Asset Protection for IRAs, Education IRA (Coverdell Accounts), 529 Plans, Qualified Plans, Qualified and Non-Qualified Annuities and Insurance in Ohio

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Author:

Edwin P. Morrow III, J.D., LL.M., MBA, CFP®, RFC®
Certified Specialist in Estate Planning, Probate & Trust
Through the Ohio State Bar Association

Wealth Strategies Specialist
Key Private Bank
Investment and Trust Services
10 W. Second St.
Dayton, OH 45042
937-285-5343
Edwin_P_Morrow@keybank.com

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Outline and Agenda

While effort is made to ensure the material is accurate, this material is not intended as legal advice and no one may rely on it as such.

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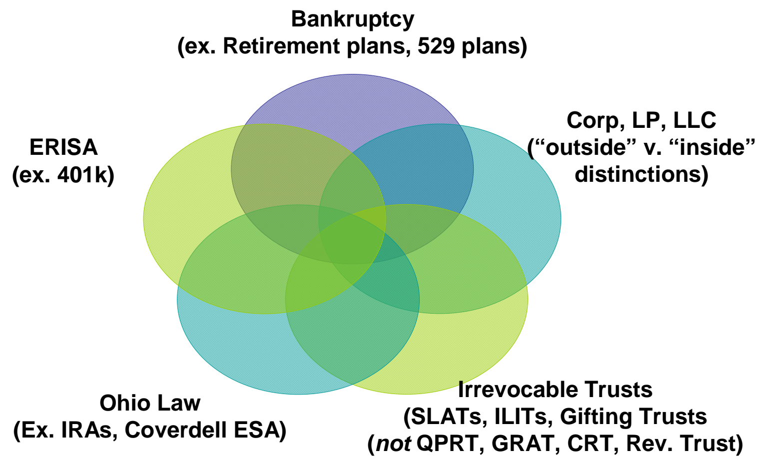
I. The Importance of Asset Protection as Part of Financial and Estate Planning

Asset Protection has become a buzz-word in the legal and financial community. It often means different things to different people. It may encompass anything from buying umbrella liability insurance to funding offshore trusts. What is most likely to wipe out a client's entire net worth? Investment scam, investment losses, a lawsuit, divorce or long-term care? "Asset Protection" may be construed to address all of these scenarios, but this outline will cover risk from creditors as opposed to risk from bad investments, divorce, medical bills or excessive spending.

Prudent business practice and limited liability entity use (LP, LLP, LLC, Corporation, etc) is the first line of defense against such risks. Similarly, good liability insurance and umbrella insurance coverage is paramount. However, there is a palpable fear among many of frivolous lawsuits and rogue juries. Damages may exceed coverage limits. Moreover, insurance policies often have gaps in coverage (e.g. intentional torts, "gross" negligence, asbestos or mold claim). As some doctors in Ohio know too well, malpractice insurance companies can fail, too.

Just as we advise clients regarding legal ways to legitimately avoid income and estate taxes or qualify for benefits, so we advise how to protect family assets from creditors. Ask your clients, "What level of asset protection do you want for yourself? For the inheritance you leave to your family?" Do any clients answer "none" or "low"? Trusts that are mere beneficiary designation form substitutes are going out of style in favor of "beneficiary-controlled trusts", "inheritance trusts" and the like.

This outline will discuss the sometimes substantial difference in legal treatment and protection for various investment vehicles and retirement accounts, with some further discussion of important issues to consider when trusts receive such assets. Beware of general observations like: "retirement plans, insurance, IRAs and annuities are protected assets" – that may often be true, but Murphy's law will make your client the exception to the general rules. The better part of this outline is pointing out those exceptions.


Overlapping Asset Protection
Bankruptcy
(ex. Retirement plans, 529 plans)
ERISA
(ex. 401k)
Corp, LP, LLC
("outside" v. "inside"
distinctions)
Ohio Law
(Ex. IRAs, Coverdell ESA)
Irrevocable Trusts
(SLATs, ILITs, Gifting Trusts
(*not* QPRT, GRAT, CRT, Rev. Trust)
Mind the Gap

II. State Non-Bankruptcy Protections

There are two important Ohio statutes that provide creditor protection for certain financial assets: 1) Ohio Revised Code § 2329.66 outlines which assets are exempt from judicial foreclosure, garnishment, sale, execution or attachment and 2) Ohio R.C. § 3911.10 is a specific provision that pertains to insurance and annuities. These are copied into Appendix A. Ohio law greatly increased its protections for IRAs in 1998. Previously, Ohio law only protected IRAs to the extent "reasonably necessary for support", a standard which has been very conservatively construed by the courts.[1] Consideration is given to spouses and dependents of the debtor, but not children who are not dependents.[2]

Aside from Ohio law, federal law may also apply to certain accounts, even when the bankruptcy court is not involved. The Employee Retirement Income Security Act of 1974 ("ERISA") preempts state law if the question "relates to" employer-sponsored plans subject to the law.[3] Courts have broadly construed what "relates to" means. This will be discussed in the next section.

This section assumes that an owner/debtor is NOT in bankruptcy and the plan is NOT subject to ERISA.

[1] *In Re Herzog*, 118 BR 529 (Bankr. ND Ohio 1990). There are many cases from various states where younger debtors who could save more later for retirement were totally denied any exemption under this standard.
[2] *In re Guikema*, 329 BR 607 (Bankr. S.D. Ohio 2005)
[3] ERISA in general is at 29 U.S.C. § 1001 et seq., preemption section at 29 U.S.C. § 1144(a), anti-alienation provision at 29 U.S.C. §1056(d)(1)

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a. Non-ERISA Qualified Plans

Not all employer-sponsored retirement plans are governed by ERISA. In addition to the self-employed exceptions noted in the ERISA section, the most common plans not subject to ERISA (and thus not receiving the ERISA-based protection) are traditional and Roth IRAs.[4] SEP and SIMPLE IRAs are in an ERISA nether world. They are covered by ERISA because they are employer-sponsored, but do not receive the same protection because they do not have the same anti-alienation protection under 28 U.S.C. § 1051(b). One might expect that Simplified Employee Pension (SEP) IRAs would be covered then by state statute, but, at least in the Sixth Circuit, they are not.[5]

In *Lampkins*, the plaintiff, a secretary in a Michigan law firm, won judgments against her employer for accrued benefits in her employer's profit sharing and pension plans. Her employer, a lawyer, refused to pay the judgments claiming he had no assets or income despite his continued law practice. The plaintiff attempted to garnish the lawyer's SEP-IRA. After the district court granted summary judgment to the plaintiff. In affirming the lower court's decision, the Sixth Circuit held that the SEP was not exempt under federal law, specifically ERISA's anti-alienation provision because IRAs are specifically excluded from protection under this provision. Thus, ERISA did not prevent the SEP from being garnished. *Furthermore*, the Sixth Circuit held that a Michigan state statute that purported to exempt from garnishment all § 408 individual retirement plans, was preempted by the language of ERISA's preemption clause which supersedes state laws relating to employee benefit plans. Consequently, the plaintiff was able to garnish the SEP to satisfy the judgments. Ohio courts have followed this.

A recent case outside the 6th Circuit has failed to follow *Lampkins'* rationale, citing older precedent in the 5th, 8th and 11th Circuits.[6] The argument was essentially that ERISA does not preempt federal law ("[n]othing in this subchapter shall be construed to alter, amend, modify, invalidate, impair, or supersede any law of the

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[4] 26 CFR §2510.3-2, there have been numerous cases trying to apply *Lampkins* ERISA preemption to traditional IRAs without success

[5] See, *Lampkins v. Golden*, 28 Fed.Appx. 409 (6th Cir. 2002) (unpublished, but often cited), *In re DiGuilio*, 303 BR 144 (Bankr. ND Ohio 2003), debtor's $30,000 SEP-IRA held not exempt under *Lampkins* type analysis.

[6] *In re Wasteney*, 2004 Bankr. LEXIS 2597 **(S.D. Iowa)**

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United States...")[7], and bankruptcy law uses state law exemptions therefore ERISA should not preempt state law exemptions. This author's opinion is that this argument is sound and persuasive ***when in bankruptcy***, but not when a debtor is in a state proceeding where the bankruptcy code is irrelevant.

IRC § 403(b) plans (which can be either mutual fund type accounts or annuities) can be ERISA or non-ERISA. For instance, a governmental plan under IRC §457 or §403(b) is specifically NOT governed by ERISA, but a 403(b) plan for employees of charities might be ERISA.[8] Generally speaking, 403(b) plans with **only** employee contributions do not fall under ERISA reporting and disclosure regulations and require no plan administration such as discrimination testing and Series 5500 tax filings. If the plan has both employee and employer contributions it becomes subject to ERISA regulations and requires plan administration similar to a 401(k) plan with a similar cost structure.

Note, however, that Ohio exempts "property that is specifically exempted from execution, attachment, garnishment, or sale by federal statutes other than the [Bankruptcy Act]".[9] Thus, since Section 457 plans should contain an anti-alienation provision, it may yet be protected. Section 403(b) plans do not have such a provision.

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[7] 29 U.S.C. §1144(d)
[8] 29 U.S.C. § 1002(32) for governmental plan, *In Re Nolen*, 175 BR 214 (Bankr. ND Ohio 1994), for 403(b) plan covering employee of charity
[9] Ohio R.C. § 2329.66(A)(17)

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b. IRAs

Most states have significant creditor protection for IRAs.[10] Some have unlimited exemptions, but many only protect for amounts reasonably necessary for support of debtor, spouse and dependents. As mentioned above, Ohio amended its statute effective March 22, 1999 to greatly increase IRA protection. It *seemingly* protects §408(k) (SEP-IRA) and §408(p) SIMPLE IRAs as well as §408A Roth IRAs. Why did Ohio give unlimited protection to IRAs and not other similar assets? Note that a rollover from a 403(b) or other plan to an IRA is included.

Also be aware that most state statutes require RESIDENCY or DOMICILE to protect such assets. Be careful if your client is in the military, for example, and may claim another state as his or her domicile – that state may not grant the same protections and Ohio's may not apply.[11]

Another "snag" to IRA protection is that if an IRA owner engages in self-dealing or other "prohibited transactions", it can lose protection under state law as well. This is more likely to happen when someone uses a self-directed IRA with "outside-the-box" investments. Consider the recent unpublished case of *Aebig v. Cox*[12], where IRA owner purchased real estate in his IRA (clearly permitted under DOL/Treasury Regulations), but then leased the property to an S Corporation owned by his wife. The state court found, without need to address veil piercing arguments, that the corporation was a "disqualified person" under 26 USC 4975(e)(2) and thus a prohibited transaction under 4975(c)(1)(A). Therefore, under IRC §408(e)(2)(A), it was no longer an IRA, and hence, no longer afforded protection under state law.

Similarly, a local case found that where the debtor pledged his IRA for a loan, which is forbidden under IRC 408(e)(4), the loss of the tax protection of the IRA account similarly negated the asset protection afforded under Ohio's statute.[13]

Distinguishing SEP and SIMPLE IRAs

[10] Although, Maine, e.g., only protects $15,000 absolutely, or more if needed for "support". ME Code Section 4422(13)(F)

[11] As was the case for Louisiana resident in Ohio court in *Pallante v. International Venture Invest., Ltd*, 622 F. Supp. 667 (N.D. Ohio 1985), which denied Ohio exemptions because he was not resident and denied Louisiana exemptions because proceedings were not in Louisiana. See Section XVII of this outline for more disturbing cases on this theme.

[12] *Aebig v. Cox*, 2006 Mich App. Lexis 1695 (note that Michigan's statute re IRAs at 600.6023(l) is similar to Ohio's.

[13] *In re Roberts*, 326 B.R. 424 (S.D. Ohio 2004)

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The *Lampkins v. Golden* case cited above creates further jeopardy for SEP and SIMPLE IRAs beyond simply limiting the protection to "support". If ERISA preempts these IRAs, yet offers no protection, it essentially eviscerates the protection altogether (forcing a debtor into bankruptcy).[14] The *Lampkins* rationale has been followed in subsequent cases that distinguish SEP and SIMPLE IRAs as employer-sponsored, in holding that ERISA does not preempt other IRAs.[15] However, since the *Lampkins* case is unreported, one might still try to fight the issue and at least try to protect what is needed for support.

However, even if one were successful in getting a court to ignore the ERISA preemption argument, precedent previous to Lampkins held that SEP-IRAs as more analogous to employer sponsored pension plans than IRAs. Accordingly, even if there were no preemption, protection for SEP-IRAs do not get the unlimited protection under paragraph (c) of Ohio's statute, but come under the less advantageous paragraph (b) that only allows protection for "support".[16] SIMPLE IRAs may be jeopardized as well under this same reasoning.

Distinguishing IRA Annuities

One might have an IRA that is an Individual Retirement *Annuity* under IRC §408(b). This should be protected in the same manner as any other IRA under Ohio law, since they are specifically mentioned. However, do NOT assume this to be the case in other states that seem to protect IRAs. For instance, one fairly recent case held under another state law that IRA annuities did not get the same protection.[17]

c. Insurance

[14] Not just in Ohio: the U.S. District Court in Virginia recently held a doctor's SEP was subject to forfeiture because ERISA's anti-alienation provisions do not apply to IRAs, including SEPs. *U.S. v. Norton*, 2002 WL 31039138, No. 2:99CV10078 (W.D.Va. 2002).

[15] *Lampkins*, supra at note 21. *In re Christine P. Mitchell*, 2002 Bankr. Lexis 1217 (Bankr. N.D. Ohio 2002), *In re Robert and Lynn Fixel*, 286 B.R. 638 (Bankr. N.D. Ohio 2002) (all holding that *Lampkins* rationale and ERISA does not preempt or apply to ordinary IRAs), *In re Buzza*, 287 B.R. 417 (Bankr. S.D. Ohio 2002).

[16] *In re Schreiner*, 255 BR 545 (Bankr. S.D. Ohio 2000), where entire $17,564.83 SEP-IRA was lost to creditors. One may question the competency of the debtor's attorney since they did not even try to claim in the alternative that this small amount was needed for support.

[17] *In re Kemmerer (Huisinga v. Kemmerer)*, 251 B.R. 50 (BAP 8th Cir. 2000), though a federal district court declined to follow the 8th circuit bankruptcy appellate court in *In re Pepmeyer*, 273 B.R. 782 (N.D. Iowa, 2002)

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Insurance, as protected by R.C. § 3911.10 (see appendix A), has fairly strong protections under Ohio law. Although courts have been harsh with annuity contracts that it sees as primarily "investments" (discussed below), they still protect insurance policies, even when they have large cash surrender value and withdrawal rights.[18] Note that, if there is no beneficiary named, or a beneficiary other than a spouse, children or dependent, that protection is unavailable.[19] This penalizes unmarried or gay and lesbian couples (query – could they be considered a "dependent"?). A trust for the above (such as a revocable living trust) also receives protection.

Other states such as Hawaii, Illinois and Tennessee have statutes similar to Ohio. Others protect regardless of who the insured is – Florida, Texas, Kansas, Michigan. Others protect specified amounts – Alaska, $10,000, Connecticut, $4,000, Arizona, $25,000).[20]

Advise any inheritors of insurance to place such assets in separate accounts that can easily be traced back to the insurance – the statute does not place a time limit on tracing the proceeds. This can be easily overlooked, and debtors should attempt to trace any inherited insurance proceeds.

Note that tax liens on an insured debtor/decedent apply to cash values of insurance, but not to death benefits. For example, Joe Debtor has a $1Million face amount insurance policy with $70,000 cash value. He dies with tax liens. The IRS may foreclose on $70,000 (the cash value accessible by decedent prior to death), but not the $1Million payable to family. While there is no case to this effect, this author believes that a tax lien may apply to a greater value if Joe Debtor had a lengthy terminal illness that caused the value of the insurance policy to skyrocket prior to death (such as to what a viatical company would pay).

Warning: Beware Cross-Ownership

Note how cross-ownership of policies, especially large cash value polices, are covered (or not covered) under the statute. Note the statute's language in Appendix A: "**free from all claims of the creditors of such insured person or annuitant**", ***not*** "free from all claims of the creditors of such **OWNER** or insured person or

[18] *Matter of Bess*, 40 BR 509 (Bankr. S.D. Ohio 1984), aff'd 47 BR 414
[19] Not protected: *In re Peacock*, 292 BR 593 (Bankr. S.D. Ohio 2002), where Mother and Aunt who were not dependents were named beneficiaries.
[20] Bove, *Protecting Assets Through Insurance and Annuities*, Estate Planning, Vol. 31, No. 6 (2004)

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annuitant." Insurance policies and annuities may have an owner different from the insured or annuitant.

Example: Mary and John both own $2Million face amount policies insuring ***the other*** with $300,000 cash value in each policy. Mary, an OB/GYN, is sued. Her policy on John is "free from claims of creditors of insured" (John), but are they free from her creditor's claims? Because of the way the insurance policies are owned, creditors now have an argument to reach the $300,000 cash value in Mary's policy insuring John. While you might be able to convince a court that the statute should be interpreted to cover such a situation, there is no reported case on this issue, and wiser proactive planning would ensure the issue does not arise by avoiding cross-ownership structures altogether.

IMPLICATIONS FOR BUY-SELL AGREEMENTS:

Note that this feature of insurance protection in Ohio creates a significant argument for cross-purchase or trusteed cross-purchase agreements as opposed to corporate owned life insurance (even aside from the estate tax/basis implications).

Example:

Billy Bob and his brother Mortimer each own 50% of the family business. They have grown it into a $10MM business. Their attorney, Joe Didntknow, drafted a buy-sell agreement wherein the business purchased and owns $5M whole life policies on each of them, naming the corporation as the beneficiary. One night to celebrate a new account, Billy Bob and Mortimer have a few tequila and red bulls. On the way home, Billy Bob practices his favorite Dukes of Hazzard driving stunts, unfortunately wrecking into Britney Spears' tour bus, sending both Britney and Billy Bob off to a better place.

Effect: Both the $5M death benefit and the cash value in Mortimer's $5M policy are at risk. If this were done with cross-owned policies in separate ILITs, the insurance would be protected from creditors (and there may be other income tax benefits to survivors, such as a step up in basis on company stock bought with the insurance).

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d. Non-Qualified Annuities

Despite what you might think reading the two statutes in the Appendix, courts have not been kind to annuity holders. In fact, there is not a single reported Ohio case under that statute that protects annuities at all, at least in the manner that they are ordinarily owned.[21] Courts look at annuity contracts as primarily available to the owner/debtor, and not really "on the life of any person" at all similar to insurance, but more analogous to an investment.[22] Thus, deferred annuity contracts in general that allow for withdrawals, surrenders, and change of investments seem to receive **no protection whatsoever under Ohio law**.

So, why are annuities even mentioned in the statutes? Annuities that might yet receive protection under this statute are immediate annuities that have no rights to change investments, surrender for additional payment, withdraw, etc. Note – nearly 99% of annuities are not annuitized, and newer, more common lifetime benefit riders (GLWB, GLIB, etc) are NOT the same as annuitization.

What *might* qualify? Say a client takes out an immediate annuity payable for the life of himself and his wife, perhaps with a 10 year period certain naming his children. While no court has addressed this, such an annuity may pass muster. Another possibility – insurance proceeds converted to an annuity for a beneficiary upon the death of insured or annuities purchased via gift for another (with the purchaser not a beneficiary in any way). One might call such annuities a "poor man's trust".

Note that some states, such as Florida, Texas, Colorado, Illinois and Michigan are much more protective of insurance and annuities than Ohio (as well as unlimited homestead and other protections).[23] Hence Ken Lay and his wife's purchase of $4,000,000 in annuities before Enron imploded while corporate management warned their own employees against buying annuities.

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[21] Not protected: *In re Fichter*, 45 BR 534 (Bankr. N.D. Ohio 1984), although this case would be decided differently today because it was an annuity within an IRA, which is now protected under 2329.66(A)(10)(c). Also, *In re Andrews*, 301 BR 211 (Bankr. N.D. Ohio 2003), *In re Domanski*, 362 BR 824 (Bankr. N.D. Ohio 2006), *In re Quintero*, 253 BR 832 (Bankr. N.D. Ohio 2000)

[22] Also see recent case of *In re Simpson* (9th Cir. 2009), holding that a non-qualified annuity cannot be analogized to a private retirement plan or insurance under California law.

[23] Bove, *Protecting Assets Through Insurance and Annuities*, supra note 29

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The prevailing view is that annuities are contracts with debtors and creditors rather than as trusts with a trustee and beneficiaries.[24] This can have negative consequences for annuity beneficiaries. Traditional "spendthrift" protection requires a trust. Thus, an annuity that was purchased as a personal injury settlement was not exempt from the creditors of the debtor/beneficiary, because it did not qualify under Ohio's garnishment statute and **parties cannot establish spendthrift protection by contract** (as opposed to trust).[25]

However, there is recent contrary case law from the Eight District (Cuyahoga County) that held that an annuity purchased under similar circumstances (lawsuit settlement) with a spendthrift clause should receive the exact same protection as a spendthrift trust, and denied the creditor access.[26] I believe this case was wrongly decided because 1) annuities are not legally the same as trusts and 2) self-settled trust are not protected in Ohio anyway.

Also unique under Ohio law is the potential protection available for beneficiaries other than the insured:

> § 3911.14. Proceeds of policy
> Any life insurance company, organized or licensed to do business under the laws of this state, **may hold the proceeds of any life** or endowment insurance **or annuity contract** issued by it upon such terms and restrictions as to revocation by the insured and control by beneficiaries, with such exemptions from legal process and the claims of creditors of beneficiaries other than the insured, and upon such other terms and conditions, irrespective of the time and manner of payment of said proceeds, as have been agreed to in writing by such company and the insured or beneficiary. Such insurance company is not required to segregate funds so held but may hold them as a part of its general corporate assets. Any life or endowment insurance or annuity contract issued by a domestic, foreign, or alien company may provide that the proceeds thereof or payments thereunder shall not be subject to transfer, anticipation, commutation, or encumbrances by any beneficiary, and **shall not be subject**

[24] *In re Adams*, 302 BR 535, 540-541 (6th Cir. BAP 2003), *Wilson v. Dixon*, 73 Ohio App.3d 706 (8th Dist. 1991)
[25] *Wilson*, supra
[26] *Seaway Acceptance Corp. v. Ligtvoet*, 2007-Ohio-405 (8th Dist. 2007), though the court did not address the *Wilson* or *Adams* case noted above and contained no support for its conclusion that annuities are the same as trusts. Discretionary appeal was denied in the case.

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to the claims of creditors of any beneficiary other than the insured or any legal process against any beneficiary other than the insured; if said contract so provides, the benefits accruing thereunder to such beneficiary other than the insured shall not be transferable nor subject to commutation, encumbrance, or legal process.

There are no cases interpreting how broadly this might be interpreted, or who the "insured" should be in the context of garden variety non-qualified annuities. Could a debtor purchase a "spendthrift trust" annuity for a spouse or children? What if he simply makes his wife or child the annuitant ("insured"?) and remains a beneficiary? What do we make of all these situations where companies buy annuity interests? With the exception of the Eight District in *Seaway*, courts interpret this statute and 3911.10 to protect third parties only, rather than the most common annuities which have owner withdrawal rights.

F. Education IRAs

Education IRAs, now known as Coverdell Education Savings Accounts (ESAs), allow a non-deductible contribution to an IRA-like account.[27] They do not have the investment straightjacket that 529 plans have, and unlike 529 plans, can be used for K-12 as well as college educational expenses, and a broader array of expenses.[28] Contributions are limited, however, to $2,000 per year.

Note that R.C. §2329.66(A)(10)(c) specifically includes education IRAs and a reference to IRC §530 that establishes them. This should presumably cover the newly named Coverdell ESAs. However, what should we make of the requirement that the plan "provides benefits by reason of illness, disability, death, or age"? It's hard to see how a Coverdell/education IRA meets this requirement (perhaps the age 30 cutoff?), but then why would these be mentioned in the statute at all unless there was at least some protection afforded by its mention? There is no case on this issue. Of course, the same argument could be made by creditors for Roth IRA accounts, which, unlike other IRAs or pensions, have no requirement to distribute based on age. However, again, a debtor would rationally argue that to interpret it thus would effectively take

[27] IRC § 530(b)(1)
[28] IRC §530(b)(2) &(3)

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the protection out of the statute altogether, a nonsensical interpretation. Our statute is very poorly worded.

G. 529 Plans

Note that Ohio's main exemption statute (Appendix A) does NOT include 529 plans. However, Title 33 contains provisions for the Ohio college savings plan and 529 plans. Ohio R.C. §3334.15 provides:

> **§ 3334.15. Credit or payment exemptions - use as security or collateral for loan**
>
> (A) The right of a person to a tuition unit or a payment under section 3334.09 of the Revised Code pursuant to a tuition payment contract, a scholarship program, or a variable college savings program account shall not be subject to execution, garnishment, attachment, the operation of bankruptcy or the insolvency laws, or other process of law.
>
> (B) The right of a person to a tuition unit or a payment under section 3334.09 of the Revised Code pursuant to a tuition payment contract, a scholarship program, or a variable college savings program account shall not be used as security or collateral for a loan.

Many of our clients, for investment reasons (lower costs, better track record and performance), establish a 529 plan in another state. I do not think the above Ohio statute would apply, so query whether another state's statute would offer protection. Illinois, Michigan and California, for instance, do not provide protection for 529 plans, so an Ohio resident setting up a plan in those states would probably not receive any protection. However, most states do have some protection granted within their statute.

Some feel the statute above is vague and may not cover the owner as well as the beneficiary (there is an EPTL committee studying the issue). Moreover, even though variable college savings plans (the most common) are specifically mentioned above, the statutory reference "Section 3334.09" is to the Ohio tuition payment contracts statute, not the variable college savings plan, which is enacted by Section 3334.18. The statute *should be* interpreted to cover variable college savings accounts, and omitting a reference to 3334.18 was probably an oversight, but this is by no means a sure outcome. Thus, education IRAs (Coverdell ESAs) have more certain protection under Ohio law than 529 plans.

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h. Other accounts or funds that Ohio may protect under A(17) or may be subject to federal preemption

Foreign Service Retirement and Disability payments, 22 U.S.C. §1104;
Social security payments, 42 U.S.C. §407;
Injury or death compensation payments from war risk hazards, 42 U.S.C. §1717;
Wages of fishermen, seamen, and apprentices, 46 U.S.C. §601;
Civil service retirement benefits, 5 U.S.C. §729, §2265;
Longshoremen's and Harbor Workers' Compensation Act death and disability benefits, 33 U.S.C. §916;
Railroad Retirement Act annuities and pensions, 45 U.S.C. §228(L);
Veterans benefits, 45 U.S.C. §352(E);
Special pensions paid to winners of the Congressional Medal of Honor, 38 U.S.C. §3101

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III. Federal ERISA Protections Outside Bankruptcy

(The slow quiet death of ERISA protection?)

As mentioned above, federal ERISA law preempts state law regarding certain employer-sponsored plans. Ohio R.C. § 2329.66(a)(17) applies federal ERISA protections in state court, but even if an Ohio court disregarded this, the defendant/debtor could file action in federal court to "remove" the case from the state court to the federal court, where the court will then likely dismiss the case unless some rare exception to ERISA protection can be availed upon. ERISA protection is broad, and can even protect against criminal conduct and state taxes.[29] However, it is not unlimited. The IRS and family creditors have special rules. Federal criminal fines, tax levies and judgments are exempted.[30] Ex-spouses and dependents of a debtor can access plans via qualified domestic relations orders (QDROs), or the government can demand withholding taxes.[31]

The amount is not limited to only what is necessary for support. A debtor could have $10 Million in a qualified plan and it may be completely exempt under ERISA. The U.S. Supreme Court has generally been extremely protective of ERISA preemption and protection for qualified plans subject to ERISA.[32]

Unlike state law protections for self-settled spendthrift trusts, it does not matter if a debtor started or controlled the ERISA plan as owner or part-owner of the business.[33]

HOWEVER, there are exceptions when there are no employees other than the business owner and his or her spouse. For ERISA protection to apply, there must be at least one employee other than an owner and/or spouse.[34] Thus, a plan may start

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[29] An example of protected criminal conduct is a union embezzler in *Guidry v. Sheetmetal Pension Fund*, 493 US 365 (1990). There are multiple cases that agree ERISA protects from state tax levies, e.g. *General Motors Corp. v. Buhau*, 623 F.2d 455 (6th Cir. 1980).

[30] Treas Reg. § 1.401(a)-13(b), See also *McIntyre v. United States*, Case No. 98-171192 (9th Cir. 2000), *In re Vermande*, 94 TNT 190-9 (Bankr. N.D. Ind. 1994). But even the IRS has acknowledged defeat if a worker is not yet entitled to benefits: see FSA 199930039, CCA 200102021 (no garnishment), *U.S. v. Snyder*, 343 F.3d 1171 (9th Cir. 2003)(too early to apply lien).

[31] IRC § 401(a)(13), 29 U.S.C. § 1056(d)(2)

[32] See, *Patterson v. Shumate*, 504 U.S. 753 (1992), *Guidry*, supra footnote 3

[33] See, e.g., *Raymond B. Yates, M.D., P.C. Profit Sharing Plan v. Hendon*, 124 S. Ct. 1330, 541 US 1 (2004).

[34] *Yates*, supra footnote 8

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as an ERISA governed plan when there are one or more employee-participants, but when the business winds down or there are otherwise no other employees, the owner/spouse may lose ERISA protection.

For instance, an old Keogh or "HR 10" plan for a sole proprietorship or partnership that has no other employees will **not** be covered under ERISA.[35] Similarly, sole shareholders of corporations who, along with spouses, are the **only** participants in the plan, are also **excluded** from ERISA protection. However, an employer can always add another legitimate employee, even a relative, and all participants, including the owner/employee, are then covered by the plan.[36] Or, husband and wife participants can get divorced and the exception would no longer apply.[37]

Other prerequisites for ERISA protection are judicially imposed requirements that: 1) assets are held in a trust; 2) that the trust contain an anti-alienation clause and 3) that the plan be qualified as tax-deferred under the Internal Revenue Code.[38]

Effect of an ERISA plan not being held in trust or as an annuity

Courts are divided, but some have interpreted these requirements to **exclude 403(b) plans** that would otherwise be subject to ERISA, simply because they are fashioned as a custodial account or annuity instead of a trust.[39] (Note that some 403(b)s are subject to ERISA and some are not). If your client loses the ERISA preemption/protection argument, remember that Ohio has a back up statute (last paragraph of 2329.66 in the appendix – A(17)). In one recent case, the bankruptcy court accepted the *Rheil/Adams* argument that the annuity in question was not a "trust", but found that it was still protected under Ohio's statute. However, neither the plaintiffs/trustee nor the court addressed a *Lampkins* type argument that Ohio's statute should be preempted by ERISA.[40]

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[35] 29 CFR § 2510.3-3(c), DOL Advisory Opinion 1999-04A – multiple cases have also so held

[36] See *Santino v. Provident Life & Accident Co.*, 276 F.3d 772 (6th Cir. 2001), where owner, spouse and stepdaughter were the only participants in the plan – held ERISA still applied.

[37] See, *McDonald v. Metz*, 225 BR 173 (9th Cir. BAP 1998)

[38] *In re Foy*, 164 BR 595 (Bankr. SD Ohio 1994)

[39] Denying ERISA protection for a 403(b) plan sponsored by the United Negro College Fund, *In re Adams*, 302 BR 535 (6th Cir. BAP 2003); *Rheil v. Adams*, 302 BR 535 (6th Cir. BAP); upholding ERISA coverage, I*n re Gould*, 322 BR 742 (Bankr. WD Pa. 2005). Upholding 403(b) in Ohio under other anti-alienation statute, *In re True*, 340 B.R. 597 (Bankr.N.D. Ohio 2006)

[40] *In re Sforzo*, 332 B.R. 294 (N.D. Ohio 2005)

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Effect of Disqualifying Actions

Another loophole in ERISA protection is to do anything that disqualifies the plan or contributions to it. For instance, although technically not an ERISA case, a recent 9th Circuit case upheld the bankruptcy court's ignoring protection where the plan participant established several plans with three different controlled corporations. This in itself would not have led to negative results, but he also 1) OVERFUNDED the plans by more than 20%; 2) In two years, the contributions were $30,000 greater than his salary. In two other years, they were about equal; 3) he underreported the contributions in IRS filings by large sums ($160,000 in one plan, $150,000 to another); 4) the plan purchased property upon which he lived rent-free; 5) he used a wholly owned offshore corporation and foreign bank account to make some contributions. These led the court to find that the purpose of the plans was not to save for retirement, and not eligible for the exemption.[41] However, note that the 9th Circuit was overturning a district court that had overruled the bankruptcy court initially even on such egregious facts on the theory that the plans were "primarily" retirement plans still entitled to protection. There was no discussion of fraudulent transfers in this case.

Equitable Ownership and Lack of "Tracing" – the "end run"

There is an even larger, gaping loophole in ERISA protection for beneficiaries that is scarcely known – that the plan ONLY provides protection while the assets are within the plan. Once the check is cut from an ERISA governed group-term life policy or other retirement plan to the beneficiary, it is **NOT** protected once it is in the hands of the beneficiary.[42] This is unlike the protection afforded many state creditor protection statutes, which "follows the money".[43] Or, for other federal statutes, such as social security proceeds. This means that clever and patient creditors may yet be able to get at these funds if they can get to a beneficiary when they have a check

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[41] *Cunning v. Rucker* (*In re Rucker)*, 570 F.3d 1155 (9th Cir. 2009)

[42] See *Guidry*, supra, 39 F.3d 1078, 1082, as well as *U.S. v. Smith*, 47 F.3d 681 (4th Cir. 1995) (distinguishing pre retirement lump sum payments (not protected) and post retirement annuity benefits (protected)), *State Treasurer v. Abbott*, 660 NW2d 714 (Mich. 2003), *Central States SE and SW Areas Pension Fund v. Howell*, 227 F.3d 672, 679 (6th Cir. 2000),

[43] See, e.g. *Daugherty v. Central Trust Co.*, 28 Ohio St.3d 441, 504 N.E.2d 1100 (1986), holding that property exempt under RC 2329.66 moved into a bank account is still exempt if the funds can be sufficiently traced. Similar holding: *In re Bresnahan*, 183 BR 506 (Bankr. SD Ohio 1995). Many states hold similarly.

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and/or funds in an account received from the ERISA plan. In addition, there may be more devious ways.

Consider the case of *In Re Hoult.*[44] A debtor had begun to withdraw $4800/mo from his plan. His creditor obtained a court order for the debtor to place all payments received into a bank account, where it was then subject to garnishment and payment to the creditor. **Because the suit/order was not against the plan, the first circuit found that anti-alienation provisions did not apply and the assets were not protected**. The court contrasted social security benefits, which were also at issue in the case, and held to be protected under the broad protection of 45 U.S.C. §231m(a), extending to funds after placed into bank accounts, and ERISA protection, which does NOT extend to funds once outside the plan.[45]

This puts the debtor in an awkward position. If a debtor simply refuses to take the money, the plan may force the distribution out by sending a check or send the money to unclaimed funds. Or, it may be considered to be an improper contribution, having other consequences. In addition, state courts will likely view the funds as being accessible to the beneficiary and may even hold the debtor/beneficiary in contempt for refusing to pay amounts owed when they have access to funds. Courts have held that the state courts' consideration of ERISA funds in its proceedings is NOT preempted.

So what kind of protection is there if a court can order a debtor/beneficiary to deposit retirement funds into an account, where it could thereafter be garnished under state law? This is exactly the case in recent litigation in Michigan, where a court ordered four prisoners to deposit their Daimler-Chrysler pension checks into a certain account where state law garnishment would take 90% of the funds. When three of the four refused, the judge ordered Chrysler to send the checks to the appropriate accounts. The Sixth Circuit held that, while state courts have jurisdiction over funds once in the hands of the debtor/pensioner, ERISA prohibited the courts from ordering Chrysler to do anything regarding these accounts.[46]

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[44] *In re Hoult*, 373 F.3d 47 (1st Cir. 2004), denied cert, *Hoult v. Hoult*, 2004 U.S. LEXIS 7730 (U.S., Nov. 29, 2004)
[45] *Id*. At 55
[46] *Daimler Chrysler Corp. et al v. Cox et al*, 447 F.3d 967 (6th Cir. 2006), http://www.ca6.uscourts.gov/opinions.pdf/06a0175p-06.pdf, cert requested from U.S. Supreme Court. The Michigan

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BUT, note the important issue for creditor protection is this: the state can impose a constructive trust on benefits once received from the ERISA retirement plan and it can probably order the debtor/retirement plan owner to change the address and/or account on file with the retirement plan administrator and hold them in contempt if they do not, or if they attempt to change it.[47]

The above concerns and cases appear to completely ***gut*** the ERISA protection of ERISA retirement plans. Can these "bad facts make bad law" cases simply be ignored? At one's peril perhaps. Most of the cases that indirectly attach retirement funds pertain to regular pension payments. What about a 401(k)? Would it matter if an employee were past his or her retired beginning date (usually April 1 of the year after turning 70 ½)? Could a court simply order an employee/debtor to deposit any payments into a particular account where it could be subject to state law garnishment?

In most circuits the surprising answer appears to be "yes" – and the debtor can be held in contempt for failure to do so. Debtors can even be jailed for continued contempt of court.[48] Whether an owner/employee is in pay status that is mandated by the plan may be relevant.

The most egregious of the above cases concern prisoners and "bad facts", but the courts' reasoning has nothing to do with the federal Mandatory Victims Restitution Act (MVRA), which applies to the federal government only (see the *U.S. v. Novak* case and later discussion in the section of this outline, *Exceptions When the Federal Government is a Creditor*).

This author accomplished a similar attachment to an ERISA account in a Butler County case several years ago. Because I knew it was futile to attack or get an order from the plan administrator regarding the pension funds, we went after the purported

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Supreme Court gave even less protection to the pension plans, holding that this process was not prohibited by ERISA: *State Treasurer v. Abbott*, 660 NW 2d. 714 (Mich 2003), cert denied at *Abbott v. Rising*, 540 U.S. 1112 (2004).

[47] *Id*., the court did not address the latter point, but it seems likely from the opinion, and from the *State Treasurer v. Abbott* case and others cited above, that such state orders would be permitted. Update – recent case of *SelfLube v JJMT Inc*., 278 Mich App. 298 (2008) in a similar fact case refused to follow its own Supreme Court precedent in *Abbott*, following the 6th Circuit's reasoning in *Daimler Chrysler* in above footnote. The Supreme Court of Michigan granted cert and changed its mind at 483 Mich. 897. Another Michigan case upheld the same concept, *State Treasurer v. Sprague*, 772 N.W.2d 452 (2009). Also followed by *Bittick v. Nixon*, 2009 US Dist Lexis 120888 (W.D. Mo. 2009)

[48] Debtor served six years for refusing to repatriate offshore trust funds, *In re Lawrence*, 279 F.3d 1294 (11th Cir. 2002)

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owner. The remedy established a constructive trust and court order to deposit pension funds into a joint account requiring two signatures with the attorney, debtor and creditor as joint owners, wherein creditor/attorney took funds after deposit.

In the case mentioned above (as well as *In re Hoult* and the various Michigan cases), the distributions from the pension were mandatory. Thus, we can conclude that ERISA plans that are not in mandatory pay status (e.g. the employee is still working, under 70 ½, etc) probably have superior protection to those that do not.

It has been held to be irrelevant that someone is no longer an employee, so simply retiring or changing jobs does not jeopardize protection at all.[49]

Even if ERISA protection is eroded, one cannot stop there in analysis, and must consider the overlapping circles of state law protection as well as federal bankruptcy protection. In Ohio, as can be seen from the statute excerpts in Appendix A, pension plans are only protected **"***to the extent reasonably necessary for the support of the person and any of the person's dependents***".**[50] As discussed previously, this is normally extremely narrowly construed and courts are sparse in their interpretation of such guidelines. Due to the Lampkins rationale, one should not count on any Ohio protection for plans governed by ERISA, such as SEP-IRAs, SIMPLE IRAs, or plans covering only the owner and/or spouse.

Of course, a debtor facing such a situation may (should) file bankruptcy to get more uniform treatment, but that brings up the complications that will be discussed in the next section.

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[49] *Corzin v. Larson (In re Larson)*, 340 BR 852 (6th Cir. 2006)
[50] Ohio R.C § 2329.66(A)(10)(b)

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IV. Federal Bankruptcy Scheme of Creditor Protection

On April 20, 2005, the President signed the Bankruptcy Abuse Protection and Consumer Protection Act of 2005 (BAPCPA), which became effective on October 17, 2005. BAPCPA substantially increased the creditor protection available to retirement accounts and clarified the protection available for those who declare bankruptcy.[51]

However, the law also made it more difficult to file and obtain a discharge of debt. For instance, debtors whose income is above the State Median Income for their state may be denied relief under Chapter 7 if the debtor can file Chapter 13 and pay as little as a hundred dollars a month to the general, unsecured creditors.[52] But Chapter 13 has limitations as well, such as unsecured debt of less than $336,900. Debtors who do not meet Chapter 13 requirements might be able to file under Chapter 11.[53]

A debtor might file in various states, but **a debtor may only claim exemptions from his state of "domicile."[54] Domicile is basically residence plus the intent of making it a permanent home.** Courts will consider which state the debtor has paid taxes, voted in, registered vehicles, and so forth. This can become an important issue for debtors who have moved

Before BAPCPA, the protection of retirement accounts from creditors during bankruptcy had been subject to multiple rules depending on the type of account and the applicable state. Employer retirement plans have received creditor protection due to the Employer Retirement Income Security Act of 1974 (ERISA), but only a limited number of retirement account types are actually subject to ERISA.

Because Ohio is an "opt-out" state, Ohio debtors must use Ohio's exemptions, not the federally provided exemptions.[55] Often this is better. Although most of this scheme of whether a debtor can choose or is forced into state versus federal bankruptcy exemptions remains the same, BAPCPA amended the "anti-stacking"

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[51] See, primarily, 11 U.S.C. § 522 in Appendix C
[52] 11 U.S.C. § 707(b)(2)(D)
[53] 11 U.S.C. § 109(e), see discussion in general, Gassmann, *Bankruptcy – What Every Estate Planner Needs to Know*, Steve Leimberg's Asset Protection Planning Newsletter #102 (May 2, 2007)
[54] 11 U.S.C. Sec. 522(b)(2)(A)
[55] See 11 USC § 522(b)(1) - Ohio's statute to "opt out' is R.C. §2329.662

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rules that forces one or the other and under Section 522(b)(3)(C), discussed below, the debtor gets the best of both worlds vis a vis retirement accounts (despite what some recent Leimberg Listserv articles on IRA protections imply).

a. ERISA Qualified Plans

BAPCPA has simplified retirement account creditor protection by eliminating much of the differentiation among types of plans and bankruptcy jurisdictions. Thus, in bankruptcy, SEP (Simplified Employee Pension) IRAs, SIMPLE (Savings Incentive Match Plan for Employees of Small Employers) IRAs, and all defined-benefit and defined-contribution employer retirement plans now receive creditor protection in bankruptcy, regardless of whether the plan is subject to ERISA, protecting "retirement funds to the extent that those funds are in a fund or account that is exempt from taxation under Sections 401, 403, 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code."[56] This exemption can be used even if the debtor is not otherwise using state exemptions.

b. IRAs

Traditional and ROTH IRAs have one catch under BAPCPA: if they are a rollover from a non-IRA qualified plan, they are completely protected, but if not, there is a $1,171,650 limit ($1,000,000 pursuant to statute, subject to inflation adjustment).[57] However, even this may be increased by the bankruptcy judge "as the "interests of justice so require".[58] BAPCPA included an explicit protection applicable to such accounts under 11 USC § 522(b)(3)(C) or § 522(d)(12) (depending on whether it's a state that applies Federal exemptions or like Ohio has uses its own 'opt-out' rules) and by extension of 11 USC § 522(n) (preserving unlimited protection for IRA accounts under IRC Section 408 that have received rollover contributions under IRC § 402(c). Note that it appears that a SEP or SIMPLE IRA to traditional IRA rollover does not qualify for the unlimited exemption, but would have to come under the

[56] BAPCPA Sec. 224; 11 USC § 522(b)(3)(C); 11 USC § 522(d)(12)
[57] 11 U.S.C § 522(n), adjusted for inflation by Federal Register Vol. 72, No. 30 (February 14, 2007), Vol. 75, No. 23 (Feb 25, 2010).
[58] Id.

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$1,171,650 limit, because IRC § 408(d)(3) inter-IRA rollovers are not mentioned in that section. This greatly simplifies the analysis when in bankruptcy. Remember that bankruptcy rules are irrelevant if in state court or even federal district court.

Thus, some of the negative precedent in Ohio may be overruled by new bankruptcy protections – ***if*** a debtor is in bankruptcy court.

Note as a practical matter it may be prudent not to commingle contributory and rollover IRAs if the amounts approach the $1,171,650 ceiling since a court could apply that rather than attempt to trace funds applicable to each.

c. Education IRAs in Bankruptcy

BAPCPA added protections for education IRAs. Contributions thereto are excluded if made more than one-year prior to filing and the designated beneficiary is a child, grandchild (or steps) of the debtor in the year of contribution. For contributions made between one year and two years prior to filing, only $5850 per beneficiary is excluded.[59]

d. Insurance and Non-Qualified Annuities in Bankruptcy

Unlike the Bankruptcy Act's special provisions and treatment for IRAs and ERISA plans, any exceptions for insurance and non-qualified annuities would be granted under Ohio law since Ohio is an opt-out (of federal exemptions) state.

If Ohio resident exemptions do not apply, there is a federal provision whereby annuities may be protected to extent reasonably necessary for support of debtor and dependents, and only if payable by reason of "illness, disability, death, age, or length of service".[60] Life insurance has some protection up to "The debtor's aggregate interest, not to exceed in value $10,775" under 11 U.S.C. §522(d)(7) and (8).

d. 529 Plans in Bankruptcy

529 Plans have some protection in bankruptcy. Note that the statute under Section 541 is an exclusion, not an exemption, and thus impervious to "opt-out" nullification. These have similar time-limit limitations to the education IRA exceptions above[61]. 11 Section 541(b)(6) provides:

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[59] 11 U.S.C. §541(b)(5)
[60] 11 U.S.C. §522(d)(10)(E)
[61] 11 U.S.C. §541(b)(6)

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(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**;

Note that the $5,000 education IRA/529 plan amounts are indexed for inflation similar to the IRA exemption, and as of February 2010 is $5850.[62]

[62] See same Federal Register adjustments as noted in Footnote 50.

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V. How Debtors Can Lose Protection for Plans

Under BAPCPA, plans must be properly exempt from tax to be protected. However, there are favorable presumptions to this effect if the plan has received a favorable ruling from the IRS, or if not, if it is in substantial compliance. Even if none of those apply, it is still considered exempt unless the debtor is material responsible for the non-compliance.[63] Yet, some people can still screw this up through self-dealing or "creative" tax and investment schemes, whether for IRAs or ERISA plans.

For instance, if you contribute more than is allowed under the plan and/or tax law to an ERISA plan, plan assets may not be excluded from bankruptcy.[64] Also, recall the discussion of *In re Rucker* (Footnote 16) in the previous section on ERISA protections.

If you pledge your IRA assets as collateral for a loan, you just blew up the tax deferral of the IRA and eviscerated the asset protection.[65]

Or, consider a very recent case from Florida where the debtor had over $1Million in his Merrill Lynch (now Bank of America) IRA. He took a series of loans/distributions from his IRA (many more than 1 per 12 month period). You have to wonder what his broker was thinking. The court held, even though neither the IRS nor the DOL ever questioned the scheme, that the prohibited transactions cancelled the asset protection of the IRA. In fact, the law is quite explicit that prohibited transactions cause an IRA to cease to be an IRA as of the first day of the year.[66] Note that most of the transactions in question occurred years (1997) before the bankruptcy, so you obviously had some diligent discovery work by creditors.[67]

Also, unlike qualified rollovers to IRAs (or other plans), note that Required Minimum Distributions and Hardship Distributions are not protected in bankruptcy once the money leaves the plan.

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[63] BAPCPA §224, 11 U.S.C. 522 - see bolded sections in Appendix B

[64] See *In re Bell & Beckwith*, 5 F.3d 150 (6th Cir. 1993), denying protection to contributions to profit sharing plan when company made no profits and thus pursuant to the plan should not have been made

[65] See *In re Roberts*, 326 BR 424 (2004)

[66] IRC §408(e)(2)(A)

[67] *Menotte v. Willis (In re Willis)*, 411 BR 783 (Bankr. S.D. Fla 2009), recently affirmed in April 2010 by *Willis v. Menotte*, 2010 U.S. Dist. LEXIS 44773

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VI. Post-Mortem – Protections for a Decedent's Estate

Imagine your client fell asleep at the wheel and drove across the line killing himself and other people. The estate faces large potential wrongful death claims. Can creditors get at these protected accounts? Let's take the easiest category first.

Insurance – Ohio R.C. §3911.10 (and §3911.14) clearly protects insurance proceeds from claims of a decedent's creditors.

Ohio R.C. §2929.66 exemptions (IRAs, $20,200 homestead, retirement plans, education IRAs, etc) – "Every person who is domiciled in this state may hold property exempt from execution, garnishment, attachment, or sale to satisfy a judgment or order, as follows:" Is the estate a "person" under Ohio law for purposes of this statute?

Other states are mixed. Under New York state's statutes, CPLR §5205(c) and more specifically, EPTL §13-3.2 (for estates/beneficiaries), NY clearly extends creditor protection for retirement plan/IRA assets to an estate from a decedent's creditors.[68]

[68] See also, *In re Estate of King*, 196 Misc.2d 250 (Sur Ct. NY 2003).

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VII. Post-Mortem –Protections for Beneficiaries

a. ERISA

ERISA generally protects beneficiaries equally to plan participants.[69] However, there is a minority of district court cases that hold that benefits derived pursuant to a QDRO are NOT exempt. While many treatises and commentators (including this author) believe they are wrongly decided, they do set a negative precedent and one of these cases is from the Southern District of Ohio.[70] So, in Ohio at least, a spouse inheriting a portion of a plan pursuant to QDRO may not be protected and should consider rolling it over into an IRA if possible.

It is also unclear whether ERISA protection fully extends to beneficiaries. In theory, it should, because ERISA is worded to protect "benefits" not "employees" or some other narrower definition. As discussed above, courts are split as to protecting QDRO interests. The U.S. Supreme Court has stated that the purpose of ERISA protection for retirement plans is to "safeguard a stream of income for pensioners (and their dependents, who may be, and perhaps usually are, blameless)".[71] This begs the questions: What about protection for beneficiaries who are not blameless? Or beneficiaries who are not dependents? Once the pensioner and potentially spouse are dead, there is really no public policy rationale to protect the retirement benefits.

b. Ohio exemption law re IRAs

If one reads Ohio's creditor exemption for IRAs carefully, one will note that it is protected to the extent of *contributions of the debtor*. It is highly doubtful that this includes inherited IRAs. Courts have not been kind to non-employees who have interests in retirement funds, previously ruling that the applicable Ohio exemption for certain retirement funds was personal to the individual whose work gave rise to the right to receive a benefit.[72] There are scant cases on this issue.

In Indiana, the legislature recently changed its statute to cover spouses ("contributions, or portions of contributions, that were made to the retirement plan

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[69] See, 11 U.S.C. § 1056(d)
[70] *In Re Hageman*, 260 BR 852, 857 (Bankr. SD Ohio 2001)
[71] *Guidry v. Sheetmetal Pension Fund*, 493 US 365, 376 (1990), protecting ERISA retirement funds for an embezzling union worker.
[72] *In re Mabrey*, 51 B.R. 383, 384-85 (Bankr. S.D. Ohio 1985)

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or fund by or on behalf of the debtor *or the debtor's spouse").*[73] Notably, Ohio's IRA protection statute has no such mention of spouses or even dependent. Other courts, cited in the section below, have uniformly refused to protect IRAs and similar plans under various states' laws – even spouses.

In Florida, recent legislation provides seemingly excellent protection to not only spouses but any beneficiaries. Note the addition of "beneficiaries" to the protected class that is notably absent in Ohio's version:[74]

> § 222.21. Exemption of pension money and certain tax-exempt funds or accounts from legal processes
>
> ****
>
> (2) [As amended by s. 5, ch. 2005-82, effective May 26, 2005.] (a) Except as provided in paragraph (b), any money or other assets payable to a participant or beneficiary from, or any interest of any participant or beneficiary in, a retirement or profit-sharing plan that is qualified under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, or *s. 409 of the Internal Revenue Code of 1986*, as amended, is exempt from all claims of creditors of the beneficiary or participant.

c. Ohio trust law for third-party created trusteed IRAs

While Ohio's creditor statute will unlikely protect a beneficiary, Ohio's Uniform Trust Code should protect third party created irrevocable trusts that happen to be in the form of IRAs. This is a minority of IRAs and is an often overlooked option.[75] IRAs can be in the legal form of a contract or a trust.

A trusteed IRA that allows the beneficiary to withdraw the entire amount at will is akin to a lifetime general power of appointment and should not offer any more protection than an ordinary custodial IRA. However, a trusteed IRA that limits distributions to the required minimum distributions (RMDs), perhaps with trustee discretion to pay more, should afford the beneficiary the same protections due to any discretionary trust with a mandatory income distribution provision.[76]

[73] IND. CODE § 34-55-10-2
[74] Fla Stat. §221.21
[75] See, *Trusteed IRAs: An Elegant Estate Planning Option,* Sept 2009 Trusts and Estates
[76] Ohio R.C. §5805 et seq for general protections, §5805.05 for protections of mandatory distributions

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VIII. Post-Mortem – Bankruptcy Protections for Beneficiaries

Where a debtor's interest in a plan is distributed after the filing of petition but prior to closure of a bankruptcy case, the distribution may be part of the estate to the extent it represents benefits accrued prebankruptcy.

Most exemptions in bankruptcy will be a result of state statutes discussed above, with the exception that the additional retirement plan exemptions are applicable whether the state or federal exemptions are used.

There are no circuit level cases that have decided whether the new federal exemptions for IRAs, SEP-IRAs, SIMPLE IRAs, 403(b)s, etc will apply to help beneficiaries, or be limited to beneficiaries who are spouses or dependents. As mentioned in the discussion of the *Guidry* case, the Supreme Court seems to say, without directly addressing the issue, that benefits are for the protection of the retirement plan contributor and dependents. This interpretation would exclude protection for adult children or others who inherit. The plain language of the statute would seem to include beneficiaries – it is based on the tax exemption and Code section rather than the status of the owner.

Bankruptcy courts that have applied state law exemptions have almost uniformly refused to provide protection for beneficiaries of IRAs and similar non-ERISA plans that could be argued to protect the beneficiaries as well.[77] These debtors arguably had better arguments under their respective statutes than Ohio does, since Ohio clearly only covers "contributions of the debtor", and as the Kirchner case cited below pointed out, an inherited IRA is not received "by reason of age, illness, disability or length of service" (note Ohio's reads "age"). Note that cases filed before October 17, 2005 are under pre-BAPCPA rules and may not be good law for cases filed after that date. Only the *Jarboe* case in the string cite below was filed post-BAPCPA.

The one exception to grant **inherited** IRA protection I have found is the recent Idaho bankruptcy court case of *In re McClelland*, but that case decided to protect the

[77] *In re Simms*, 241 BR 467 (ND. Okla. 1999), *In re Navarre*, 332 BR 24 (MD Ala. 2004), *In re Greenfield*, 289 BR 146 (SD Calif. 2003), *In re Taylor*, 2006 WL 1275400 (Bankr. CD Ill. 2006), unpublished, *In re Jarboe*, 2007 WL 987314 (Bankr. SD Tex. 2007), *In re Kirchen*, 344 BR 908 (E.D. Wisc. 2006)

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inherited IRA based on Idaho's statute rather than the federal bankruptcy exemption available under 522(n) and 522(b)(3)(C).[78]

Two recent bankruptcy court cases of *In re Nessa* and *In re Chilton* offer some light on how inherited IRAs (or similar accounts) may be treated in bankruptcy under 522(n) and 522(b)(3)(C).[79] In *Nessa*, funds were held to be exempt under those sections. In *Chilton*, funds were held to NOT be exempt. In this author's opinion, the *Nessa* case was by far the better reasoned decision (Chilton overly focused on pre-BAPCPA reasoning and decisions rather than the obviously important change in the statute), but time will tell – these are not appellate decisions.

[78] *In re McClelland*, 2008 Bankr. Lexis 41 (Bankr. D. Id. Case 07-40300, 2008)
[79] *In re Chilton* (Bk Tx 2010), *In re Nessa* (Bk Minn 2010)

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IX. Dangers and Advantages of Inheriting Retirement Plans, IRAs, Insurance and Annuities Through Trusts

People often make gifts in trusts for asset protection purposes. When someone gifts or leaves assets to other beneficiaries in trust (called a third-party discretionary or spendthrift trust), all states generally provide strong asset protection from creditors of the beneficiaries.[80] This is also true in bankruptcy court. However, trusts without a spendthrift clause (especially those without wide discretion granted to the trustee) will not receive little if any protection.[81]

But what about creditors of the grantor? Can leaving assets in a revocable living trust instead of outright or through other non-probate means evade creditors of the deceased? In most states, the answer is NO. But in Ohio, we have an anomalous case that very well may protect these assets.

Ohio Supreme Court precedent currently protects a decedent's funded revocable trusts from a decedent's creditors.[82] Obviously this is not the same if the trust were unfunded and relied on pour-over will to fund it, because such assets would pass through the probate estate.

But what if the living trust has a clause that provides that the trustee can or must help the probate estate/executor pay debts, taxes and expenses of the probate estate? In this case, asset protection may very well be lost. It may also cause assets otherwise exempt from Ohio taxation, such as insurance or employer-funded retirement plans, to become subject to Ohio estate tax.

Can the trust step in the shoes of the decedent/debtor and use Ohio's creditor exemptions in R.C. 2329.66(A)(10)? We do not have an Ohio court case on this issue, but a Kansas appellate court has argued that their state creditor exemption did not apply to a revocable living trust as beneficiary, that the exemption effectively

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[80] See, e.g. *Schierer v. Ostafin*, 1999 Ohio App. LEXIS 3261 (Ohio Ct. App. 1999).

[81] See, *In re Delmoe*, 365 BR 124 (S.D. Ohio 2007), where bankruptcy court attached beneficiary's $600/mo income interest in trust with no spendthrift clause drafted pro se by her father.

[82] *Schofield v. Cleveland Trust Co.*, 21 N.E.2d 119 (Ohio 1939), revisited/limited in recent 3d District case of *Sowers v. Luginbill*, 175 Ohio App.3d 745, 2008-Ohio-1486. See also *Greenwich Trust Co. v. Tipon*, 27 A.2d 166 (Conn. 1942). More states are contra: see, e.g., *State Street Bank and Trust Co. v. Riser*, 389 N.E.2d 768 (Mass. App. 1979)

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died with the decedent.[83] Ohio would probably rule the same way (with exception for insurance/annuities, under which the statute specifically include beneficiaries).

This is a particular danger for qualified plans, IRAs and insurance that may otherwise be completely protected, yet when they are paid to a trust that is available to estate creditors not only is this protection lost, but there may be adverse income tax consequences because the trust no longer qualifies as a see-through designated beneficiary trust,[84] and potentially Ohio estate tax consequences because the estate inadvertently becomes a beneficiary of the insurance.

For one example of this danger, see PLR 2004-40031, where this very situation occurred. Creditors of the decedent had access to the IRA through his revocable (now irrevocable) living trust. The issue for the IRS was "does this make the trust like an estate for designated beneficiary status?" The IRS was lenient in this ruling and ruled that in this instance it would not consider the estate or creditors as a beneficiary of the IRA for MRD purposes.[85]

> Example: Joe Graduate has contracted a terrible disease. He has accumulated $100,000 in private school loans and may die soon with over $100,000 in credit card debt and medical expenses. Plus, his new wife's ex-husband recently won a judgment against him for "alienation of affection" for $750,000. He has spent liquid assets but has a $100,000 IRA, $50,000 401(k), $50,000 group term life insurance and a $200,000 home with a $150,000 mortgage. If he leaves this to his family in a revocable trust his family has a fighting chance to save the insurance, home and IRA, but if the trust provides for payment of debts, taxes and expenses of the probate estate this may jeopardize both (of course, the mortgage follows regardless).

Another example of how an Ohio court may view such a provision is found in *Zahn v. Nelson*. In *Zahn*, William Zahn had filed for a divorce from his wife Donna,

[83] *Commerce Bank v. Bolander*, 2007 WL 1041760 (Kan. App. 2007), unpublished.
[84] See, e.g., LTR 200537044, LTR 200608032
[85] LTR 200440031

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but they remained married at his death. William understandably left his estate to his children from a prior marriage and used the William J Zahn revocable trust to pass most of the assets. But his trust stated that should his probate estate be insufficient, "there shall be paid" to the estate sums necessary to pay taxes and amounts requested by the executor to pay expenses, specific bequests, and statutory allowances. [86] Some call this a "pour-up" clause. The court held that the language required the trustee to pay to the estate funds necessary to pay to the decedent's surviving spouse her $40,000 statutory support allowance under R.C. § 2106.13. So much for avoiding probate.

In addition, practitioners should be concerned from an asset protection perspective about naming beneficiaries as sole trustees of their own trust share. Restricting distributions to ascertainable standards is required to avoid being considered a general power of appointment, but even with such a clause, treating the trust as a personal bank account and ignoring formalities may allow creditors to "pierce the trust veil".[87] Figurehead co-trustees can be ignored by the court.[88] An independent corporate trustee assures much better asset protection. Naming a beneficiary as sole trustee of his or her own trust invites lax administration and severely curtails the protective nature of the trust.[89]

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[86] *Zahn v. Nelson*, 2007-Ohio-667, 170 Ohio App.3d 111 (Ohio Ct. App. 2007)
[87] See, e.g., *In re Pugh*, 274 B.R. 883 (Bankr. D. Ariz. 2002); *In re Baldwin*, 142 BR 210, 215 (Bankr. SD Ohio 1992)
[88] See *Pugh* cited above, where sister was co-trustee but did not even know she was or act as one until creditor problems arose.
[89] See *Beneficiary Controlled Trusts Can Lose Asset Protection*, December 2006 Trusts and Estates by Tye Klooster and Charles Harris

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X. Exceptions for Ex-Spouses and Dependents

Ohio creditor protection law has special protections for spouses, dependents and child support. These are the exception statutes referred to in R.C. § 2329.66(A)(10).

In addition, ERISA allows qualified domestic relations orders (QDROs) to affect ERISA plans. Divorce courts can divide IRAs in a similar manner, but such divisions are not technically called "QDROs".

Ex-spouse's interests in retirement plans pursuant to a QDRO or other separation agreement might NOT be granted creditor protection. This is true under state laws.[90] It can also be true under ERISA.[91] It should not matter under bankruptcy, but most people would rather not be forced into that.

Thus, as part of divorce planning, not only should beneficiaries be renamed[92], but qualified plan assets should be rolled over to IRAs or, plan permitting, to the ex-spouse's employer plan.

Note the irony, however, that small company ERISA plans that offer no protection for husband and wife as sole owner/employees would then offer such protection upon divorce.

As for spouse's protection from disinheritance that is granted under ERISA[93] (as you will note anytime you see a change of beneficiary form that requires a spouse's signature), this protection does not extend to IRAs or other plans simply because the funds originated in ERISA protected accounts.[94]

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[90] *In Re Wilbur*, 126 F.3d 1218 (9th Cir. 1997). See also cases under Footnote 43 regarding inherited IRAs, which will use similar reasoning.

[91] Although most district/circuit courts protect ex-spouse's ERISA plan interests, there are two cases holding contrary, including one local, *In Re Hageman*, 260 BR 852 (Bankr. SD Ohio 2001). More recently, the case of *In re Hartman*, 345 B.R. 826 (N.D. Ohio 2005), rejected *Hageman's* holding and held the QDRO funded IRA exempt.

[92] Ohio's statute to disinherit beneficiaries of such plans upon divorce will be preempted by federal ERISA law pursuant to the Supreme Court's holding in *Egelhoff v. Egelhoff*, 532 U.S. 141 (2001). The Supreme Court recently addressed whether a divorce decree wherein ex-spouse apparently waives all rights to benefits from an ERISA plan (but without getting a QDRO) can function as a waiver of ERISA benefits as beneficiary. Held: the administrator cannot be bound by state decree if not a QDRO. *Kennedy v. Plan Administrator for DuPont Savings and Investment Plan*, 129 S. Ct. 865 (2009).

[93] Specifically, see 29 U.S.C. § 1055

[94] See, e.g., *Charles Schwab & Co v. Chandler*, CV-06-00119-FJM, (9th Cir. 2010), an interpleader action between surviving spouse and children from prior marriage who were named primary beneficiaries on IRA.

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XI. Exceptions when the State or IRS is the Creditor

Do not assume that the same rules apply to the state of Ohio or the federal government as a creditor.

For instance, federal tax authorities may reach ERISA qualified plan assets (discussed later herein), but state law authorities may not.[95] Indeed there is specific language in the tax code that exempts federal tax debts from ERISA's anti-alienation provisions.[96] Court cases have expanded this to include non-tax federal criminal fines[97], and the Federal Debt Collection Practices Act (FDCPA) specifically provides that a federal order of restitution shall be treated "as if the liability of the person fined were a liability of tax assessed under the Internal Revenue Code".[98]

However, this highlights one of the few advantages to ERISA plans over IRAs – potential protection for **state** tax lien/garnishments (note, however, the success of Michigan in the recent cases cited under the ERISA section).

Pre-bankruptcy petition tax liens survive the bankruptcy (yes, even for ERISA plans) and will not be affected by "discretionary" or spendthrift trust protections.[99] Ohio's spendthrift trust statute specifically precludes application to "a claim of this state or the United States to the extent provided by the Revised Code or federal law".[100] The following are from the recently amended Internal Revenue Manual, available online (**bold by author**). It is not a failure of due process if the IRS fails to follow the IRM, but it "serves as the single, official source of IRS 'instructions to staff' relating to the administration and operation of the Service."[101].

Part 5. Collecting Process
Chapter 11. Notice of Levy
Section 6. Notice of Levy in Special Cases

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[95] See cases in Footnote 4
[96] IRC §401(a)(13), Treas Reg. §1.401(a)-13(b)
[97] *U.S. v Novak*, 476 F.3d 1041 (9th Cir. 2007)
[98] 18 U.S.C. §3613(c)
[99] *Vance L. Wadleigh v. Commissioner*, 134 T.C. No. 14 (2010) – Feds intent to levy on ERISA plan for taxes that were discharged in bankruptcy allowed because lien attached to ERISA plan assets in rem. Even though plan was 9 months from payout status, the levy could attach
[100] Ohio R.C. §5805.02(B)(2)
[101] IRM pt. 1.11.2.1.1(1) (Apr. 1, 2007)

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5.11.6 Notice of Levy in Special Cases
5.11.6.2 (01-22-2010)
Funds in Pension or Retirement Plans

1. These instructions cover money accumulated in a pension or retirement plan, as well as Individual Retirement Arrangements (IRAs). They do not deal with levying retirement income. See section IRM 5.11.6.1 above. Also see Delegation Order 5-3 (Rev-1) at IRM 1.2.44.3.(23)c.
2. There are many employer and self-sponsored retirement vehicles that are **not exempt from levy**. These plans include, for example:

- Qualified Pension, Profit Sharing, and Stock Bonus Plans under ERISA
- IRAs
- Retirement Plans for the Self-Employed (such as SEP-IRAs and Keogh Plans)

3. Because these retirement vehicles provide for the taxpayer's future welfare, levy on the assets in a retirement account (as contrasted with income from the account) after following the procedures set forth below.

Note:

On January 1, 2000, a new exception to the 10 percent additional tax on early distributions from retirement plans was added to the Internal Revenue Code. If an account is levied upon, the taxpayer does not owe the 10 percent additional tax. **Because of the levy exception to the 10 percent additional tax, occasionally taxpayers may ask the Service to levy the funds in the retirement accounts. Even though the taxpayer may be able to voluntarily withdraw money in a lump sum from a retirement account and apply it to the outstanding tax liability, do not levy on retirement assets at the request of the taxpayer**. Instead, follow the procedures set forth below.

Note:

An imminent CSED, alone, does not justify levying on retirement assets. Levying on assets in retirement accounts requires application of the procedures set forth below.

4. The first step in deciding whether to levy on a retirement account is to determine what property, retirement assets and non-retirement assets, is available to collect the liability. If there is property other than retirement assets that can be used to collect the liability, or if a payment agreement can be reached, consider these alternatives before issuing a levy on retirement accounts. Also consider the expense of pursuing other assets as well as the amount to be collected.
5. The second step in deciding whether to levy on a retirement account is to determine whether the taxpayer's conduct has been flagrant. **If the taxpayer has not engaged in flagrant conduct, do not levy on retirement accounts**. Deciding whether the taxpayer has engaged in flagrant conduct must be done on a case-by-case basis. Keep in mind, however, extenuating circumstances may exist that mitigate the taxpayer's flagrant conduct.

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6. The following are some examples of flagrant conduct.

Example:

Taxpayers whose failure to pay is based on frivolous arguments which are listed in Notice 2008–14, IRB 2008–4 page 310, or subsequent updates. See IRB 2008–4 at http://www.irs.gov/pub/irs-irbs/irb08-04.pdf .

Example:

Taxpayers who continue to make voluntary contributions to retirement accounts while asserting an inability to pay an amount that is owed.

Caution:

Where a tax liability has been discharged in bankruptcy, the IRS may continue to have a valid tax lien on certain retirement assets that existed prior to the bankruptcy. See IRM 5.11.6.2(14). Voluntary contributions made to such retirement assets after the bankruptcy petition was filed are not considered flagrant.

Example:

Taxpayers who contributed to retirement accounts during the time period the taxpayer knew unpaid taxes were accruing.

Example:

Taxpayers convicted of tax evasion for the tax debt.

Example:

Taxpayers assessed with a fraud penalty for the tax debt.

Example:

Taxpayers assisting others in evading tax.

Example:

Taxpayers with liabilities based on illegal income.

Example:

Taxpayers who are in business and pyramiding unpaid trust fund taxes

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Example:

Individual taxpayers who are accumulating unpaid income taxes over multiple tax periods.

Example:

Taxpayers against whom the Trust Fund Recovery Penalty has been asserted on more than one occasion.

Example:

Taxpayers who have demonstrated a pattern of uncooperative or unresponsive behavior, e.g., failing to meet established deadlines, failing to attend scheduled appointments, failing to respond to revenue officer attempts to contact. In such cases, determining alternatives and the taxpayer's dependence on the money in the retirement accounts (final step) may not be possible, so a levy may need to be served without making those determinations.

Example:

Taxpayers who have placed other assets beyond the reach of the government, e.g., sending them outside the country, concealing them, dissipating them, or transferring them to other people.

Example:

Taxpayers with jeopardy or termination assessments subject to collection.

7. The final step in deciding whether to levy on retirement assets is to determine whether the taxpayer depends on the money in the retirement account (or will in the near future) for necessary living expenses. If the taxpayer is dependent on the funds in the retirement account (or will be in the near future), do not levy the retirement account. In determining whether the taxpayer depends on the money (or will in the near future), use the standards in IRM 5.15, *Financial Analysis,* to establish necessary living expenses. Use the life expectancy tables in Publication 590, Individual Retirement Arrangements (IRAs), to estimate how much can be withdrawn annually to deplete the retirement account in the taxpayer's remaining life. Also, consider any special circumstances in the taxpayer's specific situation, such as extraordinary expenses or additional sources of income that will be available to pay expenses during retirement.

8. The taxpayer may be able to withdraw money in a lump sum from a plan. If the taxpayer has the right to do so, a levy can reach that right. However, remember that a levy only reaches the taxpayer's present rights.

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Example:

The taxpayer has $10,000 in a plan but can only withdraw it later. The taxpayer may have a present right to the money, although it can not be withdrawn immediately. A levy may reach that right, but the money can be not paid over until the taxpayer can withdraw it. At that time, there may be $30,000 in the plan. Without a new levy, though, only $10,000 could be paid over.

Example:

The taxpayer has money in a plan. The terms of the plan do not allow for any lump sum withdrawal. The plan provides a right in the future to receive monthly payments, but the taxpayer has not paid into it long enough yet to qualify for any future payments. A notice of levy attaches nothing, because the taxpayer has no present property rights.

9. The notice of levy form says it does not attach money in pension or retirement plans. When levying on these funds, sign the notice of levy in the block to the left of, "Total Amount Due."
10. Have the SB/SE Director, Collection Area approve the notice of levy by signing the form as the Service Representative or see IRM 5.11.1.2.4, *Managerial Approval*, for methods to secure managerial approval.
11. Consider discussing the case with the Employee Plans Group before issuing the levy. Their advice, as well as advice from AIQ - Advisory and Associate Area Counsel, may be needed to determine the present right to property. Often, a levy is served before the taxpayer's precise rights are determined. Try to get a copy of the plan instruments as soon as possible to determine the taxpayer's interests in the plan.
12. When money is withdrawn from a retirement account, the taxpayer may be liable for income tax on the withdrawal. If the taxpayer is less than $59^1/_2$ years old, a 10 percent additional tax on early distributions may be assessed. However, the taxpayer is not liable for the 10 percent additional tax on early distributions if the money was withdrawn because of a notice of levy served on the retirement account. There may, however, still be income tax owed for the amount withdrawn.
13. Send Letter 3257 (DO) with the notice of levy and Letter 3258 (DO) with the taxpayer's copy of the notice of levy. These letters state the withdrawal is not subject to the tax on early distributions, even if the taxpayer is under $59^1/_2$ years old. These letters are available as macros on the Integrated Collection System.
14. **Retirement accounts that are exempted or excluded from the bankruptcy estate are still subject to being levied to collect taxes that are discharged in bankruptcy, where a Notice of Federal Tax Lien was filed before bankruptcy. Retirement accounts that are excluded from the bankruptcy estate are still subject to being levied to collect taxes that are discharged in bankruptcy, where no Notice of Federal Tax Lien was filed prior to bankruptcy; however a valid statutory lien is required.** Consider a levy on the retirement accounts if there is no other property that survived the bankruptcy. See IRM 5.19.17.4, *Exempt, Excluded, or Abandoned Property,* for guidance in determining if the retirement account is exempt or excluded.

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Note:

In this situation, the NFTL attaches to only the taxpayer/debtor's property or rights to property held as of the bankruptcy petition date. However, the lien is not limited to the value of the property as of the petition date. **Its attachment relates to any appreciation or diminution of such assets**. The federal tax lien does not attach to retirement account contributions made on or after the bankruptcy petition date. Care must be taken to limit collection to only the bankruptcy pre-petition account value. Consult with AIQ-Insolvency or Counsel prior to issuing levies on exempted or excluded retirement accounts for assistance in determining the account value the levy attaches.

Note:

Retirement accounts that are exempt from the bankruptcy estate are not subject to being levied to collect taxes that are discharged in bankruptcy where no Notice of Federal Tax Lien was filed prior to bankruptcy. See IRM 5.19.7.4(1), for details regarding exempt assets.

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XII Fraudulent Transfer (UFTA) Issues

We will not have time to go over this section in detail. But it is important to at least vaguely understand the **distinction between common fraud and a fraudulent transfer under UFTA.** Black's Law Dictionary defines fraud is a "knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his detriment." Fraud under the UFTA, however, is a completely different concept from criminal fraud or the definition above. Ohio's Uniform Fraudulent Transfer Act is found at R.C. § 1336.01 et seq.

Ignore the normal meaning of fraud when analyzing fraudulent conveyance law. A fraudulent conveyance under the UFTA may occur without any tortious intent, misrepresentation or concealment by the debtor. Even "rich" people may be "insolvent" for UFTA analysis, because exempt assets would not be considered. And a "creditor" for UFTA need not have achieved a judgment or even filed suit.[102] The federal government is not bound by state UFTA statute of limitations.[103]

While it is unlikely (but not impossible) that creditors would seek to void small retirement plan contributions from salary, the same may not be said to a $300,000 contribution to an insurance policy or NQ annuity. Similarly, contributions to defined benefit plans or even 529 plans can easily be six figures.

For more on UFTA and fraudulent transfers, email the author for separate CLE materials created on this topic, which will be updated in July 2010.

To protect IRAs, qualified plans, annuities and insurance, consider:

- Should a client make rollovers via check or trustee to trustee transfer? Why? (Consider the recent case of *Robertson v. Deeb*)
- Could a Roth conversion be a fraudulent transfer?
- How do Crummey withdrawal rights and hanging powers jeopardize an ILIT where beneficiary has creditor issues?[104]

[102] *Stein v. Brown*, 18 Ohio St.3d 305 (1985)
[103] See discussion at *U.S. v Levine*, 73 F.Supp 2d 853 (N.D. Ohio 1999) – debtors placed all their assets into irrevocable trust, court held that SOL did not apply to sovereign and lien was placed years later, after SOL had run
[104] For the surprising answer to this, see *Fraud, Funding and Future Interests – Asset Protection Traps for the Unwary*, by Rod Goodwin and Edwin P. Morrow III, J. Practical Estate Planning, April-May 2007

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XIII. Disclaimer Issues

Surprisingly, the fraudulent transfer issues discussed above are also relevant in considering qualified disclaimers as a method whereby a beneficiary of accounts discussed herein may avoid creditors. This technique is discussed in many national articles and textbooks. **Ohio attorneys should take care to note some unique Ohio case law that mandates caution in using such techniques.**

Most states and circuits allow disclaimers to defeat a disclaimant's creditors.[105] Note that federal bankruptcy cases rely on state property law regarding the effect of disclaimers. What constitutes a transfer and whether it is complete may be a matter of federal bankruptcy law (since it is defined in the statute), but property interests are defined by state law.

Many states have addressed this by statute. Note that some states, such as Minnesota and Florida, bar the disclaimer by statute if the disclaimant is insolvent.[106]

An important exception is when a federal tax lien has already attached to the property, in which case federal law will trump state law.[107]

What of Ohio? Ohio's statute arguably has the same "relation-back" fiction as Lousiana, Arizona, Texas and other states. On its face, it seems very clear:

Ohio R.C. § 5815.36 [disclaimer statute]:

(H) A disclaimer pursuant to this section is effective as of, and relates back for all purposes to, the date upon which the taker and the taker's interest have been finally ascertained.

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[105] See, e.g., *In re Costas*, No. 06-16520 (9th Cir. 2009), interpreting Arizona law, *In re Simpson*, 36 F.3d 450 (5th Cir 1994), interpreting Texas law, *In re Achison*, 925 F.2d 209 (7th Cir. 1991), *In re Laughlin* (5th Cir. 2010), interpreting Louisiana law, *Slocum v. Estate of Martin*, 666 N.E.2d 411 (1996), interpreting Indiana law. Both *Costas* and *Laughlin* are after the Supreme Court's federal tax lien preemption decision in *Drye*.

[106] See, e.g., Florida's F.S. §739.402 which states a disclaimer is barred if the "disclaimant is insolvent."` F.S. §739.102 defines insolvent for disclaimer purposes to mean that the that the person's debts exceed the assets (including exempt assets) and "the person is generally not paying his or her debts as they become due."

[107] *Drye v. U.S.,* 528 US 49 (1999)

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However, in 1985 the Ohio Supreme Court rejected the relation-back fiction and held that the power to disclaim is analogous to a lifetime general power of appointment subject to fraudulent conveyance statutes.[108]

Stein was a typical "bad facts make bad law": the debtor got drunk and ran over two young children playing on the sidewalk, killing one of them. Subsequent to this, the debtor inherited some assets under his brother's will and he attempted to disclaim (thus passing to his children). The Ohio Supreme Court held it was against public policy to allow a disclaimer. Although *Stein* appears to still be good law in Ohio, there was no discussion whatsoever of the plain language of the disclaimer statute that should arguably lead to a different result.

Because Ohio law (as well as some other states) does not recognize the relation-back fiction, might a spendthrift clause in Ohio that does not exempt disclaimers from its application inadvertently prevent disclaimers? Arguably Ohio, under *Stein*, regards a disclaimer as a transfer of property, despite the clear language of RC 5815.36. Thus, consider adding language similar to the bolded section below for spendthrift clauses:

> Any beneficiary may voluntary transfer or encumber his or her interest with the consent of a trustee who is not the beneficiary. **This spendthrift provision shall not restrict a beneficiary's right to disclaim any interest or the exercise of any power of appointment granted in this agreement.**

Therefore, to protect executors and trustees, it may be a good idea to investigate or at least get a statement from the disclaiming beneficiary as to whether 1) a disclaiming beneficiary is subject to federal tax liens and 2) whether the disclaimant is insolvent or knows of any pending claims.

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[108] *Stein v. Brown,* 18 Ohio St. 3d 305, 480 N.E.2d 1121 (1985)

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XIV. Medicaid/Government Benefit Issues

Just because ERISA provides extensive creditor protection does not mean that ERISA plans are not considered as a "resource" when determining Medicaid or other eligibility.[109] IRAs, insurance and annuities are similar, although there may be differences in calculating resources for "income streams", such as annuitized annuities, which is beyond the scope of this outline.

The government is not really a "creditor" unless and until it pays benefits. However, fraudulent transfer law can easily be applied to "Medicaid planning" involving gifts of assets.[110] Such cases will no doubt increase.

If the ERISA plan or other assets were not declared to authorities, then you have much bigger problems than creditor issues, you potentially have criminal fraud charges. An Ohio attorney in Toledo was recently disbarred for assisting a client in Medicaid fraud.[111]

Also remember 529 plans (and similarly, education IRAs (nka Coverdell Education Savings Accounts), that we think of as already gifted or "unavailable" and "outside" of the taxable estate for estate tax purposes or protected from creditors are not necessarily unavailable resources for Medicaid or other benefit calculations. A 529 plan is typically set up with the grantor as owner and kids, grandkids etc as "beneficiaries". Some may overlook the fact that the owner can name themselves as beneficiary and otherwise get such funds out, albeit with a 10% penalty. Thus, such funds may be considered "available resources".

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[109] See *Houghton ex rel. Houghton v. Reinertson*, 382 F.3d 1162 (10th Cir. 2004)

[110] See recent Hamilton County, 1st District Case of *Montgomery Care Center, Inc. v. Poulias* (2009), where a mother's transfer of assets to her son disqualified her from Medicaid but was a fraudulent transfer as to her anticipated creditor, which was the nursing home, not the government. A similar finding from a recent Clark County case, *Masonic Health Care v. Finley*, 176 Ohio App.3d 529 (2nd Dist. 2008), where elderly mom gifted Lebanon home and over $150,000 in assets to 3 kids but stiffed health care providers.

[111] *Toledo Bar Assn v. Cook*, 2007-Ohio-3253

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XV. Liability for Advisors

ACTS

Helping a client with typical estate and financial planning transfers involving insurance, IRAs, annuities and qualified plans will not typically involve liability for the advisor. Although there is potentially advisor liability for aiding and abetting contempt of court, money laundering, tax fraud, bankruptcy fraud, Medicaid fraud, wire fraud, mail fraud, obstruction of justice, R.I.C.O. or other statutes, these are usually underhanded attempts to help a client HIDE money or transactions.[112] I could find no case in the entire annotated Uniform Fraudulent Transfer Act of an attorney (or other advisor) incurring liability for aiding and abetting fraudulent transfers that were not subject to some other statute.

OMISSIONS

What if a client could have legitimately put funds into an IRA, annuity, insurance or qualified plan that is better protected, yet faults **you** the advisor for **failing** to advise him of this? Can a client sue for malpractice? It is unlikely that an average CPA or financial advisor would be found negligent for failing to address this, unless they held themselves out as having special knowledge in this area. Attorneys, however, are more likely to hold themselves as practicing "asset protection" and should be careful to exclude such planning from their scope of representation agreement unless the client is willing to pay the attorney to address this.

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[112] See, e.g., *Morganroth – Law Firm Sued for Advice to Debtor,* Jay Adkisson, Steve Leimberg's Asset Protection Planning Newsletter #32 (2003), dealing a blow to attorneys who helped John DeLorean hide assets

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XVI. Conflicts of Laws

This section might be subtitled, "sneaky ways for a creditor to get around the protections outlined in the prior 15 sections". I must admit, working for a national private bank that specializes in managing IRA rollovers for retirement, that I had some hesitancy including this section. Knowledge of these issues may severely curtail protection for insurance, annuities, IRAs, education IRAs or other type accounts that do not receive ERISA or other federal protections.

Ohio creditors and debtors are involved in most of the cases cited herein. Cases from other states usually concerned only that state's laws. But let's take a look at how the above protections may falter with interstate issues. John Stewart, a retired Columbus professional, takes a summer road trip with family to Washington, D.C. While driving in West Virginia, he accidentally causes a terrible accident, which leads to a $2M judgment, in excess of his $1Million insurance. Retired, he is comforted by the fact that he has $1Million socked away in a Roth IRA. Until, that is, he receives a writ of garnishment on the IRA from the West Virginia court.

Consider the somewhat similar case of *Clark v. Wilbur*:[113] In 1995, Dudley Allen and John Wilbur, Florida residents, lost a case and had a $6Million judgment entered against them jointly in West Virginia. In post-judgment discovery, it was determined that they owned

> "(1) Wilbur--(a) Peak Retirement Individual Retirement Account (IRA) (valued at approximately $ 40,000); (b) Charles Schwab IRA (valued at approximately $ 18,000); and (c) a beach house in Ponte Vedra, Florida (valued at approximately $ 1,000,000); (2) Allen--(a) Merrill Lynch IRA (valued at approximately $ 2,500); (b) Mass Mutual IRA Annuity (valued at over $ 100,000); and (3) Clark--Life USA IRA Annuity (valued at approximately $ 38,000)."

The question for the court became – which state's laws should apply to the motion for order to compel delivery of the above assets? Defendants claimed that Florida law should apply, of course, as it would exempt the above assets. Held – West Virginia law applied because:

"The mandate requiring resort to the law of the state where the district court is

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[113] *Clark v. Wilbur*, 913 F. Supp. 463 (S.D. WV, 1996)

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held applies to questions relating to whether assets are exempt from collection. See, e.g., *Chicago, Rock Island & Pac. Ry. Co. v. Sturm*, 174 U.S. 710, 717, 43 L. Ed. 1144, 19 S. Ct. 797 (1899) (stating "exemption laws are . . . part of the remedy and subject to the law of the forum"); ***Johns v. Rozet*, 826 F. Supp. 565, 567 (D.D.C. 1993)**; *Pallante v. Int'l Venture Invs., Ltd.*, 622 F. Supp. 667, 668 (N.D. Ohio 1985)(stating "generally . . . questions of exemption are determined solely by the laws of the forum"); *Marine Midland Bank v. Surfbelt, Inc.*, 532 F. Supp. 728, 729 (W.D. Pa. 1982) (stating "the law of the forum governs questions of exemption"); 11 Thomas J. Goger et al., Federal Procedure § 31:21 (1982).[114]

End Result?

The Court ORDERS as follows:

1. That, with respect to the property located at 837 Ponte Vedra Boulevard, Ponte Vedra Beach, Florida, Defendant Wilbur shall deliver a deed for such to Plaintiff assigning all of his right, title and interest in the property to Plaintiff, subject only to the West Virginia homestead exemption;

2. That, with respect to the Merrill Lynch IRA, Wilbur's Charles Schwab IRA, and the Peak Retirement Account (to the extent it contains assets other than annuities), Defendants Allen and Wilbur are ORDERED to convert these assets to cash and to withdraw the cash from their IRA accounts and, net of applicable tax penalties, deliver such cash to Plaintiff; and

3. That with respect to the Peak Retirement Account (to the extent it contains annuities), the Massachusetts Mutual IRA Annuity and the Life USA IRA Annuity, Defendants Wilbur, Allen and Clark shall surrender such annuities for their cash value and deliver such cash, net of any applicable tax penalties, to Plaintiff.

Ohio residents would not have fared any better. Might there have been better arguments to be made? (Defendants proceeded pro se in the above case). Perhaps. At the very least, bankruptcy may have been a good option for the defendants here. However, this brings up significant holes in state law protections that are just as disturbing as the holes in ERISA protection.

[114] *Id*. at 467

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XVII. Conclusions

Retirement Plans.

SEP-IRAs, Keogh, HR-10 and potentially 403(b)s and SIMPLE IRAs have **inferior** protection under Ohio law than an ordinary IRA. Similarly any other qualified plan that would otherwise be subject to ERISA, such as safe harbor 401(k)s and profit sharing plans, where the employer and/or spouse are the only participants, are also inferior under Ohio (and ERISA) law than an ordinary IRA in Ohio. Consider that a failing business may well lose employees to the point where only husband and wife are left in the plan – losing ERISA protection.[115] Strongly consider rolling these plans over to IRAs if possible.

Other instances where ERISA plans may be *inferior* to state law protections may be when the pension or other plan is in pay status, meaning the debtor/participant is mandatorily receiving payments (say, RMD or pension). Recall that tracing of the payments to other accounts outside the plan is not available.

If someone has spousal or child support claims, ERISA protection may be superior to state law IRA protection, since Ohio specifically exempts these creditors from its statute, though QDROs may be used to attach ERISA benefits.

Additionally, recall that for state/local tax claims, ERISA protection is superior to state law protections for IRAs (indeed, any state sanctioned protections). Thus, if there could be lingering tax claims out there (such as contingent responsible party debts), keep such funds in ERISA accounts, or even, if the plan permits, roll other retirement accounts into such plans.

Debtors in these plans can file bankruptcy to conceivably benefit from expanded coverage under BAPCPA that exempts all of these plans on near-equal footing. However, bankruptcy discharge is much more difficult than previously under the new act and this should probably not be counted on. For instance, if one does not qualify for Chapter 7 discharge (and many now do not, based on income or other factors), social security and retirement benefits (even ERISA protected and excluded from the bankruptcy estate) are counted for determining the ability to repay under

[115] See *Lowenschuss v. Selnick*, 117 F.3d 673 (9th Cir. 1999) where such attrition eviscerated ERISA protection.

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Chapter 13.

Consider maxing out such plans, including Roth 401(k), Roth 403(b) and even Roth conversions if possible. Paying the tax reduces the amount unprotected and increases the amount protected. It is unlikely to be considered a fraudulent transfer.[116] Roth conversions may also save estate taxes, particularly in states like Ohio with a separate estate tax scheme. Beware – there are a handful of states that do NOT provide the same protection for Roth IRAs as for traditional IRAs.

For "downstream" planning, consider leaving retirement plan assets in a trusteed IRA, or to a separate IRA trust that prohibits payment of probate estate debts (although apportionment of taxes should not be an issue).[117] The trusteed IRA with appropriate beneficiary designation has the unique capability in that the beneficiary/debtor may get not only state/federal protection for IRAs, but, more importantly, third-party spendthrift law protection.[118] This would require, of course, the IRA owner to place restrictions on the beneficiary's withdrawal rights similar to any other third party created spendthrift or discretionary trust.

Annuities and Insurance

As discussed, ordinary annuities should not be touted as an asset protected vehicle, at least under Ohio law. If a client moves to Florida this may be different. Insurance fares better under Ohio law, and the law in many other states. It is unclear whether "pushing the envelope" with such plans makes any difference, but it is clear that there is a better chance at protecting cash value in insurance than if it were held elsewhere. Adding so much cash that the policy becomes a Modified Endowment Contract (MEC) should be similarly protected. Although this protects more "cash" from creditors, courts may not see it as abusive since a MEC looks less like an investment than other products with more extensive "lifetime" benefits.

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[116] See, e.g., recent case of *In re Middendorf*, 381 BR 774 (Bankr. D. Kan. 2008) and *Wittmann v. Weir*, 1990 WL 63072 (Bankr. D. Kan. 1990), holding that payment of capital gains taxes from sale just prior to filing bankruptcy was neither preferential nor fraudulent transfer subject to set-aside. See also, *In re Stern*, 317 F.3d 1111 (9th Cir. 2003), where the court found that a debtor's transfer of a $1.4Million IRA to a qualified plan just prior to filing was NOT a fraudulent transfer.

[117] For pros and cons of using standalone or separate trusts for this purpose, see *Using Standalone or Separate Trusts Solely to Receive Retirement Benefits*, J. Retirement Planning, November/December 2007 by this author

[118] See generally, *Trusteed IRAs: An Elegant Estate Planning Option*, Trusts and Estates Sept 2009 and *Contrasting Conduit Trusts, Accumulation Trusts and Trusteed IRAs*, J. Retirement Planning, May-June 2007, by this author

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Appendix A

(bold, italics inserted by author **** denotes deleted sections)

R.C. §2329.66 Property that person domiciled in this state may hold exempt

(A) Every person who is domiciled in this state may hold property exempt from execution, garnishment, attachment, or sale to satisfy a judgment or order, as follows:

******

(6)(a) The person's interest in a beneficiary fund set apart, appropriated, or paid by a benevolent association or society, as exempted by section 2329.63 of the Revised Code;

(b) The person's interest in **contracts of life or endowment insurance or annuities**, as exempted by section 3911.10 of the Revised Code;

(c) The person's interest in a policy of **group insurance or the proceeds of a policy of group insurance**, as exempted by section 3917.05 of the Revised Code;

(d) The person's interest in money, benefits, charity, relief, or aid to be paid, provided, or rendered by a fraternal benefit society, as exempted by section 3921.18 of the Revised Code;

(e) The person's interest in the portion of benefits under policies of sickness and accident insurance and in lump sum payments for dismemberment and other losses insured under those policies, as exempted by section 3923.19 of the Revised Code.

******

(10)(a) Except in cases in which the person was convicted of or pleaded guilty to a violation of section 2921.41 of the Revised Code and in which an order for the withholding of restitution from payments was issued under division (C)(2)(b) of that section or in cases in which an order for withholding was issued under section 2907.15 of the Revised Code, and only to the extent provided in the order, and except as provided in sections 3105. 171, 3105.63, 3119.80, 3119.81, 3121.02, 3121.03, and 3123.06 of the Revised Code, the person's right to a **pension, benefit, annuity, retirement allowance, or accumulated contributions, the person's right to a participant account in any deferred compensation program offered by the Ohio public employees deferred compensation board**, a government unit, or a municipal corporation, or the person's other accrued or accruing rights, as exempted by section 145.56, 146.13, 148.09, 742.47, 3307.41, 3309.66, or 5505.22 of the Revised Code, and the person's right to benefits from the Ohio public safety officers death benefit fund;

(b) Except as provided in sections 3119.80, 3119.81, 3121.02, 3121.03, and 3123.06 of the Revised Code, the person's right to receive a **payment under any pension, annuity, or similar plan or contract**, not including a payment from a stock bonus or profit-sharing plan or a payment included in division (A)(6)(b) or (10)(a) of this section, on account of illness, disability, death, age, or length of service, **to the extent reasonably necessary for the support of the person and any of the person's dependents**, except if all the following apply:

(i) The plan or contract was established by or under the auspices of an insider that employed the person at the time the person's rights under the plan or contract arose.

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

(iii) The plan or contract is not qualified under the "Internal Revenue Code of 1986," 100 Stat. 2085, 26 U.S.C. 1, as amended.

(c) Except for any portion of the assets that were deposited for the purpose of evading the payment of any debt and

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except as provided in sections 3119.80, 3119.81, 3121.02, 3121.03, and 3123.06 of the Revised Code, the person's right in the assets held in, or to receive any payment under, **any individual retirement account, individual retirement annuity, "Roth IRA," or education individual retirement account** that provides benefits by reason of illness, disability, death, or age, to the extent that the assets, payments, or benefits described in division (A)(10)(c) of this section are attributable to any of the following:

(i) **Contributions of the person** that were less than or equal to the applicable limits on deductible contributions to an individual retirement account or individual retirement annuity in the year that the contributions were made, whether or not the person was eligible to deduct the contributions on the person's federal tax return for the year in which the contributions were made;

(ii) Contributions of the person that were less than or equal to the applicable limits on contributions to a Roth IRA or education individual retirement account in the year that the contributions were made;

(iii) Contributions of the person that are within the applicable limits on rollover contributions under subsections 219, 402(c), 403(a)(4), 403(b)(8), 408(b), 408(d)(3), 408A(c)(3)(B), 408A(d)(3), and 530(d)(5) of the "Internal Revenue Code of 1986," 100 Stat. 2085, 26 U.S.C.A. 1, as amended.

(d) Except for any portion of the assets that were deposited for the purpose of evading the payment of any debt and except as provided in sections 3119.80, 3119.81, 3121.02, 3121.03, and 3123.06 of the Revised Code, the person's right in the assets held in, or to receive any payment under, any **Keogh or "H.R. 10" plan** that provides benefits by reason of illness, disability, death, or age, **to the extent reasonably necessary for the support of the person and any of the person's dependents**.

*****
(17) Any other property that is **specifically exempted from execution, attachment, garnishment, or sale by federal statutes** other than the "Bankruptcy Reform Act of 1978," 92 Stat. 2549, 11 U.S.C.A. 101, as amended;

§3911.10 Proceeds exempt from claims of creditors

All contracts of **life or endowment insurance or annuities upon the life of any person**, or any interest therein, which may hereafter mature and which have been taken out for the benefit of, or made payable by change of beneficiary, transfer, or assignment to, **the spouse or children, or any persons dependent upon such person**, or an institution or entity described in division (B)(1) of section 3911.09 of the Revised Code, or any creditor, or to a **trustee for the benefit of such spouse, children, dependent persons**, institution or entity, or creditor, **shall be held, together with the proceeds or avails of such contracts, subject to a change of beneficiary if desired, free from all claims of the creditors of such insured person or annuitant**. Subject to the statute of limitations, the amount of any premium upon such contracts, endowments, or annuities, paid in fraud of creditors, with interest thereon, shall inure to their benefit from the proceeds of the contracts, but the company issuing any such contract is discharged of all liability thereon by the payment of its proceeds in accordance with its terms, unless, before such payment, written notice is given to it by a creditor, specifying the amount of the claim and the premiums which the creditor alleges have been fraudulently paid.

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Appendix B

11 USC § 522 Exemptions
(sections relating to protecting retirement plans **bolded** by author, sections completely irrelevant are deleted and replaced with ***)

SUBCHAPTER II - DEBTOR'S DUTIES AND BENEFITS

(a) In this section -

(1) "dependent" includes spouse, whether or not actually dependent; and

(2) "value" means fair market value as of the date of the filing of the petition or, with respect to property that becomes property of the estate after such date, as of the date such property becomes property of the estate.

(b)(1) Notwithstanding section 541 of this title, **an individual debtor may exempt from property of the estate the property listed in either paragraph (2) or, in the alternative, 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 (2) and the other debtor elect to exempt property listed in paragraph (3) of this subsection. If the parties cannot agree on the alternative to be elected, they shall be deemed to elect paragraph (2), where such election is permitted under the law of the jurisdiction where the case is filed.

(2) Property listed in this paragraph is property that 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) 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 730 days immediately preceding the date of the filing of the petition, 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).

(B) any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law; and

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(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.

(4) {{NOTE: Applicability.}} 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.

(B) If the retirement funds are in a retirement fund that has not received a favorable determination under such section 7805, those funds are exempt from the estate if the debtor demonstrates that--

(i) no prior determination to the contrary has been made by a court or the Internal Revenue Service; and

(ii)(I) the retirement fund is in substantial compliance with the applicable requirements of the Internal Revenue Code of 1986; or

(II) the retirement fund fails to be in substantial compliance with the applicable requirements of the Internal Revenue Code of 1986 and the debtor is not materially responsible for that failure.

(C) A direct transfer of retirement funds from 1 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, under section 401(a)(31) of the Internal Revenue Code of 1986, or otherwise, shall not cease to qualify for exemption under paragraph (3)(C) or subsection (d)(12) by reason of such direct transfer.

(D)(i) Any distribution that qualifies as an eligible rollover distribution within the meaning of section 402(c) of the Internal Revenue Code of 1986 or that is described in clause (ii) shall not cease to qualify for exemption under paragraph (3)(C) or subsection (d)(12) by reason of such distribution.

(ii) A distribution described in this clause is an amount that--

(I) has been distributed from 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; and

(II) to the extent allowed by law, is deposited in such a fund or account not later than 60 days after the distribution of such amount.

(c) Unless the case is dismissed, property exempted under this section is not liable during or after the case for any debt of the debtor that arose, or that is determined under section 502 of this title as if such debt had arisen, before the commencement of the case, except -

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(1) a debt of a kind specified in paragraph (1) or (5) of section 523(a) (in which case, notwithstanding any provision of applicable nonbankruptcy law to the contrary, such property shall be liable for a debt of a kind specified in section 523(a)(5));

(2) a debt secured by a lien that is -

(A)(i) not avoided under subsection (f) or (g) of this section or under section 544, 545, 547, 548, 549, or 724(a) of this title; and

(ii) not void under section 506(d) of this title; or

(B) a tax lien, notice of which is properly filed;

(3) a debt of a kind specified in section 523(a)(4) or 523(a)(6) of this title owed by an institution-affiliated party of an insured depository institution to a Federal depository institutions regulatory agency acting in its capacity as conservator, receiver, or liquidating agent for such institution; or

(4) a debt in connection with fraud in the obtaining or providing of any scholarship, grant, loan, tuition, discount, award, or other financial assistance for purposes of financing an education at an institution of higher education (as that term is defined in section 101 of the Higher Education Act of 1965 (20 U.S.C. 1001)).

(d) The following property may be exempted under subsection (b)(2) of this section:

(1) The debtor's aggregate interest, not to exceed $15,000 in value, in real property or personal property that the debtor or a dependent of the debtor uses as a residence, in a cooperative that owns property that the debtor or a dependent of the debtor uses as a residence, or in a burial plot for the debtor or a dependent of the debtor.

(2) The debtor's interest, not to exceed $2,400 in value, in one motor vehicle.

(3) The debtor's interest, not to exceed $400 in value in any particular item or $8,000 in aggregate value, in household furnishings, household goods, wearing apparel, appliances, books, animals, crops, or musical instruments, that are held primarily for the personal, family, or household use of the debtor or a dependent of the debtor.

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

(5) The debtor's aggregate interest in any property, not to exceed in value $800 plus up to $7,500 of any unused amount of the exemption provided under paragraph (1) of this subsection.

(6) The debtor's aggregate interest, not to exceed $1,500 in value, in any implements, professional books, or tools, of the trade of the debtor or the trade of a dependent of the debtor.

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

(8) The debtor's aggregate interest, not to exceed in value $8,000 less any amount of property of the estate transferred in the manner specified in section 542(d) of this title, in any accrued dividend or interest under, or loan value of, any unmatured life insurance contract owned by the debtor under which the insured is the debtor or an individual of whom the debtor is a dependent.

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

(10) The debtor's right to receive -

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

(B) a veterans' benefit;

(C) a disability, illness, or unemployment benefit;

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

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

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

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

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

(11) The debtor's right to receive, or property that is traceable to -

(A) an award under a crime victim's reparation law;

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

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

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(D) a payment, not to exceed $15,000, on account of personal bodily injury, not including pain and suffering or compensation for actual pecuniary loss, of the debtor or an individual of whom the debtor is a dependent; or

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

(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.

*****

(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, 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, shall not exceed $1,000,000 in a case filed by a debtor who is an individual, except that such amount may be increased if the interests of justice so require.

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Appendix C

Contrast how straightforward Florida's protection is….

§ 222.21. Exemption of pension money and certain tax-exempt funds or accounts from legal processes

(1) Money received by any debtor as pensioner of the United States within 3 months next preceding the issuing of an execution, attachment, or garnishment process may not be applied to the payment of the debts of the pensioner when it is made to appear by the affidavit of the debtor or otherwise that the pension money is necessary for the maintenance of the debtor's support or a family supported wholly or in part by the pension money. The filing of the affidavit by the debtor, or the making of such proof by the debtor, is prima facie evidence; and it is the duty of the court in which the proceeding is pending to release all pension moneys held by such attachment or garnishment process, immediately, upon the filing of such affidavit or the making of such proof.

(2) [As amended by s. 5, ch. 2005-82, effective May 26, 2005.] (a) Except as provided in paragraph (b), any money or other assets payable to a participant or beneficiary from, or any interest of any **participant or beneficiary in**, a retirement or profit-sharing plan that is qualified under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, or *s. 409 of the Internal Revenue Code of 1986*, as amended, is **exempt from all claims of creditors of the beneficiary or participant**.

(b) Any plan or arrangement described in paragraph (a) is not exempt from the claims of an alternate payee under a qualified domestic relations order. However, **the interest of any alternate payee under a qualified domestic relations order is exempt from all claims of any creditor, other than the Department of Revenue, of the alternate payee**. As used in this paragraph, the terms "alternate payee" and "qualified domestic relations order" have the meanings ascribed to them in *s. 414(p) of the Internal Revenue Code of 1986*.

(c) The provisions of paragraphs (a) and (b) apply to any proceeding that is filed on or after October 1, 1987.

(2) [As amended by s. 1, ch. 2005-101, effective June 1, 2005.] (a) Except as provided in paragraph (d), any money or other assets payable to an owner, a participant, or a beneficiary from, or any interest of any owner, participant, or beneficiary in, a fund or account is exempt from all claims of creditors of the owner, beneficiary, or participant if the fund or account is:

1. Maintained in accordance with a master plan, volume submitter plan, prototype plan, or any other plan or governing instrument that has been preapproved by the Internal Revenue Service as exempt from taxation under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, s. 409, s. 414, s. 457(b), or *s. 501(a) of the Internal Revenue Code of 1986*, as amended, unless it has been subsequently determined that the plan or governing instrument is not exempt from taxation in a proceeding that has become final and nonappealable;

2. Maintained in accordance with a plan or governing instrument that has been determined by the Internal Revenue Service to be exempt from taxation under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, s. 409, s. 414, s. 457(b), or *s. 501(a) of the Internal Revenue Code of 1986*, as amended, unless it has been subsequently determined that the plan or governing instrument is not exempt from taxation in a proceeding that has become final and nonappealable; or

3. Not maintained in accordance with a plan or governing instrument described in subparagraph 1. or subparagraph 2. if the person claiming exemption under this paragraph proves by a preponderance of the evidence that the fund or account is maintained in accordance with a plan or governing instrument that:

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a. Is in substantial compliance with the applicable requirements for tax exemption under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, s. 409, s. 414, s. 457(b), or *s. 501(a) of the Internal Revenue Code of 1986*, as amended; or

b. Would have been in substantial compliance with the applicable requirements for tax exemption under s. 401(a), s. 403(a), s. 403(b), s. 408, s. 408A, s. 409, s. 414, s. 457(b), or *s. 501(a) of the Internal Revenue Code of 1986*, as amended, but for the negligent or wrongful conduct of a person or persons other than the person who is claiming the exemption under this section.

(b) It is not necessary that a fund or account that is described in paragraph (a) be maintained in accordance with a plan or governing instrument that is covered by any part of the Employee Retirement Income Security Act for money or assets payable from or any interest in that fund or account to be exempt from claims of creditors under that paragraph.

(c) Any money or other assets that are exempt from claims of creditors under paragraph (a) do not cease to qualify for exemption by reason of a direct transfer or eligible rollover that is excluded from gross income under *s. 402(c) of the Internal Revenue Code of 1986*.

(d) Any fund or account described in paragraph (a) is not exempt from the claims of an alternate payee under a qualified domestic relations order or from the claims of a surviving spouse pursuant to an order determining the amount of elective share and contribution as provided in part II of chapter 732. However, the interest of any alternate payee under a qualified domestic relations order is exempt from all claims of any creditor, other than the Department of Revenue, of the alternate payee. As used in this paragraph, the terms "alternate payee" and "qualified domestic relations order" have the meanings ascribed to them in *s. 414(p) of the Internal Revenue Code of 1986*.

(e) This subsection applies to any proceeding that is filed on or after the effective date of this act.

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SPEAKER BIO

After receiving his *Juris Doctor* from the Northwestern School of Law of Lewis and Clark College, Ed went on to complete his masters degree in tax law (*LL.M.*) at Capital University in Columbus and his MBA from Xavier University. He practiced as Of Counsel in the area of estate planning at the Cincinnati law firm of Furnier, Flagel & Thomas, LLP and had his own solo practice in Middletown and later Springboro, Ohio. Ed is now a Wealth Specialist concentrating in estate planning and tax matters for Key Private Bank clients nationwide as well as National Manager of Wealth Strategies Communications. He is married and lives in Springboro with his wife and two daughters.

On the Bar level, Ed is a certified specialist through the Ohio State bar Association in Estate Planning, Probate and Trust Law. He is the recently outgoing Chair of the Dayton Bar Association's Estate Planning, Trust and Probate Committee, as well as on the local board of the Society of Financial Service Professionals. Ed is also a Certified Financial Planner (CFP®) and Registered Financial Consultant (RFC®) and has passed Level 1 of the Certified Financial Analyst exam. He is not currently giving any specific advice on investments or practicing law. He confines his practice with Key Private Bank to working with high net worth individuals and their attorneys, accountants and financial advisors in conjunction with KeyBank's financial planning, investment management, trust services and wealth management teams nationwide. In addition to traditional investment advisory, KeyBank's investment and trust department acts as trustee/executor, agent for trustee/executor, administrative trustee with outside financial advisors or investment advisor only for individual trustees, helping to ensure they better comply with the Uniform Prudent Investor Act.

Ed is a frequent speaker at continuing legal education courses and financial conferences. Recent Articles include: "*Asset Protection Traps for the Unwary: Fraud, Funding and Future Interests*" published in the Journal of Practical Estate Planning in April/May of 2007, "*Contrasting Conduit Trusts, Accumulation Trusts and Trusteed IRAs*" in the Journal of Retirement Planning in May/June 2007, "*Ensuring the Stretch*" July/August 2007 Journal of Retirement Planning and "*Separate or Standalone Trusts as IRA Beneficiaries*", in the October/November 2007 issue of the CCH Journal of Retirement Planning, and *Trusteed IRAs: An Elegant Estate Planning Option*, September 2009 Trusts and Estates. He is currently finishing articles entitled *Roth IRA Conversion Analysis: What Most Advisors are Missing and What Software Won't Tell You* and *Protecting Trust Assets from Super-Creditors.*

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