HOMESTEAD AND OTHER EXEMPTIONS UNDER THE BANKRUPTCY ABUSE PREVENTION AND CONSUMER PROTECTION ACT: OBSERVATIONS ON "ASSET PROTECTION" AFTER 2005

LAWRENCE R. AHERN, III*

INTRODUCTION

On April 20, 2005, President Bush signed the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,[1] which makes the most substantial changes to the Bankruptcy Code since its enactment in 1978.[2] Certain provisions of

---

* Member, Greenebaum Doll & McDonald, PLLC, Nashville, Tennessee; Adjunct Professor of Law, Vanderbilt University; Fellow, American College of Bankruptcy. Thanks for the contributions of my colleagues Darlene Marsh (who contributed much to the basic analysis), Lewis Bell (whose knowledge of the Internal Revenue Code was very helpful) and David Houston, as well as Alisa Peters, Vanderbilt Law Class of 2006 and Bill Elliott, Decosimo & Company.

[1] Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109–8, 119 Stat. 23 (2005) [hereinafter BAPCPA] (to be codified at 11 U.S.C.). The Senate had passed BAPCPA as Senate Bill 256 on March 10, 2005, and the House of Representatives passed the Act without amendment on April 14, 2005. Because the President signed the law on April 20, 2005, the effective date of most of the provisions of the law is October 17, 2005. To distinguish between the post-BAPCPA Bankruptcy Code and the 1978 version as previously amended, citations to former Code provisions that have been amended will be to the public law number, using "BAPCPA," while citations to provisions that have not been revised will be to the Code section alone.

[2] WILLIAM HOUSTON BROWN & LAWRENCE R. AHERN III, 2005 BANKRUPTCY REFORM LEGISLATION WITH ANALYSIS 10 (Thomson/West 2005) (hereinafter BROWN & AHERN); William Houston Brown, *Taking Exception to a Debtor's Discharge: The 2005 Bankruptcy Amendments Make It Easier*, 79 AM. BANKR. L.J. 419, 420 (2005); Thomas E. Carlson & Jennifer Frasier Hayes, *The Small Business Provisions of the 2005*

BAPCPA are effective immediately upon enactment or at other times specified, although the majority of BAPCPA's amendments are effective only in cases filed 180 days after enactment.[3]

A major emphasis of the legislation's consumer provisions is the restriction of state-by-state shopping for favorable exemptions and other tools for asset protection. This article will first discuss the statutory framework for exemptions in United States bankruptcy practice and the political context in which these rules were changed in 2005. Then, a review of new limitations on a variety of exemptions, as well as new restrictions on asset protection trusts ("APTs") and pertinent revisions to the discharge exceptions, will provide a framework for assessing the future of the asset protection industry.

BAPCPA made it very hard to establish domicile for the purpose of pre-bankruptcy exemption planning, without doing very long-range planning; this difficulty increases with regard to homestead exemptions. Circumventing these new rules will prove difficult for most debtors. The new retirement plan exemptions may provide a safety net for some debtors, but for asset protection purposes may not be the most desirable or effective vehicle.

The amendment of the rules limiting self-settled asset protection trusts does not change the effectiveness of domestic asset protection trust planning, as long as intentional fraud cannot be proven. This might be a good thing for debtors who would like to explore the self-settled trust vehicle for asset protection purposes. Consistent with the apparent intent of Congress, however, it leaves a cloud of uncertainty over the device because, by definition, asset protection generally means adversely affecting creditors, if not intentionally hindering, delaying or defrauding them.

I. STATUTORY AND POLITICAL BACKGROUND

A. The Statutory Framework for Exemptions in Bankruptcy

The bankruptcy process provides the unfortunate but honest debtor with a "fresh start," both by discharging his or her indebtedness and by providing a level of property exempt from liquidation whereby the debtor may be supported and support a family while rebuilding on the foundation of that fresh start. Because exemptions necessarily deprive creditors of assets which would be available to satisfy their claims, some tension develops between the debtor on the one hand and creditors and the bankruptcy trustee on the other and it has been said that the "purpose behind

---

Bankruptcy Amendments, 79 AM. BANKR. L.J. 645, 668 (2005) (noting major changes of 2005 Amendments).

[3] BAPCPA § 1501 (to be codified at 11 U.S.C. § 101).

exemptions ... is not to provide a windfall for the debtor, but rather, to protect the public from the burdens of supporting a destitute family."[4]

The objective source of standards for allowance of exemptions under the Bankruptcy Code is found in section 522, which provides at the first stage in the process for a choice between federal bankruptcy exemptions[5] and a state or local exemption scheme[6] chosen on the basis of the debtor's domicile.[7] The debtor's choice is restricted in many states, however, by means of an "opt out" system in the Code that permits each state legislature to determine that its citizens may not choose the federal system.[8] The opt out has been challenged on the basis of constitutionality[9] and on the basis that exemption policy should not be "channeled away from bankruptcy policy-makers toward a variety of state legislatures."[10] The changes made by BAPCPA in the exemption scheme under section 522 of the Bankruptcy Code are in part a reflection of this policy concern.

B. The Political Context of Homestead and Related Change in 2005

---

[4] *In re* Hill, 163 B.R. 598, 601 (Bankr. N.D. Fla. 1994) (proposing purpose of the bankruptcy exemptions is to protect the public from the burdens of supporting destitute family); Brown v. Swartz (*In re* Swartz) 18 B.R. 454, 456 (Bankr. Mass. 1982) ("The purpose of an exemption under the Bankruptcy Code is not for the personal privilege of the debtor, but for the benefit of this family who may be destitute and the public who might otherwise be burdened with the support of an insolvent debtor's family."); Centran Bank of Akron (*In re* Ambrose) 4 B.R. 395, 401 (Bankr. N.D. Ohio 1980) (indicating purpose of exemptions is not for debtor but for family and public).

[5] 11 U.S.C. § 522(d) (2000).

[6] 11 U.S.C. § 522(b) (2000).

[7] *See also* Henry E. Hildebrand, III, *Impact of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 on Chapter 13 Trustees*, 79 AM. BANKR. L.J. 373, 383–84 (2005) (explaining availability of choice between federal exemptions and state exemptions). *See generally* Margaret Howard, *Exemptions Under the 2005 Bankruptcy Amendments: A Tale of Opportunity Lost*, 79 AM. BANKR. L.J. 397, 398 (2005) (discussing available exemptions under 2005 Bankruptcy Code); Brian P. Rivera, *State Homestead Exemptions and Their Effect on Federal Bankruptcy Laws*, 39 REAL PROP. PROB. & TR. J. 71 (2004) (recounting history of federal homestead exemption and evaluating effects of exemptions on Federal Bankruptcy Law).

[8] *See* 11 U.S.C. § 522(b)(1) (2000); *see also* BAPCPA §§ 224, 308 (to be codified at 11 U.S.C. § 522(b)(2)). *See generally* WILLIAM HOUSTON BROWN, LAWRENCE R. AHERN, III & NANCY FRAAS MACLEAN, BANKRUPTCY EXEMPTION MANUAL §§ 3.01–3.07 (Thomson/West) (2005) [hereinafter EXEMPTION MANUAL] (discussing opt-out provision of Code).

[9] *See* EXEMPTION MANUAL, *supra*, note 8, § 3.04 (evaluating constitutionality of opt-outs); Hon. William Houston Brown, *Political and Ethical Considerations of Exemption Limitations: The "Opt-Out" as Child of the First and Parent of the Second*, 71 AM. BANKR. L.J. 149, 173–75 (1997) (highlighting various constitutional challenges to opt-outs); G. Marcus Cole, *The Federalist Cost of Bankruptcy Exemption Reform*, 74 AM. BANKR. L.J. 227, 248 (2000) (discussing constitutional challenge to opt-out provision).

[10] NAT'L BANKR. REVIEW COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS: NATIONAL BANKRUPTCY REVIEW COMMISSION FINAL REPORT, at 121 (W.S. Hein 2000 (1997)) (recommending elimination of opt-out); *see, eg.*, EXEMPTION MANUAL, *supra* note 8, at 714 (challenging opt-out on basis of policy considerations); William Houston Brown, *Political and Ethical Considerations of Exemption Limitations: the "Opt-out" as Child of the First and Parent of the Second*, 71 AM. BANKR. L.J. 149, 180–86 (1997) (evaluating implementation of national exemption policy); Lawrence Ponoroff, *Exemptions Limitations: A Tale of Two Solutions*, 71 AM. BANKR. L.J. 221, 222–23 (1997) (discussing National Bankruptcy Review Commission's recommendations).

Under the Bankruptcy Code in effect prior to BAPCPA, commentators suggested that abuses of the homestead exemption and asset protection schemes were rampant.[11] This led to a maze of judicial rulings on the propriety of such pre-bankruptcy planning.[12] As attorneys have attempted to guide their clients through this thicket, a particularly noisy debate over the ethical ramifications of this practice has ensued.[13]

Perhaps predictably, this has created a cottage industry for commentators who have attempted to find a solution to the problem.[14]

Asset protection planning has evolved in recent years into a veritable industry with many and varied domestic and offshore/foreign alternatives. These range from the asset protection trust, a staple in the arsenal of the planner, to more exotic and dubious schemes including offshore[15] LLCs into which a U.S. debtor is encouraged

---

[11] *See, e.g.*, Howard, *supra* note 7, at 397–400 (explaining curing abuse of homestead exemptions was one goal of BAPCPA); John M. Norwood and Marianne M. Jennings, *Before Declaring Bankruptcy, Move to Florida and Buy a House: The Ethics and Judicial Inconsistencies of Debtors' Conversions and Exemptions*, 28 SW. U.L. REV. 439 (1999) (examining ethics of planning ahead for bankruptcy by converting non-exempt assets to exempt assets); Charles Jordan Tabb, *The Death of Consumer Bankruptcy in the United States?*, 18 BANKR. DEV. J. 1, 42–3 (2001) (highlighting homestead exemption as "800-pound gorilla of loopholes" in pre-Amendment Bankruptcy Code).

[12] *See, e.g.*, Wells M. Engledow, *Cleaning up the Pigsty: Approaching a Consensus on Exemption Laws*, 74 AM. BANKR. L.J. 275, 276–78 (2000) (citing nonuniformity of exemption laws as explanation for varied treatment by courts); John M. Norwood, *An Historical Analysis of Pre-Bankruptcy Conversion Cases on a Circuit-By-Circuit Basis*, 103 COM. L. J. 154 (1998) (noting variations in determination of cases involving pre-bankruptcy planning); Eric A. Posner, *The Jurisprudence of Greed*, 151 U. PA. L. REV. 1097, 1109–11 (2003) (discussing various cases dealing with pre-bankruptcy planning).

[13] *See, e.g.*, Brown, *supra* note 9, at 187–93 (exploring various ethical issues dealing with pre-bankruptcy planning); Robin E. Phelan & John D. Penn, *Bankruptcy Ethics, An Oxymoron*, 5 AM. BANKR. INST. L. Rev. 1, 9–15 (1997) (noting fine line between permissibly pre-bankruptcy planning and fraudulent transfer of non-exempt assets to exempt assets); Nathan F. Coco & David C. Christian II, *Squirreling It Away, The Business Lawyer's Role in Pre-Bankruptcy Planning*, BUS. L. TODAY, Feb. 12, 2003, at 29 (discussing permissible extent of lawyer's involvement in client's pre-bankruptcy planning).

[14] *See, e.g.*, William Houston Brown & Lawrence Ponoroff, *A Second Look at the Proposed Uniform Bankruptcy Exemptions: Tennessee as an Example*, 28 U. MEM. L. REV. 647, 647–48 (1998) (commenting on exemption recommendations made by National Bankruptcy Review Commission); Juliet M. Moringiello, *Distinguishing Hogs From Pigs: A Proposal for a Preference Approach to Pre-Bankruptcy Planning*, 6 AM. BANKR. INST. L. REV. 103, 115 (1998) (proposing solutions to the problem of abuse of exemptions by debtors); Nancy B. Rapoport, *Our House, Our Rules: The Need for a Uniform Code of Bankruptcy Ethics*, 6 AM. BANKR. INST. L. REV. 45, 46 (1998) (questioning usefulness of creating federal bankruptcy ethics laws).

[15] "Commentators have identified the following countries as possible sites for APTs: Anguilla, Antigua, Bahamas, Barbados, Belize, Bermuda, Cayman Islands, Cook Islands, Cyprus, Gibraltar, Marshall Islands, Nevis, Niue, Seychelles, Turks and Caicos (common law jurisdictions); Liechtenstein, Channel Islands (Jersey and Guernsey) (civil law jurisdictions)." Henry J. Lischer, Jr., *Professional Responsibility Issues Associated With Asset Protection Trusts*, 39 REAL PROP. PROB. & TR. J. 561, 568 n.26 (2004) (citations omitted); *see also* Antony G.D. Duckworth, *The Trust Offshore*, 32 VAND. J. TRANSNAT'L L. 879, 930 (1999) (highlighting American professionals as clients of offshore trust centers); Elena Marty-Nelson, *Offshore Asset Protection Trusts: Having Your Cake and Eating it Too*, 47 RUTGERS L. REV. 11, 12 (1994) (discussing offshore asset protection trusts).

to transfer his or her U.S. property interests owned by U.S. LLCs, to avail such domestic entities of arrangements rendered immune to the attacks of creditors by distance and difficulty. A detailed description and analysis of all such vehicles is beyond the scope of this article. It has been argued, however, that United States tax laws and their enforcement do not effectively limit such practices. United States residence rules, for example, define a hedge fund "partnership as resident where it is organized, rather than where it is managed and controlled"[16] and the resulting compliance with requirements of reporting to the Treasury Department's Financial Crimes Enforcement Network ("FinCEN")[17] "is estimated to be less than 20 percent."[18]

The practical reality is that the efficacy of asset-protection structures may be largely a function of the complexity and difficulty of piercing such a fortress. Indeed, even the simplest of structures may have the effect of chilling a creditor's attempt to pierce it given the obstacles and difficulties attendant thereto.

Further, many U.S. jurisdictions have overtly supported asset protection through legislation authorizing "domestic asset protection trusts" ("DAPTs"), including Delaware, Rhode Island, Alaska, Nevada and Utah.[19] The advent of new states jumping on this bandwagon, including Oklahoma, which allows a DAPT to be either a revocable or irrevocable trust[20]

The advent of new states jumping on this bandwagon, including Oklahoma, which allows a DAPT to be either a revocable or irrevocable trust under its "Wealth Preservation Act",[21] have taken a creature of once foreign jurisdiction and domesticated and Americanized this traditional staple, although the statutes of limitations may be longer than that allowed offshore.

---

[16] Lee A. Sheppard, *Offshore Investments: Don't Ask, Don't Tell*, 108 TAX NOTES 171, 172 (2005).

[17] 31 U.S.C. § 5314 (2000); 31 C.F.R. § 103.24 (2004).

[18] Sheppard, *supra* note 16, at 174.

[19] David G. Shaftel & David H. Bundy, *Domestic Asset Protection Trusts Created by Nonresident Settlors*, 32–4 EST. PLANN. 17, 17 (2005) (discussing domestic asset protection trust statutes enacted in several states); *see also* John E. Sullivan III, *Gutting The Rule Against Self-Settled Trusts: How The New Delaware Trust Law Competes With Offshore Trusts*, 23 DEL. J. CORP. L. 423, 424 (1998) (detailing Delaware legislation allowing debtors to use "self-settled trusts."); Ritchie W. Taylor, *Domestic Asset Protection Trusts: The "Estate Planning Tool of the Decade" or a Charlatan?*, 13 BYU J. PUB. L. 163, 165 (underlining Alaska as first state statutorily permitting asset protection trusts, followed by Delaware).

[20] Shaftel & Bundy, *supra* note 19, at 17 ("Oklahoma's 'Family Wealth Preservation Act' is unique in that it allows a DAPT to be either a revocable or irrevocable trust…"); *cf.* Susanna C. Brennan, Comment, *Changes in Climate: The Movement of Asset Protection Trusts from International to Domestic Shores and its Effect on Creditors' Rights*, 79 OR. L. REV. 755, 766 (2000) (stating usual irrevocability of offshore asset protection trusts); Amy Lynn Wagenfeld, Note, *Law for Sale: Alaska and Delaware Compete for Asset Protection Trust Market and the Wealth that Follows*, 32 VAND. J. TRANSNAT'L L. 831, 848 (1999) (explaining characteristic of offshore asset protection trusts, one being irrevocability).

[21] OKLA. STAT. tit. 31, §§ 10–17 (2005).

Thus, it is difficult to overstate the complexity of this industry.[22] However, debtors have also been perceived as exploiting the loopholes in the system in various, more mundane ways—by paying cash for houses in states with an unlimited homestead exemption, by moving to these states 180 days before filing with a sole intent to use these unlimited exemptions and even by setting up self-settled trusts long before filing—in order to shield those assets from the creditors that helped fund them.

This concern for the integrity of the bankruptcy process was reflected in the report of the National Bankruptcy Review Commission, created by Congress in the Bankruptcy Reform Act of 1994.[23] The Commission rendered its report after three years of study and included a scathing criticism of the opt-out exemption system.

> The opportunities for pre-bankruptcy planning created by the exemption opt-out have called the integrity of the bankruptcy system into question, particularly in the context of a small handful of high-visibility debtors. People with no other familiarity with the bankruptcy system can cite celebrities who have shielded millions of dollars in an expensive homestead in certain states, a behavior that erroneously is attributed to federal law, even though the federal exemptions would not have allowed this shielding to occur. Unlimited homesteads have led to national ridicule and the efforts of some less needy and better represented families to find literal and figurative shelter in generous states.[24]

---

[22] For example, life insurance is not only an asset protected vehicle but one which is not, like most APT and LLC arrangements described above, tax neutral. *See* Stephen Z. Starr & Brian C. Bandler, *Life Insurance and Annuities May Insulate Some Assets From Loss in Unexpected Bankruptcy Filings*, 72-AUG N.Y. ST. B.A. J. 28, 30 (2000) ("Life insurance policies, to the extent of their cash or surrender value while the insured is alive and the death benefit proceeds after the insured's death, are subject to federal estate and gift taxes if the policies are owned by the insured, her/his spouse or another individual."); *see also* Joel S. Dobris, The Death of the "Death Tax"?: Federal Transfer Taxes: The Possibility of Repeal and the Post Repeal World, Presentation to "The Death of the 'Death Tax'" Conference (October 6, 2000), *in* 48 CLEV. ST. L. REV. 709, 721 (2000) (predicting in light of reduced need for insurance to fund estate tax payments, insurance will be "sold more heavily as an asset protection device and trust substitute."). *See generally* Wayne M. Gazur, *Death and Taxes: The Taxation of Accelerated Death Benefits For the Terminally Ill*, 11 VA. TAX. REV. 263, 265 (1991) (noting Congress has addressed income taxation on life insurance on several occasions). Promoters have been hawking their life insurance wares for years, stressing the combined benefits of tax deferral and asset protection.

[23] Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 601 *et seq*, 108 Stat. 4106, 4147–4150 (establishing Bankruptcy Review Commission).

[24] NAT'L BANKR. REVIEW COMM'N, *supra* note 10; *see, e.g.*, EXEMPTION MANUAL, *supra* note 8, at 715–16 (citing, *e.g.*, David Barstow, *In Florida, Simpson May Find a Financial Haven*, ST. PETERSBURG TIMES, October 19, 1995, at 1A; Peter S. Canellos, *Sheltered From Bankruptcy: Florida Home Exemption Gives Debtors A Haven*, BOSTON GLOBE, April 22, 1997, at A1; Larry Rohter, *Rich Debtors Find Shelter under a Populist Florida Law*, N.Y. TIMES, July 25, 1993, at 1; Sandra Ward, *Bailing Out: Bankruptcy, Once A Disgrace, Has Become As American As The Fourth of July*, BARRON'S, June 17, 1996, at 17). *But see* Gary Klein, *Consumer Bankruptcy in Balance: The National Bankruptcy Commission's Recommendations Tilt*

We shall see that, in 2005, Congress heard continued criticism of the homestead and other aspects of the exemption system and sought to reduce, if not eliminate, these perceived abuses by implementing BAPCPA. This evidenced some hope that the loopholes would close and the bankruptcy process would be used appropriately by those who need it, not by those who seek only to exploit it.

II. HOMESTEAD EXEMPTIONS UNDER BAPCPA

A. Domiciliary Limits

The BAPCPA domiciliary tests utilize a formula similar to prior law, with several important exceptions specific to homestead exemptions, reflecting the political concern with exploitation of lenient state laws. Under the previous test, the state whose laws applied was the domicile of the debtor for 180 days immediately preceding the date of the filing of the petition or the state where the debtor resided for the greater portion of such 180-day period.[25] The new rules enlarge that window to at least 730 days.[26]

> (b)(1) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either ~~paragraph (1)~~paragraph (2) or, in the alternative, ~~paragraph (2)~~paragraph (3) of this subsection. In joint cases filed under section 302 of this title and individual cases filed under section 301 or 303 of this title by or against debtors who are husband and wife, and whose estates are ordered to be jointly administered under Rule 1015(b) of the Federal Rules of Bankruptcy Procedure, one debtor may not elect to exempt property listed in ~~paragraph (1)~~paragraph (2) and the other debtor elect to exempt property listed in ~~paragraph (2)~~paragraph (3) of this subsection. If the parties cannot agree on the alternative to be elected, they shall be deemed to elect ~~paragraph (1)~~paragraph (2), where such election is permitted under the law of the jurisdiction where the case is filed. ~~Such property is—~~
>
> ~~(1) property that is specified under subsection (d) of this section, unless the State law that is applicable to the debtor under paragraph (2)(A) of this subsection specifically does not so authorize; or, in the alternative,~~ (2) Property listed in this paragraph is property that

---

Towards Creditors, 5 AM. BANKR. INST. L. REV. 293, 309 (1997) (criticizing commission's recommendations since implementation would serve as marriage penalty, would increase number of filings at high cost, and would inevitably cause loss of family homes).

[25] 11 U.S.C. § 522(b)(2)(A) (2000).

[26] BAPCPA § 307(1)(A) (to be codified at 11 U.S.C. § 522(b)(3)(A)).

> is specified under subsection (d), unless the State law that is applicable to the debtor under paragraph (3)(A) specifically does not so authorize.
>
> (3~~2~~) Property listed in this paragraph is
>
> > (A) subject to subsections (o) and (p), 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 at the place in which the debtor's domicile has been located for the ~~180~~730 days immediately preceding the date of the filing of the petition~~, or for a longer portion of such 180-day period than in any other place~~ or if the debtor's domicile has not been located at a single State for such 730-day period, the place in which the debtor's domicile was located for 180 days immediately preceding the 730-day period or for a longer portion of such 180-day period than in any other place . . .
>
> If the effect of the domiciliary requirement under subparagraph (A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt property that is specified under subsection (d).[27]

If domicile for that period is not continuous, then applicable law is determined by the place where debtor's domicile was located for the 180 day period preceding the 730 day period—or where the debtor's domicile was located for a longer portion of that 180 day period than any other place.[28] Evidently, Congress was not confident that this would always produce a clear answer and assured that all is not lost in case an unlucky debtor just happens to move so that the effect of that test would be to give him or her nothing in the way of exemptions. Therefore, as a default result under section 522(b)(3), if the effect of the domiciliary requirement under section 522(b)(3)(A) is to render the debtor ineligible for any exemption, the debtor may elect to exempt the property specified under section 522(d)—the federal exemptions.[29]

---

[27] BROWN & AHERN, *supra* note 2, at 216-17 (blacklining Bankruptcy Code to show changes made pursuant to BAPCPA); 11 U.S.C. § 522(b)(3).

[28] BAPCPA § 307 (to be codified at 11 U.S.C. § 522(b)(3)).

[29] *Id*. Although the concern behind this provision is not perfectly clear, it might be triggered by the wording of the chosen state's exemption laws. If the debtor filing in state A has resided in State B for the requisite 730- or 180-day period and if State B's exemptions refer explicitly to property in State B, the effect might be to deprive the debtor of any exemption. Indeed, it may be the majority rule that homestead statutes have "no extraterritorial effect." *See, e.g.*, *In re* Owings, 140 F. 739, 741 (D.N.C. 1905) (holding North Carolina constitution prevented residents from claiming Maryland property as homestead in North Carolina bankruptcy under 1898 Bankruptcy Act); Travelers Indem. Co. v. Heim, 352 N.W.2d 921, 924 (Neb. 1984) (holding, under Nebraska statute, Colorado residents could not claim homestead in Nebraska, where debtor had no "residence in habitation."). One case even suggests that such effect would be constitutionally questionable. *In re* Drenttel, 302 B.R. 26, 34 (Bankr. D. Minn. 2003) (denying claim of homestead in

B. Dollar Limits

Under BAPCPA, homestead exemptions are not only subject to more stringent domiciliary tests, but also to additional restrictions, codified in the new, renumbered Bankruptcy Code subsections 522(o),[30] (p),[31] and (q).[32] To understand Congress' actions in 2005, these new provisions must be reviewed in some detail.

New section 522(o) reduces the homestead exemption to the extent that any portion of it is attributable to the debtor's disposal of non-exempt property during the 10-year period preceding the date the bankruptcy petition is filed when such disposal was made with the intent to hinder, delay, or otherwise defraud a creditor.[33]

> (o) For purposes of subsection (b)(3)(A), and notwithstanding subsection (a), the value of an interest in—
>
> (1) real or personal property that the debtor or a dependent of the debtor uses as a residence;
>
> (2) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;
>
> (3) a burial plot for the debtor or a dependent of the debtor; or
>
> (4) real or personal property that the debtor or a dependent of the debtor claims as a homestead;
>
> shall be reduced to the extent that such value is attributable to any portion of any property that the debtor disposed of in the 10-year period ending on the date of the filing of the petition with the intent to hinder, delay, or defraud a creditor and that the debtor could not exempt, or that portion that the debtor could not exempt, under subsection (b), if on such date the debtor had held the property so disposed of.[34]

Section 522(o) applies only with respect to transfers of property that could not have been exempted (or a portion thereof that could not have been exempted) under section 522(b) if the debtor still held such property.[35] The limitation applies to real or personal property that the debtor, or a dependent of the debtor, uses as a

---

Arizona property based on Minnesota exemption) (citing Shaffer v. Heitner, 433 U.S. 186, 197 (1977)). At least two recent cases, however, have held otherwise. An Oregon debtor may exempt property located in California. *See In re* Stratton, 269 B.R. 716 (Bankr. D. Or. 2001). A debtor may claim the California homestead in real estate located in Michigan. Arrol v. Broach (*In re* Arrol), 170 F.3d 934 (9th Cir. 1999).

[30] *Id*. at § 308 (to be codified at 11 U.S.C. § 522(o)).

[31] BAPCPA § 322(a) (to be codified at 11 U.S.C. § 522(p)).

[32] *Id*. (to be codified at 11 U.S.C. § 522(q)).

[33] *Id*. at § 308 (to be codified at 11 U.S.C. § 522(o)).

[34] *Id*.

[35] *Id*.

residence.[36] It also applies to cooperatives used as residences by the debtor or a dependent of the debtor, burial plots for the debtor or a dependent of the debtor or real or personal property that the debtor or a dependent of the debtor claims as a homestead.[37] Section 522(o) became effective on April 20, 2005, the date of enactment.[38]

While new section 522(o) reduces the amount that may be converted from non-exempt assets to a homestead during the ten-year period preceding filing, new section 522(p) puts limits on the entire exemption allowed.[39] Under the old law, once domicile was established, a debtor could immediately take full advantage of whatever homestead exemption that state allowed. Understandably, states with generous homestead exemptions (*e.g.*, Florida[40]) received an influx of new citizens, purchasing exempt homes and subsequently filing bankruptcy.

Congress sought to limit, if not eliminate, this practice by enacting section 522(p).[41]

> (p)(1) Except as provided in paragraph (2) of this subsection and sections 544 and 548, as a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of interest that was acquired by the debtor during the 1215-day period preceding the date of the filing of the petition that exceeds in the aggregate $125,000 in value in—

---

[36] *Id*.

[37] *Id*.

[38] *See* BAPCPA § 1501(b)(2) ("The amendments made by sections 308, 322, and 330 shall apply with respect to cases commenced under title 11, United States Code, on or after the date of the enactment of this Act.").

[39] *See id*. at § 322(a) (to be codified at 11 U.S.C. § 522(p)) (limiting homestead exemption set forth in 11 U.S.C. § 552(o)); *see, e.g.* BAPCPA §§ 224, 308 (to be codified at 11 U.S.C § 522(b)(2)(A)). This section provides:

> [A]n individual debtor may exempt from property of the estate . . . any property that is exempt under federal law . . . or state or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer portion of such 180-day period than in any other place . . . .

Id.

[40] *See* Fla. Const. art. X, § 4 (allowing 160 acres for rural homestead exemptions and one-half acre for urban homestead exemptions); *cf.* FLA. STAT. tit. XV, §§ 222.01, 222.02, 222.05 (1998) (setting forth procedural stipulations for instituting Florida's Homestead Exemption).

[41] *See* BAPCPA § 322(a) (to be codified at 11 U.S.C. § 522(p)); Samuel K. Crocker & Robert H. Waldschmidt, *Impact of the 2005 Bankruptcy Amendments on Chapter 7 Trustees*, 79 AM. BANKR. L.J. 333, 349–54 (2005) (describing changes in exemption scheme of § 522); Richard E. Mendales, *Rethinking Exemptions in Bankruptcy*, 40 B.C. L. REV. 851, 859 (1999) (noting exemptions options debtor has under § 522).

> (A) real or personal property that the debtor or a dependent of the debtor uses as a residence;
> (B) a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence;
> (C) a burial plot for the debtor or a dependent of the debtor; or
> (D) real or personal property that the debtor or dependent of the debtor claims as a homestead.
>
> (2) (A) The limitation under paragraph (1) shall not apply to an exemption claimed under subsection (b)(3)(A) by a family farmer for the principal residence of such farmer.
> (B) For purposes of paragraph (1), any amount of such interest does not include any interest transferred from a debtor's previous principal residence (which was acquired prior to the beginning of such 1215-day period) into the debtor's current principal residence, if the debtor's previous and current residences are located in the same State.[42]

Under this new provision, if the debtor chooses to exempt property under state or local law pursuant to the rules in new section 522(b)(3)(A), or has to use the state and local rules because the state in question has opted out of the federal exemptions, then the debtor may not exempt any amount of homestead interest acquired by the debtor during the 1,215-day (approximately 40 months) period preceding the date of the filing of the petition that exceeds, in the aggregate, $125,000.[43] This limitation applies to real or personal property that the debtor or a dependent of the debtor uses as a residence.[44] It also applies to a cooperative used as a residence by a debtor or a dependent of the debtor, burial plots for the debtor or a dependent of the debtor, and real or personal property that the debtor or a dependent of the debtor claims as a homestead.[45]

The limitation in new section 522(p) is subject to two exceptions. First, it does not apply to an exemption claimed under new section 522(b)(3)(A) by a family farmer for the principal residence of such farmer.[46] Second, the value of home equity which is "rolled" into a new residence from a previous principal residence is

---

[42] BAPCPA § 322(a) (to be codified at 11 U.S.C. § 522(p)). One court has interpreted this $125,000 homestead cap to apply only in non-opt out states. *See In re* McNabb, 326 B.R. 785, 788 (Bankr. D. Ariz. 2005) (holding language of § 522(p), which applies "as a result of electing . . . to exempt property under State or local law," is inapplicable in opt-out states, where debtors may not "elect" state exemptions, because those are only exemptions available to them); Ann Morales Olazabal & Andrew J. Foti, *Consumer Bankruptcy and 11 US.C.§ 707(b): A Case-Based Analysis*, 12 B.U. PUB. INT. L.J. 317, 349 (2003) (pointing to no uniform general cap on state homestead exemptions).

[43] BAPCPA § 322(a) (to be codified at 11 U.S.C. § 522(p)(1)).

[44] *Id*. (to be codified at 11 U.S.C. § 522(p)(1)(A)).

[45] *Id*. (to be codified at 11 U.S.C. § 522(p)(1)(B–D)).

[46] *Id*. (to be codified at 11 U.S.C. § 522(p)(2)(A)).

excluded from the 1,215-day holding period.[47] To qualify for this second exception, however, both the current and the previous residences must be located in the same state and the previous principal residence must have been acquired before the 1,215-holding period.[48] Section 522(p) became effective upon enactment as well.[49]

In addition to the restrictions put in place by new sections 522(o) and (p), BAPCPA also added new section 522(q), which limits the homestead further.

> (q)(1) As a result of electing under subsection (b)(3)(A) to exempt property under State or local law, a debtor may not exempt any amount of an interest in property described in subparagraphs (A), (B), (C), and (D) of subsection (p)(1) which exceeds in the aggregate $125,000 if—
>
> (A) the court determines, after notice and a hearing, that the debtor has been convicted of a felony (as defined in section 3156 of title 18), which under the circumstances, demonstrates that the filing of the case was an abuse of the provisions of this title; or
>
> (B) the debtor owes a debt arising from—
>
> (i) any violation of the Federal securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934), any State securities laws, or any regulation or order issued under Federal securities laws or State securities laws;
>
> (ii) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 1934 or under section 6 of the Securities Act of 1933;
>
> (iii) any civil remedy under section 1964 of title 18; or
>
> (iv) any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years.
>
> (2) Paragraph (1) shall not apply to the extent the amount of an interest in property described in subparagraphs (A), (B), (C), and

---

[47] *Id*. (to be codified at 11 U.S.C. § 522(p)(2)(B)).

[48] *Id*.

[49] BAPCPA § 1501(b)(2) ("Amendments made by sections 308, 322, and 330 shall apply with respect to cases commenced . . . on or after the date of the enactment of this Act.").

> (D) of subsection (p)(1) is reasonably necessary for the support of the debtor and any dependent of the debtor.[50]

Thus, if the court determines that the debtor has any felony conviction or any debt that is attributable to securities laws violations, regardless of when the debt arose, or crimes, torts or other misconduct causing serious physical injury or death within the past five (5) years, then the homestead that might otherwise be elected under state or federal law is capped at $125,000, regardless of when the property was acquired.[51] In other words, this limitation applies even if the homestead was acquired before the 1,215-day holding period under subsection (o) and also applies if the homestead was acquired during the 1,215 days preceding the case under subsection (p).

Congress seems to have viewed these circumstances as demonstrating that the bankruptcy filing was akin to an abusive filing. However, if the property is necessary for the support of the "debtor and any dependent," then the $125,000 limitation does not apply.[52] It would seem that this relief was designed for married couples and the head of a household.[53] New subsection 522(q), like subsections (o) and (p), became effective on April 20, 2005.[54]

III. RETIREMENT PLANS AND SIMILAR FUNDS UNDER BAPCPA

A. New Federal Exemptions

While Congress limited the homestead exemptions in section 522(b)(3)(A), it also created a new class of exemptions in new paragraphs 522(b)(3)(C) (applicable in opt-out states) and 522(d)(12) (in the federal exemption scheme) for specific retirement plans that can be exempted from the bankruptcy estate by the debtor.[55] New subsection 522(b)(3)(C) provides the following exemption:

> (3) Property listed in this paragraph is . . .

---

[50] BAPCPA § 322 (to be codified at 11 U.S.C. § 522(q)).

[51] *Id*.

[52] *Id*. (emphasis added).

[53] *See* 11 U.S.C. § 522(a)(1) (2000) (defining dependent to include spouse, whether or not actually dependent).

[54] BAPCPA § 1501(b)(2) (to be codified at 11 U.S.C. § 522(q)).

[55] BAPCPA § 224 (to be codified at 11 U.S.C. § 522(b)(4)) (including exemptions for retirement funds that received favorable determination under section 7805 of Internal Revenue Code of 1986, received unfavorable determination under Code but neither courts nor Internal Revenue Service made previous determination regarding funds and funds substantially comply to applicable Code requirements, were transferred from one fund or account to another that was exempt from taxation under various Code provisions, were distributed and qualified as eligible rollover distribution under the Code, and composed assets in individual retirement funds under specific limitations of Code).

> (C) retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.[56]

Amended subsection 522(d)(12) provides the following new federal exemption:

> (d) The following property may be exempted under ~~subsection (b)(1)~~ subsection (b)(2) of this section:
>
> . . . .
>
> (12) Retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under section 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986.[57]

To translate from the numeric listing of Internal Revenue Code sections, BAPCPA creates a new federalized exemption scheme that exempts the following retirement funds, regardless of whether the state of domicile has opted out of the federal scheme for other property:

- qualified employer-sponsored and defined-contribution plans (*e.g.*, 401(k) plans);[58]
- 403(b) plans; qualified annuity plans that are established by an employer for an employee under IRC §§ 404(a)(2) or 501(c)(3), which may be thought of as "401(k)s" for the non-profit sector;[59]
- Individual Retirement Accounts (IRAs), Simplified Employee Pensions (SEPs) and Savings Incentive Match Plans for Employees (SIMPLEs), which are not eligible for rollovers because they are excluded from the definition of eligible retirement plan;[60]

---

[56] BAPCPA § 224(3), (4)(C) (to be codified at 11 U.S.C. § 522(b)(3)(C)).

[57] BROWN & AHERN, *supra* note 2, at 218-19; 11 U.S.C. § 522(d) (2000).

[58] BAPCPA § 224(a)(1)(C) (to be codified at 11 U.S.C. § 522(b)(2)(c)) (referring to 26 U.S.C. § 401 (including Keogh Plans, under 26 U.S.C. § 401(c), which are not subject to general rule contributions reduce what may be placed in another qualified retirement vehicle)).

[59] *Id*. (referring to 26 U.S.C. § 403).

[60] BAPCPA, § 224(a)(1)(C), 63 (to be codified at 11 U.S.C. § 522(b)(2)(c)) (referring to 26 U.S.C. § 408). *See* 26 U.S.C. § 408(d)(3)(A) (2000) (specifying monetary amount constitutes rollover distribution); RIA FEDERAL TAX HANDBOOK ¶ 4363, at 710 (2005) (citing 26 U.S.C. § 402(c)(8)(B) ("An 'eligible retirement plan' is: (1) an individual retirement account (not a Roth IRA), (2) an individual retirement annuity (other than an endowment contract), (3) a qualified trust, (4) an annuity plan, (5) a Code Sec. 403(b) annuity, and (6) a governmental section 457 plan."); 6 MERTENS LAW OF FEDERAL INCOME TAXATION § 25B-2:10, at 25B-2-44, 45 (2005) (describing general conception of rollovers and eligible retirement plans).

- Roth IRAs;[61]
- other retirement plans for controlled groups of employees (predecessor employers, partnerships, proprietorships, governments, churches);[62] and
- eligible deferred compensation plans established and maintained by eligible employers.[63]

In addition to the plans specifically enumerated in new paragraphs 522(b)(3) and (d)(12), there is another provision in new section 522(b)(4)(A), providing that funds in a retirement vehicle that has received a favorable determination of its tax-exempt status from the IRS shall be presumed to be exempt from the estate.

> For purposes of paragraph (3)(C) and subsection (d)(12), the following shall apply:
>
> > (A) If the retirement funds are in a retirement fund that has received a favorable determination under section 7805 of the Internal Revenue Code of 1986, and that determination is in effect as of the date of the filing of the petition in a case under this title, those funds shall be presumed to be exempt from the estate.[64]

Even plans that have not received this favorable determination are exempt from the estate, so long as the Internal Revenue Service has not found them to be otherwise and there is either substantial compliance with the IRC or the debtor is not materially responsible for such noncompliance.[65]

Now, even if some states may not allow retirement plans to be exempted from the reach of creditors, Congress has made this exemption applicable to all in bankruptcy by placing the language in section 522(b)(3)(C) to eliminate the opt-out.[66] Thus, either in an opt-out state or under the federal exemptions, the listed retirement funds are exempt from the bankruptcy estate. In addition, the qualified

---

[61] BAPCPA § 224(a)(1)(C) (to be codified at 11 U.S.C. § 522(b) (2) (c)) (referring to 26 U.S.C. § 408(A)) (showing that Roth IRAs are not eligible for rollovers because they are excluded from definition of "eligible retirement plans").

[62] *See* BAPCPA § 1501(b)(2) (to be codified at 11 U.S.C. § 101) (providing application of amendments and certain limitations applicable to debtors).

[63] *See id*. (to be codified at 11 U.S.C. § 101) (referring to I.R.C. § 457).

[64] *See id*. at § 224 (to be codified at 11 U.S.C. § 522(b)(4)(A)).

[65] *See id*. (to be codified at 11 U.S.C. § 522(b)(4)(B)) (asserting protection of retirement savings in bankruptcy).

[66] *See id*. Note that some states had questioned whether a distribution from such plans would be exempt under state law; *see, e.g., In re* Neto, 215 B.R. 939 (Bankr. D.N.J. 1997) (applying New Jersey law to hold certain annuities may not be excluded from estate). *But see In re* Schuster, 256 B.R. 701 (Bankr. D.N.J. 2000) (declaring annuities exempt from property of estate).

retirement plans are added to the list of federal exemptions.[67] These provisions thus "ensure[] that the specified retirement funds are exempt under state as well as Federal law."[68]

Both direct and indirect transfers are allowed by new section 522(b)(4)(C).[69] An example of a direct transfer would be when a debtor transfers, or "rolls," from trustee to trustee, a 401(k) into an IRA and the money never touches the debtor/taxpayer's hands.[70] Indirect rollovers are allowed as well, under section 522(b)(4)(D).[71] Analogous to the "rollover" provisions accorded new residences, it appears that qualified plan rollovers will be accorded favorable and consistent treatment under BAPCPA because only a qualified plan balance may be rolled over into a continuing plan. Here, potential for abuse is not as keen and rollover treatment is necessary to meet the mandates of qualified plan portability, so essential to a mobile and transient workforce such as the United States'. An example of such an indirect transfer is when one IRA is cashed out, the funds are delivered to the debtor/taxpayer and a new IRA account is opened within 60 days of receipt of the funds, inasmuch as the funds must be placed in the trust within 60 days.[72]

B. The $1,000,000 IRA Cap

Having established a broad base of exemptions for a variety of retirement plans, BAPCPA then set a monetary limit on the use of only one of these vehicles for asset protection. New section 522(n) imposes a $1,000,000 cap on any individual retirement account (IRA) or Roth IRA:

> (n) For assets in individual retirement accounts described in section 408 or 408A of the Internal Revenue Code of 1986, other than a simplified employee pension under section 408(k) of such Code or a simple retirement account under section 408(p) of such Code, the aggregate value of such assets exempted under this section ... shall not exceed $1,000,000 in a case filed by a debtor who is an

---

[67] *See* BAPCPA § 224 (to be codified at 11 U.S.C. § 522(b)(2)(D) (providing amendments for protection of retirement savings in bankruptcy).

[68] H.R. REP. NO. 109-31, pt. 1, at 64 (2005), *available at* 2005 U.S.C.C.A.N. 88, 133.

[69] *Id*.; *see* BAPCPA § 224(a) (to be codified at 11 U.S.C. § 522(b)(4)(C)) ("A direct transfer of retirement funds . . . shall not cease to qualify for exemption . . . by reason of such direct transfer.").

[70] *See* 26 U.S.C. § 401(a)(31)(2000) (specifying "such [eligible rollover distribution] shall be made in the form of a direct trustee-to-trustee transfer to the eligible retirement plan . . . .").

[71] *See* BAPCPA § 224(a) (to be codified at 11 U.S.C. § 522(b) (2) (D)) (exempting "any distribution that qualifies as an eligible rollover distribution within the meaning of section 402(c) of the Internal Revenue Code of 1986").

[72] *See* 26 U.S.C. § 402(c)(1), (3) (2000) (listing rules applicable to rollovers from exempt trusts). The key is for these funds to be held first in an "eligible retirement plan." *See supra,* note 60 and accompanying text.

> individual, except that such amount may be increased if the interests of justice so require.[73]

This part of the legislation effectively limits a decision of the United States Supreme Court, rendered after passage of BAPCPA by the Senate, which suggested that the federal exemption under the terms of former section 522(d)(10)(E) would be unlimited. In *Rousey v. Jacoway*,[74] the Supreme Court reversed the Eighth Circuit to hold that chapter 7 debtors with access to the federal exemption scheme (*i.e.*, whose states have not "opted out" under former section 522(b)(1))[75] could exempt their entire IRAs from the bankruptcy estate under section 522(d)(10)(E).

That provision, which was not amended by BAPCPA (except for the $1,000,000 cap on IRAs in subsection (n)), provides that a debtor may withdraw from the bankruptcy estate his or her

> right to receive—(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 . . . .[76]

Justice Thomas, speaking for a unanimous Court, concluded that IRAs fulfill the requirements of that Bankruptcy Code exemption because all of the plans enumerated in section 522(d)(10)(E) provide income that is a substitute for salary or wages.[77] The opinion rejected the chapter 7 trustee's argument that the funds should not be exempt because the debtors could use funds in their IRAs prior to reaching the age of 59½ years; the Court's rationale was that the 10% penalty for early

---

[73] BAPCPA § 224(e) (to be codified at 11 U.S.C. § 522(n)). Note again that, although BAPCPA may cap the amount of a Roth IRA that may be exempted at $1,000,000, such accounts do not qualify for rollovers because they are excluded from the definition of "eligible retirement accounts."

[74] 125 S. Ct. 1561, 1566 (2005); *see* Serena Thompson Green, *Recent Development*, 58 ARK. L. REV. 471, 471–72 (2005) (summarizing recent Supreme Court holding in *Rousey*); Hon. James D. Walker, Jr. & Amber Nickell, *Bankruptcy*, 56 MERCER L. REV. 1199, 1205–06 (2005) (discussing Supreme Court's analysis in *Rousey* in concluding that IRAs meet requirements for exemption).

[75] *See* 11 U.S.C. § 522(b)(1) (2000) (allowing exemption of property specified in subsection (d) of this section "unless the State law that is applicable to the debtor . . . specifically does not so authorize . . . .").

[76] 11 U.S.C. § 522(d)(10)(E) (2000). This exemption is limited if "(i) such plan or contract was established by or under the auspices of an insider that employed the debtor at the time the debtor's rights under such plan or contract arose; (ii) such payment is on account of age or length or service, and (iii) such plan or contract does not qualify under section 401(a), 403(a), 403(b), or 408 of the Internal Revenue Code." *Id*. (qualifying parameters of certain exemptions).

[77] *See id*. (indicating plans similar to those specifically enumerated are exempt); *Rousey*, 125 S. Ct. at 1568 (agreeing with petitioner's assertion IRA's are similar to itemized agreements exempted by Code); BROWN & AHERN, *supra* note 2, at 77 (analyzing court's decision IRA's are similar to other agreements expressly stated in Code).

withdrawal was substantial and prevented the debtor from reaching all the funds.[78] Without the amendment establishing the $1,000,000 cap found in new section 522(n), the effect of *Rousey* seems to have been to permit an unlimited amount of IRA exemptions, so long as the debtor could satisfy section 522(d)(10)(E)'s "reasonably necessary" test (*i.e.*, that the funds are reasonably necessary for the support of the debtor and any dependent). The reasonably necessary test was not disputed in *Rousey*.[79]

The Supreme Court's reasoning in *Rousey* seems applicable to a broad range of tax-qualified, retirement investment vehicles, because payments under an IRA are exempt only because the IRA is "similar" to "a payment under a stock bonus, pension, profitsharing [or] annuity . . . ."[80] In other words, the *Rousey* decision, by holding IRAs exempt, acknowledged the exemption of payments under any other such "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 . . . ."[81]

The $1,000,000 limit on the debtor's exemption for IRAs is in addition to rollovers from other kinds of more favored retirement plans. Thus, the $1,000,000 is calculated, "without regard to amounts attributable to rollover contributions under section 402(c), 402(e)(6), 403(a)(4), 403(a)(5), and 403(b)(8) of the Internal Revenue Code of 1986, and earnings thereon . . . ."[82]

---

[78] *See Rousey*, 125 S. Ct. at 1567 (holding tax penalty of 10% for early withdrawal is substantial enough to categorize IRA's as providing payment on account of age); BROWN & AHERN, *supra* note 2, at 77 (noting court's reasoning 10% early withdrawal fee defeats argument because individuals can withdraw funds before age of 59 ½, these funds should not be exempt); Hon. James D. Walker, Jr. and Amber Nickell, *Bankruptcy*, 56 MERCER L. REV. 1199, 1205–06 (2005) (discussing court's reasoning for classifying IRA's on account of age).

[79] *See Rousey*, 125 S. Ct. at 1566 (acknowledging but not addressing reasonably necessary test as applicable to exempt IRA's from bankruptcy estate); *see also supra* note 52 and accompanying text (discussing language distinctions among section 522(d) (10) (E), section 522(q) and section 523(a) (2) (C) with respect to debtors and their dependents). *But see* Serena Thompson Green, *Bankruptcy Law*, 58 ARK. L. REV. 471, 472 (2005) (stating *Rousey* court did not use reasonably necessary test).

[80] 11 U.S.C. § 522(d)(10)(E) (2000). *Rousey*, however, seems only to address IRAs, leaving uncertainty as to plans qualified under sections 408A (Roth IRAs), 401, 403 & 408, 414, 457 and 501(a). *Rousey*, 125 S. Ct. at 1561; *cf.* BROWN & AHERN, *supra* note 2, at 74–6 (showing how new Code provisions address contracts under sections 408A (Roth IRAs), 401, 403 & 408, 414, 457 and 501(a), since they were previously unresolved).

[81] 11 U.S.C. § 522(d)(10)(E) (2000). The Court recognized the breadth of this exemption, remarking that "[t]he common feature of all of these plans is that they provide income that substitutes for wages earned as salary or hourly compensation . . . . As a general matter, it makes little sense to exclude from the exemption plans that fail to qualify under § 408 , unless all plans that do qualify under § 408, including IRAs, are generally within the exemption." *Rousey*, 125 S. Ct. at 1571; *see* Green, *supra* note 79, at 472 (remarking on court's conclusion IRA's and similar plans are substitutes for wages).

[82] BAPCPA § 224(e)(1) (to be codified at 11 U.S.C. § 522(n)) (imposing $1,000.00 cap on exemption regardless of source of funds); *see* Margaret Howard, *Exemptions Under the 2005 Bankruptcy Amendments: A Tale of Opportunity Lost*, 79 AM. BANKR. L.J. 397, 417 (2005) (explaining operation of $1,000.00 cap on

While there is little legislative history explaining the provisions of BAPCPA, Congress made this broad policy in favor of retirement plans clear, "The intent of section 224 [of BAPCPA] is to expand the protection for tax-favored retirement plans or arrangements that may not be already protected under Bankruptcy Code section 541(c)(2) pursuant to *Patterson v. Shumate*, or other state or Federal law."[83]

Thus, qualified transfers between qualified plans (trustee-to-trustee transfers and the transfer from a qualified defined contribution or defined benefit plan to a self-directed IRA over which the plan beneficiary goes from "no control" to almost "total control") are permissible and protected under the new Act. In structuring the $1,000,000 cap, Congress could have taken more effective action by not only adding such a dollar volume cap but also a limitation on the number of years of prior funding involved in attaining the cap, had more serious consideration been given to anti-churning measures and the potentials for abuse in this area.

Finally, under new section 362(b)(19), the automatic stay does not apply to income withheld and used to pay down loans from retirement plans.[84] Congress thus has again shown approval of maintenance of such funds, but this could have broader consequences, as debtors may borrow against their 401(k)s, etc. and could pay the loan back ahead of other creditors. The language in section 362(b)(19), however, makes it clear that exempting income used to pay down retirement plan loans does not mean the debtor has a claim against the estate for the balance due on such loans. Compare this with section 523(a)(18) excepting such loans from discharge, where no such clarifying language appears.[85] Although it would appear that Congress intended that such loans "pass through" untouched by the bankruptcy process, one might anticipate continued litigation on this issue.

C. Exclusions from the Estate

In addition to the exemptions provided and enhanced in BAPCPA, Congress also made significant changes in exclusions from the bankruptcy estate by amendments to section 541(b), designed to protect certain education IRAs and similar funds. This was done by renumbering current subsection (5) to (9) and adding the following subsections:

> (5) funds placed in an education individual retirement account (as defined in section 530(b)(1) of the Internal Revenue Code of 1986)

---

exemptions despite its source from codified plans); *see also* BROWN & AHERN, *supra* note 2, at 77 (observing new $1,000,000.00 cap on IRA exemptions).

[83] H. Report No. 109-31 to accompany S. 256, 109th Cong., 1st Sess. (2005) pp. 63-64 (citation omitted); available at 2005 U.S.C.C.A.N. 88 at 132-33; *see* Patterson v. Shumate, 504 U.S. 753, 763 (1992). Note that *Patterson* only addressed ERISA-qualified plans and did not express any opinion on the scope of the exemption provided by section 522(d) (10) (E). *See Patterson*, 504 U.S.. at 763.

[84] BAPCPA § 224 (to be codified at 11 U.S.C. § 522).

[85] 11 U.S.C. § 523(a)(18) (2000). *See* BAPCPA § 215 (to be codified at 11 U.S.C. § 523).

not later than 365 days before the date of the filing of the petition in a case under this title, but —

(A) only if the designated beneficiary of such account was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were placed in such account;

(B) only to the extent that such funds—

(i) are not pledged or promised to any entity in connection with any extension of credit; and

(ii) are not excess contributions (as described in section 4973(e) of the Internal Revenue Code of 1986); and

(C) in the case of funds placed in all such accounts having the same designated beneficiary not earlier than 720 days nor later than 365 days before such date, only so much of such funds as does not exceed $5,000;

(6) funds used to purchase a tuition credit or certificate or contributed to an account in accordance with section 529(b)(1)(A) of the Internal Revenue Code of 1986 under a qualified State tuition program (as defined in section 529(b)(1) of such Code) not later than 365 days before the date of the filing of the petition in a case under this title, but—

(A) only if the designated beneficiary of the amounts paid or contributed to such tuition program was a child, stepchild, grandchild, or stepgrandchild of the debtor for the taxable year for which funds were paid or contributed;

(B) with respect to the aggregate amount paid or contributed to such program having the same designated beneficiary, only so much of such amount as does not exceed the total contributions permitted under section 529(b)(7) of such Code with respect to such beneficiary, as adjusted beginning on the date of the filing of the petition in a case under this title by the annual increase or decrease (rounded to the nearest tenth of 1 percent) in the education expenditure category of the Consumer Price Index prepared by the Department of Labor; and

(C) in the case of funds paid or contributed to such program having the same designated beneficiary not earlier than 720 days nor later than 365 days before such

> date, only so much of such funds as does not exceed $5,000.[86]

The debtor has a special duty related to these education IRAs and similar funds:

> (c) In addition to meeting the requirements under subsection (a), a debtor shall file with the court a record of any interest that a debtor has in an education individual retirement account (as defined in section 530(b)(1) of the Internal Revenue Code of 1986) or under a qualified State tuition program (as defined in section 529(b)(1) of such Code).[87]

Section 541(b) is further expanded to exclude from the bankruptcy estate

> (7) any amount—
>
> (A) withheld by an employer from the wages of employees for payment as contributions—
>
> (i) to—
>
> (I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;
>
> (II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986; or
>
> (III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986; except that such amount under this subparagraph shall not constitute disposable income as defined in section 1325(b)(2); or
>
> (ii) to a health insurance plan regulated by State law whether or not subject to such title; or

---

[86] BAPCPA § 521 (to be codified at 11 U.S.C. § 541(b)) (adding another new subsection to clarify whether "the relationships specified in paragraph (5)(A) or (6)(A) of subsection (b) exists [sic]," by including as if "a child of such individual by blood" a legally adopted child and a child who is a member of the household, if placed there by an authorized placement agency for legal adoption and a foster child if the debtor's home is that child's "principal place of abode.").

[87] BAPCPA § 521 (to be codified at 11 U.S.C. § 541(c)).

> (B) received by an employer from employees for payment as contributions—
>
> (i) to—
>
> (I) an employee benefit plan that is subject to title I of the Employee Retirement Income Security Act of 1974 or under an employee benefit plan which is a governmental plan under section 414(d) of the Internal Revenue Code of 1986;
>
> (II) a deferred compensation plan under section 457 of the Internal Revenue Code of 1986;
>
> or
>
> (III) a tax-deferred annuity under section 403(b) of the Internal Revenue Code of 1986; except that such amount under this subparagraph shall not constitute disposable income, as defined in section 1325(b)(2); or
>
> (ii) to a health insurance plan regulated by State law whether or not subject to such title;[88]

Thus, the "exclusions include ERISA employee benefit plans and others types of benefit plans or tax-sheltered trusts or plans referred to in specific Internal Revenue Code sections:"[89]

> - "Coverdell" education savings accounts, "meaning a trust created or organized in the United States exclusively for the purpose of paying the qualified education expenses of an individual who is the designated beneficiary of the trust;"[90]
> - a "qualified tuition program," meaning "a program established and maintained by a State or agency or instrumentality thereof or by 1 or more eligible educational institutions," under which tuition credits may be purchased for a beneficiary;[91]

---

[88] BAPCPA § 322 (to be codified at 11 U.S.C. § 522(b)(7)).
[89] BROWN & AHERN, *supra* note 2, at 73.
[90] *Id*.
[91] BAPCPA § 225(a)(6) (to be codified at 11 U.S.C. § 541(b)(6)) (referring to 26 U.S.C. § 529(b)(1)).

- a "governmental plan" for retirement established and maintained by the United States, any state or political subdivision of a state;[92]
- an "eligible deferred compensation plan" established and maintained by an eligible employer;[93] and
- a "qualified annuity plan" purchased for an employee by certain employers that generally include religious, charitable, scientific, public safety, literary, or educational corporations and organizations.[94]

IV. SELF-SETTLED TRUSTS

Having thus established the broadly exempt status of qualified retirement funds and IRAs, at least up to the monetary cap on IRAs, BAPCPA makes one more attempt to limit the use of fiduciary accounts for asset protection.

> (e)(1) In addition to any transfer that the trustee may otherwise avoid, the trustee may avoid any transfer of an interest of the debtor in property that was made on or within 10 years before the date of the filing of the petition, if—
>
> (A) such transfer was made to a self-settled trust or similar device;
>
> (B) such transfer was by the debtor;
>
> (C) the debtor is a beneficiary of such trust or similar device; and
>
> (D) the debtor made such transfer with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made, indebted.
>
> (2) For the purposes of this subsection, a transfer includes a transfer made in anticipation of any money judgment, settlement, civil penalty, equitable order, or criminal fine incurred by, or which the debtor believed would be incurred by—
>
> (A) any violation of the securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(47))), any State securities laws, or any regulation or order issued under Federal securities laws or State securities laws; or

---

[92] *Id*. § 323(7)(A)(i)(I) (to be codified at 11 U.S.C. § 541(b)(7)(A)(i)(I)) (referring to 26 U.S.C. § 414(d)).

[93] *Id*. § 323(7)(A)(i)(II) (to be codified at 11 U.S.C. § 541(b)(7)(A)(i)(II)) (referring to 26 U.S.C. § 457).

[94] *Id*. § 323(7)(A)(i)(III) (to be codified at 11 U.S.C. § 541(b)(7)(A)(i)(III)) (referring to 26 U.S.C. § 403(b)).

> (B) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78l and 78o(d)) or under section 6 of the Securities Act of 1933 (15 U.S.C. 77f).[95]

Under this new provision of the trustee's independent powers under section 548 to avoid fraudulent transfers, the trustee in bankruptcy may avoid any transfer by the debtor, within 10 years before the filing of the petition, to a self-settled trust or :similar device," if the debtor is a beneficiary of the trust/device and the transfer was made with "actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made, indebted."[96]

A self-settled trust may be defined as a trust in which the settlor is also the person who is to receive the benefits from the trust, often established in an attempt to protect the trust assets from creditors.[97] As noted above,[98] such trusts have been the subject of recent legislation in several states, in an effort to avoid this long-standing rule and, in 2004, Oklahoma took the additional step of allowing such a vehicle to be either a revocable or irrevocable trust.[99]

In order to show the requisite, fraudulent intent that new section 548(e) requires, the trustee must relate the debtor's intent to actual (contemporaneous or subsequent) creditors, rather than merely showing that the debtor created the device and transferred an asset to it.[100] This "actual intent" language in new section 548(e) is substantially identical to the existing fraudulent transfer language of section

---

[95] *Id*. § 1402(4) (to be codified at 11 U.S.C. § 541(e)).

[96] *Id*. § 1402(4)(D) (to be codified at 11 U.S.C. § 541(e)(1)(D)). During the debate on Senate Bill 256, which became BAPCPA, the *New York Times* published an article describing domestic asset protection trusts as the "millionaires' loophole" in the legislation. Senator Charles Schumer introduced an amendment that would have protected only $125,000 in a DAPT. That amendment was defeated and the language quoted accompanying note 74 was the compromise offered by Senator Talent. *See supra* note 73, and accompanying text. David G. Shaftel & David H. Bundy, *Impact of New Bankruptcy Provision on Domestic Asset Protection Trusts*, 32 EST. PLAN. 28, 28 (July 2005); *see* 151 CONG. REC. S1980 (daily ed. Mar. 3, 2005) (dictating Senator Schumer's amendment); Gretchen Morgenson, *Proposed Law on Bankruptcy Has Loophole*, N.Y. TIMES, Mar. 2, 2005, at C1, C4.

[97] BLACK'S LAW DICTIONARY 1552 (8th ed. 2004) ("[A self-settled trust is a] trust in which the settlor is also the person who is to receive the benefits from the trust, usu[ally] set up in an attempt to protect the trust assets from creditors."); *see* RESTATEMENT (SECOND) OF TRUSTS § 156 (1959) (discussing self-settled trusts); Randall J. Gingiss, *Putting a Stop to "Asset Protection" Trusts*, 51 BAYLOR L. REV. 987, 1007 (1999) ("[T]he definition of a self-settled trust is one in which the grantor is or may become a beneficiary.").

[98] *See supra* notes 19–21 and accompanying text.

[99] *See supra* notes 20–21 and accompanying text.

[100] *See* BAPCPA § 1402(4) (to be codified at 11 U.S.C. § 548(e)) (indicating that trustee may avoid any transfer of an interest of debtor if it was made with intent to "hinder, delay, or defraud" creditor); BROWN & AHERN, *supra* note 2, at 77 (remarking that trustee must prove debtor made transfer to self-settled trust with intent to hinder, delay, or defraud specific creditor); Shaftel & Bundy, *supra* note 96, at 30 (noting if creditor discovered transfer to DAPT after four-year limitation period expired, creditor can file action and argue that transfer to DAPT was made with "intent to hinder, delay, or defraud creditor").

548(a)(1)(A). That general, fraudulent transfer avoidance power was expanded by extending its reach-back period from one year to two years under BAPCPA.[101] The language is also substantially identical to the language used in the Uniform Fraudulent Transfers Act ("UFTA"), which has been enacted in 42 states.[102] Thus, the new provision in section 548(e) is largely duplicative of existing law. It does not dramatically change the ground rules for asset protection planning, although it does enlarge the window through which a trustee may reach to set aside transfers without being required to find an actual unsecured creditor as to whom a particular transfer was voidable under UFTA and section 544(b) of the Bankruptcy Code.[103]

This is not all bad news for those with the means to set up an asset protection trust. Counsel should be cognizant, however, that the law is fairly ambiguous as to what "actual intent" may be and plan conservatively. Counsel should also be aware that while *Patterson v. Shumate*[104] has settled the question of inclusion of ERISA-qualified plans in the estate and *Rousey*[105] has settled the federal exemption question with respect to IRAs, several issues remain open, including the status of non-qualified plans and other, "similar" vehicles that may fall under the auspices of these provisions. It appears that asset protection planning may be business as usual without, for example, more adverse consequences to the planner for aiding and abetting criminality.

V. CHANGES IN DISCHARGE EXCEPTIONS

---

[101] BAPCPA § 1402(1) (to be codified at 11 U.S.C. § 548(1)(a), (b)) (extending reach-back to two years); *Id*. § 1406(b)(2) (to be codified at 11 U.S.C. § 507) (making § 1402(1) effective only in cases commenced on and after April 20, 2006); *see* Shaftel & Bundy, *supra* note 96 (indicating other transfers trustee may avoid such as a transfer of interest of debtor in property that was made on or within 10 years before the date of filing as long as certain conditions are met).

[102] *See* N.J. ANN. tit. § 25:2–25 (2005) (setting forth that transfer made by debtor is fraudulent if there was actual intent to hinder, delay, or defraud creditor); *see also* BROWN & AHERN, *supra* note 2, at 77 (stating terms for trustee to avoid any transfer of interest of debtor in property made on or within 10 years before filing of petition); Shaftel & Bundy, *supra* note 96, at 30 (asserting operative language "actual intent to hinder, delay, or defraud" is identical to language in Uniform Fraudulent Transfer Act).

[103] *See* 11 U.S.C. § 544(b) (putting forth trustee can avoid a transfer of interest of debtor or an obligation incurred by debtor "that is voidable under applicable law by a creditor holding an unsecured claim allowable under § 502 of this title or not allowable only under § 502 (e) of this title"); Shaftel & Bundy, *supra* note 96, at 31 (remarking that changes would clarify scope of amendment and make applications more certain); *see generally* BROWN & AHERN, *supra* note 2, at 31 (showing ways debtor may protect assets).

[104] 504 U.S. 753 (1992) (holding debtor's interest in ERISA-qualified pension plan may be excluded from property of bankruptcy estate pursuant to Code); *see* Ostrander v. Lalchandani (*In re* Lalchandani), 279 B.R. 880, 883 (B.A.P. 1st Cir. 2002) (noting *Patterson* decision and affirming court's ability to remove interest from bankruptcy estate); Shadduck v. Rodolakis, 221 B.R. 573, 581 (D. Mass. 1998) (agreeing with Bankruptcy Court's decision that debtor's interest in ERISA-qualified plan was excluded from estate).

[105] Rousey v. Jacoway, 125 S. Ct. 1561 (2005) (asserting that IRAs can be exempted from bankruptcy estate); *see In re* Guikema, No. 04-55750, 2005 Bankr. LEXIS 1558, at *11 (S. D. OH, April 14 2005) (indicating Federal bankruptcy law allows debtor to exempt basic necessities, such as car or home, from bankruptcy estate); *In re* Hand, 323 B.R. 14, 20 n.5 (stating *Rousey* allowed 10% of monies from IRA to be exempted from bankruptcy and estate and withdrawn).

Several revisions to the discharge rules in section 727(a) may also have an adverse effect on asset protection efforts. New subsection (12) provides that the court should not grant a discharge when there is "reasonable cause to believe" that the new $125,000 cap on exemptions, contained in section 522(q), applies or when there is a pending proceeding that may result in the application of section 522(q), to limit the debtor's exemption to $125,000.[106] Thus, the felonious debtor is penalized twice. First, section 522(q) may reduce the debtor's homestead to $125,000, regardless of when acquired. Then section 727(a)(12) may be applied to delay a discharge until the section 522(q) proceeding is concluded and the Court may determine the applicability of the $125,000 cap, the process of which may produce grounds for one or more exceptions to discharge.

Another revision of the dischargeability rules appears in new section 523(a)(18), which excepts from discharge loans from pension, profit-sharing, stock bonus, or other tax-sheltered plans.[107] This exception parallels the new exception to the automatic stay, extended to collection of such loans.[108]

---

[106] *See* BAPCPA § 330 (to be codified at 11 U.S.C. § 727(a)) (amending section 727(a) by inserting the following after paragraph (11): "the court . . . finds that there is reasonable cause to believe that — (A) section 522(q) (1) may be applicable to the debtor; and (B) there is pending any proceeding in which the debtor may be found guilty of a felony . . . described in section 522(q) (1) (A) or liable for a debt . . . described in section 522(q) (1) (B)[]"). Recall that new section 522(q) applies this limitation when the debtor has any felony conviction or any debt which is attributable to securities laws violations, regardless of when the conviction occurred, or crimes, torts or other misconduct causing serious physical injury or death within the past five (5) years. *See* BAPCPA § 322 (to be codified at 11 U.S.C. § 522) (indicating application of limitation if debt arises from "any violation of the Federal [or State] securities laws . . . fraud, deceit, or manipulation in a fiduciary capacity . . . any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years"); Samuel K. Crocker & Robert H. Waldschmidt, *Impact of the 2005 Bankruptcy Amendments on Chapter 7 Trustees*, 79 AM. BANKR. L.J. 333, 352 (2005) ("The homestead exemption may . . . be limited to $ 125,000 if the debtor has committed certain criminal or tortious acts defined within the section, under a new 522(q)."); COLLIER PORTABLE PAMPHLET: TEXT OF THE BANKRUPTCY CODE AND ADDITIONAL STATUTORY PROVISIONS 172–75 (Alan N. Resnick & Henry J. Sommer eds., Mathew Bender & Company, Inc. 2005) (explaining the new section 522(q) restricts the homestead exemption based on certain types of misconduct); *see also supra* notes 50–52 and accompanying text.

[107] *See supra* note 85 and accompanying text (discussing whether combined effect of this section and section 362(b) (19) means debtor has a claim against estate for balance due on loan); *see also* William Houston Brown, *Taking Exception to a Debtor's Discharge: The 2005 Bankruptcy Amendments Make It Easier*, 79 AM. BANKR. L.J. 419, 441 (2005) (noting debts covered by former subsection (18) are "now covered by the new definition of domestic support obligation[,] and stating new subsection (18) relates to exemptions related to a bankruptcy debtor); Melissa B. Jacoby, *Ripple or Revolution? The Indeterminacy of Statutory Bankruptcy Reform*, 79 AM. BANKR. L.J. 169, 174, 174 n.31 (2005) (citing section 523(a)(18) as revision intended to improve protection of debtor's assets by "insulat[ing] qualified retirement and educational funds from reach of creditors"); Lisa A. Napoli, *The Not-So-Automatic Stay: Legislative Changes to the Automatic Stay in a Case Filed by or against an Individual Debtor*, 79 AM. BANKR. L.J. 749, 752 (2005) (explaining under section 523(a)(18), debt owed to retirement plans "will be excepted from a debtor's discharge").

[108] *See supra* notes 84–85 and accompanying text; *see also* Brown, *supra* note 107, at 442 n.108 (explaining section 362(d)(19) excludes from automatic stay withholding of income and collections of amounts withheld from a debtor's wages for funds listed in 523(a) (18)); Jacoby, *supra* note 107, at 174 n.31 (noting section 362(b)(19) creates "exception to automatic stay for withholding of wages for pension loan

Language was also added by BAPCPA to section 727(d)(4), providing new grounds for revocation of a discharge. If the debtor fails to satisfactorily explain a material misstatement made in reference to an audit that is randomly required under new 28 U.S.C. § 586(f)[109] or fails to make required information available for such an audit, then the discharge is subject to revocation by request of the trustee, a creditor or the U.S. Trustee.

---

repayment" and section 523(a)(18) creates an "exception to discharge for debt to pension plan[s]"); Napoli, *supra* note 107, at 752 (stating in conjunction with new section 523(a)(18) which exempts debt owed to retirement plans, new section 362(b) (19) "provides that the automatic stay does not apply to withholding of income from a debtor's wages if the withheld funds are used to repay loans from retirement plans").

[109] *See* BAPCPA § 603 (to be codified at 11 U.S.C. § 727(d)) (amending paragraph 3 of section 727(d) to include, among other things, the following: "(B) a failure to make available for inspection all necessary accounts, papers, documents, financial records, files, and all other papers, things, or property belonging to the debtor that are requested for an audit referred to in section 586(f) of title 28"); Brown, *supra* note 107, at 422 (describing under new section 727(d) (4), a debtor's failure to cooperate in a randomly selected audit under new section 586 is grounds for revocation of discharge); COLLIER PAMPHLET, *supra* note 106, at 25 ("Section 727(d) is amended to provide that a discharge may be revoked for failure to satisfactorily explain a material misstatement found in an audit or to make documents or property available in an audit."). Section 586(f) is another new section added by BAPCPA. *See* BAPCPA § 603 (to be codified at 11 U.S. C. § 586(f)) (indicating addition of 586(f) to title 11 of the United States Code); *see generally* Brown, *supra* note 107, at 429 (discussing § 586(f)'s application in § 727(d) (4)); Jack Seward, *Empowerment of Creditor Rights: Section 727 Denial of Discharge and the BAPCPA of 2005*, AM. BANKR. INST. J., June 2005, at 18 (noting § 727(d) (4) applies when "the debtor has failed under §§ 727(d) (4) (A) and (B) to explain satisfactorily a material misstatement under § 586(f) of Title 28 and/or failed to make available documents, records, things or property belonging to the debtor under § 586(f) of Title 28"); Eugene R. Wedoff, *Means Testing in the New 707(b)*, 79 AM. BANKR. L.J. 231, 278, 278 n.124 (2005) (noting § 586(f) as a new section added by BAPCPA). It provides for random audits of the petitions, schedules or other information that the debtor is required to provide in chapter 7 and 13 cases. *See* BAPCPA § 603 (to be codified at 11 U.S.C. § 586(f)) (amending § 586 of title 28 of United States Code to include "(f) (1) The United States trustee for each district is authorized to . . . perform audits in cases designated by the United States trustee, in accordance with the procedures established under section 603(a) of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005[]"); Wedoff, *supra*, at 277, 278 n.124 (indicating all scheduled information are subject to random audit under new § 586(f); *see also* Brown, *supra* note 107, at 422 n.10 (indicating under BAPCPA, United States trustee must "conduct random audits in at least one out of every 250 bankruptcy cases in each judicial district"). Audits are also required when the debtor's schedules of income and expenses reflect greater than average variances from the statistical norm for the district in which the case is filed. BAPCPA § 603 (to be codified at 11 U.S.C. § 586) (requiring "audits of schedules of income and expenses that reflect greater than average variances from the statistical norm of the district in which the schedules were filed if those variances occur by reason of higher income or higher expenses than the statistical norm of the district"); COLLIER PAMPHLET, *supra* note 106, at 25 (discussing amendment requiring "audits of cases with greater than average variations above the statistical norm for income or expenses"); *see generally* Susan Jensen, *A Legislative History of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 79 AM. BANKR. L.J. 485, 486, 489–90 (2005) (commenting dissenting commissioners of National Bankruptcy Review Commission in 1994 proposed "requiring audits, under certain circumstances"). The audits are conducted under generally accepted auditing standards; and, upon the discovery of a material misstatement, the U.S. Trustee is authorized to commence an adversary proceeding to revoke the debtor's discharge. *See* BAPCPA § 603 (to be codified at 11 U.S.C. § 586) (providing "[s]uch audits shall be in accordance with generally accepted auditing standards . . . . If a material misstatement of income or expenditures or of assets is reported, the United States trustee shall . . . commenc[e] an adversary proceeding to revoke the debtor's discharge pursuant to section 727(d) of title 11[]"); Brown, *supra* note 107, at 429 (noting amendment's authorization of revocation for failing to satisfactorily explain a material misrepresentation in an audit); COLLIER PAMPHLET, *supra* note 106, at 25 (explaining audit procedure as amended by BAPCPA); Brown, *supra* note 107, at 429 (indicating revocation of discharge requires an adversary proceeding).

In the spirit of the asset-protection changes, several changes have also been made to section 523(a)(2)(C), the presumption that certain debts for luxury goods or services[110] are nondischargeable under section 523(a)(2)(A) if they are incurred on the eve of bankruptcy. Under former law, the exception applied to debts incurred in an aggregate amount of more than $1,225 to a single creditor within sixty (60) days before commencement of the case. The amount is now reduced to $500 and the time period extended to ninety (90) days, thereby enlarging the basket of nondischargeable "luxury" debts in two dimensions. Similarly, under former law, cash advances aggregating more than $1,225 to a single creditor, and incurred during the sixty (60) days preceding the filing of the bankruptcy case, were presumed nondischargeable. Now, the amount has been reduced to $750 and the time period lengthened to seventy (70) days, again casting a much larger net.[111]

---

[110] *See* BAPCPA § 310 (to be codified at 11 U.S.C. § 523(a)(2)(C)) (amending limitation on luxury goods); Brown, *supra* note 107, at 431–32 (explaining BAPCPA lowered "threshold amount for excepted purchase of luxury goods and services by a consumer debtor" to $500, and increased look-back period to ninety days); Jacoby, *supra* note 107, at 173, 173 n.23 (citing § 523(a)(2)(C) as a revision to the Bankruptcy Code). "Luxury goods and services" is a phase not defined in the Code and has become a source of much litigation with little clarity resulting. *See In re* Lacrosse, 244 B.R. 583, 587 (Bankr. M.D. Pa. 1999) (stating Bankruptcy Code only defines "luxury goods and services" in the negative and courts have "'considered whether under circumstances of each particular case the purchases or transactions were 'extravagant,' 'indulgent,' or 'nonessential.'" (quoting *In re* Hernandez, 208 B.R. 872, 880 (Bankr. W.D. Tex. 1997)); *In re* Meyer, 296 B.R. 849, 865 (Bankr. N.D. Ala. 2003) ("Section 523(a)(2)(C) does not define what 'luxury goods and services' are, but it defines what they are not"); *In re* Simpson, 319 B.R. 256, 261 (Bankr. M.D. Fla. 2003) (declaring Bankruptcy Code gives "no precise definition" for "luxury goods or services"). For example, Ohio would not let the debtor have his discharge when the item purchased was personal investment strategies tapes. *In re* Orecchio, 109 B.R. 285, 288 (Bankr. S.D. Ohio 1989) (concluding "[d]ebtor's debt to FCC for [strategies tapes] incurred within the 40 day period does not aggregate more than $ 500.00 and is, therefore, not within presumption of § 523(a)(2)(C)" which presumes nondischargeability); *see In re Simpson*, 319 B.R. at 262 n.15 (noting *Orecchio* court found personal investment strategy tapes luxury goods since not needed for debtor's support); *see generally In re* Larisey, 185 B.R. 877, 881 (Bankr. M.D. Fla. 1995) ("The presumption of nondischargeability is invoked when the debts were for 'luxury goods or services' exceeding $ 500.00 and incurred within 40 days of filing bankruptcy."). If he could keep the tapes, might he not learn how to avoid bankruptcy?

[111] *See* BAPCPA § 310 (to be codified at 11 U.S.C. § 523(a) (2) (C)) (amending § 523(a)(2)(C) of Bankruptcy Code to include "cash advances aggregating more than $ 750 that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within 70 days before the order for relief under this title, [which] are presumed to be nondischargeable"); COLLIER PAMPHLET, *supra* note 106, at 11 (explaining amendment to § 523(a)(2)(C) creates a presumption of fraud if the debtor "obtains cash advances on an open end credit account in excess of $ 750 within 70 days before the order for relief"). Similar to both section 522(q) (which limits exemptions on otherwise qualified property to $125,000 if the debtor has any felony conviction or any debt arising from securities laws violations, regardless of when they occurred, or crimes, torts or other misconduct causing serious physical injury or death within the past five (5) years) and section 522(d) (10) (E) (exempting payments under certain IRC qualified plans), 523(a)(2)(C) also carves out amounts required for the support and maintenance of the debtor OR any dependent. *See* 11 U.S.C § 522(d)(10)(E) (2000) (exempting "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" unless exceptions apply); BAPCPA § 322 (to be codified at 11 U.S.C. § 522(q)) (providing "a debtor may not exempt . . . [above-described] . . . which exceeds in the aggregate $ 125,000 if— . . . debtor has been convicted of a felony . . . or . . . the debtor owes a debt arising from— any violation of [securities laws violations] . . . or . . . any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or

VI. THE FUTURE OF ASSET PROTECTION

What can we anticipate of the long-term effect of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 generally on the practice of asset protection planning? This consideration of future possibilities must begin with another word of history because IRAs and similar devices, themselves, are often in the nature of self-settled trusts. Thus, much early litigation over the status of these assets in bankruptcy turned on the proposition that such trusts historically could not be placed beyond the reach of creditors.[112]

This long-standing view of self settled trusts changed significantly with the Supreme Court's decision in *Patterson v. Shumate*.[113] In *Patterson*, the Court declared that an ERISA-qualified plan could in fact be excluded from the

---

death to another individual in the preceding 5 years"); BAPCPA § 310 (to be codified at 11 U.S.C. § 523(a)(2)(C)) ("[T]he term 'luxury goods or services' does not include goods or services reasonably necessary for the support or maintenance of the debtor or a dependent of the debtor."). However, section 522(q) and section 522(d)(10)(E) are phrased in the conjunctive, "debtor *and* any dependent," rather than the alternative "or." *See* 11 U.S.C. § 522(d)(10)(E) (2000) (exempting payments under certain plans "to the extent reasonably necessary for the support of the debtor and any dependent of the debtor"); BAPCPA § 322 (to be codified at 11 U.S.C. § 522(q)) (providing "[p]aragraph (1) shall not apply to the extent the amount of [the] interest in property . . . is reasonably necessary for the support of the debtor and any dependent of the debtor"); Brown, *supra* note 107, at 427 (explaining amendments to § 522). Why would Congress use "debtor and any dependent" in section 522(d)(10)(E) and section 522(q), but use "debtor or any dependent" in section 523(a)(2)(C)? *See generally id*; Crocker & Waldschmidt, *supra* note 41, at 349–54 (discussing 2005 amendments to exemption scheme in § 522); Jacoby, *supra* note 107, at 174, 174 n.31 (citing 2005 amendments to § 522 as those which increase protection of certain debtor assets); *see also supra* notes 52–53 and accompanying text (discussing language distinctions among section 522(d)(10)(E), section 522(q) and section 523(a)(2)(C) with respect to debtors and their dependents). Although dependent does include a spouse in section 522 (and only in section 522, for some reason), what about single debtors without dependents? *See* 11 U.S.C. § 522 (2000) (providing "dependent includes spouse"); *see generally* 4 COLLIER ON BANKRUPTCY § 522.03 (Alan N. Resnick, & Henry J. Sommer eds., 15th ed. rev. 2005) ("The definition of dependent in section 522(a) (1) indicates only that the debtor's spouse is included in the definition. It does not indicate what other persons are considered dependents for purposes of section 522(d)."); Crocker & Waldschmidt, *supra* note 41, at 349–54 (discussing 2005 amendments to exemption scheme in § 522). In contrast, under subsection 522(q), even the single debtor may also be the wrongdoer that has a felony conviction or debt attributable to securities laws violations that occurred any time prior to filing or any other debt arising from wrongdoing that caused serious physical injury or death within the past five years, suggesting that the restrictive provision in section 522 may be deliberate. *See generally* BAPCPA § 322 (to be codified at 11 U.S.C. § 522(q)) (providing "a debtor may not exempt . . . [above-described] . . . which exceeds in the aggregate $ 125,000 if— . . . debtor has been convicted of a felony . . . or . . . the debtor owes a debt arising from-- any violation of [securities laws violations] . . . or . . . any criminal act, intentional tort, or willful or reckless misconduct that caused serious physical injury or death to another individual in the preceding 5 years"); Crocker & Waldschmidt, *supra* note 41, at 349–54 (discussing 2005 amendments to exemption scheme in § 522); COLLIER ON BANKRUPTCY, *supra*, § 522.03 (discussing incorporation of spouse as dependent in § 522(a)(1)).

[112] There has historically been "a well accepted conclusion, that a revocable trust is subject to the claims of the settlor's creditors while the settlor is living. *See* Restatement (Third) of Trusts § 25 cmt. e (tentative draft No. 1, approved 1996." Uniform Trust Code § 15-505 cmt. (observing "the drafters rejected the approach taken in the states like Alaska and Delaware, both of which allow a settlor to retain a beneficial interest immune to creditor claims").

[113] 504 U.S. 753 (1992).

bankruptcy estate, based on the fact that ERISA contains a mandate that all qualified plans contain anti-alienation language, which effectively places them outside the reach of creditors. In the underlying case, the trustee in bankruptcy sought to set aside the debtor's ERISA-qualified plan using section 544(a) of the Bankruptcy Code, the so-called "strong-arm clause" that vests the trustee with all the powers of a hypothetical judgment lien creditor.

> Following *Patterson*, courts have held that bankruptcy estates do not include a debtor's beneficial interest in assets held by the trustees of a municipal employees' retirement plan, a retirement plan that might no longer qualify under ERISA, a 401(k) Plan in which the Service sought to secure a claim, a Keogh plan, a 403(b) Plan, or an IRA.[114]

Several questions still remain after *Patterson* and BAPCPA. Can such plans still be set aside as fraudulent transfers? Such an attack could be brought by the trustee two ways. First, the trustee can proceed under section 548,[115] which gives the trustee expanded, free-standing power to set aside fraudulent transfers and now allows the trustee to reach back two years prior to bankruptcy. The attack might also be launched from section 544(b) of the Bankruptcy Code[116] if there is an actual, unsecured creditor as to whom the transfer was subject to attack under non-bankruptcy law. Such attacks have been successful.[117]

The question resolved by *Rousey* was whether IRAs could be held to be exempt under section 522(d)(10)(E). *Rousey* answered that question in the affirmative but also did so using very broad language to describe IRAs as "similar" to the various benefit plans described in that federal exemption. It seems, from a view of the new language in section 522 that this semantic effect of *Rousey* has been expanded to reach a broad range of federal exemptions for retirement plans, while the economic effect has been capped at $1,000,000 with respect to IRAs.

---

[114] *See* Richard W. Nenno, *Planning With Domestic Asset-Protection Trusts: Part 1*, 40 REAL PROP. PROB. & TR. J. 263, 321 (2005) (citations omitted); *Rousey*, 125 S. Ct. at 1566 (2005) (concluding "IRA's can be exempted from the bankruptcy estate"); *see, e.g.*, Ostrander v. Laichandani (*In re* Laichandani), 279 B.R. 880, 886 (B.A.P. 1st Cir. 2002) (holding debtor's undistributed interest in her former husband's pension plan "is not property of her bankruptcy estate").

[115] 11 U.S.C. § 548(a) (2000).

[116] 11 U.S.C. § 544(b) (2000).

[117] *See, e.g.*, Tavenner v. Smoot, 257 F.3d 401, 404 (4th Cir. 2001) (holding trustee may "avoid a transfer of potentially exempt property on the ground that the debtor transferred the property with the intent to hinder, delay or defraud creditors under 11 U.S.C. § 548"). *See also* COLLIER, COLLIER LENDING INST. AND THE BANKR. CODE ¶ 3.06 (2004) (admonishing "creditors should also bear in mind that courts have also held that property that is potentially exempt from the debtor's estate can still be amenable to avoidance and recovery actions"). *But see* Anderson v. Hooper (*In re* Hooper), 274 B.R. 210, 216 (Bankr. D. S.C. 2001) (finding insufficient evidence in trustee's claim that debtor "retained a secret interest in the property").

This is done in the first instance by new subsection 522(n), which exempts both qualified plans and nearly-qualified plans and, when coupled with *Patterson*, builds on a broad inclination by the Supreme Court to defer to Congress in the placement of such assets outside the estate. This suggests that these new sections will make it very difficult to attack such plans as self-settled trusts.

The remaining question, however, is the approach that the Supreme Court will take to the interplay of exemptions and avoidance actions after BAPCPA. Because the Supreme Court has demonstrated a reluctance to look hard at the devices adopted by this Congress for exempting such funds, it may be difficult to expand the attack beyond the new allowance under section 548(e). However, if the courts do not choose to view all retirement plans as simply out of reach, as suggested by *Patterson* and *Rousey*, trustees may still hope to implement their powers under sections 544(b) and 548(a), to supplement the new power under section 548(e).

Perhaps the strongest argument in favor of this approach for trustees, within the four corners of BAPCPA, is the detailed exclusionary language added to section 541(b) and described in detail above.[118] The statutory argument here is that Congress clearly selected education trusts, healthcare plans and similar funds to be placed completely outside the bankruptcy estate. The other protections for retirement and similar funds are merely exemptions and such funds are inherently part of the estate, simply subject to being claimed as an exemption. Exempt property is first included as property of the estate and then, if properly claimed, revested in the debtor.[119] Thus, "[t]o claim an exemption, a debtor must file a list of the property claimed as exempt under § 522(b)."[120] It is the debtor's burden to claim and establish the exemption.[121] The courts should recognize this distinction, despite the Supreme Court's broad deference to congressional exemptions in its limited exposure to the issue.

CONCLUSION

---

[118] *See supra* text accompanying note 86–93.

[119] *See* EXEMPTION MANUAL § 2.21; *In re* Luttrell, 313 B.R. 751, 754 (Bankr. E.D. Tenn. 2004) (indicating "assets are property of estate" and then, if properly claimed, are "subtracted from the bankruptcy estate and not distributed to creditors"); *In re* Latham, 317 B.R. 733, 736 (Bankr. E.D. Tenn. 2004) (stating exempted property "is subtracted from the bankruptcy estate and not distributed to creditors"); *see also In re* Arwood, 289 B.R. 889, 892 (Bankr. E.D. Tenn. 2003) (explaining policy of subtracting exempted property from bankruptcy estate "is to provide the debtor with the basic necessities of life so that he will not be left entirely destitute by his creditors").

[120] *See generally In re* Rolland, 317 B.R. 402, 413 (Bankr. C.D. Cal. 2004) (citing language from 11 U.S.C. § 522(l)).

[121] *In re* Edmonds, 27 B.R. 468, 469 (Bankr. M.D. Tenn. 1983) (stating "the burden is upon the debtor to claim property as exempt"); *In re* Hill, 95 B.R. 293, 299 (Bankr. N.D. N.Y. 1988) (quoting Bankruptcy Judge Keith M. Lundin noting "the burden is upon the debtor to claim property as exempt"). *But see* Hodes v. Jenkins (*In re* Hodes), 308 B.R. 61, 66 (B.A.P. 10th Cir. 2004) (indicating a presumption towards exemptions that creditor must first produce evidence to rebut before burden "shifts back to the debtor to show the exemption was proper").

Congress made a credible attempt in BAPCPA to limit venue-shopping for homestead and exemption planners and also made a comprehensive effort to exempt and exclude a variety of retirement and other savings funds, designed to promote a public policy in favor of encouraging such saving. Beyond that, however, BAPCPA imposes a dollar limitation on only a small number of such funds (IRAs and Roth IRAs), which are capped at $1,000,000 and, while Congress has opened the door to attacks on self-settled trusts, with a larger, ten-year period within which such transfers may be examined, this examination is limited to trusts set up with actual intent to hinder, defraud or delay actual creditors. This may be supported by the expansion of the trustee's general power to set aside fraudulent conveyances by reaching back as much as two years.

This enhancement of the fraudulent transfer provisions of the Bankruptcy Code may not be sufficient to reverse the Supreme Court's strong apparent inclination to defer to Congress whenever such funds are the subject of exclusion or exemption. The fact that BAPCPA distinguishes between certain funds that are exempt and others that are excluded, however, provides the trustee in bankruptcy an argument with which to seek the limitation of the broad deference to Congress that is evidenced by the *Patterson* and *Rousey* decisions.

In sum, however, it seems unlikely that these provisions add little to discourage the determined asset protection planner who is inclined to move assets into offshore vehicles, which seem to be poorly regulated by other federal law. Thus, while the revised Bankruptcy Code implements a public policy with respect to retirement funds that may be worthy, it seems unlikely to impede substantially the growth of the asset-protection industry.