. The state money judgment exemptions apply in bankruptcy, but the alternative bankruptcy exemptions in Section 703.140 do not apply in money judgment enforcement proceedings governed by the Enforcement of Judgments Law. Of course, non-bankruptcy federal law provides a number of exemptions applicable to money judgment enforcement as a matter of supremacy, but bankruptcy exemptions apply only in the bankruptcy arena, whether drawn from Section 703.140(b) or Section 704.010 *et seq.* .

The Commission has been consistent in not considering substantive changes in the alternative bankruptcy exemptions. That is, in SB 832, the only revision that the Commission has recommended relating directly to bankruptcy exemptions is to conform Section 703.140 to recent federal legislation. This is intended to preserve the consistency that has existed since 1984 between the alternative bankruptcy exemptions and the federal statute. The staff believes this is the correct approach, but it means that any revisions in exemptions, retirement or otherwise, will occur only in the state money judgment enforcement provisions, not in Section 703.140.

This restraint avoids getting into the details of the federal bankruptcy exemptions and opening up a large barrel of snakes.

Background on California Retirement Exemption

Public employee pensions have been protected for most of this century. (See, e.g., Code Civ. Proc. § 690(20), as added by 1907 Cal. Stat. ch. 479, § 1.) The current statute exempting public pensions from creditor claims is Code of Civil Procedure Section 704.110. (See Exhibit pp. 3-4.) Like its predecessors, Section 704.110 provides a complete exemption from the claims of general creditors, both before and after payment:

> (b) All amounts held, controlled, or in process of distribution by a public entity derived from contributions by the public entity or by an officer or employee of the public entity for public retirement benefit purposes, and all rights and benefits accrued or accruing to any person under a public retirement system, are exempt without making a claim.
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> ….
>
> (d) All amounts received by any person, a resident of the state, as a public retirement benefit or as a return of contributions and interest thereon from the United States or a public entity or from a public retirement system are exempt.

It should be remembered that all pension exemptions are subject to exceptions for child, family, and spousal support enforcement. See Sections 704.110(c), 704.115(c).

Private pensions first received protection under state law starting in 1970, when an exemption applicable only in bankruptcy proceedings was enacted. (See Code Civ. Proc. § 690.18, as added by 1970 Cal. Stat. ch. 1523, § 44.5.) In 1976, the exclusion of Keogh plans from the special bankruptcy exemption was deleted. (1976 Cal. Stat. ch. 948, § 1.) Finally, in 1978, the limitation to bankruptcy proceedings was deleted, so that the exemption applied in money judgment enforcement proceedings (as well as in bankruptcy by operation of federal law). The language of former Section 680.18 pertaining to private retirement plans, developed in the 1970's, persists in the current statute; compare the older language below to Section 704.115 (set out in Exhibit p. 4-5):

> All money held, controlled, or in process of distribution by any private retirement plan, including, but not limited to, union retirement plans, or any profit-sharing plan designed and used for retirement purposes, or the payment of benefits as an annuity, pension, retirement allowance, disability payment or death benefit from such retirement or profit-sharing plans, and all contributions and interest thereon returned to any member of any such

> retirement or profit-sharing plan, whether the same shall be in the actual possession of such pensioner or beneficiary, or deposited by him, are exempt from execution, attachment, or garnishment. Except with regard to moneys withheld from employees' wages and contributions based on wages in employment under provisions of the Unemployment Insurance Code, and except with regard to court-ordered child or spousal support payments, the exemption given by this subdivision shall apply to any moneys held in self-employed retirement plans and individual retirement annuities or accounts provided for in the Internal Revenue Code of 1954 as amended by the federal "Employee Retirement Income Security Act of 1974" (P.L. 93-406, 29 U.S.C. 1001 et seq.) and by the "Tax Reform Act of 1976" (P.L. 94-455), provided that such moneys do not exceed the maximum amounts exempt from federal income taxation under these acts. [Code Civ. Proc. § 690.18(c), as amended by 1978 Cal. Stat. ch. 494, § 1.]

This basic language was in place when the Commission revised and restructured the exemption statutes as part of the Enforcement of Judgments Law recommendation, enacted in 1982. In its original recommendation to the Legislature, the Commission did not propose revision of the substance of this exemption. (See *Tentative Recommendation Proposing the Enforcement of Judgments Law*, 15 Cal. L. Revision Comm'n Reports 2001, 2083-84, 2407-08 (1980).) However, as the staff recalls, there was concern in the Assembly Judiciary Committee that IRA's and Keogh plans could be abused under the then new exemption for such plans, which had existed since 1978. It was felt that the exemption was too generous and that excessively large amounts of money could be insulated from creditors under the rule based on the maximum amount exempt from federal income tax. (The staff does not recall a similar concern being expressed about any of the other pension plans covered by the statute.) As a result, the bill was amended in committee to add the need-based standard to the tax exempt standard in the case of self-employed plans and IRA's. This law has remained essentially unchanged since it became operative in mid-1983.

The statutory language is not clear on the scope of non-self-employed, non-IRA, private retirement plans. Unlike statutes in many other states, there is no tax exemption qualification requirement provided for this type of plan. Unless "plan" has an accepted special meaning, the language on its face does not exclude an arrangement where an individual puts a bit away each month for her golden years. It is not known whether this sort of claim has ever been made. We have a difficult time distinguishing in theory between a sincere effort to plan for one's retirement by saving money and a "non-qualified" plan under federal law. Failure to take advantage of the available tax benefits under federal law does not bear directly on the issue of whether a fund is an appropriate retirement "plan." However, the general approach in statutes of other states and federal law assumes a conceptual relation between tax qualification and retirement plan legitimacy.

In sum, the state money judgment law provides the following exemptions:

Type	Before Payment	After Payment
Public retirement plans (§ 704.110): including pension or annuity, retirement, disability, death, or other benefit, under state, city, county, or other political subdivision, public trust, public corporation, public board (but not United States)	Totally exempt without making a claim	Totally exempt (including benefits and returns of contributions from United States); claimed exemption
Private retirement plans (§ 704.115(a)(1)-(2)): including , but not limited to union retirement plans, and profit-sharing plans designed and used for retirement purposes, annuity, pension, retirement allowance, disability payment, or death benefit (b)	Totally exempt claimed exemption	Totally exempt claimed exemption
Self-employed retirement plans (§ 704.115(c)): including pension or annuity, retirement, disability, death, or other benefit, under state, city, county, or other political subdivision, public trust, public corporation, public board (but not United States)	Exempt to extent necessary to support debtor upon retirement and spouse and dependents of debtor, considering all resources likely to be available claimed exemption	Same standard; if paid periodically, exemption determined under Wage Garnishment Law (about 1/4 subject to creditor claims)

The state alternate bankruptcy exemption, like the federal Bankruptcy Code, provides the following exemption available only in bankruptcy:

Right to receive payment under stock bonus, pension, profit-sharing, annuity, or similar plan or contract on account of illness, disability, death, age, or length of service (except for non-IRC qualified plans of insiders based on age or length of service): § 703.140(b)(10)(E))	Exempt to extent reasonably necessary for support of debtor and dependents	

Additional Bankruptcy Considerations

In bankruptcy, "ERISA-qualified" pension plans are not included in the bankruptcy estate. Patterson v. Shumate, 504 U.S. ____, 112 S. Ct. 2242 (1992). This means that the question of exemption of a qualified plan does not even arise in bankruptcy, if the case is handled properly, because the property is not part of the estate that is available to discharge claims. This principle is an application of a provision of Section 541 of the Bankruptcy Code that excludes from the bankrupt's estate any property that is subject to a restriction on transfer (an “anti-alienation” clause in ERISA terms) enforceable under “applicable nonbankruptcy law.” The Supreme Court determined in *Patterson v. Shumate* that the anti-alienation provision required by ERISA in qualified plans meets the terms of Section 541.

Note that in California this rule would apply to exclude such plans from the bankruptcy estate regardless of whether the debtor elects to claim the money judgment exemptions or the alternate bankruptcy exemptions. This means that under current law, the necessary-for-support standard applicable to retirement plans under Code of Civil Procedure Section 703.140(b)(10)(E) (like that under Bankruptcy Code Section 522(d)(10)(E)) is inapplicable to ERISA-qualified plans since they are not part of the bankruptcy estate. The necessity standard would apply to retirement plans that do not or need not qualify under ERISA, such as governmental plans and church plans, assuming they do not contain anti-alienation provisions enforceable under “applicable nonbankruptcy law,” and individual retirement accounts.

As a result of these rules, there is a perhaps surprising degree of consistency between the state money judgment exemptions and the alternate bankruptcy exemptions as applied to private retirement plans in a bankruptcy case: ERISA-qualified retirement plans are completely exempt under both schemes, and non-ERISA-qualified private plans and accounts are subject to a necessity standard. (The staff is not clear on the treatment of government plans under *Patterson*, but if they have effective anti-alienation provisions, they would seem to be excluded from bankruptcy and are completely exempt under state money judgment exemptions.)

Federal Retirement Law: Qualified Plans, Contribution Limitations, etc.

At the March meeting, the Commission requested additional information on the applicable federal law governing plan alternatives and limits and how that may relate to exemptions in state money judgment proceedings and bankruptcy. As noted at that meeting, this law is extremely complex and constantly subject to change. There have been at least 10 substantial revisions of ERISA and applicable Internal Revenue Code since 1982. This law defies easy summarization and the staff suspects that it could take years of intensive study to gain a minimal competence in this area. Be that as it may, we have tried to assemble some basic ideas in response to the Commission’s direction.

Most of the discussion of private retirement plans in the materials the staff has examined focuses on “qualified” plans. The terms used may vary; reference is made to IRC- or tax-qualified plans or to ERISA-qualified plans, with apparently the same intent. Some plans are, in a sense, automatically qualified since they are tax-exempt, such as church plans, but “qualified” seems reserved for plans that go through a process of becoming qualified through an IRS determination letter. See, e.g., Markun & Uzes, *Qualifying the Plan and Trust,* in Attorney’s Guide to Pension and Profit-Sharing Plan § 5.1 *et seq.* (Cal. Cont. Ed. Bar, 3d ed. 1994). Conceptually, it seems possible for a plan to satisfy all of the ERISA requirements but not be tax exempt because the IRS hoops have not been jumped through. But practically speaking, reasonable people will not attempt to set up a plan without pursuing the goal of tax exemption. It should be kept in mind, however, that a plan is not qualified until the IRS says it is (and may lose qualified status retroactively), so that using the words “qualified plan” in a statute may raise technical issues — this will be considered later.

There are a number of types of plans and accounts that qualify under ERISA and the IRC. A host of highly technical rules apply to these plans, including provisions on vesting, contribution limitations, distribution limitations, etc. Qualified plans fall into two main classes:

Defined contribution plan; including cash or deferred arrangements (CODA) (IRC § 401(k)). A defined contribution plan, as the name suggests, sets the level of contributions to the plan, and benefits are determined solely on the basis of the contributions to an employee’s individual account in the plan. See IRC § 414(i).) Employer contributions are limited to a base amount of $30,000, subject to complicated adjustment rules; employee elective deferrals are limited to an amount currently over $9200. (See IRC § 415(c), in Exhibit pp. 12-13.)

Defined benefit pension plan. Employer contributions are limited to an amount necessary to fund an annual benefit of up to $90,000 (plus cost-of-living adjustments), (and subject to other limitations), at a level determined in the plan. (See IRC § 415(b)(1), in Exhibit pp. 12-13.). For the purpose of applying Internal Revenue Code Sections 401-448 (Part 1), all plans that are not defined contribution plans are considered as defined benefit plans. See IRC § 414(j).

In addition, there are simplified employee pension plans (SEP, a form of IRA for employees under IRC § 408(k)), profit-sharing plans, money purchase pension plans, and others. There is specific recognition of nonqualified plans — 29 U.S.C. Section 1002 (ERISA) provides:

> (36) The term "excess benefit plan" means a plan maintained by an employer solely for the purpose of providing benefits for certain employees in excess of the limitations on contributions and benefits imposed by section 415 of Title 26 on plans to which that section applies, without regard to whether the plan is funded. To the extent that a separable part of a plan (as determined by the Secretary of Labor) maintained by an employer is maintained for such purpose, that part shall be treated as a separate plan which is an excess benefit plan.

And, of course, there is a specific rule for a "qualified football coaches plan". See 29 U.S.C. § 1002(37)(F)(i).

For self-employed and non-employed persons, we most frequently encounter Keogh (HR 10) plans and individual retirement accounts (IRA's).

Keogh plans. Contributions are limited under IRC Section 401(c)-(d) based on the earned income of the trade or business of the self-employed person and on general limitations applicable to most plans.

IRA's. Contributions under IRC Section 408(a) (individual retirement accounts) and 408(b) (individual retirement annuities) are limited to $2,000, but rollovers from other plans can greatly increase what would otherwise be permissible as an initial contribution to an IRA. See, e.g., IRC § 408(d).

Loans

It appears that the controls on borrowing from a corporate plan, as in the case of a professional corporation, have been tightened at least since the 1986 Tax Reform Act. Borrowing by a self-employed person from a retirement plans is a prohibited transaction. (See IRC § 4975(d), in Exhibit pp. 13-16.) Significant restrictions have been placed on the ability of shareholder-employees, key employees, and participants under corporate retirement plans. IRC §§ 72(p), 4975(d). See Reed, *The Decision Whether or Not To Incorporate*, in Attorney's Guide to California Professional Corporations § 1.6 (Cal. Cont. Ed. Bar, 4th ed. 1994). A loan is treated as a taxable distribution if it exceeds certain limits; without delving into the intricacies, it appears that as an outer limit there is a $50,000 cap on outstanding loans before they are treated as distributions. (See IRC § 72(p)(2), in Exhibit p. 11.)

Policy of Retirement Exemption

The policy of protecting retirement funds is well-established. The exemption is obviously intended to encourage people to save so that they can support themselves and their dependents, particularly in old age. The exemption protects the reliance interest of those who participate in a plan. As noted earlier, the law is not entirely consistent in implementing this general policy, since savings outside of a "plan" are not protected in money judgment enforcement proceedings. But earnings, a certain level of life insurance, social security, and many specific retirement benefits and plans are exempt in furtherance of the general policy of protecting the ability of debtors to continue to be self-supporting. Put another way, the state has an interest in keeping productive citizens off welfare rolls should they fall on hard times.

In implementing the policy of protecting what individuals need for their support and the support of their dependents, the law could adopt a procedure in which a court would have to decide what is necessary in each case, with no categorical exemptions for types of retirement plans. This would not be an efficient approach, particularly in a non-bankruptcy setting where all the assets of the debtor are not before the court. Consequently, the law has traditionally looked for sensible categorical exemptions or percentage figures, as in wage garnishment, as a means of accomplishing general justice with a minimum of administrative burden. The staff assumes that the Commission does not to reexamine these fundamental ideas, but rather consider more limited revisions to make minor adjustments in the retirement exemption scheme.

Possible Revision — Restricting General Language in Section 704.115

The prior memorandum presented only the issue of whether and how to control small corporations where the plan beneficiaries have dominion over the plan, leading to potential abuse. While the applicable federal law has been tightened up in recent years, this is not a complete answer to the problem raised by Judge Ahart. This conclusion follows from two factors: First, it is still possible for one- or two-person professional corporations, for example, to insulate relatively large amounts of money from the reach of creditors, and they can create an operating loss in doing so. Second, remember that the California statute is not necessarily restricted to tax-qualified plans — it provides an exemption for "private retirement plans" — leaving open the argument that a plan that does not satisfy federal rules may still be entitled to the exemption, and not just the necessity exemption. The staff does not believe this was the intent of the statutory language, but it is open to that interpretation.

In re Bloom, 839 F.2d 1376 (9th Cir. 1988), — one of the cases cited by Judge Ahart — is illustrative. The court does not engage in any discussion of whether Dr. Bloom's plan (she was 50% owner of the medical corporation plan) was qualified under the Internal Revenue Code. The court notes that it is not addressing the income tax status of the plan, and ERISA qualification is not considered. Whatever its status, Dr. Bloom had accumulated $475,000 in her plan between 1977 and 1985, and had borrowed $300,000 from it between 1978 and 1982 on unsecured notes. The court found that the plan was “designed and used for retirement purposes” even if not prudently managed, since Dr. Bloom had followed the plan procedures in getting the loans, made regular interest payments at a reasonable rate, and did not try to hide other assets in the plan immediately before bankruptcy. The law has changed in many ways, and become more restrictive, since 1985 (in particular in the 1986 Tax Reform Act). Dr. Bloom would not be able to operate in this same fashion today and be in compliance with the tax statutes. But consider whether loss of a tax exemption and the imposition of penalties is of great concern to a debtor who is bankrupt.

The general language in Code of Civil Procedure Section 704.115(a) can be applied free of any qualification requirements under the Internal Revenue Code or ERISA. Should the language be clarified or tightened up? Or can we conclude that the *Bloom* result is an aberration that would be far less likely to occur today or that the amounts involved under current law would not be large enough to offend the policy of the retirement exemption?

It may be a tricky proposition to limit the general language without either making the exemption overly rigid and restrictive or requiring resolution of difficult issues. The first revision that comes to mind is to limit the “private retirement plan” language to plans that satisfy tax exemption standards or to plans that are “qualified.” But a plan may not have been qualified or may have lost its tax exemption for reasons unrelated to the policy of the exemption statutes. “Qualification” of a plan involves many issues, including nondiscrimination, coverage, participation, vesting, contributions and benefits limitations, anti-top-heaviness, and reporting and disclosure. While many of these issues are not important in a one- or two-person professional corporation, they can be relevant in determining “qualification” of a plan of a small, closely-held corporation.

If the exemption determination depends on a finding that the plan is actually qualified at the time the exemption claim is made, it could be difficult to determine. A professional actuary may have to be called in some plans.

A statute could grant the exemption “to the extent” that the plan is tax exempt, which would avoid the possibility of an all or nothing procedure. But the issue of determining complicated qualification issues could still arise in exemption proceedings.

Additional fine-tuning could be legislated to minimize the risk of burdensome procedures. A plan that has been qualified could be presumed to remain qualified unless the creditor proves otherwise, putting the burden on the creditor to attack a nominally qualified plan.

Several states use language like that in Section 522 of the Bankruptcy Code, referring to qualified plans under IRC Sections 401(a) (private plans in general), 403 (annuities), and 408 (IRA's). (See, e.g., the sampling of several state statutes, Exhibit pp. 5-11.) Note, however, that the Bankruptcy Code reference appears in a prong of an exception to the exemption. (See the parallel language in Section 703.140(b)(10)(E), in Exhibit pp. 2-3.) In other words, the Bankruptcy Code protects retirement and similar plans to the extent necessary for support, unless the plan is an insider plan based on age or length of service that does not qualify under the referenced IRC sections. (Remember that under *Patterson v. Shumate*, ERISA-qualified plans, and perhaps others with anti-alienation provisions, are excluded from bankruptcy estates before the question of exemptions arises.)

Section 6(a)(5) of the Uniform Exemptions Act (1979) exempts to the extent reasonably necessary for support of the debtor and dependents "assets held, payments made, and amounts payable under a stock bonus, pension, profit-sharing, annuity, or similar plan or contract, providing benefits by reason of age, illness, disability, or length of service." This language was drawn from the Bankruptcy Code, but does not have the exception noted above for insiders. The uniform act formulation is not directly tied to federal plan qualification law, although the comment discusses that law. The benefit of this type of language is that it sets up a standard for determining whether a plan is a retirement plan, independent of issues of qualification.

The staff suggests consideration of making a technical revision in Section 704.115 to flesh out the references in subdivisions (a)(1) ("Private retirement plans, including, but not limited to, union retirement plans.") and (a)(2) ("Profit-sharing plans designed and used for retirement purposes.") and conform the language to the more commonly used terms in the Bankruptcy Code and the Uniform Exemptions Act.

Possible Revision — Restricting Plans Where Beneficiaries Have Dominion

Now that the Commission has had a chance to consider more background on the retirement exemption, it is appropriate to reconsider Judge Ahart's recommendation to restrict the options available to small corporate plan beneficiaries who have dominion over plan operation. (The issue was presented in more detail in Memorandum 95-25, but is summarized here for convenience.)

Judge Ahart would apply the necessity standard to one-person corporation retirement plans. This would not be a complete solution to the problem, as noted earlier, because any small corporation where the beneficiary has dominion can involve the same problem. In *In re* Cheng, 943 F.2d 1114 (9th Cir. 1991), the Ninth Circuit stated:

> Although the legislative history indicates that the policy behind section 704.115(e) is to limit the exemption for plans that are controlled by one person, the statute says what it says, and it was improper for the bankruptcy court to read beyond it. If the California legislature intended to treat closely held corporations differently than large corporations, it could have done so explicitly.
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> The bankruptcy court's observations have immense practical significance, and probably constitute a *better* approach than the California statute. We recognize the odd result the statute creates — one-person medical corporations are treated the same as General Motors, creating the opportunity for shareholders of tiny corporations to abuse the exemption scheme — but we may not disregard the statute's language to address problems left to the legislature.
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> We also fear that the bankruptcy court's approach creates an unnecessary ambiguity in the plain language of the statute.… If corporations with one shareholder are not really corporations, how about corporations with two shareholders? Or three? Or four? When would a closely held corporation become a "real" corporation for the purpose of California exemption law? We are not willing to open the floodgate for this sort of litigation.…

There are a number of possible approaches:

Apply necessity standard to all private plans. Section 704.115 could be amended to apply the necessity standard to all funds described in the section. This would treat private retirement plans, including, but not limited to, union retirement plans (subdivision (a)) and profit-sharing plans designed and used for retirement purposes (subdivision (b)) the same as self-employed retirement plans and IRA's (subdivision (c)). This would be a dramatic change in the law, and would broaden the disparity between the state money judgment exemption and the alternative federal bankruptcy exemption. Presumably it would encounter significant opposition, as it invades what is now absolutely protected. It would also entail greater administrative costs, since a court would be required to determine the amount "necessary to provide for the support of the judgment debtor when the judgment debtor retires and for the support of the spouse and dependents of the judgment debtor, taking into account all resources that are likely to be available for the support of the judgment debtor when the judgment debtor retires."

Degree of control. The bankruptcy judge in *Cheng* noted that the debtor, a doctor, was "the sole shareholder, president, and controlling executive officer of Cheng, M.D., Inc., and also served as the plan's trustee." Some states have adopted exemption statutes that turn on the degree of control of the debtor over the fund. Connecticut finds dominion if the debtor is self-employed, is a partner, or is a shareholder with 1% or more interest, or if the court finds that dominion is exercised — this standard mixes relatively easy standards with the fallback court determination. (See Exhibit pp. 5-6.) Wisconsin defines an "owner-dominated plan" as one "under which 90% or more of the present value of the accrued benefits or 90% or more of the aggregate of the account is for the benefit of one or more individuals who are owner-employees" and an "owner-employee" is "any individual who owns, directly or indirectly, the entire interest in an unincorporated trade or business, or 50% or more of the combined voting of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation, or 50% or more of the capital interest or profits interest of a partnership or limited liability company." (See Exhibit p. 10.) Attempting a statutory definition of dominion can be complicated and may be difficult to apply, especially in non-bankruptcy situations.

The staff believes that fashioning an appropriate dominion standard would be the best starting place for revising Section 704.115 to deal with Judge Ahart's suggestion.

Anti-shuffling. As a general rule, a debtor may convert non-exempt assets into exempt assets of equivalent value despite the fact that this may have the effect of defeating creditors. This is true in state collections as well as bankruptcy proceedings (although the standards are different in bankruptcy). A true retirement plan should not be too manipulable in this regard, and the court's have indicated in the bankruptcy context an unwillingness to exempt a "retirement plan" where the debtor has borrowed the plan dry and then tries to pay back the loan with whatever can be scraped together on the eve of bankruptcy. The potential problem can be treated statutorily by precluding the exemption as to certain transfers made to debtor-controlled funds within a minimum period before the creditor's claim arose. Thus, in the case of a debtor with dominion over the fund, Connecticut denies the exemption for transfers occurring less than 90 days before the filing of creditor claims. (See Exhibit pp. 5-6.) Kentucky provides a 120-day exclusion rule. (See Exhibit p. 7.) It appears that Hawaii may apply a three-year rule. This type of provision would help solve the most obvious abuse of the exemption statute, where certain debtors are permitted to exempt large amounts of previously non-exempt funds.

The staff believes a statutory anti-shuffling rule applicable to certain retirement fund contributions is worth consideration. Such a rule can be combined with dominion considerations, as in Connecticut and Kentucky. Other combinations are possible. The anti-shuffling rule could be applied only to contributions over a certain amount or percentage of the fund, or could be applied only to irregular contributions as opposed to regular, periodic contributions.

Fund value limitations. Several states set a flat amount exemption of pension accounts (such as $100,000), perhaps with an additional necessity exemption for amounts over $100,000. This approach resembles the homestead exemption which sets flat amounts for certain classes of debtors based on presumed need. Some states determine the exempt dollar value through application of statutory actuarial tables or principles. The staff does not recommend this approach. A flat amount has no particular relation to the debtor's age, obligations, other assets, employment prospects, or other factors, and is an arbitrarily selected figure. A flat amount exemption is easier to administer, however, since no hearing is required if the fund is valued below the amount set. Actuarial tables or principles are a mix of arbitrarily selected standards and complexity, but even then may omit crucial factors such as the length of the contribution period. Overly specific exemptions stating expected rates of return and dollar amounts are also undesirable in that they require frequent legislative attention to keep pace with inflation and other economic conditions.

Respectfully submitted,

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Study D-353
Memo 95-31

June 14, 1995

Exhibit

STATUTORY MATERIAL

CONTENTS

California

Code Civ. Proc. § 703.140 (as proposed to be amended in SB 832). Election of exemptions if bankruptcy petition is filed

703.140. (a) In a case under Title 11 of the United States Code, all of the exemptions provided by this chapter including the homestead exemption, other than the provisions of subdivision (b) are applicable regardless of whether there is a money judgment against the debtor or whether a money judgment is being enforced by execution sale or any other procedure, but the exemptions provided by subdivision (b) may be elected in lieu of all other exemptions provided by this chapter, as follows:

(1) If a husband and wife are joined in the petition, they jointly may elect to utilize the applicable exemption provisions of this chapter other than the provisions of subdivision (b), or to utilize the applicable exemptions set forth in subdivision (b), but not both.

(2) If the petition is filed individually, and not jointly, for a husband or a wife, the exemptions provided by this chapter other than the provisions of subdivision (b) are

applicable, except that, if both the husband and the wife effectively waive in writing the right to claim, during the period the case commenced by filing the petition is pending, the exemptions provided by the applicable exemption provisions of this chapter, other than subdivision (b), in any case commenced by filing a petition for either of them under Title 11 of the United States Code, then they may elect to instead utilize the applicable exemptions set forth in subdivision (b).

(3) If the petition is filed for an unmarried person, that person may elect to utilize the applicable exemption provisions of this chapter other than subdivision (b), or to utilize the applicable exemptions set forth in subdivision (b), but not both.

(b) The following exemptions may be elected as provided in subdivision (a):

(1) The debtor's aggregate interest, not to exceed ~~seven thousand five hundred dollars ($7,500)~~ *fifteen thousand dollars ($15,000)* in value, in real property or personal property that the debtor or a dependent of the debtor uses as a residence, in a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence, or in a burial plot for the debtor or a dependent of the debtor.

(2) The debtor's interest, not to exceed ~~one thousand two hundred dollars ($1,200)~~ *two thousand four hundred dollars ($2,400)* in value, in one motor vehicle.

(3) The debtor's interest, not to exceed ~~two hundred dollars ($200)~~ *four hundred dollars ($400)* in value in any particular item, in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, or musical instruments, that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

(4) The debtor's aggregate interest, not to exceed ~~five hundred dollars ($500)~~ *one thousand dollars ($1,000)* in value, in jewelry held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

(5) The debtor's aggregate interest, not to exceed in value ~~four hundred dollars ($400)~~ *eight hundred dollars ($800)* plus any unused amount of the exemption provided under paragraph (1), in any property.

(6) The debtor's aggregate interest, not to exceed ~~seven hundred fifty dollars ($750)~~ *one thousand five hundred dollars ($1,500)* in value, in any implements, professional books, or tools of the trade of the debtor or the trade of a dependent of the debtor.

(7) Any unmatured life insurance contract owned by the debtor, other than a credit life insurance contract.

(8) The debtor's aggregate interest, not to exceed in value ~~four thousand dollars ($4,000)~~ *eight thousand dollars ($8,000)* in any accrued dividend or interest under, or loan value of, any unmatured life insurance contract owned by the debtor under which the insured is the debtor or an individual of whom the debtor is a dependent.

(9) Professionally prescribed health aids for the debtor or a dependent of the debtor.

(10) The debtor's right to receive any of the following:

(A) A social security benefit, unemployment compensation, or a local public assistance benefit.

(B) A veterans' benefit.

(C) A disability, illness, or unemployment benefit.

(D) Alimony, support, or separate maintenance, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

(E) A payment under a stock bonus, pension, profitsharing, 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 all of the following apply:

(i) That 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 the plan or contract arose.

(ii) The payment is on account of age or length of service.

(iii) That plan or contract does not qualify under Section 401(a), 403(a), 403(b), *or* 408~~,~~ ~~or 409~~ of the Internal Revenue Code of ~~1954~~ *1986*.

(11) The debtor's right to receive, or property that is traceable to, any of the following:

(A) An award under a crime victim's reparation law.

(B) A payment on account of the wrongful death of an individual of whom the debtor was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

(C) A payment under a life insurance contract that insured the life of an individual of whom the debtor was a dependent on the date of such individual's death, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

(D) A payment, not to exceed ~~seven thousand five hundred dollars ($7,500)~~ *fifteen thousand dollars ($15,000)*, on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent.

(E) A payment in compensation of loss of future earnings of the debtor or an individual of whom the debtor is or was a dependent, to the extent reasonably necessary for the support of the debtor and any dependent of the debtor.

Comment. Section 703.140 is amended to conform to the amounts in the federal Bankruptcy Code and to correct references to sections in the Internal Revenue Code. See 11 U.S.C. § 522. [This section shows amendments in SB 832, currently in the Assembly.]

Code Civ. Proc. § 704.110. Public retirement and related benefits and contributions

704.110. (a) As used in this section:

(1) "Public entity" means the state, or a city, city and county, county, or other political subdivision of the state, or a public trust, public corporation, or public board, or the governing body of any of them, but does not include the United States except where expressly so provided.

(2) "Public retirement benefit" means a pension or an annuity, or a retirement, disability, death, or other benefit, paid or payable by a public retirement system.

(3) "Public retirement system" means a system established pursuant to statute by a public entity for retirement, annuity, or pension purposes or payment of disability or death benefits.

(b) All amounts held, controlled, or in process of distribution by a public entity derived from contributions by the public entity or by an officer or employee of the public entity for public retirement benefit purposes, and all rights and benefits accrued or accruing to any person under a public retirement system, are exempt without making a claim.

(c) Notwithstanding subdivision (b), where an amount described in subdivision (b) becomes payable to a person and is sought to be applied to the satisfaction of a judgment for child, family, or spousal support against that person:

(1) Except as provided in paragraph (2), the amount is exempt only to the extent that the court determines under subdivision (c) of Section 703.070.

(2) If the amount sought to be applied to the satisfaction of the judgment is payable periodically, the amount payable is subject to an earnings assignment order for support as defined in Section 706.011 or any other applicable enforcement procedure, but the amount to be withheld pursuant to the assignment order or other procedure shall not exceed the amount permitted to be withheld on an earnings withholding order for support

under Section 706.052. The paying entity may deduct from each payment made pursuant to an earnings assignment order under this paragraph an amount reflecting the actual cost of administration caused by the assignment order up to two dollars ($2) for each payment.

(d) All amounts received by any person, a resident of the state, as a public retirement benefit or as a return of contributions and interest thereon from the United States or a public entity or from a public retirement system are exempt.

Comment (1982). Section 704.110 continues the substance of subdivisions (a) and (b) of former Section 690.18, with drafting changes for purposes of clarity and uniformity. Subdivision (c) governs the application of the exemption for payable but unpaid benefits against the enforcement of child or spousal support judgments. Subdivision (c)(1) applies the general rule governing exemptions in support cases. Subdivision (c)(2) incorporates the standard applicable to wage garnishments to enforce support judgments. See Section 706.052 and the Comment thereto. See also Civil Code § § 4701 (wage assignment for child support), 4801.6 (wage assignment for spousal support). The one dollar fee for administrative costs provided by former Section 690.18(b) is increased to two dollars in subdivision (c)(2) of this section. The two dollar fee is the same as that formerly provided in Government Code Section 21201 (public employees' retirement).

The exemption provided in subdivision (d) applies whether the benefits are in the actual possession of the retirement benefit recipient or have been deposited. See Section 703.080 (tracing exempt funds). The general rule governing exemptions in support cases provided by Section 703.070 applies to benefits after they have been paid. For the exemption of vacation credits, see Section 704.113. For the exemption of benefits under the Unemployment Insurance Code, see Section 704.120.

Comment (1992). Section 704.110 is amended to conform to the terminology of the Family Code. See Chapter 8 (commencing with Section 5200) of Part 5 of Division 9 of the Family Code (earnings assignment order for support). A reference to "family" support has been added to subdivision (c). See Fam. Code § 4501 (family support order enforceable in same manner and to same extent as child support order). See also Section 680.145 ("child support" includes family support).

Code Civ. Proc. § 704.115. Private retirement and related benefits and contributions

704.115. (a) As used in this section, "private retirement plan" means:

(1) Private retirement plans, including, but not limited to, union retirement plans.

(2) Profit-sharing plans designed and used for retirement purposes.

(3) Self-employed retirement plans and individual retirement annuities or accounts provided for in the Internal Revenue Code of 1954 as amended, to the extent the amounts held in the plans, annuities, or accounts do not exceed the maximum amounts exempt from federal income taxation under that code.

(b) All amounts held, controlled, or in process of distribution by a private retirement plan, for the payment of benefits as an annuity, pension, retirement allowance, disability payment, or death benefit from a private retirement plan are exempt.

(c) Notwithstanding subdivision (b), where an amount described in subdivision (b) becomes payable to a person and is sought to be applied to the satisfaction of a judgment for child , family, or spousal support against that person:

(1) Except as provided in paragraph (2), the amount is exempt only to the extent that the court determines under subdivision (c) of Section 703.070.

(2) If the amount sought to be applied to the satisfaction of the judgment is payable periodically, the amount payable is subject to an earnings assignment order for support as defined in Section 706.011 or any other applicable enforcement procedure, but the amount to be withheld pursuant to the assignment order or other procedure shall not

exceed the amount permitted to be withheld on an earnings withholding order for support under Section 706.052.

(d) After payment, the amounts described in subdivision (b) and all contributions and interest thereon returned to any member of a private retirement plan are exempt.

(e) Notwithstanding subdivisions (b) and (d), except as provided in subdivision (f), the amounts described in paragraph (3) of subdivision (a) are exempt only to the extent necessary to provide for the support of the judgment debtor when the judgment debtor retires and for the support of the spouse and dependents of the judgment debtor, taking into account all resources that are likely to be available for the support of the judgment debtor when the judgment debtor retires. In determining the amount to be exempt under this subdivision, the court shall allow the judgment debtor such additional amount as is necessary to pay any federal and state income taxes payable as a result of the applying of an amount described in paragraph (3) of subdivision (a) to the satisfaction of the money judgment.

(f) Where the amounts described in paragraph (3) of subdivision (a) are payable periodically, the amount of such periodic payment that may be applied to the satisfaction of a money judgment is the amount that may be withheld from a like amount of earnings under Chapter 5 (commencing with Section 706.010) (Wage Garnishment Law).

Comment (1982). Section 704.115 supersedes subdivision (d) of former Section 690.18. Subdivision (c) governs the application of the exemption for payable but unpaid benefits against enforcement of child or spousal support. Subdivision (c)(1) applies the general rule governing exemptions in support cases. Subdivision (c)(2) recognizes that federal law requires the protection of periodic payments pursuant to a pension or retirement program to the same extent as wages. See Section 706.052 and the Comment thereto. The exemption provided in subdivision (d) applies whether money received by the judgment debtor is in the actual possession of the recipient or has been deposited. See Section 703.080 (tracing exempt funds). The general rule governing exemptions in support cases provided by Section 703.070 applies to benefits after they have been paid.

Subdivisions (e) and (f) are new. Subdivision (e) requires that the court consider all resources — such as social security payments and other income and assets — that are likely to be available to the judgment debtor when the judgment debtor retires. Accordingly, where it will be a number of years before the judgment debtor will retire, the court will take into account not only all the assets of the judgment debtor at the time the exemption claim is determined but also all the assets and income (including pension rights) that the judgment debtor is likely to acquire prior to retirement. Subdivision (f) recognizes that the federal law requires the protection of periodic payments pursuant to a retirement program. See 15 U.S.C. § § 1672(a), 1673(a).

Comment (1992). Subdivision (c) of Section 704.115 is amended to conform to the terminology of the Family Code. See Chapter 8 (commencing with Section 5200) of Part 5 of Division 9 of the Family Code (earnings assignment order for support). A reference to "family" support has been added to subdivision (c). See Fam. Code § 4501 (family support order enforceable in same manner and to same extent as child support order). See also Section 680.145 ("child support" includes family support).

Other States

Connecticut

Conn. Gen. Stat. § 52-321a (1992):

(a) Except as provided in subsection (b) of this section, any interest in or amounts payable to a participant or beneficiary from (1) any trust, custodial account, annuity or insurance contract established as part of a Keogh plan or a retirement plan established by a corporation which is qualified under Section 401, 403, 404 or 409 of the Internal Revenue Code of 1986, or any subsequent corresponding internal revenue code of the United States, as from time to time amended, (2) any individual retirement account which is qualified under Section 408 of said internal revenue code to the extent funded, including income and appreciation, (A) as a rollover from a qualified retirement plan, as provided in subdivision (1) of this section, pursuant to Section 402(a)(5), 403(a) or 408(d)(3) of said internal revenue code or (B) by annual contributions which do not exceed the maximum annual limits set forth in Section 219(b) of said internal revenue code, determined without regard to any reduction or limitation for active participants required by Section 219(g) of said internal revenue code or (3) any pension plan, annuity or insurance contract or similar arrangement not described in subdivision (1) or (2) of this subsection, established by federal or state statute for federal, state or municipal employees for the primary purpose of providing benefits upon retirement by reason of age, health or length of service, shall be exempt from the claims of all creditors of such participant or beneficiary. Any such trust, account, contract, plan or other arrangement shall be (A) conclusively presumed to be a restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under the laws of this state and (B) considered a trust which has been created by or which has proceeded from a person other than such participant or beneficiary, even if such participant or beneficiary is a self-employed individual, a partner of the entity sponsoring the Keogh plan or a shareholder of the corporation sponsoring the retirement plan.

(b) Nothing in this section shall impair the rights of an alternate payee under a qualified domestic relations order, as defined in Section 414(p) of the Internal Revenue Code of 1986, or any subsequent corresponding internal revenue code of the United States, as from time to time amended.

(c) Nothing in this section shall affect the status of additions or contributions to a trust, account, contract, plan or other arrangement described in subsection (a) of this section if (1)(A) the debtor-participant or the debtor-beneficiary is a self-employed individual, partner of the entity sponsoring the Keogh plan or a one per cent or more shareholder of the corporation sponsoring the retirement plan, or in the opinion of a court of competent jurisdiction, exercises dominion and control over such proprietorship, partnership, corporation or other entity and (B) the addition or contribution is made less than ninety days before the filing of the claim on which the judgment is thereafter entered or (2) such additions or contributions are determined to be a fraudulent conveyance under applicable federal or state law.

Georgia

O.C.G.A. § 18-4-22 (1994):

(a) Funds or benefits from a pension or retirement program as defined in 29 U.S.C. Section 1002(2)(A) or funds or benefits from an individual retirement account as defined in Section 408 of the United States Internal Revenue Code of 1986, as amended, shall be exempt from the process of garnishment until paid or otherwise transferred to a member of such program or beneficiary thereof. Such funds or benefits, when paid or otherwise transferred to the member or beneficiary, shall be exempt from the process of garnishment only to the extent provided in Code Section 18-4-20 for other disposable earnings, unless a greater exemption is otherwise provided by law.

(b) The exemption provided by this Code section shall not apply when the garnishment is based upon a judgment for alimony or for child support, in which event such funds or benefits shall then be subject to the process of garnishment to the extent provided in subsection (f) of Code Section 18-4-20.

Staff Note. The reference to 29 U.S.C. § 1002(2)(A) incorporates the following:

(2)(A) Except as provided in subparagraph (B), the terms "employee pension benefit plan" and "pension plan" mean any plan, fund, or program which was heretofore or is hereafter established or maintained by an employer or by an employee organization, or by both, to the extent that by its express terms or as a result of surrounding circumstances such plan, fund, or program—

(i) provides retirement income to employees, or

(ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond,

regardless of the method of calculating the contributions made to the plan, the method of calculating the benefits under the plan or the method of distributing benefits from the plan.

Kentucky

KRS Ann. § 427.150 (Baldwin):

…. (2) An individual shall be entitled to exemption of the following property:

…. (f) The right or interest of a person in an individual retirement account or annuity, deferred compensation account, tax sheltered annuity, simplified employee pension, pension, profit-sharing, stock bonus, or other retirement plan described in the Internal Revenue Code of 1986, as amended which qualifies for the deferral of income tax until the date benefits are distributed. This exemption shall also apply to the operation of the Federal Bankruptcy Code, as permitted by Section 522 of Title 11 of the United States Code, 11 U.S.C. 522. This exemption shall not apply to any amounts contributed to an individual retirement account or annuity, deferred compensation account, a pension, profit-sharing, stock bonus, or other qualified retirement plan or annuity if the contribution occurs within one hundred twenty (120) days before the debtor files for bankruptcy. This exemption shall not apply to the right or interest of a person in an individual retirement account or annuity, deferred compensation account, pension, profit-sharing, stock bonus, or other retirement plan to the extent that that right or interest is subject to any of the following:

1. An order of a court for payment of maintenance;
2. An order of a court for payment of child support.

Massachusets

Mass. Ann. Laws ch. 235, § 34A (1994):

The right or interest of any person in an annuity, pension, profit sharing or other retirement plan maintained in accordance with the federal Employee Retirement Income Security Act of 1974, or in any annuity or similar contract purchased with assets distributed from any of the foregoing, or in any plan maintained by an individual as a Keough Plan, a Simplified Employee Plan, or an Individual Retirement Account shall be exempt from the operation of any law relating to insolvency and shall not be attached or taken on execution or other process to satisfy any debt or liability of such person, except as may be necessary to satisfy (i) an order of a court concerning divorce, separate maintenance or child support under chapters two hundred and eight, two hundred and nine, and two hundred and seventy-three or (ii) , in the event of the conviction of such person of a crime, an order of a court requiring him to satisfy a monetary penalty or make restitution to the victim of such crime. The exemption in this section for plans maintained by an individual shall not apply to sums deposited in said plans in excess of seven percent of the total income of such individual within five years of the individual's declaration of bankruptcy or entry of judgment.

Nevada

Nev. Rev. Stat. Ann. § 21.090 (1993):

…. (q) Money, not to exceed $100,000 in present value, held in:

(1) An individual retirement arrangement which conforms with the applicable limitations and requirements of 26 U.S.C. § 408;

(2) A written simplified employee pension plan which conforms with the applicable limitations and requirements of 26 U.S.C. § 408;

(3) A cash or deferred arrangement which is a qualified plan pursuant to the Internal Revenue Code; and

(4) A trust forming part of a stock bonus, pension or profit-sharing plan which is a qualified plan pursuant to sections 401 et seq. of the Internal Revenue Code (26 U.S.C. §§ 401 et seq.).

Tennessee

Tenn. Code Ann. § 26-2-104 (1994):

(a) All moneys received by a resident of the state, as pension from the state of Tennessee, or any subdivision or municipality thereof, before receipt, or while in his hands or upon deposit in the bank, shall be exempt from execution, attachment or garnishment other than an order for assignment of support issued under § 36-5-501, whether such pensioner is the head of a family or not.

(b) Except as provided in subsection (c), any funds or other assets payable to a participant or beneficiary from, or any interest of any participant or beneficiary in, a retirement plan which is qualified under §§ 401(a), 403(a), 403(b), and 408 of the federal Internal Revenue Code of 1986, as amended, are exempt from any and all claims of creditors of the participant or beneficiary, except the state of Tennessee. All records of the debtor concerning such plan and of the plan concerning the debtor's participation in the plan, or interest in the plan, are exempt from the subpoena process.

(c) Any plan or arrangement described in subsection (b), except a public plan under subsection (a), is not exempt from the claims of an alternate payee under a qualified domestic relations order. However, the interest of any and all alternate payees under a qualified domestic relations order are exempt from any and all claims of any creditor, other than the state of Tennessee. As used in this subsection, "alternate payee" and "qualified domestic relations order" have the meaning ascribed to them in § 414(p) of the federal Internal Revenue Code of 1986, as amended.

Staff Note.

Failure of individual retirement account established by debtor to meet Employee Retirement Income Security Act definitions of pension plan or employee pension benefit plan did not preclude finding that IRA was "retirement plan" exempt under Tennessee law; Tennessee legislature determined that retirement plan qualified under Internal Revenue Code as IRA was exempt from execution by creditors of participant or beneficiary, excluding state of Tennessee, without any reference to ERISA definitions. In re Martin, Bkrtcy.E.D.Tenn.1989, 102 B.R. 639.

Washington

Rev. Code Wash. (ARCW) § 6.15.020 (1994):

(1) It is the policy of the state of Washington to ensure the well-being of its citizens by protecting retirement income to which they are or may become entitled. For that purpose generally and pursuant to the authority granted to the state of Washington under 11 U.S.C. Sec. 522(b)(2), the exemptions in this section relating to retirement benefits are provided.

(2) Unless otherwise provided by federal law, any money received by any citizen of the state of Washington as a pension from the government of the United States, whether the same be in the actual possession of such person or be deposited or loaned, shall be exempt from execution, attachment, garnishment, or seizure by or under any legal process whatever, and when a debtor dies, or absconds, and leaves his or her family any money exempted by this subsection, the same shall be exempt to the family as provided in this subsection. This subsection shall not apply to child support collection actions issued under chapter 26.18, 26.23, or 74.20A RCW, if otherwise permitted by federal law.

(3) The right of a person to a pension, annuity, or retirement allowance or disability allowance, or death benefits, or any optional benefit, or any other right accrued or accruing to any citizen of the state of Washington under any employee benefit plan, and any fund created by such a plan or arrangement, shall be exempt from execution, attachment, garnishment, or seizure by or under any legal process whatever. This subsection shall not apply to child support collection actions issued under chapter 26.18, 26.23, or 74.20A RCW if otherwise permitted by federal law. This subsection shall permit benefits under any such plan or arrangement to be payable to a spouse, former spouse, child, or other dependent of a participant in such plan to the extent expressly provided for in a qualified domestic relations order that meets the requirements for such orders under the plan, or, in the case of benefits payable under a plan described in sections 403(b) or 408 of the internal revenue code of 1986, as amended, or section 409 of such code as in effect before January 1, 1984, to the extent provided in any order issued by a court of competent jurisdiction that provides for maintenance or support. This subsection shall not prohibit actions against an employee benefit plan, or fund for valid obligations incurred by the plan or fund for the benefit of the plan or fund.

(4) For the purposes of this section, the term “employee benefit plan” means any plan or arrangement that is described in RCW 49.64.020, including any Keogh plan, whether funded by a trust or by an annuity contract, and in sections 401(a) or 403(a) of the internal revenue code of 1986, as amended; or that is described in sections 403(b) or 408 of the internal revenue code of 1986, as amended, or section 409 of such code as in effect before January 1, 1984. The term “employee benefit plan” shall not include any employee benefit plan that is established or maintained for its employees by the government of the United States, by the state of Washington or any political subdivision thereof, or by any agency or instrumentality of any of the foregoing.

(5) An employee benefit plan shall be deemed to be a spendthrift trust, regardless of the source of funds, the relationship between the trustee or custodian of the plan and the beneficiary, or the ability of the debtor to withdraw or borrow or otherwise become entitled to benefits from the plan before retirement. This subsection shall not apply to child support collection actions issued under chapter 26.18, 26.23, or 74.20A RCW, if otherwise permitted by federal law. This subsection shall permit benefits under any such plan or arrangement to be payable to a spouse, former spouse, child, or other dependent of a participant in such plan to the extent expressly provided for in a qualified domestic relations order that meets the requirements for such orders under the plan, or, in the case of benefits payable under a plan described in sections 403(b) or 408 of the internal revenue code of 1986, as amended, or section 409 of such code as in effect before

January 1, 1984, to the extent provided in any order issued by a court of competent jurisdiction that provides for maintenance or support.

Wisconsin

Wis. Stat. § 815.18 (1994):

…. (j) Retirement benefits. 1. Assets held or amounts payable under any retirement, pension, disability, death benefit, stock bonus, profit sharing plan, annuity, individual retirement account, individual retirement annuity, Keogh, 401-K or similar plan or contract providing benefits by reason of age, illness, disability, death or length of service and payments made to the debtor therefrom.

2. The plan or contract must meet one of the following requirements:

a. The plan or contract complies with the provisions of the internal revenue code.

b. The employer created the plan or contract for the exclusive benefit of the employer, if self-employed, or of some or all of the employes, or their dependents or beneficiaries and that plan or contract requires the employer or employes or both to make contributions for the purpose of distributing to the employer, if self-employed, the employes, or their dependents or beneficiaries, the earnings or the principal or both of a trust, annuity, insurance or other benefit created under the plan or contract and makes it impossible, at any time prior to the satisfaction of all liabilities with respect to beneficiaries under a trust created by the plan or contract, for any part of the principal or income of the trust to be used for or diverted to purposes other than for the exclusive benefit of those beneficiaries.

3. The plan or contract may permit the income created from personal property held in a trust created under the plan or contract to accumulate in accordance with the terms of the trust. The trust may continue until it accomplishes its purposes. The trust is not invalid as violating the rule against perpetuities or any law against perpetuities or the suspension of the power of alienation of title to property.

4. The benefits of this exemption with respect to the assets held or amounts payable under or traceable to an owner-dominated plan for or on behalf of a debtor who is an owner-employe shall be limited to the extent reasonably necessary for the support of the debtor and the debtor's dependents.

5. This exemption does not apply to an order of a court concerning child support, family support or maintenance payments, or to any judgment of annulment, divorce or legal separation.

6. In this paragraph:

a. "Employer" includes a group of employers creating a combined plan or contract for the benefit of their employes or the beneficiaries of those employes.

b. "Owner-dominated plan" means any plan or contract that meets the requirements of subd. 2 and under which 90% or more of the present value of the accrued benefits or 90% or more of the aggregate of the account is for the benefit of one or more individuals who are owner-employes. For purposes of this definition, the accrued benefits or account of an owner-employe under a plan or contract shall include the accrued benefits or account of the spouse and any ancestor, lineal descendant or spouse of a lineal descendant of the owner-employe under the same plan or contract.

c. "Owner-employe" means any individual who owns, directly or indirectly, the entire interest in an unincorporated trade or business, or 50% or more of the combined voting of all classes of stock entitled to vote or the total value of shares of all classes of stock of a corporation, or 50% or more of the capital interest or profits interest of a partnership or limited liability company.

Federal

IRC § 72(p) (in part) (taxation of loans from qualified plan)

…(p) Loans treated as distributions.—For purposes of this section—

(1) Treatment as distributions.—

(A) Loans.—If during any taxable year a participant or beneficiary receives (directly or indirectly) any amount as a loan from a qualified employer plan, such amount shall be treated as having been received by such individual as a distribution under such plan.

(B) Assignments or pledges.—If during any taxable year a participant or beneficiary assigns (or agrees to assign) or pledges (or agrees to pledge) any portion of his interest in a qualified employer plan, such portion shall be treated as having been received by such individual as a loan from such plan.

(2) Exception for certain loans.—

(A) General rule.—Paragraph (1) shall not apply to any loan to the extent that such loan (when added to the outstanding balance of all other loans from such plan whether made on, before, or after August 13, 1982), does not exceed the lesser of—

(i) $50,000, reduced by the excess (if any) of—

(I) the highest outstanding balance of loans from the plan during the 1-year period ending on the day before the date on which such loan was made, over

(II) the outstanding balance of loans from the plan on the date on which such loan was made, or

(ii) the greater of (I) one-half of the present value of the nonforfeitable accrued benefit of the employee under the plan, or (II) $10,000.

For purposes of clause (ii), the present value of the nonforfeitable accrued benefit shall be determined without regard to any accumulated deductible employee contributions (as defined in subsection (o)(5)(B)).

(B) Requirement that loan be repayable within 5 years.—

(i) In general.—Subparagraph (A) shall not apply to any loan unless such loan, by its terms, is required to be repaid within 5 years.

(ii) Exception for home loans.—Clause (i) shall not apply to any loan used to acquire any dwelling unit which within a reasonable time is to be used (determined at the time the loan is made) as the principal residence of the participant.

(C) Requirement of level amortization.—Except as provided in regulations, this paragraph shall not apply to any loan unless substantially level amortization of such loan (with payments not less frequently than quarterly) is required over the term of the loan.

….

IRC § 401(a) [in part]. Qualified pension, profit-sharing, and stock bonus plans

(a) Requirements for qualification.—A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries shall constitute a qualified trust under this section—

(1) if contributions are made to the trust by such employer, or employees, or both, or by another employer who is entitled to deduct his contributions under section 404(a)(3)(B) (relating to deduction for contributions to profit-sharing and stock bonus plans), for the purpose of distributing to such employees or their beneficiaries the corpus and income of the fund accumulated by the trust in accordance with such plan;

(2) if under the trust instrument it is impossible, at any time prior to the satisfaction of all liabilities with respect to employees and their beneficiaries under the trust, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, purposes other than for the exclusive benefit of his employees or their beneficiaries (but this paragraph shall not be construed, in the case of a multiemployer plan, to prohibit the return of a contribution within 6 months after the plan administrator determines that the contribution was made by a mistake of fact or law (other than a mistake relating to whether the plan is described in section 401(a) or the trust which is part of such plan is exempt from taxation under section 501(a), or the return of any withdrawal liability payment determined to be an overpayment within 6 months of such determination);

(3) if the plan of which such trust is a part satisfies the requirements of section 410 (relating to minimum participation standards); and

(4) if the contributions or benefits provided under the plan do not discriminate in favor of highly compensated employees (within the meaning of section 414(q)). For purposes of this paragraph, there shall be excluded from consideration employees described in section 410(b)(3)(A) and (C).

(5) Special rules relating to nondiscrimination requirements.— ….

Staff Note. There are 75 references to “qualified” in IRC § 401 alone.

IRC § 415 [in part]. Limitations on benefits and contribution under qualified plans

(a) General rule.—

(1) Trusts.—A trust which is a part of a pension, profit-sharing, or stock bonus plan shall not constitute a qualified trust under section 401(a) if—

(A) in the case of a defined benefit plan, the plan provides for the payment of benefits with respect to a participant which exceed the limitation of subsection (b),

(B) in the case of a defined contribution plan, contributions and other additions under the plan with respect to any participant for any taxable year exceed the limitation of subsection (c), or

(C) in any case in which an individual is a participant in both a defined benefit plan and a defined contribution plan maintained by the employer, the trust has been disqualified under subsection (g).

(2) Section applies to certain annuities and accounts.—In the case of—

(A) an employee annuity plan described in section 403(a),

(B) an annuity contract described in section 403(b), or

(C) a simplified employee pension described in section 408(k),

such a contract, plan, or pension shall not be considered to be described in section 403(a), 403(b), or 408(k), as the case may be, unless it satisfies the requirements of subparagraph (A) or subparagraph (B) of paragraph (1), whichever is appropriate, and has not been disqualified under subsection (g). In the case of an annuity contract described in section 403(b), the preceding sentence shall apply only to the portion of the annuity contract which exceeds the limitation of subsection (b) or the limitation of subsection (c), whichever is appropriate, and the amount of the contribution for such portion shall reduce the exclusion allowance as provided in section 403(b)(2).

(b) Limitation for defined benefit plans.—

(1) In general.—Benefits with respect to a participant exceed the limitation of this subsection if, when expressed as an annual benefit (within the meaning of paragraph (2)), such annual benefit is greater than the lesser of—

(A) $90,000, or

(B) 100 percent of the participant's average compensation for his high 3 years.

….

(c) Limitation for defined contribution plans.—

(1) In general.—Contributions and other additions with respect to a participant exceed the limitation of this subsection if, when expressed as an annual addition (within the meaning of paragraph (2)) to the participant's account, such annual addition is greater than the lesser of—

(A) $30,000, or

(B) 25 percent of the participant's compensation.

….

IRC § 4975 [in part]. Tax on prohibited transactions

(a) Initial taxes on disqualified person.—There is hereby imposed a tax on each prohibited transaction. The rate of tax shall be equal to 5 percent of the amount involved with respect to the prohibited transaction for each year (or part thereof) in the taxable period. The tax imposed by this subsection shall be paid by any disqualified person who participates in the prohibited transaction (other than a fiduciary acting only as such).

(b) Additional taxes on disqualified person.—In any case in which an initial tax is imposed by subsection (a) on a prohibited transaction and the transaction is not corrected within the taxable period, there is hereby imposed a tax equal to 100 percent of the amount involved. The tax imposed by this subsection shall be paid by any disqualified person who participated in the prohibited transaction (other than a fiduciary acting only as such).

(c) Prohibited transaction.—

(1) General rule.—For purposes of this section, the term "prohibited transaction" means any direct or indirect—

(A) sale or exchange, or leasing, of any property between a plan and a disqualified person;

(B) lending of money or other extension of credit between a plan and a disqualified person;

(C) furnishing of goods, services, or facilities between a plan and a disqualified person;

(D) transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a plan;

(E) act by a disqualified person who is a fiduciary whereby he deals with the income or assets of a plan in his own interest or for his own account; or

(F) receipt of any consideration for his own personal account by any disqualified person who is a fiduciary from any party dealing with the plan in connection with a transaction involving the income or assets of the plan.

….

(d) Exemptions.—The prohibitions provided in subsection (c) shall not apply to—

(1) any loan made by the plan to a disqualified person who is a participant or beneficiary of the plan if such loan—

(A) is available to all such participants or beneficiaries on a reasonably equivalent basis,

(B) is not made available to highly compensated employees (within the meaning of section 414(q)) in an amount greater than the amount made available to other employees,

(C) is made in accordance with specific provisions regarding such loans set forth in the plan,

(D) bears a reasonable rate of interest, and

(E) is adequately secured;

(2) any contract, or reasonable arrangement, made with a disqualified person for office space, or legal, accounting, or other services necessary for the establishment or operation of the plan, if no more than reasonable compensation is paid therefor;(3) any loan to an leveraged employee stock ownership plan (as defined in subsection (e)(7)), if—

(A) such loan is primarily for the benefit of participants and beneficiaries of the plan, and

(B) such loan is at a reasonable rate of interest, and any collateral which is given to a disqualified person by the plan consists only of qualifying employer securities (as defined in subsection (e)(8));

(4) the investment of all or part of a plan's assets in deposits which bear a reasonable interest rate in a bank or similar financial institution supervised by the United States or a State, if such bank or other institution is a fiduciary of such plan and if—

(A) the plan covers only employees of such bank or other institution and employees of affiliates of such bank or other institution, or

(B) such investment is expressly authorized by a provision of the plan or by a fiduciary (other than such bank or institution or affiliates thereof) who is expressly empowered by the plan to so instruct the trustee with respect to such investment;

(5) any contract for life insurance, health insurance, or annuities with one or more insurers which are qualified to do business in a State if the plan pays no more than adequate consideration, and if each such insurer or insurers is—

(A) the employer maintaining the plan, or

(B) a disqualified person which is wholly owned (directly or indirectly) by the employer establishing the plan, or by any person which is a disqualified person with respect to the plan, but only if the total premiums and annuity considerations written by such insurers for life insurance, health insurance, or annuities for all plans (and their employers) with respect to which such insurers are disqualified persons (not including premiums or annuity considerations written by the employer maintaining the plan) do not exceed 5 percent of the total premiums and annuity considerations written for all lines of insurance in that year by such insurers (not including premiums or annuity considerations written by the employer maintaining the plan);

(6) the provision of any ancillary service by a bank or similar financial institution supervised by the United States or a State, if such service is provided at not more than reasonable compensation, if such bank or other institution is a fiduciary of such plan, and if—

(A) such bank or similar financial institution has adopted adequate internal safeguards which assure that the provision of such ancillary service is consistent with sound banking and financial practice, as determined by Federal or State supervisory authority, and

(B) the extent to which such ancillary service is provided is subject to specific guidelines issued by such bank or similar financial institution (as determined by the Secretary after consultation with Federal and State supervisory authority), and under such guidelines the bank or similar financial institution does not provide such ancillary service—

(i) in an excessive or unreasonable manner, and

(ii) in a manner that would be inconsistent with the best interests of participants and beneficiaries of employee benefit plans;

(7) the exercise of a privilege to convert securities, to the extent provided in regulations of the Secretary, but only if the plan receives no less than adequate consideration pursuant to such conversion;

(8) any transaction between a plan and a common or collective trust fund or pooled investment fund maintained by a disqualified person which is a bank or trust company supervised by a State or Federal agency or between a plan and a pooled investment fund of an insurance company qualified to do business in a State if—

(A) the transaction is a sale or purchase of an interest in the fund,

(B) the bank, trust company, or insurance company receives not more than reasonable compensation, and

(C) such transaction is expressly permitted by the instrument under which the plan is maintained, or by a fiduciary (other than the bank, trust company, or insurance company, or an affiliate thereof) who has authority to manage and control the assets of the plan;

(9) receipt by a disqualified person of any benefit to which he may be entitled as a participant or beneficiary in the plan, so long as the benefit is computed and paid on a basis which is consistent with the terms of the plan as applied to all other participants and beneficiaries;

(10) receipt by a disqualified person of any reasonable compensation for services rendered, or for the reimbursement of expenses properly and actually incurred, in the performance of his duties with the plan, but no person so serving who already receives full-time pay from an employer or an association of employers, whose employees are participants in the plan or from an employee organization whose members are participants in such plan shall receive compensation from such fund, except for reimbursement of expenses properly and actually incurred;

(11) service by a disqualified person as a fiduciary in addition to being an officer, employee, agent, or other representative of a disqualified person;

(12) the making by a fiduciary of a distribution of the assets of the trust in accordance with the terms of the plan if such assets are distributed in the same manner as provided under section 4044 of title IV of the Employee Retirement Income Security Act of 1974 (relating to allocation of assets);(13) any transaction which is exempt from section 406 of such Act by reason of section 408(e) of such Act (or which would be so exempt if such section 406 applied to such transaction) or which is exempt from section 406 of such Act by reason of section 408(b) of such Act;

(14) any transaction required or permitted under part 1 of subtitle E of title IV or section 4223 of the Employee Retirement Income Security Act of 1974, but this

paragraph shall not apply with respect to the application of subsection (c)(1)(E) or (F); or

(15) a merger of multiemployer plans, or the transfer of assets or liabilities between multiemployer plans, determined by the Pension Benefit Guaranty Corporation to meet the requirements of section 4231 of such Act, but this paragraph shall not apply with respect to the application of subsection (c)(1)(E) or (F).

The exemptions provided by this subsection [d] (other than paragraphs (9) and (12)) shall not apply to any transaction with respect to a trust described in section 401(a) which is part of a plan providing contributions or benefits for employees some or all of whom are owner-employees (as defined in section 401(c)(3)) in which a plan directly or indirectly lends any part of the corpus or income of the plan to, pays any compensation for personal services rendered to the plan to, or acquires for the plan any property from or sells any property to, any such owner-employee, a member of the family (as defined in section 267(c)(4)) of any such owner-employee, or a corporation controlled by any such owner-employee through the ownership, directly or indirectly, of 50 percent or more of the total combined voting power of all classes of stock entitled to vote or 50 percent or more of the total value of shares of all classes of stock of the corporation. For purposes of the preceding sentence, a shareholder-employee (as defined in section 1379, as in effect on the day before the date of the enactment of the Subchapter S Revision Act of 1982), a participant or beneficiary of an individual retirement account or an individual retirement annuity (as defined in section 408), and an employer or association of employees which establishes such an account or annuity under section 408(c) shall be deemed to be an owner-employee.…