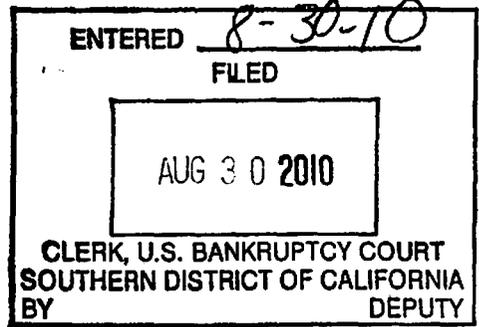


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WRITTEN DECISION - NOT FOR PUBLICATION



**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF CALIFORNIA**

In re:

Robert Alan Weilhammer and Adele
Villalobos Weilhammer,

Debtors.

} BK. No. 09-15148-LT7

} MEMORANDUM DECISION

Debtor Robert Alan Weilhammer ("Debtor") inherited his mother's individual retirement account (the "Initial IRA") on her death and directly transferred the funds held therein to an individual retirement account established in his name as beneficiary (the "Recipient IRA"). Thereafter, Debtor and his wife filed a chapter 7 case and claimed an exemption in the Recipient IRA. The chapter 7 trustee objects to this claim of exemption. Thus, this Court now must determine whether Debtor appropriately claims an exemption in the Recipient IRA under 11 U.S.C. § 522(b)(3)(C)¹.

¹ Hereinafter: references to code sections refer to Title 11 of the United States Code, also referred to as the "Bankruptcy Code" and references to "IRC sections" refer to Title 26 of the United States Code, also referred to as the "Internal Revenue Code", unless otherwise specified. References to rules refer to the Federal Rules of Bankruptcy Procedure, unless otherwise specified.

STATEMENT OF THE FACTS

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2
3 During her lifetime, the Debtor's mother, Mary Weilhammer, established and funded
4 the Initial IRA. While the evidence underlying this dispute is thin, there is no dispute that
5 the Initial IRA was a properly established retirement account that was exempt from taxation
6 under IRC section 408.

7 The Initial IRA named Debtor as the beneficiary properly entitled to inherit the Initial
8 IRA upon his mother's death.

9 Ms. Weilhammer died prior to October 5, 2009, the petition date in this case (the
10 "Petition Date"). Debtor then inherited the Initial IRA. Again, the chapter 7 trustee
11 ("Trustee") does not dispute that Debtor properly preserved the tax-exempt character of the
12 funds held therein. In particular, through a trustee-to-trustee transfer authorized by IRC
13 section 402, Debtor transferred the funds in the tax-exempt Initial IRA to the tax-exempt
14 Recipient IRA. Trustee acknowledges indirectly through her argument that Debtor did not
15 contribute any of his own funds to the Recipient IRA.

16 After creation of the Recipient IRA and prior to the Petition Date, the Debtor
17 withdrew approximately \$55,182.12 from the Recipient IRA. These distributions were
18 taxable to the Debtor, but the funds remaining in the Recipient IRA remained tax exempt as
19 of the Petition Date.

20 Debtor and his wife, Adele Villalobos Weilhammer, filed their joint chapter 7 case
21 on the Petition Date. On schedule C, Debtor and his wife selected 11 U.S.C. § 522(b)(3)² as
22 the exemptions to which they are entitled, listed the Recipient IRA as an exempt asset, and
23 specified Cal. Code Civ. Proc. § 703.140(b)(10)(E) as the "Law Providing [] Exemption."
24 The Trustee filed a timely objection to this claim of exemption,³ and the Debtor responded
25

26 ² The form "Schedule C – Property Claimed As Exempt" requires that debtors select the
27 appropriate Bankruptcy Code exemption section to which they are entitled by checking a box—
28 either 11 U.S.C. § 522(b)(2) (the federal exemptions) or 11 U.S.C. § 522(b)(3) (the state
exemptions).

³ The Trustee also objected to the Debtor's claim of exemption in a second IRA, but that

1 and set this matter for hearing. In this response, the Debtor argued, among other things, that
2 the Recipient IRA also is exempt under subsection (C) of section 522(b)(3).

3 The Court held an initial hearing on this matter on April 22, 2010 and requested
4 further briefing. The Court received additional documents and held final oral argument on
5 June 16, 2010. This matter is now ready for decision.

7 DISCUSSION

9 **A. The Court Must Construe Exemptions Liberally In Favor Of The Debtor, And** 10 **The Trustee Bears The Burden Of Proof Here.**

11 Section 522(b) allows a chapter 7 debtor to exempt certain property otherwise
12 includable in his bankruptcy estate. Properly exempted property is not available to pay the
13 claims of the debtor's creditors. The Court must construe the claim of exemption in the
14 Recipient IRA liberally in favor of the Debtor. *See, Arrol v. Broach (In re Arrol)*, 170 F.3d
15 934, 937 (9th Cir. 1999). And the Trustee, as the party objecting to a claim of exemption,
16 bears the burden of proving that the Debtor improperly claims this exemption. *Kelley v.*
17 *Locke (In re Kelley)*, 300 B.R. 11, 14 (9th Cir. BAP 2003) [citing *In re Carter*, 182 F.3d
18 1027, 1029 (9th Cir. 1999)]. The critical date for determining exemptions is the petition
19 date. *Goswami v. MTC Distributing (In re Goswami)*, 304 B.R. 386, 391-92 (9th Cir. BAP
20 2003).

21 **B. As A Result Of BAPCPA, The Debtor Is Entitled To An Exemption Under** 22 **Section 522(b)(3)(C).**

23 The Bankruptcy Code allows for exemptions under either or both of state or federal
24 law. It further permits each state to preclude the use of the federal exemptions set forth in
25 section 522(d) and to require that a debtor utilize exemptions as provided for by state law.
26 11 U.S.C. § 522(b)(2). Pursuant to this authority, California elected state exemptions for its
27 citizens. Cal. Code Civ. Proc. § 703.130(a).

28 _____
matter was resolved by the parties, and a decision by this Court is not required.

1 In 2005, Congress enacted the Bankruptcy Abuse Prevention and Consumer
2 Protection Act of 2005 ("BAPCPA"). BAPCPA provides an additional retirement fund
3 exemption for individuals in states that opt out of the federal exemption scheme. A
4 California debtor, thus, still may use the California retirement fund exemption, but the
5 California debtor also has a right to the specific federal exemption listed in
6 section 522(b)(3)(C), which provides an exemption for: "retirement funds to the extent that
7 those funds are in a fund or account that is exempt from taxation under section 401, 403,
8 408, 408A, 414, 457, or 501(a) of the Internal Revenue Code of 1986." 11 U.S.C.
9 § 522(b)(3)(C); *and see* H. Rep. No. 109-31(I), 109th Cong., 1st Sess. 63-64 (2005),
10 *reprinted in* 2005 WL 832198, 2005 U.S.C.C.A.N. 88 (the BAPCPA amendment to
11 section 522 "ensures that the specified retirement funds are exempt under state as well as
12 Federal law.").

13 The language of section 522(b)(3)(C) is identical to the language of
14 section 522(d)(12), the statute containing the federal retirement fund exemption.
15 Section 522(b)(3)(C), thus, protects debtors residing in states that opt out of the federal
16 exemption scheme, as it creates a uniform minimum for exemptions for retirement funds in
17 all bankruptcy cases notwithstanding the provisions and limitations of state law.

18 In schedule C, the Debtor specified the statutory section under California state law
19 for his exemption of the Recipient IRA. After receipt of the Trustee's objection, however,
20 the Debtor also argued, in the alternative, that he is entitled to the exemption under
21 section 522(b)(3)(C). As Debtor selected exemptions under section 522(b)(3) this is
22 sufficient, but in any event, the Trustee did not object to this Court's consideration of issues
23 arising under section 522(b)(3)(C) and, instead, directly addressed this issue in papers filed
24 with the Court.

25 **C. Is An Inherited IRA Entitled To The Section 522(b)(3)(C) Exemption?**

26 In the present case, the Initial IRA was an "individual retirement account" within the
27 meaning of IRC section 408(a). The parties appear to agree that the Recipient IRA is an
28

1 "inherited individual retirement account" within the meaning of IRC section 408(d)(3)(C).⁴
2 Recently, several courts have wrestled with the applicability of the sections 522(d)(12) and
3 522(b)(3)(C) exemptions to inherited IRAs. A review of this case law provides a path for
4 decision in this case.

5 1. *In re Nessa*. The Bankruptcy Appellate Panel for the Eighth Circuit recently
6 considered this issue. *Doeling v. Nessa (In re Nessa)*, 426 B.R. 312 (8th Cir. BAP 2010).
7 In *Nessa*, the debtor made a trustee-to-trustee transfer of the funds in an IRA she had
8 inherited from her father prior to initiating a chapter 7 case. *Id.* at 313. The *Nessa* court
9 emphasized that Ms. Nessa complied fully with the rules required to maintain the tax
10 exempt character of an inherited IRA; she did not withdraw any funds prior to rollover to a
11 newly created IRA, and she did not make contributions of her funds to the IRA. *Id.* at 313;
12 *see also* 26 U.S.C. § 408(d)(3)(C). The *Nessa* court then found that the debtor properly
13 claimed her inherited IRA as exempt under section 522(d)(12). It noted that a
14 section 522(d)(12) exemption must meet only two requirements: "(1) the amount the debtor
15 seeks to exempt must be retirement funds; and (2) the retirement funds must be in an
16 account that is exempt from taxation under one of the provisions of the Internal Revenue
17 Code set forth [in section 522(d)(12)]." *Id.* at 314. It then concluded that the debtor's
18 inherited IRA satisfied both requirements.

19 First, the *Nessa* court found that the funds at issue were retirement funds, albeit those
20 of Ms. Nessa's father. The *Nessa* court rejected the argument that retirement funds for
21 purposes of section 522(d)(12) must be created from a debtor's own efforts and assets and
22 pointed out that the statute makes no such distinction and that to so define retirement funds
23 would: ". . . impermissibly limit the statute beyond its plain language." *Id.* at 314 [citing
24 *United States v. Ron Pair Enters.*, 489 U.S. 235, 241 (1989)].

25 The *Nessa* court next addressed the requirement that the funds at issue be exempt
26 from taxation and determined that an inherited IRA is tax exempt under IRC section 408(e).

27
28 ⁴ The Court will use the term "inherited IRA" to refer to an IRA fitting the definition of IRC
section 408(d)(3)(C) hereafter.

1 The *Nessa* court dismissed the argument that an inherited IRA is somehow distinguishable
2 from other IRC section 408 tax exempt IRAs because it is uniquely subject to certain rules
3 and limitations in other sections of the Internal Revenue Code, particularly as regards
4 distributions:

5 It is irrelevant whether a traditional IRA and an inherited IRA
6 have different rules regarding minimum required distributions.
7 *Section 408(e) of the Internal Revenue Code* provides, in
8 pertinent part, that "[a]ny individual retirement account is
9 exempt from taxation."

10 *Id.* at 315 (citation omitted; emphasis in original).

11 Finally, the *Nessa* court found support for its decision in section 522(b)(4)(C), which
12 provides that retirement funds directly transferred from a section 408(a) tax-exempt fund or
13 account to another such account continue to qualify for exemption under section 522(d)(12).

14 Section 522(b)(4)(C) states:

15 For the purposes of paragraph (3)(C) and subsection
16 (d)(12), the following shall apply:

17 ...
18 (C) A direct transfer of retirement funds from 1 fund or account
19 that is exempt from taxation under section 401, 403, 408, 408A,
20 414, 457, or 501(a) of the Internal Revenue Code of 1986, under
21 section 401(a)(31) of the Internal Revenue Code of 1986, or
22 otherwise, shall not cease to qualify for exemption under
23 paragraph (3)(C) or subsection (d)(12) by reason of such direct
24 transfer.

25 11 U.S.C. § 522(b)(4)(C).

26 The *Nessa* court concluded that section 522(b)(4)(C) directly supported its decision that
27 inherited IRAs qualify for the section 522(d)(12) exemption. *Nessa*, 426 B.R. at 315.

28 **2. *In re Tabor.*** Subsequent to the decision in *Nessa*, the bankruptcy court for the
Middle District of Pennsylvania determined that inherited IRAs also are exempt under
section 522(b)(3)(C). *See, Bierbach v. Tabor (In re Tabor)*, 2010 Bankr. LEXIS 2051
(Bankr. M.D. Pa. 2010). In *Tabor*, the debtor inherited an IRA pre-petition, appropriately

1 created an inherited IRA, and took substantial distributions from the inherited IRA pre-
2 petition. *Id.* at *3.

3 The *Tabor* court acknowledged that the Internal Revenue Code treats inherited IRAs
4 differently than it does accounts funded by an individual's own employment earnings in
5 certain respects. *Id.* at *8. It then noted that BAPCPA expanded the exemption status of
6 IRAs to include any retirement funds held in an account exempt from taxation under
7 specific Internal Revenue Code sections, without reference to whether such funds were
8 necessary for the support of the debtor or the debtor's dependents. *Id.* at *12. And it further
9 emphasized that as a result of section 522(b)(4)(C): "[t]his increased protection is afforded
10 not only to an IRA account created by the debtor, but also extends to accounts that are
11 transferred directly between trustees (e.g., inherited accounts) and to roll over distributions."
12 *Id.* at *13. The *Tabor* court held that the language of section 522(b)(3)(C) unambiguously
13 applies to inherited IRAs, although it also acknowledged that it was unclear whether
14 Congress realized that inherited IRAs were "trustee to trustee" accounts. *Id.* Based on the
15 above and expressly agreeing with the *Nessa* court's analysis, the *Tabor* court held that the
16 funds in an inherited IRA are retirement funds, that an inherited IRA is tax exempt under
17 IRC section 408, and that, as a result, an inherited IRA is exempt under section
18 522(b)(3)(C). *Id.* at *17.

19 3. *In re Chilton.* While the Court finds the *Nessa* and *Tabor* analyses
20 compelling, the Court recognizes that at least one well-written recent decision argues to the
21 contrary.⁵ In *In re Chilton*, 426 B.R. 612 (Bankr. E.D. Tex. 2010), the court determined that
22 an inherited IRA was not exempt under section 522(d)(12). Given the identity of language
23 between section 522(d)(12) and section 522(b)(3)(C), the *Chilton* analysis could also control
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26 ⁵ During the period of time the Court had this matter under submission, a decision was
27 entered by the bankruptcy court for the Southern District of Indiana, which cited with approval to
28 the reasoning in *Chilton*. See, *In re Klipsch*, 2010 Bankr. LEXIS 1845 (Bankr. S.D. Ind. 2010).
The *Klipsch* decision focused solely on Indiana state exemption law, however, and for that reason is
not further discussed herein.

1 in this case. *Chilton* involved an inherited IRA, and its facts are not distinguishable from
2 those of *Nessa, Tabor*, or the case here.

3 The *Chilton* court's analysis differed from that of the *Nessa* and *Tabor* courts in three
4 significant ways. First, the *Chilton* court determined that the term "retirement funds" must
5 be interpreted so as to exclude inherited IRAs. It determined that: "[an argument that funds
6 in an inherited IRA are retirement funds] collapses the question of whether an inherited IRA
7 is a tax exempt account with whether an inherited IRA contains retirement funds." *Chilton*,
8 426 B.R. at 617. The *Chilton* court, thus, ultimately concluded that the plain language of
9 the statute required the conclusion that funds in an inherited IRA are not retirement funds as
10 they are not funds intended for retirement purposes but instead are distributed to the
11 beneficiary of the account without regard to age or retirement status. *Id.* at 618.

12 Also, the *Chilton* court concluded that an inherited IRA is not a "traditional IRA
13 exempt from taxation under [IRC section] 408(e)(1)." *Id.* at 622 (emphasis added). The
14 *Chilton* court reached this conclusion notwithstanding the broad language of IRC section
15 408(e) which actually states that: "[a]ny individual retirement account is exempt from
16 taxation under this subtitle unless such account has ceased to be an individual retirement
17 account by reason of paragraph (2) or (3)."⁶ 26 U.S.C. § 408(e)(1) (emphasis added). The
18 *Chilton* court then concluded that an inherited IRA is actually exempt under IRC section
19 402 (c)(11). *Id.* at 621. Section 402(c)(11) allows the trustee-to-trustee rollover necessary
20 to create an inherited IRA and states that an inherited IRA: "shall be treated as an inherited
21 individual retirement account or individual retirement annuity (within the meaning of
22 section 408(d)(3)...for purposes of this title." 11 U.S.C. §402(c)(11)(A)(ii).

23 Finally, while the *Chilton* court discussed a myriad of other factors, it failed to
24 discuss section 522(b)(4)(C). Thus, it failed to consider the impact of this portion of the
25 statute on its conclusion that inherited IRAs are not subject to the section 522(d)(12)
26 exemption.

27
28 ⁶ Paragraphs (2) and (3) pertain to factual scenarios not implicated here (prohibited transactions and borrowing on annuity contracts). *See*, 26 U.S.C. § 408(e)(2) & (3).

1 **D. The Court Adopts The Analysis In *Nessa* And *Tabor* And Reaches The**
2 **Conclusion That The Debtor May Claim The Recipient IRA Exempt Under**
3 **Section 522(b)(3)(C).**

4 For this Court, the closest question when considering the applicability of section
5 522(b)(3)(C) to an inherited IRA is whether the funds in an inherited IRA are "retirement
6 funds" within the meaning of section 522(b)(3)(C). Both sides of the debate assert that the
7 "plain language" of the statute supports its view. *Nessa*, 426 B.R. at 314; *Chilton*, 426 B.R.
8 at 617-18. And the Court is well aware that where the statutory language is clear: "the sole
9 function of the courts is to enforce it according to its terms." *United States v. Ron Pair*
10 *Enters.*, 489 U.S. at 241 (citation omitted). Each side in the debate also points to a rule of
11 statutory construction to bolster its reading of the statute.

12 The *Chilton* court argues that determining that funds in an inherited IRA are
13 retirement funds inappropriately requires that the Court read the word "retirement" out of
14 the statute. *Chilton*, 426 B.R. at 617. In essence, it argues that Congress could have
15 exempted "funds" in any tax-exempt IRA, but did not. As a result, the court concludes, the
16 word "retirement" must have meaning and asserts that such meaning is found only where the
17 funds are necessary for a debtor's own retirement needs. *Id.* at 618, 620-21. The *Chilton*
18 court correctly notes that the funds in an inherited IRA may not be required by a debtor for
19 retirement or used to meet a debtor's retirement needs. The Court finds this analysis logical
20 and would be inclined to adopt it, but for the fact that the *Chilton* court fails to consider and
21 discuss the express language of section 522(b)(4)(C).

22 The *Nessa* and *Tabor* courts correctly recognize that the entirety of the statute must
23 be considered. *Nessa*, 426 B.R. at 315; *Tabor*, 2010 Bankr. LEXIS at *16. The plain
24 language of section 522(b)(4)(C) expressly provides that transfers of the type that create an
25 inherited IRA do not cause a loss of exemption eligibility. The Court agrees with the *Nessa*
26 and *Tabor* courts that this statutory provision makes it difficult to adopt the *Chilton* view.

27 Further, there is an answer to the *Chilton* court's concern. The funds in an inherited
28 IRA are, in fact, retirement funds within the definitional constraints erected by that court,

1 albeit that they are retirement funds of a non-debtor. Thus, as the *Nessa* and *Tabor* courts
2 argue, one could conclude that it is the *Chilton* court that fails to enforce the statute's plain
3 language as it reads the statute as meaning the "debtor's retirement funds." In so doing, it
4 arguably adds a word to the statute that creates a limitation unintended by Congress and
5 inconsistent with the statute's plain meaning.

6 Thus, the Court concludes that the funds in an inherited IRA are retirement funds
7 within the meaning of section 522(b)(3)(C). To determine otherwise would require the
8 Court to ignore that these funds were retirement funds within any reasonable view of the
9 definition, albeit of the debtor's relative and not the debtor, to assume that Congress limited
10 the term retirement funds in a manner not clear from the plain language, and to ignore the
11 impact of another provision of the statute. While this is a close call, the Court ultimately
12 finds the analysis in the *Nessa* and *Tabor* cases to be the more compelling.

13 The Court has less trouble with other portions of the *Chilton* analysis. The Court
14 disagrees with the suggestion that an inherited IRA is exempt under IRC section 402(c)(11).
15 That statute expressly states that certain transfers, rather than constituting taxable
16 distributions, are treated as eligible rollover distributions, and the individual retirement plan
17 treated as an inherited IRA under IRC section 408 and subject to IRC section 401(a)(9)(B).
18 26 U.S.C. § 402(c)(11)(A). And, contrary to the *Chilton* court's reading of IRC
19 section 408(e)(1) as limited to "traditional" IRA's, the code section expressly states that
20 "any" individual retirement account is exempt from taxation under IRC section 408.⁷ The
21 Court finds nothing in IRC section 402 that independently provides for tax-exemption.

22 Finally, as the *Nessa* and *Tabor* courts note, the *Chilton* court failed to take into
23 account the express statutory language that provides that a trustee-to-trustee rollover, such
24 as the rollover that creates an inherited IRA, will not have an impact on the exempt status of
25 an individual retirement account. This Court agrees that this point is significant and that this
26 omission makes it impossible to follow the *Chilton* analysis.

27
28 ⁷ Unless the employee engages in a prohibited transaction or borrows from an annuity
contract—neither of which circumstance is alleged here. See, 26 U.S.C. § 408(e)(2) & (3).

1 Thus, the Court determines that an inherited IRA may be claimed as exempt under
2 section 522(b)(3)(C). An inherited IRA contains retirement funds. It is exempt from
3 taxation under IRC section 408. Thus, the statutory requirements are met.

4 Because the Court determines that the Recipient IRA is exempt under
5 section 522(b)(3)(C), the Court does not need to determine whether the Recipient IRA also
6 is exempt under Cal. Code Civ. Proc. 703.140(b)(10)(E).⁸

8 CONCLUSION

9 The Court assumes the Debtor's claim of exemption to be modified to explicitly
10 include section 522(b)(3)(C) as a basis for exemption of the Recipient IRA. The Court
11 requires that the Debtor modify the schedules immediately to reflect this modification.
12 Concurrent with this modification, the Trustee's objection to the debtor's claim of exemption
13 of the Recipient IRA is overruled, and the Debtor may submit his order so providing.

14
15 DATED: August 30, 2010


16 LAURA S. TAYLOR, JUDGE
17 United States Bankruptcy Court
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19
20

21 ⁸ In a pre-BAPCPA decision cited by the court in *Chilton*, a colleague carefully and
22 appropriately analyzed the similar provisions of California law and concluded that the funds in an
23 inherited IRA would not be exempt as they were not "retirement funds." See, *In re Greenfield*, 289
24 B.R. 146 (Bankr. S.D. Cal. 2003). In so doing, the court focused on the probable intent of the
25 California legislature in using the term retirement funds. *Id.* at 150. The court concluded that the
26 term "retirement funds" was best understood in that context as referring to retirement funds intended
27 for the Debtor's retirement. *Id.* This Court does not disagree here. When evaluating the federal
28 statute, as opposed to the California statute, a different conclusion regarding legislative intent is
required given the inclusion in the Bankruptcy Code of section 522(b)(4)(C). As discussed above,
this portion of the statute makes clear that retirement funds do not lose their exempt character as a
result of a direct trustee-to-trustee transfer. Here, the funds in question were clearly "retirement
funds" of the Debtor's mother. They came into the Debtor's hands only as a result of such a direct
trustee-to-trustee transfer. Thus, this legislative language suggests that Congress had a legislative
intent perhaps different from that of the California legislature. Thus, were this Court analyzing the
statutory language of the California law, a different result might be appropriate.