

ERISA, EMPLOYEES, AND CREDITORS' RIGHTS: A SEARCH FOR A CONSISTENT THEME

This Note examines the effect of the Employees Retirement Income Security Act of 1974 (ERISA)¹ on the attempts of third party creditors of employees to reach employees' benefit plan funds. Through ERISA, Congress intended to ensure the equitable character and financial soundness of employee benefit plans.² That intent, however, combined with congressional silence on the rights of creditors to reach plan funds to satisfy employee debts³ has prevented the development of a consistent theme in allowing creditor access to the funds in ERISA qualified plans.

I. INTRODUCTION: THE PROBLEM CREATED BY ERISA'S SILENCE ABOUT CREDITOR'S RIGHTS

Enacted in 1974, ERISA governs the establishment, operation and disposition of employee benefit plans.⁴ ERISA distinguishes between welfare and pension benefit plans.⁵ Welfare plans are those established or

1. Pub. L. No. 93-406, 88 Stat. 829 (codified at 29 U.S.C. §§ 1001-1461 (1982, Supp. I 1983, Supp. II 1984, Supp. III 1985, & Supp. IV 1986)).

2. ERISA § 2 (29 U.S.C. § 1001 (1982)) sets forth the congressional findings and declaration of policy behind ERISA:

The Congress finds that the growth in size, scope, and numbers of employee benefit plans in recent years has been rapid and substantial; that the operational scope and economic impact of such plans is increasingly interstate; that the continued well-being and security of millions of employees and their dependents are directly affected by these plans; . . . that owing to the lack of employee information and adequate safeguards concerning their operation, it is desirable in the interests of employees and their beneficiaries, and to provide for the general welfare and the free flow of commerce, that disclosure be made and safeguards be provided with respect to the establishment, operation and administration of such plans; . . . that owing to the inadequacy of current minimum standards, the . . . funds to pay promised benefits may be endangered; that owing to the termination of plans before requisite funds have been accumulated, employees and their beneficiaries have been deprived of anticipated benefits; and that it is therefore desirable in the interests of employees and their beneficiaries, for the protection of the revenue of the United States, and to provide for the free flow of commerce, that minimum standards be provided assuring the equitable character of such plans and their financial soundness.

ERISA § 2 (29 U.S.C. § 1001 (1986)).

3. Prior to ERISA, the common law of trusts governed access to retirement plans. Courts disagreed about whether retirement trusts could be protected from the reach of a beneficiary's creditors. See generally 2 A. SCOTT, THE LAW OF TRUSTS, § 151 (3rd ed. 1967 and Supp. 1987).

4. For an in-depth discussion of ERISA and relevant tax code provisions see M. CONAN, QUALIFIED RETIREMENT AND OTHER EMPLOYEE BENEFIT PLANS, §§ 3.1-21.7 (1988). For a very brief summary of the structure of ERISA see G. BOREN, QUALIFIED DEFERRED COMPENSATION PLANS § 1:04 (1983).

5. ERISA § 3(3) (29 U.S.C. § 1002(3)) states: "The term 'employee benefit plan' or 'plan'

maintained by an employer that provide for employees' health care, sick-time, vacation, holiday, training, daycare, scholarships, legal services or other non-income providing benefits.⁶ Pension plans are plans established or maintained by an employer that provide for employees' retirement income or income deferred to the end of employment with the plan sponsor.⁷

Congress enacted ERISA to protect the anticipated benefits to employees and their beneficiaries under these plans. ERISA provides minimum standards for both types of benefit plans.⁸ ERISA's governance of pension benefit plans is more stringent; for example, pension plans must contain an anti-alienation and anti-assignment of benefits provision.⁹ In addi-

means an employee welfare benefit plan or an employee pension benefit plan or a plan which is both an employee welfare plan and an employee pension benefit plan." *Id.*

This Note adopts this definition of "benefit plan" and will specify welfare plan or pension plan when addressing only that particular type of plan.

6. ERISA provides:

The terms "employee welfare benefit plan" and "welfare plan" mean any plan, fund or program . . . established or maintained by an employer or by an employee organization, or by both, to the extent that such plan, fund or program was established or is maintained for the purpose of providing for its participants or their beneficiaries, through the purchase of insurance or otherwise, (A) medical, surgical, or hospital care or benefits, or benefits in the event of sickness, accident, disability, death or unemployment, or vacation benefits, apprenticeship or other training programs, or day care centers, scholarship funds, or prepaid legal services, or (B) any benefit described in § 186 (c) [§ 302(c) of the Labor Management Relations Act of 1947] of this title (other than pensions on retirement or death, and insurance to provide such pensions).

ERISA § 3(1) (29 U.S.C. § 1002(1)).

7. ERISA provides:

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

- (i) provides retirement income to employees, or
- (ii) results in a deferral of income by employees for periods extending to the termination of covered employment or beyond, regardless of the method of calculation the contributions made to the plan, the method of calculating the benefits under the plan or the method of distributing benefits from the plan.

ERISA § 3(2) (29 U.S.C. § 1002(2)). *See generally* G. BOREN, *supra* note 4, at § 1:07 (discussing the attributes of defined benefit pension plans).

8. *See supra* note 2. A mere promise to pay welfare-type benefits can constitute an ERISA covered welfare benefit plan. Thus, arguably, a written instrument is not required to create a welfare plan. *See, e.g.,* Scott v. Gulf Oil Corp., 754 F.2d 1499, 1502-04 (9th Cir. 1985) ("[E]xistence of a written instrument is not a prerequisite to ERISA coverage."); Donovan v. Dullingham, 688 F.2d 1367, 1372 (11th Cir. 1982) ("ERISA does not require a formal written plan.").

9. ERISA provides:

- (1) Each pension plan shall provide that benefits provided under the plan may not be assigned or alienated.
- (2) For the purposes of paragraph (1) of this subsection, there shall not be taken into

tion, plans containing such provisions fulfill some of the requirements for tax breaks under the Internal Revenue Code (I.R.C.).¹⁰ The Secretary of Labor, Secretary of Treasury and the Pension Benefit Guaranty Corporation have the duty of enforcing and applying ERISA.¹¹

Section 514(a) of ERISA preempts all state law relating to employee benefit plans.¹² Based on ERISA's legislative history,¹³ and this broad preemption provision, both courts and commentators have suggested that Congress intended the courts to create a federal common law of employee benefit plans to fill the gaps Congress left open in the original

account any voluntary and revocable assignment of not to exceed 10 percent of any benefit payment, or of any irrevocable assignment or alienation of benefits executed before September 2, 1974 [the date of enactment]. The preceding sentence shall not apply to any assignment or alienation made for the purpose of defraying plan administration costs. For purposes of this paragraph a loan made to a participant or beneficiary shall not be treated as an assignment or alienation if such loan is secured by the participant's accrued nonforfeitable benefit and is exempt from the tax imposed by section 4975 of Title 26 [Internal Revenue Code of 1954] (relating to tax on prohibited transactions).

ERISA § 206(d)(1),(2) (29 U.S.C. § 1056(d)(1),(2) (1982)). ERISA subjects pension plans to many other requirements to which welfare plans are not subjected. *See, e.g.*, 29 U.S.C. §§ 1051-1086 (1982) (participation and vesting, and funding requirements).

10. I.R.C. § 401(a)(13) (1986). This section is almost identical to ERISA's § 206(d), *supra* note 9. There are other tax qualifying requirements imposed by the IRS. *See G. BOREN, supra* note 4, §§ 2:09-2:15. (discussing general requirements for qualification).

11. Reorg. Plan No. 4 of 1978, 3 C.F.R. § 332 (1978), *reprinted in* 29 U.S.C. § 1001 (1982), and *in* 92 Stat. 3790 (1978), arranges responsibilities between the Secretary of Treasury and the Secretary of Labor. The Plan is not a statute. However, as a result of the plan ERISA statutes do not accurately reflect the responsibilities for enforcement and interpretation of ERISA. BOREN, *supra* note 4, § 1:04 n.2. The Pension Benefit Guaranty Corporation is a government agency within the Department of Labor. Among other things the corporation is empowered to insure many defined pension plans in order to provide uninterrupted payment of pension benefits. 29 U.S.C. § 1302 (1982). Title III of ERISA (29 U.S.C. §§ 1201-42) describes the division of power between the Secretary of Labor, Secretary of Treasury and the Corporation. However, Title III must be read in conjunction with the Reorganization Plan. Title IV (29 U.S.C. §§ 1301-68) of ERISA describes the powers of the Pension Benefit Guaranty Corporation. *See generally* BOREN, *supra* note 4, § 1:04 (summarizing the division of authority over ERISA and the powers of the Pension Plan Guaranty Corporation); CONAN, *supra* note 4, §§ 22.1-21.5 (discussing enforcement of ERISA).

12. ERISA provides:

Except as provided in subsection (b) of this section, the provisions of this title and title IV shall supersede any and all State laws insofar as they may now or hereafter relate to any employee benefit plan described in section 4(a) [29 U.S.C. § 1003(a)] and not exempt under section 4(b) [29 U.S.C. § 1003(b)]. This section shall take effect on January 1, 1975.

ERISA § 514(a) (29 U.S.C. § 1144(a)). Part (b) of section 514 contains several exemptions to this broad preemption clause, most notably the exemption for state laws regulating insurance.

13. "It is also intended that a body of Federal substantive law will be developed by the courts to deal with issues involving rights and obligations under private welfare and pension plans." 120 CONG. REC. 29,942 (1974) (statement of Sen. Javits), *reprinted in* 3 LEGISLATIVE HISTORY OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974, at 4771 (1976) [hereinafter ERISA LEGISLATIVE HISTORY].

legislation.¹⁴ One such area was the right of creditors of employees to have access to the employees' benefit funds.¹⁵ This congressional silence, combined with ERISA's general purpose to protect the funds of retirement plans, and the need of creditors to be paid, have hindered the courts' development of consistent guidelines in creditors' attempts to reach an employee's benefit plan funds.

In examining this problem, Part II of this Note explains the law pertaining to dependent or ex-spouse creditors of employees. Part III discusses the effect of ERISA on creditors' attempts to reach employees' pension and welfare funds. Part IV explores the effect of conflicts between ERISA and the Bankruptcy Code upon bankruptcy creditors' success in accessing benefit plan funds. Finally, Part V discusses several solutions that would create a consistent theme in the law of creditors' rights to reach employees' funds in ERISA benefit plans.

II. THE RIGHTS OF CREDITORS WHO ARE DEPENDENTS OR EX-SPOUSES OF THE EMPLOYEE-DEBTOR

A. *Pre-ERISA*

Prior to ERISA, the common law of trusts governed creditors' access to employee benefit plans¹⁶ Trust funds were considered property of the debtor-beneficiary and available for payment of the beneficiary's debts.¹⁷ To reach these funds, creditors needed a judgment for the amount owed. In addition, the debtor-beneficiary must have had access to the trust funds.¹⁸

Problems for creditors arose when a trust contained a spendthrift provision.¹⁹ Such a provision explicitly bars the alienation and assignment of trust funds and may restrict the beneficiary's access to the trust funds.

14. See, e.g., G. BOREN, *supra* note 4, at § 16:17.60; Sherman, *Spendthrift Trust and Employee Pensions: The Problem of Creditor's Rights*, 55 IND. L.J. 247, 257-58 n.42-45 (1980) (quoting Senator Javits).

15. ERISA § 206(d)(1) does not mention anything about creditors. See *supra* note 9. See also *Ellis Nat'l Bank of Jacksonville v. Irving Trust Co.*, 786 F.2d 466 (2d Cir. 1986); *Tenneco Inc. v. First Virginia Bank of Tidewater*, 698 F.2d 688-89 (4th Cir. 1983).

Many federal courts struggling to fill this gap have turned to state laws for analogies. See *infra* notes 41-105 and accompanying text.

16. *Sherman*, *supra* note 14, at 250-52.

17. G. BOGERT, *TRUST & TRUSTEES* § 193 (2d ed. 1965).

18. In addition, the creditor had to show the debtor lacked enough property to pay his or her debts before the court would grant access to the fund. *Sherman*, *supra* note 14 at 250-51.

19. Spendthrift trusts are "[t]rusts in which the interest of a beneficiary cannot be assigned by him or reached by his creditors . . ." 2 A. SCOTT, *supra* note 3, at § 151.

Generally, spendthrift provisions are held to deny creditors access to the funds.²⁰ Some states' statutes provide that spendthrift provisions can protect funds only to the extent necessary for the beneficiaries' support.²¹ Courts have relied considerably upon the law of spendthrift trusts to determine the rights of creditors to ERISA qualified pension plan funds.²²

Prior to ERISA, dependents and ex-spouses could reach retirement trusts containing a spendthrift provision only if the trust was in pay status.²³ The family support exception to spendthrift trust law, provided access into the trust. The courts created this exception because of the public policy that child support and alimony were continuing obligations, not debts, and thus transcended the limits of a spendthrift clause.²⁴

B. Federal Common Law Exception to Section 206(d)(1) of ERISA.

ERISA Section 206(d)(1) prevents alienation or assignment of pension plan benefits.²⁵ The Secretary of Treasury and various courts have interpreted this section to bar garnishment and attachments of ERISA protected pension plans.²⁶ In addition, the ERISA state law preemption

20. When a person creates a spendthrift trust for his or her own benefit, however, creditors are not generally barred from access to the funds. "[I]t is against public policy to permit a man to tie up his own property in such a way that he can still enjoy it but can prevent his creditors from reaching it." 2 A. SCOTT, *supra* note 3, at § 156.

21. *Id.* at § 152.1.

22. See *infra* notes 127-36 and accompanying text.

23. By "pay status" I mean that the funds are accessible to the debtor-employee. Absent a spendthrift provision, presumably, retirement trusts were accessible by family members in the same manner as other creditors. See 2 A. SCOTT, *supra* note 3, at § 147.2.

24. *Keller v. Keller*, 284 Ill. App. 198, 206, 1 N.E. 2d 773, 777 (1936) (support of children transcends all contractual obligations); *Safe Deposit & Trust of Baltimore v. Robertson*, 192 Md. 653, 663, 65 A.2d 292, 246 (1949) (alimony is an obligation continuing during the joint lives of the parties and is a duty not a debt). See also 2 A. SCOTT, *supra* note 3, at § 157.1; *Sherman*, *supra* note 14, at 271.

25. See *supra* note 9.

26. Treas. Reg. 1.401(a)-13(b)(1) (1978) provides:

(b) No assignment or alienation.

(1) *General Rule.* Under § 401(a)(13), a trust will not be qualified unless the plan of which the trust is a part provides that benefits provided under the plan may not be anticipated, assigned (either at law or in equity), alienated or subject to attachment, garnishment, levy, execution or other legal process.

ERISA § 3002(c) (29 U.S.C. § 1202(c)) allows the Secretary of Treasury to promulgate regulations covering ERISA's minimum vesting, funding and participation standards. Section 206(d) is part of ERISA's vesting standards. By virtue of this grant of authority, the Secretary of Treasury's regulation interpreting I.R.C. § 401(a)(13) has been viewed as the controlling interpretation of ERISA § 206(d). In addition, I.R.C. § 401(a)(13) and ERISA § 206(d) are almost identical, leading courts to conclude that the regulation is also an interpretation of ERISA § 206(d). Further, the Secretary's authority granted in ERISA § 3002(c) is legislative in nature, giving the Treasury's regulations great

provision, section 514(a),²⁷ would seem to preempt the common law family support provision, because, contrary to ERISA, the exception permitted attachment of pension plan benefits.²⁸ The inequity of preempting this well-established exception led courts to develop a family exception to section 206(d)(1).²⁹

Federal courts seized upon the language in section 2 of ERISA to find that one of ERISA's purposes was to protect the employee's family.³⁰ Courts further reasoned that ERISA was not intended to alter traditional family support obligations.³¹ Federal courts almost unanimously upheld state laws allowing garnishments to fulfill family support obligations such as child support, alimony, and community property rights.³²

C. Congress Responds: The Retirement Equity Act of 1984

The Retirement Equity Act of 1984 codified the family support exception to section 206(d)(1).³³ The statute requires a Qualified Domestic Relations Order (Q.D.R.O.)³⁴ as a condition precedent to benefit plan

weight. See *Ellis Nat'l Bank of Jacksonville v. Irving Trust Co.*, 786 F.2d 466 (2d Cir. 1986); *Tenneco v. First Virginia Bank of Tidewater*, 698 F.2d 688 (4th Cir. 1983); *General Motors Corp. v. Buha*, 623 F.2d 455 (6th Cir. 1980); Note, *ERISA and Tenneco: A One-Two Punch on Judgment Creditors Garnishing Pension Accounts*, 41 WASH. & LEE L. REV. 556, 566 (1984) (discussing the weight given to the Secretary's regulation).

27. See *supra* note 12 and accompanying text.

28. *General Motors v. Townsend*, 468 F. Supp. 466 (E.D. Mich. 1976) (literal reading of ERISA § 206(d) precludes an attachment of benefit plans for support of dependent family members).

29. *Stone v. Stone*, 450 F. Supp. 919 (N.D. Cal. 1978), *aff'd*, 632 F.2d 740 (9th Cir. 1980) (one of the first cases to develop a family support exception to § 206(d)(1)).

30. *American Tel. & Tel. Co. v. Merry*, 592 F.2d 118, 124 (2d Cir. 1979) (citing § 2 of ERISA as supporting an implied exception to § 206(d)(1) for the support and well-being of an employee's family); *Stone v. Stone*, 450 F. Supp. 919, 926, 930-31 (N.D. Cal. 1978), *aff'd*, 632 F.2d 740 (9th Cir. 1980) (members of an employee's family part of the class of people ERISA protects). See *supra* note 2 (goals of ERISA).

31. *Savings and Profit Sharing Fund of Sears Employees v. Gago*, 717 F.2d 1038 (7th Cir. 1983) (ERISA interpreted not to preempt all conflicting state domestic relations law); *Operating Engineers Local 428 Pension Trust Fund v. Zamborsky*, 650 F.2d 196 (9th Cir. 1981) (recognizing that ERISA does not preempt obligations to pay alimony). See *supra* note 30.

32. See *supra* notes 30-31; G. BOREN, *supra* note 4, at § 2:13.

33. Pub. L. No. 98-397, 98 Stat 1433 (codified at 29 U.S.C. §§ 1001-1461 (1986)). The family support exception now appears in ERISA 206(d)(3)(A) (codified at 29 U.S.C. § 1056(d)(3)). The I.R.C. parallel provision to § 206(d)(3)(A) is § 414(p)(1)-(13) (1986). The I.R.C. parallel provision to ERISA § 206(d)(3)(A) allows the payment from pension funds in accord with a Qualified Domestic Relations Order. See *infra* note 34 and accompanying text.

34. ERISA § 206(d)(3)(A),(B) defines the Qualified Domestic Relations Order exception to 206(d)(1). § 206(d)(3)(A),(B) (29 U.S.C. 1056(d)(3)(A),(B)) provides:

(A) Paragraph (1) shall apply to the creation, assignment, or recognition of a right to any benefit payable with respect to a participant pursuant to a domestic relations order, except

fund access. A Q.D.R.O. is a court order, decree, or judgment for the garnishment of benefit plan funds that assigns or recognizes ex-spouses' or dependents' right to receive benefits, specifies the amount to be paid, defines the payment period, and specifies other minor requirements.³⁵ The legislative history to the Retirement Equity Act indicates that Q.D.R.O.'s may only require payment up to the amount the employee is entitled to under the pension plan.³⁶ Further, the amendments provide that state garnishment and attachment laws are not preempted so far as they are used to enforce Q.D.R.O.'s.³⁷

that paragraph (1) shall not apply if the order is determined to be a qualified domestic relations order. Each pension plan shall provide for the payment of benefits in accordance with the applicable requirements of any qualified domestic relations order.

(B) For purposes of this paragraph—

- (i) the term "qualified domestic relations order" means a domestic relations order—
 - (I) which creates or recognizes the existence of an alternate payee's right to, or assigns to an alternate payee the right to, receive all or a portion of the benefits payable with respect to a participant under a plan, and
 - (II) with respect to which the requirements of subparagraphs (C) and (D) are met, and
- (ii) the term "domestic relations order" means any judgment, decree, or order (including approval of a property settlement agreement) which—
 - (I) relates to the provision of child support, alimony payments, or marital property rights to a spouse, former spouse, child, or other dependent of a participant, and
 - (II) is made pursuant to a State domestic relations law (including a community property law).

Id.

35. ERISA § 206(d)(3)(C),(D) provides:

(C) A domestic relations order meets the requirements of this subparagraph only if such order clearly specifies—

- (i) the name and the last known mailing address (if any) of the participant and the name and mailing address of each alternate payee covered by the order,
- (ii) the amount or percentage of the participant's benefits to be paid by the plan to each such alternate payee, or the manner in which such amount or percentage is to be determined,
- (iii) the number of payments or period to which such order applies, and
- (iv) each plan to which such order applies.

(D) A domestic relations order meets the requirements of this subparagraph only if such order—

- (i) does not require a plan to provide any type or form of benefit, or any option, not otherwise provided under the plan,
- (ii) does not require the plan to provide increased benefits (determined on the basis of actuarial value), and
- (iii) does not require the payment of benefits to an alternate payee which are required to be paid to another alternate payee under another order previously determined to be a qualified domestic relations order.

Id. See generally G. BOREN, *supra* note 4, at § 2:13.50 (discussing Q.D.R.O.'s.)

36. See, e.g., G. BOREN, *supra* note 4, at § 2:13.50 n.8 (citing 2 H.R. CONF. REP. NO. 841, 99th Cong., 2d Sess. 858 (1986)).

37. See ERISA § 514(b)(7) (codified at 29 U.S.C. § 1114(b)(7)).

III. CREDITORS' ACCESS TO EMPLOYEES' PENSION AND WELFARE PLAN FUNDS

A. Pension Plan Access

An ERISA pension plan is an arrangement between an employer and its employees creating or maintaining a fund to provide retirement income for employees and must contain a restriction preventing alienation or assignment of plan funds.³⁸ ERISA section 206(d)(2), however, explicitly allows employees to make voluntary and revocable assignments not exceeding ten percent of a benefit payment.³⁹ Also, section 206(d)(2) allows employees to use nonforfeitable benefits as collateral for a loan.⁴⁰

The Fourth Circuit expressed the dominant interpretation of section 206(d)(1) in *Tenneco, Inc. v. First Virginia Bank of Tidewater*.⁴¹ The court held that section 206(d)(1) bars garnishment, attachment, levy or other legal process aimed at accessing pension benefits.⁴² In *Tenneco*, a significant portion of the funds in the employee's stock ownership and thrift plans were payable to the employee at will. The court nonetheless granted protection from judgment creditors.⁴³ The Fourth Circuit based its reading of the statute on the Treasury Regulation implementing sec-

38. See *supra* note 7 and accompanying text.

39. See *supra* note 9 and accompanying text.

40. See *supra* note 9 and accompanying text. Nonforfeitable benefits are those obtained by a participant or his beneficiary by virtue of the participant's service and are unconditional and legally enforceable against the plan. ERISA § 3(19) (29 U.S.C. 1002(19)).

41. 698 F.2d 688 (4th Cir. 1983).

42. *Id.* at 688-90. Barring creditors' access to funds payable at the will of the employee departs from some of the law of spendthrift trusts. Historically, a trust created by a person for his or her own benefit would not be protectable from creditors. See 2 A. SCOTT, *supra* note 3 at § 156. In *Tenneco*, up to 75% of the employee's contributions to the plan were withdrawable at will when the employment relationship ended or after two years of participation in the plan. 698 F.2d at 690. Thus, the employee was able to tie up his own funds and enjoy them at will while his creditors went unpaid. Commentators have considered this contrary to public policy; see *supra* note 19.

Aside from the *Tenneco* court's § 206(d) ruling, the Fourth Circuit's opinion arguably could be read to hold by implication that pre-retirement withdrawal of pension funds are protected from creditors for 60 days. During these 60 days the employee is given the opportunity to roll over the money into another ERISA protected plan. Once the 60 days are over, however, the funds originating from a ERISA plan, and not rolled, over are subject to garnishment. 698 F.2d at 691. See also I.R.C. § 403(a)(4) (1986).

43. The court stated that ERISA prohibits garnishment of pension plan benefits, despite the method by which they are payable. *Id.* at 690. But see *infra* notes 127-43 and accompanying text (discussion of bankruptcy courts' rulings that benefits freely accessible by an employee are not protected from creditors).

tion 206(d)(1).⁴⁴ While section 206(d) only prohibits assignment or execution, the regulation in addition, prohibits levy and garnishment.⁴⁵ The court, without explanation, adopted these additional restrictions finding the regulation to be the controlling interpretation of section 206(d)(1) because the secretary, in promulgating the regulation, did not abuse his discretion.⁴⁶

The majority of courts have adopted the implicit holding in *Tenneco*,⁴⁷ that ERISA section 514(a) preempts state laws that allow creditors access to pension benefits.⁴⁸ One district court has extended this reasoning to allow preemption of a state law permitting a levy upon an ERISA pension plan to pay state taxes.⁴⁹

On the other hand one commentator, Professor Young, argues that the Treasury Regulation incorrectly interprets ERISA's legislative history.⁵⁰ Young argues that sections 206(d)(1) and (2) should be read to prevent voluntary assignments of not more than ten percent of plan funds. In addition, because garnishments and attachments are not voluntary, they

44. See *supra* note 26. The Secretary promulgated this regulation pursuant to his authority to establish standards governing several sections of ERISA, including § 206(d).

45. Treas. Reg. § 1.401(a)-(13)(b)(1).(1978). See *supra* note 26 (text of regulation).

46. 698 F.2d at 689-90. Implicit in the court's holding is the belief that the Treasury did not abuse its discretion in promulgating the Regulations. As a general rule, regulations promulgated pursuant to a statutory grant of authority have legislative effect as long as the regulation is not an abuse of discretion. *Batterton v. Francis*, 432 U.S. 416, 425 (1977). See *Helvering v. Winmill* 305 U.S. 79, 83 (1938) ("[t]reasury regulations and interpretations long continued without substantial change, applying to an unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law."). See also *supra* note 26.

47. See, e.g., *United Metal Products Corp. v. National Bank of Detroit*, 811 F.2d 297, 300 (6th Cir. 1987); *Ellis Nat'l Bank of Jacksonville v. Irving Trust*, 786 F.2d 466 (2d Cir. 1986) (§ 206(d)(1) bars garnishment of funds in a pension plan wrongfully acquired by the employee); *General Motors Corp. v. Buha*, 623 F.2d 455, 462 (6th Cir. 1980) (ERISA bars garnishment of qualified pension funds); *Commercial Mortgage Ins., Inc. v. Citizens Nat'l Bank of Dallas*, 526 F. Supp. 510, 520 (N.D. Tex. 1981).

48. The court ruled that garnishments, attachments, levies and other state procedures directed towards accessing pension funds were prohibited by ERISA § 206(d)(1). This reasoning is similar to that found in the Supreme Court's decision in *Alessi v. Raybestos-Manhattan, Inc.*, 451 U.S. 504 (1981) (state law prohibiting what ERISA explicitly allows is preempted). See *supra* note 12 (text of ERISA § 514(a)); Note, *ERISA and Tenneco: A One-Two Punch on Judgment Creditors Garnishing Pension Accounts* 41 WASH. & LEE. L. REV. 556, 563 (1984).

49. *Northwest Airlines Inc. v. Roemer*, 603 F. Supp. 7, 9-10 (D. Minn. 1986) (ERISA § 206(d) implicitly indicates Congress' intent to preempt a state's authority to levy on an ERISA protected pension plan).

50. S. YOUNG, PENSION AND PROFIT-SHARING PLANS § 13.03 (1987).

should not generally be prevented by section 206(d)(1).⁵¹ Professor Young's argument must be based on a belief that the Treasury Secretary acted either arbitrarily or capriciously, or abused his discretion in promulgating the Regulations.⁵²

The Eleventh Circuit and the District of Columbia Circuit, however, have recognized one exception to *Tenneco*.⁵³ According to these courts, section 206(d)(1) does not bar access to ERISA pension benefits when the employee-debtor obtained the funds through wrongdoing against the employer. In *St. Paul Fire and Marine Insurance Co. v. Cox*⁵⁴ the Eleventh Circuit held that ERISA does not preempt the equitable principle that a person should not benefit from his wrongful acquisition of funds.⁵⁵

51. This reasoning is based on ERISA's legislative history contained in H.R. REP. NO. 93-1280, 93rd Cong., 2d Sess. 280 reprinted in ERISA LEGISLATIVE HISTORY, *supra* note 13 at 4547.

However, the plan may provide that after a benefit is in pay status, there may be a voluntary revocable assignment (not to exceed 10 percent of any benefit payment) by an employee which is not for purposes of defraying the administrative costs of the plan. For purposes of this rule, a garnishment or levy is not to be considered a voluntary assignment.

Id.

In S. YOUNG, *supra* note 50, at § 13.03, the author asserts that the second sentence in the above quote merely defines what is not a voluntary assignment in connection with the preceding sentence. The author further states that ERISA's anti-assignment rule (§ 206(d)(1)) does not prevent garnishments or levies generally. *Id.*

A line of New York cases support Young's argument. See, e.g., *National Bank of North America v. International Bhd. of Elec. Workers, Local 3*, 69 A.D. 2d 679, 419 N.Y.S.2d 127 (1979) (state law allowing judgment creditor to garnish property of judgment debtor neither in conflict nor preempted by ERISA); *Pepitone v. Pepitone*, 108 Misc. 2d 12, 436 N.Y.S.2d 966 (N.Y. Sup. Ct. 1981) (ERISA does not immunize pension payments from family support obligations); *Plymouth Rock Fuel Corp. v. Bank of New York*, 102 Misc. 2d 235, 425 N.Y.S.2d 908 (N.Y. Sup. Ct. 1979) (statutory prohibition of assignments of plans did not exempt Keogh plan from garnishment by judgment creditors). More recent New York cases, however, appear to adopt the approach of the Fourth Circuit in *Tenneco*. See, e.g., *Helmsley-Spear, Inc. v. Winter*, 74 A.D.2d 195, 426 N.Y.S.2d 778 (1980), *aff'd*, 52 N.Y.S.2d 984, 438 N.Y.S.2d 79, 419 N.E. 2d 1078 (1981) (Appellate Division, First Department refused to follow the Appellate Division, Second Department's ruling in *National Bank*); *Long Island Jewish Hillside Medical Center v. Prendergast*, 134 Misc.2d 93, 509 N.Y.S.2d 697 (N.Y. Sup. Ct. 1986) (Court of Appeals affirmance of *Helmsley-Spear* means, by implication, the court overruled *National Bank*).

52. Because the Secretary promulgated the regulation pursuant to a congressional grant of authority, a rejection of the regulation's provisions implies that it was improperly promulgated. See *supra* notes 26, 46. See also *General Motors Corp. v. Buha*, 623 F.2d 455, 462-63 (6th Cir. 1980) (appropriate standard of review for rejecting the Treasury Regulation interpreting ERISA § 206(d), and its companion, I.R.C. § 401(a)(13), is abuse of discretion).

53. *St. Paul Fire and Marine Ins. Co. v. Cox*, 752 F.2d 550, 551-52 (11th Cir. 1985); *Crawford v. La Boucherie Bernard, Ltd.*, 815 F.2d 117 (D.C. Cir. 1987).

54. 752 F.2d 550 (11th Cir. 1985).

55. *Id.* at 552. The court focused on the financial security of other employees, noting that garnishment of funds wrongfully accumulated from the employer financially stabilizes the employer, and thus, stabilizes the pension plan. *Id.*

Similarly, the District of Columbia Circuit, in *Crawford v. La Bouchiere Bernard, Ltd.*,⁵⁶ allowed access to pension plan assets of participants who were fiduciaries of the plan, because the fiduciaries wrongfully acquired pension funds at the expense of the other participants.⁵⁷

In *Ellis National Bank of Jacksonville v. Irving Trust Co.*,⁵⁸ however, the Second Circuit held the "criminal misconduct" exception to preemption in *St. Paul Fire* contrary to the basic purpose of ERISA, and refused to adopt it.⁵⁹ The court reasoned that Congress' primary objective was to ensure that an employee receive his benefits on retirement, once that individual had fulfilled the necessary prerequisites.⁶⁰ In addition, the court stated that allowing access to wrongfully accumulated funds would undermine the stability of pension plans because it creates an uncertainty of receiving promised benefits.⁶¹

Preemption of state attachment and garnishment of ERISA pension benefits as implied in *Tenneco* and asserted *Ellis National Bank* presents a problem when the employee-debtor is self-employed or voluntarily contributes to his or her employer's sponsored plan. In such situations ERISA's protection of pension plan funds may be abused in order to defeat creditors. At common law, many courts held that a debtor could not create a trust for his own benefit and prevent access to it by creditors.⁶² The courts maintained that public policy prohibited a person from enjoying his own property, yet preventing creditors from reaching it.⁶³ The IRS recognized this type of problem when it adopted a regulation that disqualifies a qualified pension plan from tax breaks if the contributions to the plan amount to more than ten percent of the employee's earn-

56. 815 F.2d 117 (D.C. Cir. 1987).

57. *Id.* at 121-22. "A contrary interpretation would permit trustee wrongdoers to benefit from their misdeeds at the expense of those who ERISA was designed to protect." *Id.*

58. 786 F.2d 466 (2d Cir. 1986).

59. *Id.* at 471. See also *United Metal Products v. National Bank of Detroit*, 811 F.2d 297 (6th Cir. 1987) (no criminal misconduct exception to § 206(d)(1) because only Congress may create exceptions).

60. 786 F.2d at 471. See also *Vink v. SHV North American Holding Corp.*, 549 F. Supp 268 (S.D.N.Y. 1982); *Helmsley-Spear, Inc. v. Winter*, 74 A.D. 195, 426 N.Y.S.2d 778 (1st Dep't 1980), *aff'd.*, 52 N.Y.2d 984, 438 N.Y.S.2d 79, 419 N.E.2d 1078 (1981).

61. 786 F.2d at 471-72. The court explicitly disagreed with the holding in *St. Paul Fire* that ERISA's purpose outweighs general principles of equity. *Id.* See Note, *Weakening ERISA's Preemptive Powers: St. Paul Fire & Marine Insurance Co. v. Cox Creates An Implied Exception to the Anti-Alienation Provision for Employee Fraud*, 6 VA. TAX L. REV. 185 (1986) (arguing that ERISA preempts actions seeking wrongfully acquired employer funds placed in an employee's ERISA plan).

62. See generally A. SCOTT, *supra* note 3, at § 156. See also *Sherman*, *supra* note 14 at 261.

63. *Id.*

ings.⁶⁴ This limit indicates that the IRS considers contributions over the ten percent limit to take undue advantage of the more favorable tax treatment.

Absolute preemption of state law allows an employee or sole proprietor to place a large percentage of income into ERISA protected pension plans, whether or not the plans qualify for tax breaks.⁶⁵ In addition, the Fourth Circuit in *Tenneco* stated that funds accessible at will by an employee were protected by section 206(d)(1).⁶⁶ ERISA's broad preemption of state common law, therefore, allows an employee to shield more earnings than required for retirement support. As the amount of money protected increases, so does the likelihood that creditors may go unpaid.⁶⁷

The Fourth Circuit's decision in *Tenneco* continues the trend towards barring any access to pension benefits.⁶⁸ The benefit of this trend is that it provides consistent treatment of creditors rights to the benefits. On the other hand, the Second Circuit's decision in *Ellis National Bank* overextends *Tenneco's* rationale. That decision may give employees a legal expectation in funds they wrongfully accumulated at their employers' expense.⁶⁹ The Eleventh Circuit in *St. Paul Fire* and the D.C. Circuit in *Crawford* present a more common sense view of *Tenneco*, applying it to protect only funds legally accumulated by employees.⁷⁰

Universal preemption of state law governing the garnishment of pension benefits, provides a method to avoid creditors and is, therefore, not equitable. Recognizing that a gap exists in ERISA's coverage in this area, federal courts could avoid this result by adopting a cut-off for voluntary contributions similar to the one employed by the IRS.⁷¹ Any

64. G. BOREN, *supra* note 4 at § 1:13 (citing Rev. Rul. 80-350, 1980-82 CB 133); Sherman, *supra* note 14 at 264 § 264 n.77 (citing Rev. Rul. 59-185, 1959-1CB 86). The limit prevents contributions motivated solely for tax avoidance. Rev. Rul. 80-350, 1980-82 CB 133,133.

65. ERISA governs all pension plans, and subjects most of them to disclosure, funding, reporting and vesting requirements. Therefore, an employee's funds may not receive tax breaks yet ERISA will govern and protect the funds. There are several exceptions to ERISA's governance of pension plans. See Sherman *supra* note 14 at 248 n.8. (listing twelve exceptions).

66. 698 F.2d at 690. See *supra* note 43.

67. Sherman, *supra* note 14 at 261-71 (discussing problems with ERISA protection of funds donated in excess of what is needed upon retirement).

68. See *supra* notes 41-49 and accompanying text.

69. See *supra* notes 53-61 and accompanying text.

70. See *supra* notes 53-57 and accompanying text.

71. This proposal is discussed in Sherman, *supra* note 14, at 264-65. He argues that adopting the ten percent cut off protects those contributions made for a protectable purpose and allows access to funds not necessary for retirement. *Id.* See also *supra*, note 64 and accompanying text. However,

amount an employee contributes over the limit would be accessible to creditors. This proposal is more equitable with regards to debtor-creditor relations, than universal preemption for access to pension plan funds. Further, the limit allows a significant portion of voluntary contributors to be protected by ERISA, fulfilling ERISA's purpose.⁷² Such a provision might require special consideration to avoid the undue burden on sole proprietors, who would require a higher limit to offset other employees' advantage.⁷³

B. Access to Welfare Plan Benefits

Employee welfare plans are not explicitly included in section 206(d)(1).⁷⁴ Prior to 1988, three views existed concerning access to an employee welfare plan by a creditor.⁷⁵ First, the Missouri Supreme Court, in *Electrical Workers Credit Union v. IBEW-NECA Holiday Trust Fund*, held that states may decide for themselves whether to allow access.⁷⁶ Second, the Ninth Circuit, in *Franchise Tax Board v. Construction Workers Vacation Trust Fund*, held that ERISA's underlying policy implicitly bars creditors' access to welfare plan benefits.⁷⁷ Finally, the Georgia Supreme court, in *Mackey v. Lanier Collection Agency*, held that

the author does not discuss under what authority such a cut off would be implemented. Clearly, when enacting ERISA, Congress envisioned that a federal common law of pensions would develop to fill in the gaps. See *supra* note 13-14. Arguably, Congress did not completely address creditors rights and thus courts should fill in the gap. See *supra* note 14. The cut off would have to limit contributions to a certain percentage of an employee's yearly income. The IRS allows contributions not exceeding ten percent of "an employee's aggregate compensation for all years since the employee became a participant thereunder." (Rev. Rul 80-350, 1980-82 CB 133,133). Obviously, in the debtor-creditor area the limit could not be easily applied in an aggregate manner.

72. See *supra* note 2.

73. Sole proprietors require a higher cut off limit because all of their contributions to a self-sponsored pension plan are voluntary. Limiting those contributions to ten percent of their gross income would put sole proprietors at a disadvantage vis-a-vis corporate-sponsored plans. Sherman, *supra* note 14, at 270-71.

74. See *supra* note 9.

75. This conflict arose because of courts' divergent interpretations of § 514(a) of ERISA which preempts state laws "relating to" ERISA benefit plans.

76. 583 S.W.2d 154 (Mo. 1979). For cases that follow this approach, see *Vacation Trust Fund v. Local Union 212 IBEW, Credit Union*, 549 F. Supp. 1299, 1300-02 (S.D. Ohio 1982) (no implied restriction upon the alienation and assignment of welfare plan funds), *aff'd* 735 F.2d 1010 (6th Cir. 1984); *MISIC v. Building Serv. Employees Health*, 789 F.2d 1374, 1377 (9th Cir. 1986) (allowing assignment of health care reimbursements); *Arizona Laborers, Local 395, Pension Trust Fund v. Nevarez*, 661 F. Supp. 365, 368-70 (D. Ariz. 1987) (Congress only provided specific protection regarding pension funds and did not provide protection regarding welfare plans).

77. 679 F.2d 1307 (9th Cir.), *vacated*, 463 U.S. 1 (1983) (vacated for lack of jurisdiction).

states may not bar access to welfare plan funds.⁷⁸

The Supreme Court in *Mackey v. Lanier Collection Agency, Inc.*,⁷⁹ resolved this conflict by holding that a state may not explicitly exempt ERISA plans from state garnishment laws.⁸⁰ The Court also held that Congress did not intend ERISA "to forbid the use of state-law mechanisms of executing judgments against ERISA welfare benefit plans, even when those mechanisms prevent plan participants from receiving their benefits."⁸¹ The result of the *Mackey* case is that any state with a law allowing attachment, garnishment or levy must allow such access to ERISA welfare plans. The Court recognized that ERISA allows attachment of plan funds through state law procedures with regard to suits to enforce a participant's rights under a particular plan.⁸² Further, the Court recognized that ERISA plans also may be sued for "run-of-the-mill" state-law claims.⁸³ Judgments received in such suit are enforceable through state-law procedures, including attachment.⁸⁴ By analogy, the Court reasoned that attachment of an individual's welfare plan funds to enforce a judgment against the individual is equally allowable; such an action does not "relate to" an ERISA plan.⁸⁵

In support of its analogy, the Court pointed out that ERISA section 206(d)(1) bars attachment only of an individual's pension plan funds.⁸⁶ Therefore, Congress' preclusion of garnishments of an individual's plan funds extends only to pension plan funds.⁸⁷ Thus, if ERISA section

78. 350 S.E.2d 439 (Ga. Sup. Ct.), *aff'd*, 108 S. Ct. 2182 (1988).

79. 108 S. Ct. 2182 (1988).

80. *Id.* at 2184-85, 2191. The Court also preempted a Georgia law that specifically barred garnishments of ERISA plan funds. The Court held that state law that applied solely to ERISA plans "relates to" ERISA plans and was thus, preempted by § 514(a). *Id.* at 2185.

81. *Id.* at 2191.

82. 108 S. Ct. at 2186-87. Section 502 of ERISA (29 U.S.C. § 1132), allows an ERISA plan to sue and be sued by a participant or beneficiary to recover benefits due under the plan. Section 502(d)(2), (29 U.S.C. § 1132(d)(2)), further provides that money judgments are enforceable against plans as entities.

83. 108 S. Ct. at 2187 n.8. Such claims include those for unpaid rent, failure to pay creditors, and torts committed by ERISA plans. *Id.*

84. *Id.* at 2187 n.9.

85. *Id.* at 2188. "[T]here is simply no logical way to construe the English language so that garnishment or attachment laws 'relate to' benefit plans when they are invoked by creditors of the beneficiaries, but not when they are invoked by beneficiaries or creditors of the [plan] itself." *Id.* (quoting Brief of Amicus Curiae in Support of Judgment Below at 24).

86. *Mackey v. Lanier Collection Agency*, 108 S. Ct. at 2183-84.

87. *Id.* at 2188. "Where Congress intended in ERISA to preclude a particular method of state-law enforcement of judgments, or extend anti-alienation protection to a particular type of ERISA plan, it did so expressly in the statute." *Id.*

514(a) is allowed to preempt garnishments of all ERISA plan funds, section 206(d)(1) would be redundant.⁸⁸

Finally, the Court dismissed the argument that because the Retirement Equity Act of 1984 allow Q.D.R.O.'s to garnish an individual's welfare plan funds,⁸⁹ Congress never intended to allow garnishments of an individual's welfare plan funds generally.⁹⁰

In dissent, Justice Kennedy opined that "state garnishment laws necessarily relate to employee benefit plans to the extent they require such plans to act as garnishees, which is a substantial and onerous obligation."⁹¹ Therefore, ERISA preempts such laws with regard to an individual's welfare plan funds.⁹² The dissent noted that Congress intended section 514(a)'s broad reach to encompass state laws specifically preempted by other provisions of ERISA.⁹³ Thus, section 514(a)'s mere redundancy with section 206(d)(1) should not bar its ability to preempt state garnishment laws as they relate to ERISA welfare plans.⁹⁴ In addition the dissent argued that garnishment of an individual's plan funds forces the plan to be a garnishee and would have a significant effect on the administration of the plan.⁹⁵

The Court is correct in not extending section 206(d)(1)'s protection to welfare plans.⁹⁶ Both opinions fail, however, to recognize the fundamental difference between welfare and pension plans. Equating the two ignores the fact that pension plans play a more vital role in an employee's future security than do welfare plans. ERISA's greater protection of pension plan funds is indicative of congressional recognition of this point.⁹⁷ Pensions deserve greater protection from disbursement before retirement.⁹⁸ In addition, vacation or holiday trusts merely defer wages

88. *Id.* at 2189.

89. *See supra* notes 33-37 and accompanying text.

90. 108 S. Ct. at 2189-91. The Court explained that Congress enacted the 1984 Amendments to remedy erroneously decided court cases on the issue, and to clarify the original meaning of §§ 206(d) and 514(a). *Id.*

91. *Id.* at 2192.

92. *Id.*

93. *Id.* at 2194.

94. *Id.* at 2193-94.

95. *Id.* at 2193.

96. Nowhere in § 206(d) is the term welfare plan or benefit plan used. The section speaks only of assignment and alienation of pension plan benefits. *See supra* note 9.

97. ERISA only subjects pension plans to its participation and vesting and funding requirements. *See* 29 U.S.C. §§ 1051-86.

98. *See, e.g.,* Local Union 212 Vacation Trust Fund v. Local Union 212 Credit Union, 549 F. Supp. 1299 (S.D. Ohio 1982) (Congress did not view welfare plans as so vital to employees' financial

and do not serve the purpose of generating future employee income through long-term investments. Allowing creditors' access to welfare plan funds does not hamper the fulfillment of the public policy of protecting employees' future financial stability.⁹⁹

One can make the following observations regarding the preemption of state garnishment laws by section 514(a). The Supreme Court in a recent case on ERISA preemption, *Fort Halifax Packing Co., Inc. v. Coyne*,¹⁰⁰ upheld a state law requiring a one-time severance payment to be made by employers.¹⁰¹ The Court reasoned that the severance law did not regulate an ERISA plan, because the law did not interfere with the employer's ability to operate its plan in a uniform manner.¹⁰² Similarly, a state law allowing garnishment of vested welfare plan funds merely alters the distribution of the benefits,¹⁰³ and does not affect the employer's ability to uniformly administer ERISA's disclosure, funding, reporting, vesting or enforcement of benefit plan provisions.¹⁰⁴ Thus, under the rationale of *Fort Halifax Packing*, section 514(a) does not preempt state garnishment laws because ERISA does not govern the payment of benefits except for specifying the date by which payments must be made.¹⁰⁵

stability that plans should be protected from creditors), *aff'd*, 735 F.2d 1010 (6th Cir. 1984); Arizona Laborers, Local 395 Pension Trust Fund v. Nevarez, 661 F. Supp. 365, 370 (D. Ariz. 1987) (no indicating in ERISA's legislative history of concern for protecting welfare plan funds from creditors).

99. A reading of the congressional declaration of policy for ERISA clearly indicates that Congress' concern was for the financial stability and well-being of employees and their families. Allowing the garnishment of vacation or holiday funds does not offend this concern. *See supra* note 2.

100. 107 S. Ct. 2211 (1987).

101. *Id.* at 2223.

102. *Id.* at 2219. The Court stated the state law did not in any way create "the potential for the type of conflicting regulation of benefit plans that ERISA preemption was intended to concern." *Id.*

103. When vacation or holiday benefits are vested at the end of each fiscal year, employers calculate how much vacation or holiday pay an employee is to receive. Thus, a garnishment of vested vacation or holiday pay will only require the plan administrator to pay the creditor a percentage of the calculated benefits pursuant to a court judgment. *See Electrical Workers Local No. 1 Credit Union v. IBEW-NECA Holiday Trust Fund*, 583 S.W.2d 154 (Mo. 1979) (holiday benefits calculated as a fixed percentage of total hours worked per year and were calculated at the end of the year).

104. *See Martori Bros. Distributors v. James-Massengale*, 781 F.2d 1349 (9th Cir. 1986). In that case, the court stated that the principle underlying all of the ERISA preemption decisions appears to be that the state law is preempted by § 514(a) "if . . . it regulates the matters regulated by ERISA: disclosure, funding, reporting, vesting, and enforcement of benefit plans. *Id.* at 1357-58 (citations omitted).

105. ERISA § 206(a) (29 U.S.C. § 206(d)) governs only the commencement date for payments of benefits.

IV. BANKRUPTCY CREDITORS' ACCESS TO BENEFIT PLAN FUNDS

A. Introduction

While judgment creditors, as shown above, excluding family members, may not reach an employee's pension plan funds, they are not entirely without recourse. A majority of courts have held that the Bankruptcy Code (Code)¹⁰⁶ does not protect benefit plan funds from access by creditors.¹⁰⁷ This result allows creditors, through Chapter 7 of the Code, to circumvent ERISA section 206(d)(1) waiting until the debtor voluntarily declares bankruptcy or even forcing the debtor into bankruptcy.¹⁰⁸ One commentator has characterized this result as a clash of social policies.¹⁰⁹ ERISA's purpose is to protect retirement funds to ensure employees will receive their expected benefits at retirement.¹¹⁰ The Code, however, has the dual purpose of reimbursing creditors to the greatest extent possible, while also rehabilitating debtors.¹¹¹

There are two primary means by which an employee-debtor can protect his benefit funds from bankruptcy creditors. First, a creditor can be barred from access to benefit funds if the debtor's interests and rights in the funds are excluded from the debtor's bankruptcy estate pursuant to section 541(c)(2) of the Code.¹¹² If the debtor's rights and interests are so excluded, they are not available to satisfy bankruptcy creditors because they never enter the bankruptcy estate.¹¹³ Second, a debtor can deny a creditor access to benefit plan funds if the debtor can exempt totally or partially his rights and interests in benefit plans pursuant to section 522(b)(2)(A) of the Code.¹¹⁴ An exemption bars access to funds that are included in the bankruptcy estate. This Note examines each of these avenues in turn below.

106. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. §§ 101-151, 326 (1978)).

107. See *infra* notes 120-126.

108. Chapter 7 of the Code requires that the debtor's assets be turned over to the creditors to pay as much of the debtor's liabilities as possible. This Note will only address Chapter 7 because Chapters 11 and 13 address supervised reorganization to pay creditors without liquidation and, therefore, have no application here.

109. Wohl, *Pension and Bankruptcy Laws: A Clash of Social Policies*, 64 N.C.L. REV. 3 (1985).

110. See *supra* note 8 and accompanying text.

111. See Wohl, *supra* note 109, at 5 n.8 (citing *Burlingham v. Crouse*, 228 U.S. 459, 473 (1913)).

112. The bankruptcy estate "consists, essentially, of every kind of interest in property possessed by the debtor prior to bankruptcy; the term 'property' is to be given it widest and most expansive meaning." *Id.* at 11-12.

113. See *infra* notes 115-33 and accompanying text.

114. See *infra* notes 137-49 and accompanying text.

B. Exclusion of ERISA Benefit Plans Under Section 541(c)(1),(2).

Section 541(c)(1)(A) of the Code provides that except as specified in section 541(c)(2), "any provision" that restrains alienation of property of the debtor is ineffective in bankruptcy.¹¹⁵ On the other hand, section 541(c)(2) excludes from the bankruptcy estate interest in a trust in which restraints on the interests therein are enforceable under "applicable non-bankruptcy law."¹¹⁶ Courts have created three different interpretations of whether a debtor's interest in an ERISA protected plan may be excluded from the estate.¹¹⁷

In *In re Goff* the Fifth Circuit expressed the majority view,¹¹⁸ holding that section 541(c)(2) does not include ERISA as applicable non-bankruptcy law. Hence, ERISA section 206(d)(1)'s restriction in a pension plan accessible at will by the employee-debtor does not exclude the plan from the bankruptcy estate.¹¹⁹ The *Goff* court and others with the same view of section 541(c)(2) find support for their view in three areas of the Code.

First, these courts interpreted the legislative history of section 541(c)(2) to show that Congress intended applicable non-bankruptcy law

115. Section 541 (11 U.S.C. § 541) entitled "Property of the Estate" provides in pertinent part:

(a) The commencement of a case under § 301, 302 or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

.....

(c)(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section not with standing any provision. . .

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title, or on the appointment of or the taking possession by a trustee in a case under this title of a custodian, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

116. See *supra* note 115.

117. See *In re Dagnall*, 78 Bankr. 531 (C.D. Ill. 1987) (brief discussion of the three interpretations); Seiden, *Chapter 7 Cases: Do ERISA and the Bankruptcy Code Conflict as to Whether a Debtor's Interest in or Rights Under a Qualified Plan Can Be Used to Pay Claims*, 61 AM. BANKR. L.J. 219 (1987) (discussing in depth the conflicts between ERISA and the Bankruptcy Code).

118. 706 F.2d 574 (5th Cir. 1983).

119. *Id.* The pension plan involved was a Keogh Plan. Such plans are retirement plans for the self-employed. Access to the funds is allowable at will, but at the expense of losing tax breaks. See Wohl, *supra* note 109, at 110. See *infra* notes 147-50 and accompanying text for a discussion of the *Goff* court's analysis of the Bankruptcy Code's § 522(b)(2)(A).

to exempt from the bankruptcy estate only traditional spendthrift trusts.¹²⁰ Specifically, these courts assert ERISA is not applicable non-bankruptcy law because ERISA section 206(d) merely requires non-alienation and non-assignment of the funds, and allows the beneficiary-employee to reach the entire amount at will. On the other hand, spendthrift trusts only dole out a percentage to the beneficiary, who has no control over the additional sums.¹²¹ Second, section 522(b)(2)(A) of the Code allows debtors to choose either state or federal bankruptcy law to protect certain interests in property. If a state scheme is chosen, the provision permits debtors to exempt certain property under "other federal law".¹²² Significantly, the legislative history to section 522(b)(2)(A) provides an illustrative list of federal laws that would exempt property under that section, yet does not include ERISA.¹²³ Thus, if the legislative history to section 522(b)(2)(A) of the Code explicitly omits ERISA from its list, then section 541(c)(2) hardly would include it by implication.¹²⁴ Lastly, these courts rely heavily on the requirement in ERISA section 514(a) that ERISA is not to affect the operation of other federal laws.¹²⁵ In addition, excluding benefit plans from the bankruptcy estate contra-

120. See *In re Daniel*, 771 F.2d 1352, 1360 (9th Cir. 1985); *In re Lichstrahl*, 750 F.2d 1488, 1490 (11th Cir. 1985); *In re Goff*, 706 F.2d 574 (5th Cir. 1983); *In re Dagnall*, 78 Bankr. 531, 533 (C.D. Ill. 1987).

121. The court in *Goff* stated:

In general terms a spendthrift trust is a trust created to provide a fund for the maintenance of a beneficiary, with only a certain portion of the total amount to be distributed at any one time. The settlor places 'spendthrift' restrictions on the trust, which operate in most states to place the fund beyond the reach of the beneficiary's creditors, as well as to secure the fund against the beneficiary's own improvidence. 706 F.2d at 580.

See also *In re Daniel*, 771 F.2d 1352, 1360 (9th Cir. 1985) (" 'applicable nonbankruptcy law' refers only to state spendthrift trust law" and not broad reference to all other laws, including ERISA); *In re Lichstrahl*, 750 F.2d 1488, 1490 (11th Cir. 1985) (applicable nonbankruptcy law only relates to state spendthrift law). *In re West*, 64 Bankr. 738, 742 (D.Utah 1986) ("There will be instances where ERISA plans will be included in the estate because they do not qualify as enforceable spendthrift trusts under state law, either because that state does not enforce spendthrift provisions or because the provision is invalid.").

122. See *infra* note 138.

123. ERISA was enacted four years prior to the new Bankruptcy Code, and was also mentioned specifically in § 522. 11 U.S.C. § 522(d)(10)(E)(iii). See *In re Goff*, 706 F.2d at 585 (Congress did not "overlook" ERISA in illustrative list.).

124. *In re Goff*, 706 F.2d at 582-86. The petitioner debtors in that case claimed only that the § 541(c)(2) "other applicable bankruptcy law" provision included ERISA-qualified Keogh plans. Even though they had chosen the state bankruptcy route, petitioner's did not alternatively assert that § 522(b)(2)(A)'s "federal law" exemption did so as well. Nonetheless, the court found it instructive to make the comparison on its own. *Id.* at 582. Accord *In re Daniel*, 771 F.2d 1352, 1360-61 (9th Cir. 1985); *In re Lichstrahl*, 750 F.2d 1488, 1490-91 (11th Cir. 1985).

125. ERISA § 541(d) (29 U.S.C. § 1144(d)) provides in part: "Nothing in this title shall be

dicts the Code's policy of broad inclusion of property in bankruptcy estates.¹²⁶

A line of Bankruptcy Court cases directly conflict with *Goff* and its progeny by holding that ERISA is applicable non-bankruptcy law. In *In Re Threewit*,¹²⁷ the court held that because section 541(c)(2) does not expressly use the term "spendthrift trust," no reason exists to give that section such a narrow reading.¹²⁸ Thus, section 541(c)(2) should extend to all pensions to bar creditors from reaching the employee's interest.¹²⁹ The court further reasoned that "under the plain and simple language of section 541(c)(2), if the ERISA anti-alienation provisions are enforceable against general creditors, they are enforceable against the bankruptcy trustee."¹³⁰

Responding to the argument that section 522(d)(10)(E) of the Code¹³¹ expressly governs the exemption of pensions from the bankruptcy estates, the *Threewit* court recognized that section 522(d)(10)(E) includes retirement plans governed as well as not governed by ERISA. Therefore, the court maintained that section 541(c)(2) is applicable only to pensions governed by ERISA.¹³² In addition, section 522(d)(10)(E) exempts only the amount "reasonably necessary for the support of the debtor," while 541(c)(2) excludes the entire pension if it is ERISA governed, and thus

construed to alter, amend, modify, invalidate, impair, or supersede any law of the United States . . . or any rule or regulation issued under any such law."

126. 706 F.2d at 586-87. The court stated that ERISA § 206(d)(1) does not, by itself, exclude pensions from the bankruptcy estate. In addition, the policy of the Code is to broaden the property of the estate available to bankruptcy creditors. Therefore, if ERISA were considered "applicable nonbankruptcy law" under § 541(c)(1), this would frustrate the operation of federal bankruptcy law and ERISA § 541(a). *Id.*

127. 24 Bankr. 927 (Bankr. D. Kan. 1982).

128. *Id.* at 929. See also *In re Ralstin*, 61 Bankr. 502 (Bankr. D. Kan. 1986); *Lisciski v. Mosley*, 42 Bankr. 181 (D.N.J. 1984); *Warren v. G.M. Scott & Sons*, 34 Bankr. 543 (S.D. Ohio 1983). Seiden, *supra* note 117, at 236-40. But see *In re Matteson*, 58 Bankr. 909, 910 (D. Colo. 1986) (§ 541(c)(2) must be read to exclude only spendthrift trusts enforceable under state law).

129. 24 Bankr. at 929. The court reasoned that because "spendthrift trust" appears only in the legislative history to § 541(c)(2) and not in the language of the section, the term should not be used as a term of art. Instead, "spendthrift trust" should be given its ordinary meaning as inclusive of any trust barring creditors' access to the beneficiary's interest. *Id.* (quoting 76 AM. JUR.2D *Unemployment Compensation* § 148, at 389 (1975)).

130. 24 Bankr. at 929. See also *supra* note 126.

131. This section allows a debtor to exempt from the estate payments made from the employee benefit plans. See *infra* notes 137-149 and accompanying text.

132. 24 Bankr. at 929-30. The court stated that simply because § 522(d)(10)(E) and § 541(c)(2) overlap, § 541(c)(2) is not prevented from excluding ERISA funds from the estate.

inaccessible by general creditors.¹³³

A third line of cases holds that all ERISA qualified pension plans are part of the bankruptcy estate.¹³⁴ These courts reason that because section 522(d) of the Code already includes an exception for certain pensions, section 541(c)(2) was not intended to exclude other pensions from the estate.¹³⁵ In addition, these cases find a congressional intent in section 541(c)(2)'s legislative history not to exclude exclusively ERISA governed benefit interests from the bankruptcy estate.¹³⁶

C. ERISA Benefit Plans and the Bankruptcy Code's Exemption Scheme

If the debtor-employee fails to exclude his or her benefit plan from the bankruptcy estate, then the debtor still may be able to bar creditors' claims to the funds through section 522 of the Code. An exemption under section 522 operates differently from an exclusion of an interest in property under section 541: the interests excluded in section 541 never enter the bankruptcy estate, while interests under section 522 are within the estate but entirely or partially exempt from creditors' claims.¹³⁷ The debtor may choose to exempt his or her benefit plan by virtue of section

133. The court noted these two characteristics, but did not connect them to create a logical distinction. *Id.* at 929-30. *See also* Lisciski v. Mosley, 42 Bankr. 181 (D.N.J. 1984); Warren v. G.M. Scott & Sons, 34 Bankr. 543 (S.D. Ohio 1983). *But see In re Di Piazza*, 29 Bankr. 916, 921 (N.D. Ill. 1983) (criticizing *In re Threewit*).

134. *See In re Graham*, 726 F.2d 1268, 1272-73 (8th Cir. 1984) ("A debtor's interest in pension funds first comes into the bankruptcy estate to the extent they are needed for a fresh start they may then be exempted out."). *See also* Regan v. Ross, 691 F.2d 81, 85 (2d Cir. 1981) (legislative history to § 541(c)(2) unambiguously indicates that pension funds are not excluded from Chapter 13 estates); *In re Flygstad*, 56 Bankr. 884, 887 (N.D. Iowa 1986) (§ 541(a)(1) includes pension funds in the estate, precluding examination of provisions of a pension plan to determine if it is a valid spendthrift trust); *In re McKenna*, 58 Bankr. 221 (N.D. Iowa 1985) ("*Graham* mandates that a debtor's interest in an ERISA plan is to be included in the estate.>").

135. *See Graham*, 726 F.2d at 1271-73; *Regan* 691 F.2d at 85-86. The impact of the courts' reliance § 541(c)(2)'s legislative history is unclear. The courts cite to H.R. No. 595, 95th Cong. 1st Sess. 175-76, 364 (1977), reprinted in 1978 U.S. CODE CONG. & ADMIN. NEWS 6136, 6325, which states that § 541(c)(2) preserves restrictions on transfers in a spendthrift trust if the trust is enforceable under applicable nonbankruptcy law. The *Graham* and *Regan* courts, however, do not look to applicable state law, but rather conclude that § 541(c)(2) was not intended to keep all of a debtor's ERISA plan benefits out of the bankruptcy estate. *Graham*, 726 F.2d at 1272, *Regan*, 691 F.2d at 85-86. *But see In re Lichstrahl*, 750 F.2d 1488 (11th Cir. 1985); *In re McLean*, 762 F.2d 1204 (4th Cir. 1985) (declining to follow *Graham*, holding applicable nonbankruptcy law to determine a plan's proper inclusion in the estate).

136. *Graham*, 726 F.2d at 1272-73; *In re McKenna*, 58 Bankr. 221, 223 (N.D. Iowa 1985).

137. *See Wohl*, *supra* note 109, at 24-28 (discussing the workings of the bankruptcy exemptions in § 522). *See also supra* note 133 and accompanying text.

522(d)'s "federal exemption" scheme, or the debtor may use the law of the state in which he or she is a citizen.¹³⁸

Section 522(d) lists the exemptions available to a debtor who uses the federal exemption scheme. Section 522(d)(10)(E) allows the debtor-employee to exempt payments by employee benefit plans, but only to the "extent reasonably necessary for the support of the debtor and any dependents of the debtor."¹³⁹ One commentator asserts that the primary method of determining what is "reasonably necessary" is to ensure that the presumed future earnings combined with some amount of funds in the exempted benefit plans will allow the debtor to "sustain basic needs upon retirement."¹⁴⁰ Several courts, however, have characterized the purpose of the Code as ensuring only the fresh start of the debtor, not future financial stability. These courts, thus, refuse to exempt pension plan funds.¹⁴¹ Thus in some jurisdictions, creditors may gain access to

138. The federal exemption scheme exempts property "recognized as necessary for ordinary life . . ." 3 COLLIER ON BANKRUPTCY 522.02 (L. King 15th ed. 1987) [hereinafter COLLIER]

The exemption provision of Bankruptcy Code § 522 provides in pertinent part:

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

(1) property that is specified under subsection (d) of this section, unless the State law that is applicable to the debtor under paragraph (2)(a) of this subsection specifically does not so authorize; or, in the alternative,

(2)(A) any property that is exempt under Federal Law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for 180 days immediately preceding the date of the filing of the petition . . .

....

(d) The following property may be exempted under subsection (b)(1) of this section:

....

(10) The debtor's right to receive-

....

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

11 U.S.C. § 522 (1986). Most states require use of the state's bankruptcy exemption by its citizens. See 7 COLLIER, *supra* note 138, at 1 n.6 (listing the 35 states that have opted-out of the federal bankruptcy exemptions).

139. See *supra* note 138.

140. Wohl, *supra* note 109, at 25-26.

141. See *In re Clark*, 711 F.2d 21, 23 (3d Cir. 1983), in which the court states that: "[t]he exemption of present Keogh payments, to the extent they are necessary for the support of the debtor, is consistent with this goal [of ensuring a fresh start]. The exemption of *future* payments, however, demonstrates a concern for a debtor's long-term security which is absent from the statute." *Id.* at 23. (emphasis in original) See also *In re Woodford*, 73 Bankr. 675 (N.D.N.Y. 1987) (retirement plan interests reasonably necessary for support only if present needs so indicate). *But see In re Turpin*,

pensions by the forced or voluntary bankruptcy of an employee-debtor, without which they could not gain access. While ERISA was designed to be the primary authority in employee benefit law, it has been preempted when a conflict exists with another federal law such as the Code.¹⁴²

If the debtor chooses or is required to follow the state scheme most states have provisions parallel to the federal scheme in section 522(d).¹⁴³ Under all state schemes, though, a debtor may, by virtue of section 522(b)(2)(A) of the Code, exempt "any property that is exempt under Federal Law, other than subsection(d) of this section."¹⁴⁴ This exemption is characterized as the "federal exemption."

The issue for employees and their creditors is whether ERISA section 206(d)(1), or the compatible IRS section, creates a federal non-bankruptcy exemption. If either does, then the entire interest in the benefit plan is exempt from the bankruptcy estate. Section 522(b)(2)(A) of the Code exempts "any property". The exemption, however, is not based on what is reasonably necessary for the support of the debtor. The legislative history to section 522(b)(2)(A) of the Code lists several federal statutes that Congress intended to be illustrative of exempt federal non-bankruptcy statutes.¹⁴⁵ Employee pension plans are not included in the list. The overwhelming majority of cases hold that section 522(b)(2)(A)

644 F.2d 472, 474 (5th Cir. Unit A May, 1981) (decided under old Bankruptcy Act) ("Providing the bankrupt with a 'fresh start' means assuring him that assets to which he may become entitled in the future will be acquired free of any prebankruptcy obligations.").

142. See *supra* note 125.

143. It is beyond the scope of this Note to discuss the various state law schemes. For a discussion of the various state laws see 7 COLLIER, *supra* note 138, at 5-776.

144. See *supra* note 138 (text of § 522(b)(2)(A)).

145. The House and Senate Reports explaining the "Federal law other than subsection(d)" provision in § 522(b)(2)(A) provide an illustrative list of property exempted under federal law other than the Code:

Foreign Services 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 Fisherman, 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. 229 (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;
 and

Federal homestead lands on debts contracted before issuance of the patent, 43 U.S.C. 175.

S. REP. NO. 989, 95th Cong., 2d Sess. 75, *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5787, 5861; H. REP. NO. 595, 95th Cong., 2d Sess. 360 (1977), *reprinted in* 1978 U.S. CODE CONG. & ADMIN. NEWS 5963, 6316.

does not recognize ERISA as a federal non-bankruptcy law. These cases find ERISA's exclusion from the list to be highly probative of congressional intent not to include ERISA as a federal non-bankruptcy exemption.¹⁴⁶

In addition, the Fifth Circuit in *Goff* noted that ERISA section 206(d)(1) was fundamentally different from the statutes listed in the legislative history to section 522(b)(2)(A) of the Code.¹⁴⁷ The court recognized that the property covered by ERISA includes a wide range of benefit plans while the statutes listed in the Code's legislative history are systems funded or created by the federal government.¹⁴⁸ The court stated that the narrow characteristics of the listed plans make up an "operational thread" that federal statutes must contain to come within the section.¹⁴⁹ Only one court has reached a contrary conclusion.¹⁵⁰

ERISA benefit plans are not likely to be excluded from the bankruptcy estate unless, as permitted in some jurisdictions, the plan has restrictions on the transfer of interests and the applicable state law recognizes the restrictions as a spendthrift clause. Also, federal and state exemption schemes will likely protect only the part of an employee's benefit plan funds necessary for his support. Therefore, if a creditor forces a debtor-employee into bankruptcy, the creditor may very well gain access to funds not accessible prior to bankruptcy.

146. See, e.g., *In re Daniel*, 771 F.2d 1352, 1360-61 (9th Cir. 1985); *In re Lichstrahl*, 750 F.2d 1488, 1491 (11th Cir. 1985); *In re Graham*, 726 F.2d 1268, 1273-74 (8th Cir. 1984); *In re Goff*, 706 F.2d 574, 582-86 (5th Cir. 1983).

147. *Goff*, 706 F.2d at 583-84.

148. *Id.* at 585-86.

149. *Id.* The court reasoned private pension and welfare legislation is much broader than the federally funded or created plans listed. *Id.* The court also noted that to qualify for tax benefits and protection from creditors ERISA, through § 206(d)(1), only requires restrictions on transfers of interests in benefit plans. The statutes in the legislative history also require similar restrictions as a condition precedent to protection of the particular statute. *Id.* at 585. See also *In re Daniel*, 771 F.2d 1352, 1361 (9th Cir. 1985) (statutes in § 522(b)(2)(A)'s legislative history cover benefit plans federal in nature while ERISA covers private plans). One commentator asserts, however, that the operational thread is actually whether the statute exempts the property it covers from voluntary and involuntary alienation. Therefore, ERISA should be considered as a federal exemption. See Note, *Exemption of ERISA Benefits Under Section 522(b)(2)(A) of the Bankruptcy Code*, 83 MICH. L. REV. 214, 231-33 (1984).

150. *In re Hinshaw*, 23 Bankr. 233, 235 (D. Kan. 1982) ("Statutes . . . recognized as giving rise to a Federal exemption of the type here being considered [considering § 522(b)(2)(A)] may be characterized as nothing more than prohibitions against assignment or alienation.").

V. PROPOSALS

A. *Summary of Previous Arguments*

This Note has demonstrated the lack of a consistent theme in the law of creditors' rights to ERISA protected benefit plan funds. Part II described the judicially created and congressionally adopted exception to section 206(d) of ERISA. Part III demonstrated that regardless of the employee's ability to access his pension funds, creditors are almost always barred from doing so, absent extraordinary circumstances. Part III also noted that welfare plan funds are not protected from creditors and, once vested, are garnishable. Part IV examined the effect of bankruptcy law provisions, under which creditors may have access to pension and welfare plan funds regardless of the policy concerns of ERISA.

B. *Proposal: Federal Courts Should Consider the Purpose of Funds in a Benefit Plan*

Assuming that the policy of the Bankruptcy Code is to include pension funds in the estate, then ERISA, by virtue of section 514(a),¹⁵¹ cannot affect the operation of the Code.¹⁵² Prior to the debtor-employee's bankruptcy, general creditors will be denied access to pension funds but, likely will have access to welfare funds. Bankruptcy creditors, however, likely will have access to at least some of the funds of either type of employee benefit plan.¹⁵³ Consequently, to remedy the inconsistencies, either the federal courts or Congress should modify the current application of ERISA section 206(d)(1).¹⁵⁴

151. The majority of courts view the policy of the Bankruptcy Code to include benefit plans in the estate unless applicable state law recognizes a plan as a valid spendthrift trust. *See supra* notes 130-36 and accompanying text. Many states will not protect funds in an alleged spendthrift trust if more than necessary for the debtor's support. *See* 2 A. SCOTT, *supra* note 3, at §§ 151, 152.1. In addition, many states will not hold a spendthrift clause valid if doing so violates public policy or a statute. *See, e.g.,* *Electrical Workers Local 1 Credit Union v. IBEW Holiday Trust Fund*, 583 S.W.2d 154, 161 (Mo. 1979) (spendthrift provision invalid to protect vacation benefits because they are wages and thus garnishable by statute). Further, several courts will not exclude any pension funds from the bankruptcy estate. *See supra* notes 134-36 and accompanying text. As set forth earlier, the overwhelming majority of cases will not exempt a debtor's entire interest in an ERISA benefit plan from the bankruptcy estate. In light of the above, courts rarely will protect an employee's interest in a benefit plan from bankruptcy creditors.

152. *See supra* note 146.

153. Under the federal or state bankruptcy schemes, the debtor-employee can exempt interest in benefit plans to the extent they are reasonably necessary for the debtor's support. *See supra* notes 139-42 and accompanying text.

154. Because Congress did not explicitly address creditors' rights in ERISA, the federal courts

Although section 206(d)(1) has been interpreted to protect pension plan funds from creditors,¹⁵⁵ the protection need not cover all of the funds in a plan. Creditors should have access to funds donated by an employee to a pension in excess of an amount reasonably needed for the employee's support later in life.¹⁵⁶ Employees can hardly have a justified expectation to excess funds put in pension plans to evade creditors.¹⁵⁷ In addition, vacation and holiday plan funds pay the employee his or her wages only over a short period of time. Allowing access to those funds does not endanger the employee's future financial stability. ERISA should not be used to preempt basic principles of debtor-creditor law that allow creditors to be paid from the debtor's excess funds. Access to these excess funds should not turn on whether an employee-debtor voluntarily declares or is forced into bankruptcy. This Note's proposal allows equal access by general creditors and bankruptcy creditors to the employees' interest in their benefit plans.

In addition, access to excess funds should follow the plan laid out by Congress in the Retirement Equity Act of 1984. Judgment creditors should secure orders resembling Qualified Domestic Relation Orders (Q.D.R.O.'s).¹⁵⁸ Such orders do not significantly increase the work of plan administrators and allow these administrators to manage plans uniformly.¹⁵⁹ Unlike Q.D.R.O.'s, however, general creditors, like bank-

may develop federal common law to fill in the gap left open by the legislature. *See supra* notes 13-14 and accompanying text.

155. *See supra* notes 41-48 and accompanying text.

156. *See Wohl, supra* note 109, at 26-27 (courts should distinguish between voluntary employee contributions reasonably necessary for retirement savings and contributions in excess of that amount, consequently made for unlawful purposes).

157. This does not violate ERISA's purpose of ensuring the financial stability of benefit plans and guaranteeing that employees will receive the benefits they expect. ERISA's purpose is to protect funds so that employees will not lack financial support during retirement. Protecting anything more would allow debtors to avoid creditors while ensuring their own enjoyment of surplus funds. *See S. REP. NO. 93-127, 93rd Cong., 2d Sess. (1974), reprinted in U.S. CODE CONG. & ADMIN. NEWS 4734 (1974); see also A. SCOTT, supra* note 3, at § 151. *But see* *Ellis Nat'l Bank v. Irving Trust Co.*, 786 F.2d 466 (2d Cir. 1986) (ERISA's purpose of ensuring receipt of expected benefits given great weight in barring access to plan funds).

158. A plan administrator need only reduce the employee-debtor's accrued funds by the amount specified in the order. *See supra* notes 34-35, 103 and accompanying text.

159. Q.D.R.O.'s allow payments to be made from a pension plan only when the debtor has reached minimum retirement age. However, creditors should have access to welfare and pension funds once they are payable to the employee. Calculation of what is necessary for reasonable support of the debtor can be done in the same manner in which bankruptcy courts calculate what is needed. *See supra* notes 138-41 and accompanying text; *Wohl, supra* note 109, at 25-27 (discussing methods of calculating what is reasonably necessary for support).

ruptcy creditors, should have access to funds that are payable to an employee, regardless of whether the employee has reached minimum retirement age.¹⁶⁰ Finally, employing a Q.D.R.O. format would address some of the concerns expressed by the dissent in *Mackey v. Lanier Collection Agency*.¹⁶¹

C. *Proposal: Alter the Terms of a Pension Plan at Bankruptcy*

Another solution, espoused by at least one commentator, is for bankruptcy courts to place restrictions on the terms of pension plans.¹⁶² If an employee-debtor desires to protect his or her pension plan funds, then courts should require the employee to consent to restrictions barring access to the funds until the termination of the employment with the plan sponsor.¹⁶³ Such restrictions would transform ERISA's restrictions on fund transfers into a traditional spendthrift clause.¹⁶⁴ Most courts would thus exclude the newly restricted funds from the bankruptcy estate.¹⁶⁵ This proposal, however, only protects the employee. Creditors would have few ways in which to reach pension plan funds if this proposal were accepted. The additional argument has been made that the added restrictions should exempt from the bankruptcy estate only those benefit plan funds that are reasonably necessary for the debtor's support.¹⁶⁶

VI. CONCLUSION

Often, courts bar access by judgment creditors to ERISA protected pension plan funds. Recently, the Supreme Court ruled that judgment creditors can reach the funds in an employee's welfare plan.¹⁶⁷ The argument has been made, however, that such access will hamper the effective administration of welfare plans. Bankruptcy courts, on the other hand,

160. See Wohl, *supra* note 109, at 31-36.

161. See *supra* note 95 and accompanying text.

162. Wohl, *supra* note 109, at 34.

163. Courts that do not recognize ERISA § 206(d)(1) as a spendthrift clause reason that, because the section does not bar free access to the funds, Congress did not intend to exclude the funds. The danger in excluding such funds is that the debtor will access them after bankruptcy proceedings and have more money than needed for his or her fresh start. These added restrictions would remove this concern. See *supra* notes 130-33 and accompanying text.

164. But see *supra* notes 134-36 and accompanying text.

165. See *supra* notes 118-33 and accompanying text.

166. Wohl, *supra* note 109, at 34-36.

167. *Mackey v. Lanier Collections Agency, Inc.*, 108 S. Ct. 2182 (1988).

are likely to allow creditors access to benefit plan funds and most of these courts will only protect a portion of the funds in a pension plan.

To create a consistent theme in the rights of creditors to ERISA benefit plan funds, this Note has discussed two solutions. Either courts should allow all creditors to have access to benefit plan funds except those funds needed to endure financial stability upon retirement, or bankruptcy courts should place restrictions on the terms of pension plans and exclude the plans from the bankruptcy estate.

Charles G. Huber, Jr.