Honorable Mike K. Nakagawa
United States Bankruptcy Judge

Entered on Docket
April 06, 2016

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

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In re:	Case No.: 15-14717-MKN
	Chapter 7
WORTHINGTON LARRY SWECKER,	
	Date: January 27, 2016
Debtor.	Time: 2:30 p.m.

ORDER ON TRUSTEE'S OBJECTION TO EXEMPTION AND SECOND OBJECTION TO EXEMPTION[1]

On January 27, 2016, the court heard the Trustee's Objection to Exemption (ECF Nos. 67-69) and Second Objection to Exemption (ECF No. 71) (collectively, the "Objections"), both of which were filed by the Chapter 7 trustee, Brian D. Shapiro ("Trustee"). The appearances of counsel were noted on the record. After arguments were presented, the matter was taken under submission.

BACKGROUND

On August 18, 2015, Worthington Larry Swecker ("Debtor") filed a voluntary Chapter 7 petition and his initial Schedules. (ECF No. 1). On his initial Schedule "B," Debtor listed his interest in the "Swecker & Company Ltd. Profit Sharing Plan" ("PSP") valued at $880,770.00. On his initial Schedule "C," Debtor claimed $500,000 of the PSP as exempt under NRS 21.090(1)(r) and $380,770.00 as exempt under Section 522(n).

On December 12, 2015, the Trustee filed his Objections. On January 13, 2016, Debtor

[1] In this Order, all references to "ECF No." are to the numbers assigned to the documents filed in the case as they appear on the docket maintained by the clerk of the court. All references to "Section" are to the provisions of the Bankruptcy Code, 11 U.S.C. §§ 101-1532, unless otherwise indicated. All references to "FRBP" are to the Federal Rules of Bankruptcy Procedure.

filed his Response to Trustee's Second Objection to Exemption of Profit-Sharing Plan Based on NRS 21.090(1)(r)(4) ("Response"). (ECF No. 102). On January 20, 2016, Trustee filed a Notice of Non-Opposition regarding the first Objection and a reply to Debtor's Response regarding the second Objection ('Reply"). (ECF Nos. 111-112). On January 21, 2016, Debtor filed his Supplemental Response to Trustee's Objection to Exemption (Profit-Sharing Plan) [Dockets 67 and 71] ("Supplemental Response"),[2] and the Trustee filed his Supplemental Reply to Debtor's Supplemental Response ("Supplemental Reply"). (ECF Nos. 121-122).

On January 22, 2016, Debtor filed an amended Schedule "C," under which he continued to claim $500,000 of the PSP as exempt under NRS § 21.090(1)(r), but now claimed the remaining $380,770 as exempt under Sections 522(b)(1) and (3). (ECF No. 130).[3] Debtor also stated on Schedule "C" that the PSP was "[n]ot property of the estate."

DISCUSSION

Exemptions are intended to preserve property interests essential for an individual to survive. An individual who is subject to collection proceedings is able to retain such essential items by claiming exemptions. See In re Bower, 234 B.R. 109, 112 (Bankr. D. Nev. 1999) ("The historical purpose of exemptions in Nevada is to protect a debtor by permitting him to retain the basic necessities of life so that he and his family will not be left destitute."). See also In re Fox, 302 P.3d 1137, 1139 (Nev. 2013) ("The legislative purpose of NRS 21.090 is 'to secure to the debtor the necessary means of gaining a livelihood, while doing as little injury as possible to the creditor.'"). The list of items considered to be essential varies widely from state to state. See generally, BANKR. EXEMPTION MANUAL APPENDIX B (2014 ed. West Bankruptcy Series). When

[2] Debtor represented that the Supplemental Response was filed "[w]ith the consent of Trustee's counsel." (ECF No. 121 at p. 1 n.1).

[3] Debtor's Amended Schedule "C" amended Debtor's initial exemption of $380,770 under Section 522(n). On December 9, 2015, the Trustee objected to Debtor's initial exemption under Section 522(n). (ECF No. 63). On January 13, 2016, Debtor conceded that the reference to Section 522(n) "was a mistake of counsel . . . ." (ECF No. 100 at p. 1). On January 22, 2016, the court approved a stipulated order which sustained Trustee's objection regarding Section 522(n). (ECF No. 127). At the January 27, 2016 hearing, Trustee's counsel reserved his right to object to Debtor's amended exemption under sections 522(b)(1) and (3). Trustee's current Objections only relate to Debtor's exemption of $500,000 of the PSP under NRS § 21.090(1)(r).

individuals file for bankruptcy protection, their property interests become property of their bankruptcy estate under Section 541(a). See Rousey v. Jacoway, 544 U.S. 320, 325 (2005).

Section 522(b)(1) authorizes an individual debtor to exempt property of the bankruptcy estate. Section 522(d) sets forth a variety of specific exemptions that may be claimed in bankruptcy cases, but Section 522(b)(2) allows individual states to "opt out" of those exemptions so that their residents may claim only the exemptions provided under state law and non-bankruptcy federal law. Under NRS 21.090(3), Nevada has "opted out" of the federal bankruptcy exemptions. See Leavitt v. Alexander (In re Alexander), 472 B.R. 815, 821 (B.A.P. 9th Cir. 2012).

Section 522(l) requires an individual debtor to file a list of the property he or she claims as exempt. FRBP 4003(a) requires the list to be included in the schedules of information that the debtor is required to file under Section 521(a)(1)(B)(i). Section 522(l) also specifically provides that "[u]nless a party in interest objects, the property claimed as exempt on such list is exempt." The official form on which the list of exempt property must appear is Schedule "C."

In order for Debtor to claim an exemption under NRS 21.090(1)(r)(4), his PSP must be a "qualified plan" under 26 U.S.C. §§ 401 et seq. In both Objections, the Trustee argued that the PSP is not such a "qualified plan" and that Debtor's exemption under NRS 21.090(1)(r)(4) should be denied. In his Response and Supplemental Response, Debtor stated, in pertinent part, that the Trustee's Objections to exemptions are irrelevant because the PSP is an ERISA-qualified plan which does not constitute property of the estate.[4] In his Reply, the Trustee stated that Debtor's "property of the estate" arguments were premature, and, as a procedural matter, Debtor must instead file a motion[5] if he wants a court determination regarding whether or not the PSP is property of the estate. In his Supplemental Reply, the Trustee appeared to retreat from this

[4] Debtor also responded to the Trustee's arguments under 26 U.S.C. § 401 et seq, which the court need not and does not address in light of its ruling, as discussed in more detail herein, that the PSP is not property of the estate.

[5] The court interpreted the Trustee's comments as stating that Debtor was required to file an adversary proceeding under FRBP 7001(2).

procedural argument and instead asked the court to find that the PSP was, in fact, property of the estate. However, at the January 27, 2016, hearing, the Trustee again raised, in passing, the procedural argument raised in his Reply. Although the court concludes that the Trustee waived this procedural argument, the court nevertheless disagrees with the Trustee that it is procedurally improper to consider issues regarding whether or not the PSP is property of the estate.

With exceptions not applicable to this case, FRBP 7001(2) requires an adversary "to determine the validity, priority, or extent of a lien or other interest in property . . ." However, the Trustee will not be prejudiced if the court decides whether or not the PSP constitutes property of the estate in the context of this contested matter. See Korneff v. Downey Reg'l Med. Ctr.-Hosp., Inc. (In re Downey Reg'l Med. Ctr.-Hosp., Inc.), 441 B.R. 120, 127 (B.A.P. 9th Cir. 2010) (A bankruptcy court's decision to not require an adversary proceeding is subject to a harmless error analysis, under which "form should not be elevated over substance" in the absence of prejudice.). The Trustee was served with Debtor's response, was aware of Debtor's argument that the PSP was not property of the estate, and either responded or had the opportunity to respond to Debtor's arguments both in his Reply, Supplemental Reply, and at the January 27, 2016, hearing. As in Korneff, the Trustee "received the process that was due to him." Id. at 128. Further, an authenticated copy of the PSP is available in the record. (ECF Nos. 63 at Ex. 1; 101 at ¶ 2). Therefore, as in Korneff, all material facts are undisputed and the court can decide whether or not the PSP is property of the estate in a summary judgment fashion. Finally, the Ninth Circuit has instructed that bankruptcy courts should not decide exemption issues without first deciding whether or not the property claimed to be exempt constitutes property of the estate. See Spirtos v. Moreno (In re Spirtos), 992 F.2d 1004, 1007 (9th Cir. 1993) ("The exemption question arises only if the plans are first determined to be property of the estate. 11 U.S.C. § 522(b). In fact, if the plans are not property of the estate, the bankruptcy court should not make a decision on the exemption question."). For all these reasons, it is procedurally necessary for the court to decide whether the PSP is or is not property of the estate before deciding the Trustee's Objections to Debtor's exemptions. The court therefore rejects the Trustee's procedural arguments.

Section 541(c)(2) provides that "[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." According to the Supreme Court:

> The natural reading of the provision entitles a debtor to exclude from property of the estate any interest in a plan or trust that contains a transfer restriction enforceable under any relevant nonbankruptcy law.

Patterson v. Shumate, 504 U.S. 753, 758 (1992). In Shumate, the Supreme Court held that section 541(c)(2) excludes from the property of the estate ERISA-qualified plans that contain the anti-alienation language required under ERISA. The Ninth Circuit has interpreted Shumate as holding that "this court need look no further than whether the ERISA-qualified plan at issue has an anti-alienation provision that satisfies the literal terms of § 541(c)(2)." Arkison v. UPS Thrift Plan (In re Rueter), 11 F.3d 850, 852 (9th Cir. 1993).[6] Here, Article XVII.C of the PSP contains the anti-alienation provision required under ERISA.[7] The Trustee has not disputed that the PSP

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[6] Three years after the Ninth Circuit's opinion in Rueter, one bankruptcy judge in this district, in dicta, appeared to take a position perhaps contrary to Rueter:

> [T]he reason for ERISA qualified plan[s] is the tax relief which is the usual inducement. Tax deferral approved by the IRS . . . is necessary to the definition . . .

In re Watson, 192 B.R. 238, 242 (Bankr. D. Nev. 1996), aff'd on other grounds, 214 B.R. 597 (B.A.P. 9th Cir. 1998), aff'd, 161 F.3d 593 (9th Cir. 1998). However, such dicta is contrary to the Ninth Circuit's decision in Rueter and is not binding on this court.

[7] ERISA states that "[e]ach pension plan shall provide that benefits provided under the plan may not be assigned or alienated." 29 U.S.C. § 1056(d)(1). Article XVII.C of the PSP states, in pertinent part:

> Any attempt by a Participant or Beneficiary to assign, alienate, sell, transfer, pledge or encumber his or her benefits shall be void. A Participant's or Beneficiary's interest shall not be subject in any manner to transfer by operation of law, and shall be exempt from the claims of creditors or other claimants (including but not limited to, debts, contracts, liabilities or torts) from all orders, decrees, levies, garnishments and/or executions and other legal or equitable process or proceedings against such Participant or Beneficiary to the full extent which may be permitted by law.

contains the anti-alienation language required under ERISA. Therefore, under Shumate and Rueter, the PSP is an ERISA-qualified plan and, under Spirtos, the court does not even reach issues relating to exemptions.

To the extent the Trustee argues that the PSP is not a tax qualified plan under the Internal Revenue Code because it violates various subsections of 26 U.S.C. 401(a) and therefore a tax qualification under the Internal Revenue Code is necessary for a plan to be ERISA-qualified under Shumate and section 541(c)(2), the court disagrees. In deciding whether or not the PSP is an ERISA-qualified plan, the court need not decide the PSP's status under the Internal Revenue Code because "[t]axation has nothing to do with the question at hand . . . ." In re Baker, 114 F.3d 636, 638 (7th Cir. 1997). Although the court acknowledges that there is a disagreement among the lower courts regarding this issue, see Traina v. Sewell (In re Sewell), 180 F.3d 707, 712 (5th Cir. 1999), the court finds more persuasive the holdings reached by the Fifth and Seven Circuits that an ERISA-qualified plan is excluded from the property of the estate regardless of whether such plan is or is not tax qualified. See id. at 712-13; In re Baker, 114 F.3d at 638. The court finds particularly persuasive the following analysis from the Fifth Circuit:

> Nowhere in ERISA, however, is there a requirement that, to be an ERISA plan and thus be governed by ERISA, a plan must be tax qualified. Indeed, the converse is true: An ERISA plan that is not or may not be tax qualified nevertheless continues to be governed by ERISA for essentially every other purpose. It would be perverse, indeed, if the negligent or intentional act of an ERISA plan sponsor, administrator, or other fiduciary, that results in disqualification for tax purposes could, *ipso facto*, remove the plan – and thus the beneficial interests of the employees/participants – from the aegis of ERISA and its protections of the very interests for which the legislation was adopted and is administered in parallel by the Treasury and Labor Departments. The instant case is a perfect example: Were the rule otherwise, the Debtor's beneficial interest in her ERISA employee pension benefit plan, replete with restrictions on voluntary and involuntary alienation and thus facially excludable from the Debtor's bankruptcy estate under § 541(c)(2) of the Bankruptcy Code, could be stripped of all ERISA protection, including enforceable nonbankruptcy restrictions on transfer, by the failure of her employer – beyond any control of the Debtor – to maintain tax qualification of the Plan.

In re Sewell. 180 F.3d at 711.

The conclusions reached by the Fifth and Seventh Circuits are consistent with the Ninth

Circuit's directive in Rueter that, under Shumate, a plan is ERISA-qualified so long as it contains the anti-alienation language required under ERISA. These holdings are also consistent with ERISA, which contains separate enforcement mechanisms for pension plans depending on whether or not they are tax-qualified plans. See 29 U.S.C. § 1132(a)-(b).

Finally, several courts of appeals have either expressly or implicitly acknowledged that 26 U.S.C. § 401, under which the Trustee relies, is not incorporated into ERISA. See Stamper v. Total Petroleum, Inc. Ret. Plan For Hourly Rated Emps. With The Bargaining Unit Represented By Local 642 Of The Int'l Union Of Operating Eng'rs (AFL-CIO), 188 F.3d 1233, 1238 (10th Cir. 1999), quoting, Reklau v. Merchs. Nat'l Corp., 808 F.2d 628, 631 (7th Cir. 1986) ("'There is no basis, under . . . ERISA, to find that the provisions of [26 U.S.C.] § 401 – which relate solely to the criteria for tax qualification under the Internal Revenue Code – are imposed on pension plans by the substantive terms of ERISA. We are convinced that had Congress intended that § 401 of the I.R.C. be applicable to ERISA, it would have so stated in clear and unambiguous language as it did in 29 U.S.C. § 1202(c) with §§ 410(a), 411 and 412 of the I.R.C. We thus refuse to read § 401(a) of the I.R.C. as applicable to ERISA."); see also McDaniel v. Chevron Corp., 203 F.3d 1099 (9th Cir. 2000) (approvingly citing to Stamper and Reklau); West v. Clarke Murphy, Jr. Self Employed Pension Plan, 99 F.3d 166, 169 (4th Cir. 1996) (approvingly citing to Reklau).

For all of these reasons, the PSP is not property of the estate, and the court "should not make a decision on the exemption question." In re Spirtos, 992 F.2d at 1007.

IT IS THEREFORE ORDERED that the Trustee's Objection to Exemption, Docket No. 67, be, and the same hereby is, **OVERRULED AS MOOT**.

IT IS THEREFORE ORDERED that the Second Objection to Exemption, Docket No. 71, be, and the same hereby is, **OVERRULED AS MOOT**.

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