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I. Introduction

The U.S. Supreme Court recently held in *Patterson v. Shumate*[1] that a bankruptcy debtor's interest in a pension plan is not property of the bankruptcy estate (and therefore beyond the reach of creditors) if the pension plan contains the type of anti-alienation provision required to qualify for special tax treatment under the Employee Retirement Income Security Act of 1974 (hereinafter "ERISA").[2] *Pat-*

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1. 112 S. Ct. 2242 (1992).

2. Pub. L. No. 93-406, 88 Stat. 829 (1974) (codified as amended at 29 U.S.C. § 1001). ERISA was enacted by Congress in order to promote uniform treatment of retirement plans and to protect employees from abuses in the administration of plans. Congress recognized that many employees and their beneficiaries were being deprived of anticipated retirement benefits, and found it necessary to provide minimum standards for such plans. *See* 29 U.S.C. § 1001 (1988).

terson resolved most issues in the controversy over whether creditors could reach the debtor's pension benefits to satisfy their claims.[3] Bankruptcy trustees have battled with debtors and pension plan trustees for several years over this issue and the circuits were divided.[4] While the *Patterson* case has resolved much of the uncertainty in this area, there are still unanswered questions.

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3. 112 S. Ct. at 2242.

4. The Supreme Court granted certiorari in *Patterson v. Shumate* in order to resolve the conflict among the courts of appeals concerning whether creditors can levy on pension plan assets. The Third, Fourth, Sixth and Tenth Circuits held that the bankruptcy trustee cannot reach qualified pension benefits. *See* Gladwell v. Harline (*In re* Harline), 950 F.2d 669 (10th Cir. 1991) (ERISA constitutes "applicable nonbankruptcy law" under 11 U.S.C. § 541(c)(2).), *cert. denied,* 112 S. Ct. 2991 (1992); Velis v. Kardanis, 949 F.2d 78 (3d Cir. 1991) (ERISA constitutes "applicable nonbankruptcy law" under 11 U.S.C. § 541(c)(2).); Shumate v. Patterson, 943 F.2d 362 (4th Cir. 1991) (ERISA constitutes "applicable nonbankruptcy law" under 11 U.S.C. § 541(c)(2).); Forbes v. Lucas (*In re* Lucas), 924 F.2d 597 (6th Cir. 1991) (ERISA constitutes "applicable nonbankruptcy law" under 11 U.S.C. § 541(c)(2).), *cert. denied,* 111 S. Ct. 2275 (1991); Anderson v. Raine (*In re* Moore), 907 F.2d 1476 (4th Cir. 1990)(ERISA constitutes "applicable nonbankruptcy law" under 11 U.S.C. § 541(c)(2).). The Fifth, Eighth, Ninth and Eleventh Circuits held that the bankruptcy trustee can reach the pension benefits, unless they are exempt. *See* Heitkamp v. Dyke (*In re* Dyke), 943 F.2d 1435 (5th Cir. 1991) (The phrase "applicable nonbankruptcy law" as used in 11 U.S.C. § 541(c)(2) refers only to state spendthrift trust law.); Daniel v. Security Pac. Nat'l Bank (*In re* Daniel), 771 F.2d 1352 (9th Cir. 1985) (The phrase "applicable nonbankruptcy law" as used in 11 U.S.C. § 541(c)(2) refers only to state spendthrift trust law.), *cert. denied,* 475 U.S. 1016 (1986); Lichstrahl v. Bankers Trust (*In re* Lichstrahl), 750 F.2d 1488 (11th Cir. 1985) (The phrase "applicable nonbankruptcy law" as used in 11 U.S.C. § 541(c)(2) refers only to state spendthrift trust law.); Samore v. Graham (*In re* Graham), 726 F.2d 1268 (8th Cir. 1984) (The phrase "applicable nonbankruptcy law" as used in 11 U.S.C. § 541(c)(2) refers only to state spendthrift trust law.); Goff v. Taylor (Matter of Goff), 706 F.2d 574 (5th Cir. 1983) (The phrase "applicable nonbankruptcy law" as used in 11 U.S.C. § 541(c)(2) refers only to state spendthrift trust law.). *See also* Richard A. Montague, Jr., *Are Retirement Funds Exempt From the Reach of Creditors in Mississippi?*, 10 MISS. C. L. REV. 125 (1990).

The Court in *Patterson* ruled that the anti-alienation provision[5] required in ERISA-qualified pension plans[6] constitutes an enforceable restriction on transfer within the meaning of section 541(c)(2) of the Bankruptcy Code.[7] Therefore, as a general rule, ERISA-qualified pension benefits cannot be reached by creditors. The *Patterson* decision recognizes the integrity of ERISA's anti-alienation clause and promotes Congress's expressly declared policy of protecting "the interests of participants in [employee benefit] plans and their beneficiaries."[8] The *Patterson* case did not involve a fraudulent debtor. In fact, the debtor in *Patterson* argued that excluding pension benefits from the debtor's estate would not prejudice creditors if the debtor had transferred funds into an ERISA-qualified plan to hinder, defraud

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5. One of the requirements that a plan must meet in order to maintain qualified status is that it must provide that "benefits . . . may not be assigned or alienated." *See* I.R.C. § 401(a)(3) (1988). This requirement is often referred to as the "anti-alienation provision." *Id.*; *see infra* note 6 for a discussion of qualification. The Treasury Department regulation addressing section 401(a)(13) of the Internal Revenue Code provides:

> Under § 401(a)(13), a trust shall not constitute a qualified trust unless the plan of which such 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 or equitable process.

Treas. Reg. 1.40(a)-13(b)(1)(1985).

Title I, § 206 (d)(1) of ERISA reads: "[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) (1988).

A sample anti-alienation provision in an ERISA-qualified plan reads as follows:

> Subject to the exceptions provided below, no benefit which shall be payable out of the Trust Fund to any person (including a participant or his beneficiary) shall be subject in any manner to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance, or charge, and any attempt to anticipate, alienate, sell, transfer, assign, pledge, encumber or charge the same shall be void; and no such benefit shall in any manner be liable for, or subject to, the debts, contracts, liabilities, engagements, or torts of any such person, nor shall it be subject to attachment or legal process for or against such person, and the same shall not be recognized by the Trustee, except to such extent as may be required by law.
>
> This provision shall not apply to the extent a participant or beneficiary is indebted to the Plan, for any reason, under any provision of this Agreement.
>
> This provision shall not apply to a "qualified domestic relations order" defined in Code Section 414(p) and those other domestic relations orders permitted to be so treated by the Administrator under the provisions of the Retirement Equity Act of 1984.

In re Leimbach, 99 B.R. 796, 798 (Bankr. S.D. Ohio 1989).

6. An "ERISA-qualified pension plan" or "qualified pension plan" is one that meets certain requirements set forth in the Internal Revenue Code. *See* I.R.C. § 401(a)(1988). Included among these requirements is the requirement that a plan must provide that "benefits provided under the plan may not be assigned or alienated." *See* I.R.C. § 401(a)(13)(1988); *see also supra* note 5. Other qualification requirements include minimum vesting standards, minimum distribution requirements, and limits on the amount that can be contributed annually to a plan. *See* I.R.C. § 401(a)(1988). If the plan satisfies the requirements for qualification, the employer and employee are afforded favorable tax treatment. For instance, the employer can claim a tax deduction for its contributions, subject to certain limits. I.R.C. § 404 (1988). The plan's earnings are tax-exempt. I.R.C. § 501(a) (1988). Also, employees are not taxed until they actually receive funds from the pension plan. I.R.C. §§ 402(a), (e) (1988). These tax benefits reflect Congress's intent to provide uniform treatment of retirement benefits for employees upon retirement.

7. 112 S. Ct. at 2248. 11 U.S.C. § 541(c) states in pertinent part:

> (c)(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate . . . notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law—
>
> * * *
>
> (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.

11 U.S.C. § 541(c)(2) (1988).

8. ERISA §§ 2(b)-(c), 29 U.S.C. §§ 1001(b)-(c) (1988).

and delay creditors.[9] The Fourth Circuit Court of Appeals adopted this position in a footnote in its opinion in this case.[10] Is the Fourth Circuit right on this issue? Can a fraudulent transfer to an ERISA-qualified pension plan be avoided? Consider the following hypothetical.

II. THE HYPOTHETICAL

Attorney Tom Cheatham is a sole bankruptcy practitioner who has formed a professional corporation (hereinafter "P.C."). His P.C. has an ERISA-qualified pension plan which contains an anti-alienation clause. Mr. Cheatham is an employee of the corporation, is the plan administrator and serves as trustee of the plan. After Mr. Cheatham specialized his practice to exclusively represent single asset Chapter 11 debtors, he began to suffer severe financial difficulties. He let his malpractice insurance lapse and started advertising on television for personal injury cases. In his first three personal injury cases, Mr. Cheatham settled one of the cases for $1 million, resulting in a $300,000 fee. His other two cases were tried, and his negligence resulted in defense verdicts. Mr. Cheatham's unhappy clients sued him for a total of $10 million. Mr. Cheatham took the fee from his successful settlement and contributed the maximum amount allowed by law to his ERISA-qualified pension plan. Mr. Cheatham then filed for bankruptcy protection under Chapter 7. Relying on the *Patterson v. Shumate* case, Cheatham listed the contribution to his ERISA-qualified plan in his schedules but excluded it from property of the estate under 11 U.S.C. § 541(c)(2).[11] The trustee filed an adversary proceeding to recover the contributions made to the pension plan. Assuming that the trustee can prove the elements of a fraudulent transfer into the pension plan, can he recover the fraudulent transfer from the plan?[12]

III. THE FOURTH CIRCUIT FOOTNOTE

Creditors and trustees who argued against the result reached in *Patterson* sought to limit pension plan assets that would be excluded from the bankruptcy estate to those pension plans that would also qualify as state spendthrift trusts.[13] The ra-

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9. 60 U.S.L.W. 3743, 3744 (1992).

10. Shumate v. Patterson, 943 F.2d at 365; *see* discussion *infra* part III.

11. Since Mr. Cheatham's ERISA plan contains an anti-alienation provision, *Patterson v. Shumate* would permit him to exclude his pension interest from his bankruptcy estate under section 541(c)(2). *See* discussion *infra* part V.

12. This hypothetical is just one situation in which a fraudulent transfer to a pension plan could occur. The following activities may also raise a question as to whether a debtor is acting with fraudulent intent in anticipation of his bankruptcy filing. Suppose a debtor causes a self-employed retirement plan (which would not be excluded under *Patterson v. Shumate*) to be converted to a plan which covers employees as well as owners (which would be excluded under *Patterson v. Shumate*). What if a debtor rolls an IRA account (not subject to ERISA's anti-alienation provision) into a new retirement plan covered by ERISA's anti-alienation provision? What if a debtor converts an unfunded "top hat" plan (unqualified plan) into a funded plan or into a plan which covers employees (which brings the plan within the scope of *Patterson v. Shumate*)? *See* Paul Puchot, *What's Left to Recover From Employee Benefit Plans After* Patterson v. Shumate?, 8 NAB TALK 25, 27, No. 3 (National Association of Bankruptcy Trustees, 1992).

13. A spendthrift trust is "one which provides a fund for [the] benefit of another than [the] settlor, secures it against [the] beneficiary's own improvidence, and places it beyond his creditors' reach." BLACK'S LAW DICTIONARY 1400 (6th ed. 1990).

tionale for this position is that in situations where a debtor has control over his pension plan assets, the trustee or his creditors should be able to reach those assets to satisfy claims. This argument was rejected by the Fourth Circuit in *Shumate v. Patterson* and also by the Supreme Court in *Patterson v. Shumate.*[14] In reaching this result, both courts focused on the plain meaning of the language of Bankruptcy Code § 541(c)(2) in determining that "applicable nonbankruptcy law" includes ERISA as well as state spendthrift trust law.[15]

The Fourth Circuit, *in dicta,* addressed the concern voiced by creditors seeking recovery from a pension plan over which the debtor has control.[16] This footnote stated as follows:

> Creditors concerned that a non-alienation provision is ineffective because of a debtor's control over a pension plan, either before or after bankruptcy, are not without other means of protection. Under 11 U.S.C. § 548, a bankruptcy estate trustee can void a debtor's transfer of property that was made in the prior twelve months and was made with the intent to hinder, delay, or defraud creditors. In this way, creditors can block a debtor in Shumate's position from actually taking advantage of his control position and depleting the estate.[17]

This footnote is missing in the Supreme Court opinion affirming the Fourth Circuit. There is no mention of the fraudulent transfer question in the Supreme Court opinion. The Fourth Circuit apparently equated avoidance of the transfer under section 548 with recovery of the avoided transfer under section 550.[18] The assumption that a bankruptcy trustee can recover an avoided fraudulent transfer from an ERISA-qualified plan apparently influenced the Fourth Circuit in reaching its conclusion that excluding all ERISA-qualified plans from the bankruptcy estate would not unduly prejudice creditors. This assumption may not be well-founded. What role this concept may have played in the Supreme Court's opinion is unclear, but the issue of a debtor's control over a pension plan was argued before the court.[19] Addressing the issue of a debtor's control over a pension plan, debtor's

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14. *See* Patterson v. Shumate, 112 S. Ct. at 2242.

15. *See supra* note 7 for the text of section 541(c)(2). In order to reach the result that limited the exclusion of pension plan assets to those held in a spendthrift trust, courts had to interpret the phrase "applicable nonbankruptcy law" as it appears in 11 U.S.C. § 541(c)(2) to mean "state spendthrift trust law." Many courts, including the Fifth, Eighth, Ninth and Eleventh Circuits, had reached this result, relying primarily on legislative history. *See supra* note 4. Justice Blackmun had harsh words for these courts in footnote 4 to the *Patterson* decision:

> Those Courts of Appeals that have limited "applicable nonbankruptcy law" to state spendthrift trust law by ignoring the plain language of § 541(c)(2) and relying on isolated excerpts from the legislative history thus have *misconceived the appropriate analytical task. See, e.g.*, Daniel v. Security Pacific Nat. Bank (*In re* Daniel), 771 F.2d at 1359-1360; Lichstrahl v. Bankers Trust (*In re* Lichstrahl), 750 F.2d at 1490; Samore v. Graham (*In re* Graham), 726 F.2d at 1271-1272; Goff v. Taylor (*In re* Goff), 706 F.2d at 581-582. (emphasis added).

112 S. Ct. at 2248 n.4.

16. *See* Shumate v. Patterson, 943 F.2d at 365.

17. 943 F.2d at 365 n.4.

18. *See* discussion *infra* parts IV and V.

19. 60 U.S.L.W. at 3744.

counsel contended that ERISA had "adequate safeguards."[20] According to United States Law Week:

> ERISA limits the amount a participant can contribute, the development of short-term plans, and the types of employees who can be covered, [debtor's counsel] pointed out. *Further, the attorney observed, Bankruptcy Code Section 548 allows a trustee to avoid a fraudulent conveyance by a debtor with control over a pension plan.*[21]

Neither the debtor in *Patterson* nor the Fourth Circuit explained exactly how section 548 could be used to *recover* a fraudulent conveyance by a debtor with control over the pension plan. An analysis of *avoidance* of fraudulent transfers under sections 544 and 548 and *recovery* of fraudulent transfers under section 550 is necessary to test their assumption.

IV. TRUSTEE'S REMEDIES TO RECOVER FRAUDULENT TRANSFERS

11 U.S.C. §§ 548 and 544 give a bankruptcy trustee the right to avoid fraudulent transfers. The operative language of each section is as follows.

> 11 U.S.C. § 548(a):
> The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily—
> (1) made such transfer or incurred such obligation with actual intent to hinder, delay or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted . . . .[22]

> 11 U.S.C. § 544(b) incorporates state fraudulent transfer remedies:
> The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.[23]

If a trustee is successful under either section 544 or section 548 in avoiding a transfer, the trustee must then resort to section 550 to recover the transfer from the transferee. In Mr. Cheatham's case, the transferee is his ERISA-qualified plan. 11 U.S.C. § 550(a) states in pertinent part as follows:

> Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544 . . . [or] 548, . . . of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—

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20. *Id.*
21. *Id.* (Emphasis added).
22. 11 U.S.C. § 548(a) (1991).
23. 11 U.S.C. § 544(b) (1991).

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made . . . .[24]

Under the hypothetical, the transfer to be avoided is the transfer to the pension plan. Under section 550 the property transferred or the value of such property could be recovered from the initial transferee of the transfer (the pension plan) or from the entity for whose benefit the transfer was made (Cheatham). Since Cheatham has filed Chapter 7 and has no other assets, we will focus on whether section 550 authorizes the bankruptcy trustee to recover from a pension plan notwithstanding the anti-alienation provision in Cheatham's ERISA-qualified plan. We do not consider whether Cheatham's actions have affected ERISA qualification of the plan.

V. Section 550 Versus ERISA's Anti-Alienation Provision

Even though *Patterson* did not involve a fraudulent debtor, a reading of the *Patterson* opinion, together with the earlier Supreme Court case *Guidry v. Sheet Metal Workers National Pension Fund*,[25] reveals some clues as to how the Supreme Court might resolve the apparent conflict between section 550 and ERISA's anti-alienation provision.

A. *The Scope of Patterson*

In *Patterson,* the debtor was the chairman of the board of directors, president and majority shareholder of Coleman Furniture Company.[26] Shumate was a participant in the company pension plan, which satisfied all requirements under ERISA and qualified for favorable tax treatment under the Internal Revenue Code.[27] In particular, the pension plan contained the anti-alienation provision required for qualification under ERISA.[28]

When Coleman Furniture filed for bankruptcy, the trustee received approval to terminate and liquidate the company's pension plan.[29] All of the participants received their benefits from the trustee, with the exception of Shumate.[30] Shumate himself had filed for bankruptcy, and his bankruptcy trustee, Patterson, sought to recover Shumate's interest in the pension plan for Shumate's bankruptcy estate.[31] Shumate moved to compel the trustee to pay the plan benefits directly to him.[32]

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24. 11 U.S.C. § 550(a) (1991). Section 550 also provides for the recovery of transfers avoided under several other provisions of the Bankruptcy Code, including 11 U.S.C. § 547 providing for the avoidance of preferences. Would a preferential transfer to an ERISA-qualified plan be recoverable under § 550? *See, e.g., In re* Ottawa Cartage, Inc., 55 B.R. 371 (Bankr. N.D. Ill. E.D. 1985).

25. 493 U.S. 365 (1990).

26. Creasy v. Coleman Furniture Corp., 83 B.R. 404, 405 (W.D. Va. 1988).

27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.*

32. *Id.*

The United States District Court for the Western District of Virginia rejected Shumate's argument that the pension plan's anti-alienation provision was an "applicable nonbankruptcy law" transfer restriction and thus could be excluded under section 541(c)(2).[33] The district court ruled that section 541(c)(2)'s reference to "nonbankruptcy law" covered only state law, not federal laws like ERISA.[34] The Court of Appeals for the Fourth Circuit reversed, holding that the debtor's interest in an ERISA-qualified plan should be excluded from his estate under section 541(c)(2) since the plan contained an ERISA-qualified anti-alienation provision.[35]

The Supreme Court, in holding for the exclusion of the pension plan, relied on the plain meaning of the Bankruptcy Code and ERISA.[36] In the Court's view, section 541(c)(2) clearly entitles a debtor to exclude from his estate any interest in a trust or plan that contains a restriction on transfer enforceable under "any relevant nonbankruptcy law."[37] The Court went on to state that there is nothing in section 541 suggesting that the phrase "applicable nonbankruptcy law" refers only to *state* law.[38] The Court found that the plan contained an anti-alienation provision which complied with the requirements of ERISA and the Internal Revenue Code concerning anti-alienation.[39] Furthermore, the Court found that the anti-alienation provision is "enforceable," as required by section 541(c)(2).[40] Under ERISA, plan fiduciaries or trustees are required to perform their duties in accordance with the plan, and a civil action may be filed to enjoin any act that violates ERISA or the plan.[41] The Court concluded that the anti-alienation provision contained in the plan constituted an enforceable transfer restriction under section 541(c)(2)'s exclusion of property.[42]

An important policy underlying the Court's decision in *Patterson* was the uniform treatment of pension assets, without regard to the beneficiary's bankruptcy status. Noting its earlier decision in *Guidry,* the Court stated,

> [w]e previously have declined to recognize any exceptions to ERISA's anti-alienation provision *outside* the bankruptcy context . . . . Declining to recognize any exceptions to that provision *within* the bankruptcy context minimizes the possibility that creditors will engage in strategic manipulation of the bankruptcy laws in order to gain access to otherwise inaccessible funds.[43]

33. *Id.* at 406.
34. *Id.*
35. 943 F.2d at 365.
36. 112 S. Ct. at 2246; *see supra* note 7 for the text of section 541(c)(2).
37. 112 S. Ct. at 2246.
38. *Id.*
39. *Id.* at 2247.
40. *Id.*
41. *Id.*
42. *Id.* at 2248.
43. *Id.* at 2250.

In addition, the Court stated that its decision would give full effect to ERISA's goal of protecting pension assets.[44]

The *Patterson* opinion focused on the anti-alienation provision required for ERISA qualification.[45] The scope of the decision is thus limited to pension plans that are subject to ERISA's anti-alienation provision. The following types of plans are ordinarily not subject to this provision:

1) Individual retirement accounts and individual retirement annuities ("IRAs");
2) Self-employed Retirement Plans ("Keoghs");
3) "Top Hat" Plans -A top hat plan is a retirement plan that provides unfunded benefits for a select group of employees;
4) Government and church plans;
5) Unfunded Excess Benefit Plans -An unfunded excess benefit plan provides retirement benefits for a limited group of employees;
6) Public School Retirement Annuities;
7) Severance Benefits.[46]

The Court's decision appears to make the anti-alienation provision the determinative factor in excluding a plan from the bankruptcy estate, but the Court referred to "ERISA-qualified plans." The Court did not explain how qualification is relevant to exclusion under section 541(c)(2), nor did it define the term "ERISA qualified." In using this term, the *Patterson* Court could have meant any one of the following: (1) a plan subject to ERISA that contains the anti-alienation clause required under section 206(d) of ERISA, (2) a plan subject to ERISA, or (3) a plan that is subject to ERISA and is qualified under section 401(a) of the Internal Revenue Code.[47] *Patterson* did not address the issue of whether an ERISA plan that contains the anti-alienation provision but does not meet the requirements for qualification would be excluded from the bankruptcy estate. For example, if a debtor's contributions to a plan exceed the limitations set forth in section 415 of the Internal Revenue Code (one of the requirements for qualification), but the plan contains the anti-alienation provision as required under *Patterson,* could the plan be excluded from the bankruptcy estate? Could a bankruptcy trustee argue that a debtor's pension plan should be included in the bankruptcy estate because it is not a qualified plan? The *Patterson* case was not clear on this point.[48] To the extent that a pension plan does not meet all of the requirements for qualification, an issue

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44. *Id.*

45. *See* Patterson v. Shumate, 112 S. Ct. 2242 (1992). *See also supra* note 5 and accompanying text.

46. *See* Puchot, *supra* note 12, at 26. While these types of pension plans are not excluded from the bankruptcy estate, they may be exempt under 11 U.S.C. § 522(d)(10)(E) or under state law exemptions.

47. J. Gordon Christy & Sabrina Skeldon, *Shumate and Pension Benefits in Bankruptcy* 2 J. BANKR. L. & PRAC. 719 (Nov.-Dec., 1992).

48. In a case decided before *Patterson,* the Tenth Circuit held that qualified ERISA plans are not property of the bankruptcy estate. *In re* Harline, 950 F.2d 669 (10th Cir. 1991). The court was not able to make a determination as to whether the plan was "qualified" under ERISA, and therefore remanded the case for findings on that issue. The court did state, however, that if the plan was not qualified at the time of the bankruptcy, then it would not be protected. *Id.* at 676.

might arise as to whether the bankruptcy trustee has standing to challenge the plan's qualification in order to reach the plan assets.[49]

B. *The* Guidry *Bright Line Test and the Call to Congress to Enumerate Equitable Exceptions*

Prior to the *Patterson* decision, the Supreme Court had adopted a strict interpretation of the anti-alienation provision in *Guidry v. Sheet Metal Workers National Pension Fund.*[50] The *Guidry* case expanded the Supreme Court's earlier analysis in *Mackey v. Lanier Collection Agency & Service, Inc.*,[51] in which the Court stated that the garnishment of pension plan benefits is prohibited by ERISA's anti-alienation provision.[52] In *Guidry*, a former union official and trustee of a union pension plan pled guilty to embezzling money from the union (not the plan).[53] Guidry violated section 501(c) of the Labor Management Reporting and Disclosure Act of 1959 (hereinafter "LMRDA").[54] Guidry filed suit against two of the three plans in which he had benefits when those plans declared that he had forfeited his right to benefits due to his criminal activity.[55] The union intervened, joined the third pension plan as a party, and stipulated with Guidry to the entry of a money judgment in favor of the union.[56]

The district court rejected the argument asserted by the pension funds that Guidry had forfeited his right to benefits, but held that a constructive trust should be imposed on Guidry's pension plan benefits in favor of the union until the union's judgment was satisfied.[57] The court of appeals affirmed, stating, "the district court's use of a constructive trust to redress breaches of ERISA was proper. The Supreme Court has consistently emphasized the inherent equitable jurisdiction of the federal district courts."[58]

The Supreme Court reversed the imposition of a constructive trust on the pension plan in favor of the union, holding that this violated ERISA's anti-alienation provision.[59] The Court analogized the constructive trust remedy to the prohibition of garnishments outlined in *Mackey* and concluded that there is "no meaningful distinction between a writ of garnishment and the constructive trust remedy im-

49. Under ERISA, only plan beneficiaries, the employer, the plan administrator, the I.R.S. and the Pension Benefit Guaranty Corporation have standing to challenge a plan's qualification. *See* I.R.C. § 7476(b) (1988); *see also In re* Komet, 104 B.R. 799 (Bankr. W.D. Tex. 1989). *See supra* note 6 for a discussion of qualification under ERISA.

50. 493 U.S. at 375-76.

51. 486 U.S. 825 (1988).

52. *Id.* at 836.

53. Guidry v. National Sheet Metal Workers' Nat'l Pension Fund, 641 F. Supp. 360, 361 (D. Colo. 1986).

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.* at 363.

58. Guidry v. Sheet Metal Workers Nat'l Pension Fund, 856 F.2d 1457, 1460 (10th Cir. 1988) (footnote omitted) (citations omitted), *rev'd*, 493 U.S. 365 (1990).

59. 493 U.S. 365, 375-76 (1990).

posed in this case."[60] The *Guidry* Court stated that the constructive trust remedy is prohibited by the anti-alienation provision unless an exception to the statutory ban is applicable.[61] The Court then refused to approve any generalized equitable exception to the prohibition on alienation of pension benefits.[62] The Court stated:

> Nor do we think it appropriate to approve any generalized equitable exception—either for employee malfeasance or for criminal misconduct—to ERISA's prohibition on the assignment or alienation of pension benefits. Section 206(d) [the anti-alienation provision] reflects a considered congressional policy choice, a decision to safeguard a stream of income for pensioners (and their dependents, who may be, and perhaps usually are, blameless), even if that decision prevents others from securing relief for the wrongs done them. If exceptions to this policy are to be made, it is for Congress to undertake that task.[63]

The *Guidry* Court called on Congress to identify equitable exceptions to the anti-alienation provision rather than create judicial exceptions:

> As a general matter, courts should be loath to announce equitable exceptions to legislative requirements or prohibitions that are unqualified by the statutory text. The creation of such exceptions, in our view, would be especially problematic in the context of an anti-garnishment provision. Such a provision acts, by definition, to hinder the collection of a lawful debt. A restriction on garnishment therefore can be defended *only* on the view that the effectuation of certain broad social policies sometimes takes precedence over the desire to do equity between particular parties. It makes little sense to adopt such a policy and then to refuse enforcement whenever enforcement appears inequitable. A court attempting to carve out an exception that would not swallow the rule would be forced to determine whether application of the rule in particular circumstances would be "especially" inequitable. The impracticability of defining such a standard reinforces our conclusion that the identification of any exception should be left to Congress.[64]

In rejecting the union's argument that the remedial provisions of the LMRDA supersede ERISA's anti-alienation provision pursuant to ERISA § 514(d), 29 U.S.C. § 1144(d) " 'nothing in this title shall be construed to alter, amend, modify, invalidate, impair or supersede any law of the United States . . . or any rule or regulation issued under such law' ",[65] the Court stated, "[w]ere we to accept respondents' position, ERISA's anti-alienation provision would be inapplicable whenever a judgment creditor relied on the remedial provisions of a federal statute . . . . [W]e decline to adopt so broad a reading of section 514(d)."[66]

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60. *Id.* at 372.

61. *Id.*

62. *Id.*

63. *Id.* at 376. *See,* for example, section 104(a) of the Retirement Equity Act of 1984, 98 Stat. 1433, 29 U.S.C. § 1056(d)(3) (1982 ed. Supp. V), where Congress mandated that the anti-alienation provision should not apply to a "qualified domestic relations order." *Id.* at 376 n.18.

64. *Id.* at 376-77.

65. 29 U.C.C. § 1144(d) (1988).

66. *Id.* at 375 (quoting 29 U.S.C. § 1144(d) (1982)) (footnote omitted).

The Supreme Court's analysis in *Guidry* suggests that the ERISA anti-alienation statute will prevail whenever it conflicts with a judgment creditor relying on a "remedial provision of a federal statute."[67] Is there any difference between the union in *Guidry* trying to recover money stolen by Guidry and a bankruptcy trustee pursuing a fraudulent transfer? Notwithstanding the clear language of the Supreme Court in the *Guidry* case, does the nature of the remedy of avoidance of a fraudulent transfer in and of itself allow for an equitable exception?[68]

VI. Is a Constructive Trust Really the Same as a Garnishment?

Though the Supreme Court in *Guidry* stated, "[w]e see no meaningful distinction between a writ of garnishment and the constructive trust remedy imposed in this case,"[69] the Court failed to reveal its analysis of these remedies. Differences in these remedies may hold the key to a judicial solution to the problem of a fraudulent debtor shielding assets in a pension plan.

Garnishment is a statutory collection remedy directed at a third party, the garnishee, who has property of the debtor or owes property to the debtor.[70] Garnishment is generally a remedy available to *all* judgment creditors.[71] The garnishment procedure is governed by statute and varies with local practice, but ordinarily garnishment involves the following procedural steps which are required by Mississippi's garnishment statute.[72] When a judgment creditor has an unsatisfied judgment, he can proceed against a debtor by filing an affidavit with the court to obtain the issuance of a writ of garnishment.[73] The court next issues a writ of garnishment that is served on the garnishee.[74] The most common examples of garnishees are the debtor's employer and the debtor's bank in which he has an account.[75] The writ of garnishment requires the garnishee to answer whether he has in his possession any property belonging to the debtor.[76] In Mississippi, upon service of the writ of garnishment, a lien is created on the debtor's property in the hands of a garnishee, in favor of the plaintiff.[77] In states with this type of statutory provision, the date of the service of the writ of garnishment is a critical date because it gives the plaintiff a lien on the property of the debtor in possession of the garnishee.[78] This is the

67. *Id.*

68. For an excellent discussion of judicially created implied exceptions to the ERISA anti-alienation clause leading up to and including *Guidry*, see Mary F. Radford, *Implied Exceptions to the ERISA Prohibitions Against the Forfeiture and Alienation of Retirement Plan Interests*, 1990 Utah L. Rev. 685 (1990).

69. 493 U.S. at 372.

70. *See* 6 Am. Jur. 2d *Attachment and Garnishment* §§ 2, 13 (1963 & Supp. 1992).

71. *See id.* § 61.

72. *See id.* §§ 332-56 (outlining the general requirements for garnishment); *see also* Miss. Code Ann. §§ 11-35-1 through 11-35-61 (1972 & Supp. 1992.)

73. *See, e.g.*, Miss. Code Ann. § 11-35-1 (1972 & Supp. 1992).

74. *See, e.g.*, Miss. Code Ann. § 11-35-9 (1972).

75. *See, e.g.*, Delta Fertilizer, Inc. v. Weaver, 547 So. 2d 800 (Miss. 1989).

76. *See, e.g.*, Miss. Code Ann. § 11-35-25 (Supp. 1992).

77. *See, e.g.*, Miss. Code Ann. § 11-35-23(1) (Supp. 1992). In Mississippi, "wages, salary [and] other compensation" are excluded from this rule. *Id.*

78. *See, e.g.*, Miss. Code Ann. § 11-35-23(1) (Supp. 1992).

effective date of the garnishment action.[79] A garnishment generally is binding on the garnished property only to the extent of the defendant's interest, and the garnishment lien continues as security for the plaintiff's judgment until the garnishment is dissolved, discharged or abandoned.[80]

A constructive trust, on the other hand, is an *equitable* remedy imposed by courts to prevent unjust enrichment.[81] There is no technical statutory procedure to follow. A constructive trust is remedial in nature, and can be used in a wide variety of situations to recover wrongfully-held property. It is often imposed in cases of fraud, where one party claims that the other party fraudulently holds property that equitably belongs to the first party.[82] The person holding title to the property in question is subject to an equitable duty to convey the property to the plaintiff.[83] The effect of the constructive trust is to take property from the defendant and restore it to the plaintiff.[84]

In order for a constructive trust to arise, there must be a *res* or identifiable property which can be identified as belonging to the defendant.[85] In other words, a constructive trust can be imposed only where the plaintiff's property is located or where the property can be traced into other property or funds of the defendant.[86] The principle of "tracing" is an important characteristic of constructive trusts.[87] In the case of embezzled money, for example, tracing allows the constructive trust to attach not only to the money embezzled but to any property into which the money may be traced.[88] However, a constructive trust cannot be imposed on a third per-

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79. *Id.*

80. *See* 6 AM. JUR. 2D *Attachment and Garnishment* § 457 (1963).

81. *See, e.g., In re* Seneca Oil Co., 906 F.2d 1445 (10th Cir. 1990) (constructive trust imposed where oil company overcharged customers for oil in violation of federal pricing regulations, resulting in unjust enrichment to the oil company and its creditors); Spinner v. Fulton, 777 F. Supp. 398 (M.D. Pa.), (Insured's parents were entitled to have constructive trust impressed on life insurance proceeds to which estranged husband held legal title by default.), *aff'd*, 947 F.2d 937 (3d Cir. 1991); L.P. Maun, M.D., Ltd. v. Salyapongse, 105 B.R. 464 (S.D. Ill. 1989) (constructive trust appropriate equitable remedy where former employee wrongfully acquired accounts receivable and it would be unjust to permit him to retain the funds). *See generally* 76 AM. JUR. 2D *Trusts* § 200 (1992) (discussing circumstances for imposing constructive trust).

82. *See, e.g.,* Matter of Carolin Paxson Advertising, Inc., 938 F.2d 595 (5th Cir. 1991) (Constructive trust may be imposed when one acquires property by fraudulent means.); Spinner v. Fulton, 777 F. Supp. 398 (M.D. Pa. 1991) (Constructive trust may be imposed when facts show fraud, duress, undue influence, mistake or breach of confidential relationship, resulting in unjust enrichment.), *aff'd*, 947 F.2d 937 (3d Cir. 1991); MDO Dev. Corp. v. Kelly, 726 F. Supp. 79 (S.D.N.Y. 1989) (constructive trust imposed on land and residence that were purchased and constructed with embezzled funds), *amend. denied*, 735 F. Supp. 591 (S.D.N.Y. 1990). *See generally* 76 AM. JUR. 2D *Trusts* § 201 (1992) (discussing circumstances for imposing constructive trust).

83. *See* RESTATEMENT OF THE LAW OF RESTITUTION § 160 (1988) ("To prevent . . . unjust enrichment an equitable duty to convey the property is imposed upon [the person holding title to the property.]").

84. *See id.* "In most cases where a constructive trust is imposed the result is to restore to the plaintiff property of which he has been unjustly deprived . . . ."

85. *See* RESTATEMENT OF THE LAW OF RESTITUTION § 160 (1988); *see also* 76 AM. JUR. 2D *Trusts* § 207 (1992).

86. *See* 76 AM. JUR. 2D *Trusts* § 207 (1992).

87. *See* DAN B. DOBBS, HANDBOOK ON THE LAW OF REMEDIES §§ 4.3, 5.16 (1973).

88. *Id.* If the defendant uses the embezzled money to buy land, the plaintiff may impress a constructive trust on the land so as to require the conveyance back to him. *Id. See, e.g.,* MDO Dev. Corp. v. Kelly, 726 F. Supp. at 79 (constructive trust imposed on land and residence that were purchased and constructed with embezzled funds).

son who is a bona fide purchaser for value and without notice of the circumstances surrounding the wrongful conduct.[89] If the property is transferred to a bona fide purchaser for value, the constructive trust is ordinarily cut off.[90]

A constructive trust can take effect at the time the wrongful act occurs.[91] Conceptually, there is uncertainty as to whether the constructive trust arises at the time of the fraud or wrongful act or whether it arises when it is imposed by the court, but then relates back to the time of the wrong.[92] Nevertheless, under either theory the *effective* date of the constructive trust is the date of the wrong.[93] Courts of equity have the power to undo a wrong from its inception.[94] In the case of a fraudulent transfer, a constructive trust is an appropriate remedy that may be imposed as a matter of state law,[95] and therefore the constructive trust remedy is available to a bankruptcy trustee under 11 U.S.C. § 544.[96]

In contrast to a constructive trust, a garnishment action does not relate back to an earlier date. A garnishment takes effect only after a writ of garnishment has been entered.[97] The possibility that a constructive trust can arise from the date of a fraudulent transfer may be the "meaningful distinction" between constructive trust and a garnishment that would allow an equitable exception to the ERISA anti-alienation rule if a transfer to a plan is avoided as fraudulent. The trust follows the debtor's identifiable property. Theoretically, the debtor's pension assets, if fraudulently transferred, would be subject to the trust. If the debtor conveys assets to his pension plan that he holds in an express trust for the benefit of another, would the holding in *Guidry* require the holding that the beneficiaries of the trust cannot recover their benefits?[98]

VII. A LEGISLATIVE PROPOSAL

If we take the Supreme Court at its word, it may be necessary for Congress to create an exception to the anti-alienation rule to provide for the recovery of fraudu-

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89. *See* 76 AM. JUR. 2D *Trusts* § 207 (1992).

90. *See* 76 AM. JUR. 2D *Trusts* § 311 (1992).

91. *See In re* Seneca Oil Co., 906 F.2d at 1445; Meyer v. Kneip, 457 N.W.2d 463 (S.D. 1990); Pioneer Annuity Life Ins. Co. v. Nat'l Equity Life Ins. Co., 765 P.2d 550 (Ariz. Ct. App. 1988).

92. 906 F.2d at 1453 ("There is some dispute conceptually whether a constructive trust arises at the time of the wrongful act or whether it arises only at the time it is so declared by the court, but then applied retroactively to the time of the wrongful act.").

93. *Id.* "[U]nder either theory, the *effective* date of the constructive trust is the date the wrongful act occurred."

94. *See id.*; *see also* Voest-Alpine Trading U.S.A. Corp. v. Vantage Steel Corp., 919 F.2d 206, 224 (3d Cir. 1990).

95. *See In re* Sergio, Inc., 16 B.R. 898 (Bankr. D. Haw. 1981); Voest-Alpine Trading U.S.A. Corp. v. Vantage Steel Corp., 919 F.2d at 206.

96. *See supra* part IV for the text of § 544(b).

97. *See, e.g.*, MISS. CODE ANN. § 11-35-23 (Supp. 1992).

98. Recall that in *Guidry*, the lower court imposed the constructive trust as a remedy, notwithstanding the fact that the money embezzled from the Union was not traced to the pension funds. *See* 641 F. Supp. at 360.

lent transfers from pension plans.[99] One such proposal is as follows. 29 U.S.C. § 1056 could be amended by adding an exception to the anti-alienation provision.

29 U.S.C. § 1056(d)(1) currently states:

> Each pension plan shall provide that benefits provided under the plan may not be assigned or alienated.[100]

The proposed Section 1056(d)(4) reads:

> (A) Paragraph (1) of this section shall not apply to prevent the recovery of a fraudulent transfer from a participant's plan pursuant to –
> (i) 1 U.S.C. § 548;[101]
> (ii) 11 U.S.C. § 544(b) and applicable state law;
> (iii) applicable state law; or
> (iv) 11 U.S.C. § 550.
> Each pension plan shall provide that funds deposited into the plan in violation of (i), (ii) or (iii) of this subparagraph may be recovered in accordance with applicable fraudulent transfer law and state law.
> (B) Paragraph (1) of this section shall not apply to prevent the enforcement of a constructive trust on a participant's plan under state law in conjunction with the recovery of a fraudulent transfer into the plan.
> For purposes of this paragraph –
> (i) the term "fraudulent transfer" has the meaning given such term under the relevant provision in (i), (ii) or (iii) of subparagraph (A).
> (ii) the term "constructive trust" has the meaning given such term under applicable state law.

Similarly, the Internal Revenue Code's anti-alienation provision could be amended. The pertinent provision in the Internal Revenue Code concerning anti-alienation states:

> "A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part provides that benefits provided under the plan may not be assigned or alienated."[102]

This section should be amended to include a new section 401(a)(13)(C):

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99. The following legislative amendments are proposed solutions to problems caused by abuses of the pension system by fraudulent debtors with actual control over their ERISA-qualified pension plans. A more exhaustive review of the interworkings of ERISA and the Bankruptcy Code if these changes were made will be left for another day.

100. 29 U.S.C. § 1056(d)(1) (1976).

101. Section 548(a)(1) empowers the trustee to avoid transfers made with *actual* (subjective) intent to hinder, delay or defraud creditors. 11 U.S.C. § 548(a)(1) (1988). *See supra* part IV for the text of § 548(a)(1). Section 548 also covers *constructively* fraudulent transfers. Section 548(a)(2) may be used to avoid transfers made for less than a reasonably equivalent value provided the debtor was insolvent or became insolvent, was engaged in a business with an unreasonably small capital, or intended to incur debts that would be beyond his ability to repay. 11 U.S.C. § 548(a)(2) (1988). For purposes of this legislation, should actual fraud be distinguished from constructive fraud?

102. I.R.C. § 401(a)(13)(A).

Subparagraph (A) shall not apply to prevent the recovery of a fraudulent transfer from a participant's plan pursuant to—
(i) 11 U.S.C. § 548;
(ii) 11 U.S.C. § 544(b) and applicable state law;
(iii) applicable state law; or
(iv) 11 U.S.C. § 550.

In order to preclude a debtor from taking advantage of an anti-alienation clause by shielding his pension plan from the bankruptcy trustee while he is violating other provisions of ERISA, the anti-alienation clause could further be amended to state:

29 U.S.C. § 1056(d)(5):

Paragraph (1) of this section [the anti-alienation provision] shall not apply to prevent a bankruptcy trustee from reaching a participant's plan for inclusion in the participant's bankruptcy estate pursuant to 11 U.S.C. § 541 if—
(i) the participant engages in a prohibited transaction under 26 U.S.C. § 4975(c), or
(ii) the participant's plan does not meet any one of the requirements for qualification set forth in I.R.C. § 401(a).

The Internal Revenue Code's anti-alienation should also be amended to include a similar provision.

Finally, in order to provide a bankruptcy trustee with standing to challenge a plan's qualification, the Internal Revenue Code provision authorizing a proceeding on qualification could be amended. Section 7476(b)(1) of the Internal Revenue Code, declaratory judgments relating to qualification of certain retirement plans, provides:

A pleading may be filed under this section only by a petitioner who is the employer, the plan administrator, an employee who has qualified under regulations prescribed by the Secretary as an interested party for purposes of pursuing administrative remedies within the Internal Revenue Service, or the Pension Benefit Guaranty Corporation.[103]

The following provision could be included at the end of section 7476(b)(1) of the Internal Revenue Code:

A pleading may also be filed under this section by the trustee in bankruptcy of a participant who has filed for bankruptcy under any chapter of the Bankruptcy Code, for purposes of recovering a transfer in violation of § 548 of the Bankruptcy Code or § 544(b) of the Bankruptcy Code and applicable state law.

VIII. CONCLUSION

As it now stands, it appears that there are no equitable exceptions to ERISA's anti-alienation provision, unless the Supreme Court will modify its analysis in *Guidry*. However, this analysis, which assumes no distinction between a garnish-

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103. I.R.C. § 7476(b)(1).

ment and a constructive trust, seems flawed. If a creditor avoids a fraudulent transfer made to a pension plan and obtains a judicial determination that the transfer is avoided *ab initio,* the Court may recognize an exception to the ERISA anti-alienation provision. Otherwise, congressional action is needed to prevent the potential abuses of a fraudulent debtor with control over his pension plan.