UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
WESTERN DIVISION

In Re:	)	Case No. 03-31666
	)	
Seanene Hoyles,	)	Chapter 7
	)	
	)	
Debtor	)	JUDGE MARY ANN WHIPPLE

MEMORANDUM OF DECISION
REGARDING TRUSTEE'S OBJECTION TO EXEMPTION

Debtor Seanene Hoyles claims an exemption from property of her bankruptcy estate for payments due to her under a separation agreement and state court judgment entry arising in the pre-petition dissolution of her marriage. The payments relate to her ex-husband's entitlement to Voluntary Separation Incentive payments from the United States military. The Trustee objects to her claimed exemption. For the reasons that follow, the court grants the Trustee's objection.

Background

The Court of Common Pleas of Marion County, Ohio, dissolved Ms. Hoyles's marriage to Ricky Hoyles on November 1, 2000. Debtor's Hearing Ex. A. In 1995, her ex-husband left active service in the Air Force after being offered the Voluntary Separation Incentive program ("VSI"). Congress enacted the VSI in 1991 to expedite the downsizing of the United States military. *Mackey v. Mackey,* 95 Ohio St. 3d 396, 397-98 (2002); 10 U.S.C. § 1175. The statute authorizes a program for separation incentive payments based on a member of the armed service's years of service and salary at separation. The payments are made through a fund established on the books of the United States Treasury known as the Voluntary Separation Incentive Fund ("Fund"), to be administered by the Secretary of the Treasury. 10 U.S.C. § 1175(h). The Fund "shall be used for the accumulation of funds in order to finance on an actuarially sound basis the liabilities of the Department of Defense under this section." 10 U.S.C. § 1175(h)(1). The statute provides that the "member's right to incentive payments shall not be transferable, except that the member

may designate beneficiaries to receive the payments in the event of the member's death." 10 U.S.C. § 1175(f).

Under the VSI, Mr. Hoyles receives, based on his salary at separation and length of service, $7,000 per year for twenty-eight years, with payments beginning in 1995. The Judgment Entry dissolving the marriage, which incorporated the Separation Agreement between Ms. Hoyles and her ex-husband, provides that Ms. Hoyles "shall receive from Husband's voluntary separation incentive payouts from the Air Force the sum of $1,750.00, with the first payment due on or about June 1, 2001 and approximately the same date for six consecutive years thereafter." Debtor's Hearing Ex. A, ¶ 9. Ms. Hoyles testified that she receives her interest in the VSI payments directly from her ex-husband. The Separation Agreement also provides that "[n]either party has any pension or retirement programs from their place of employments" and "[n]either party shall pay unto the other any periodic or lump sum spousal support." *Id.* at ¶¶ 10, 11.

Ms. Hoyles filed for relief under Chapter 7 of the Bankruptcy Code on March 11, 2003, disclosing the VSI payment that was to be made in June, 2003, and claiming it as exempt. The Trustee timely objected to the exemption. Although in Schedule C of her petition Ms. Hoyles claims that her interest in the VSI payments is exempt under Ohio Rev. Code § 2329.66(A)(11) as spousal support, at the hearing on the objection, she also argued that the VSI payments are akin to retirement pay and, as such, are exempt under § 2329.66(A)(10). The Trustee counters Debtor's arguments by contending that Ms. Hoyles' interest in the VSI payments are part of the division of marital property rather than spousal support and that the payments represent severance pay rather than retirement pay.

Law and Analysis

The bankruptcy estate generally consists of "all legal or equitable interests of the debtor in property as of the commencement of the case." 11 U.S.C. § 541(a)(1). Congress permits individual debtors, like Ms. Hoyles, to exempt certain property from the bankruptcy estate to facilitate their fresh start after obtaining bankruptcy relief. 11 U.S.C. § 522(b). Section 522(d) of the Bankruptcy Code, 11 U.S.C., sets out the federal exemptions. Alternatively, Congress authorized individual states to opt out of the federal exemptions, which then limits debtors to claiming the exemptions available in their state of domicile and

under general nonbankruptcy federal law. 11 U.S.C. § 522(b)(1). Ms. Hoyles is domiciled in Ohio, which is an opt out state. Ohio Rev. Code § 2329.662. Accordingly, Ms. Hoyles is limited to claiming exemptions available under Ohio law. As to her interest in the VSI payments, Ms. Hoyles claims they are exempt under either Ohio Rev. Code § 2329.66(A)(11) or (A)(10).

Under Fed. R. Bankr. P. 4003(c), the Chapter 7 Trustee bears the burden of proving that the exemption is not properly claimed. If state courts have interpreted an exemption statute, that interpretation guides federal courts in construing the statute. *See Doethlaff v. Penn. Mut. Life Ins. Co.*, 117 F.2d 582, 584 (6th Cir. 1941), *cert. denied*, 313 U.S. 579 (1941). If state courts have not interpreted the provision, a bankruptcy court must do so. *Doethlaff*, 117 F.2d at 584. Exemption statutes are generally to be liberally construed in the debtor's favor. *Id*. A liberal construction does not, however, give the court license to enlarge the statute or strain its meaning. *Wicheff v. Baumgart (In re Wicheff)*, 215 B.R. 839, 843 (B.A.P. 6th Cir. 1998)

Payments as Spousal Support Under Ohio Rev. Code § 2329.66(A)(11)

Debtor first contends that her interest in the VSI payments constitutes spousal support. As such, she contends that they are exempt under § 2329.66(A)(11) which "exempts a person's right to receive spousal support. . . ." In determining whether an obligation under a divorce decree or separation agreement constitutes support, as opposed to a division of marital property, the Sixth Circuit has counseled deference to state court decrees and has explained that the bankruptcy court should look to traditional state law indicia that are consistent with a support obligation. These state law indicia include: (1) how the obligation is labeled, (2) whether the payment is direct to the spouse or to third parties, and (3) whether the payments are contingent upon such events as death, remarriage, or eligibility for Social Security benefits. *Sorah v. Sorah (In re Sorah)*, 163 F.3d 397, 401 (6th Cir. 1998).

Applying this analysis, the Trustee has met his burden of demonstrating that Debtor is not entitled

to exempt the payments from Mr. Hoyles under § 2329.66(A)(11) for spousal support. The separation agreement does not designate Mr. Hoyles' obligation to pay Debtor a portion of the VSI payments as support. Moreover, the agreement, which the state court incorporated into its judgment entry, expressly provides that "[n]either party shall pay unto the other any periodic or lump sum spousal support." Debtor's Hearing Ex. A, ¶ 11. Although payments are made directly by Mr. Hoyles to Debtor, the agreement does not provide for termination of the obligation upon Debtor's death, remarriage, or eligibility for Social Security.

Ms. Hoyles also testified about her income and Mr. Hoyles' income. Ms. Hoyles is employed outside the home, and was at the time of the dissolution. She does not have children or other dependents. Now, she works two jobs. According to her testimony, Mr. Hoyles' income was greater than hers at the time of the divorce. However, it appears that her income then (and now) is sufficient to support herself with a reasonable standard of living, which mitigates against the payments as support or maintenance for her. And the difference between her income and Mr. Hoyles' income was not so great as to otherwise suggest that the payments would be in the nature of support or maintenance of a particular pre-dissolution lifestyle.

With the exception of payments being made directly to Debtor, the traditional indicia of support do not exist. Mr. Hoyles' right to receive the VSI payments was acquired during his marriage to Debtor and, as such, is divisible "marital property." Ohio Rev. Code § 3105.171(A)(3)(a) (defining "marital property" to include "[a]ll interest that either or both of the spouses currently has in any real or personal property, including, but not limited to, the retirement benefits of the spouses, and that was acquired by either or both of the spouses during the marriage."); *Mackey*, 95 Ohio St. 3d at 399. The court finds that Debtor's interest in the payments from Mr. Hoyles, on account of his participation in the VSI and as provided in the Separation Agreement, simply represents a division of marital property. As such, the payments do not constitute exemptible support or maintenance within the scope of Ohio Rev. Code § 2329.66(A)(11).

Payments as Exempt Retirement Benefits Under Ohio Rev. Code § 2329.66(A)(10)

Debtor alternatively contends that her interest in the VSI payments constitutes retirement benefits and, as such, is exempt under Ohio Rev. Code § 2329.66(A)(10). That section provides an exemption

for a "person's right to receive a payment under any pension, annuity, or similar plan or contract . . . on account of illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the person and any of the person's dependants. . . ." Ohio Rev. Code § 2329.66(A)(10)(b).[1] Applying this exemption to the payments to Ms. Hoyles raises two issues. First, are the payments retirement or pension benefits within the scope of the exemption statute? Second, is an interest obtained derivatively through a divorce decree instead of through the debtor's own service or employment within the scope of the exemption statute?

Although the Trustee argues that the VSI payments from the Air Force are more accurately characterized as severance pay, there is considerable support for Debtor's contention that the benefits qualify as retirement benefits. *See Mackey* , 95 Ohio St.3d at 399-400(and cases cited therein). In *Mackey*, the issue presented to the Ohio Supreme Court was whether VSI payments qualified as retirement benefits and, therefore, were divisible as marital property under Ohio law. *Id.* at 399. In finding that they did so qualify, the court explained that the VSI provided an annuity based on rate of pay and years of service, like retirement pay, and that if the service member thereafter reenlists and becomes eligible for retirement, the VSI payments must be recouped from the retirement benefit. *Id.* at 399-400. In independently analyzing the federal statute, this court tends to agree with the Trustee. Section 1175 of Title 10 of the United States Code distinguishes retirement pay per se from payments made under the VSI. And the Ohio Supreme Court seems incorrect in its statements that the payments come from an annuity, given the establishment and statutory description of the Fund. *Cf*. 10 U.S.C. § 1175(h). But more critical for the Ohio Supreme Court than the source of the payments were the length of service-based component of the payments, which pointed to the aptness of their characterization as retirement benefits. And as this characterization was being made by the Ohio Supreme Court for purposes of applying Ohio law, which is also at issue in this case, this court will defer to the Ohio Supreme Court's characterization of the VSI payments as retirement benefits for purposes of applying the Ohio exemption.

Nevertheless, an exemption under § 2329.66(A)(10)(b) applies only to a *"person's right to*

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[1] Subsections (A)(10)(a), (c) and (d) of Ohio Rev. Code § 2329.66 are not even arguably applicable to the payments in issue.

receive a payment under any pension, annuity, or similar plan or contract... *on account of* illness, disability, death, age, or length of service, to the extent reasonably necessary for the support of the person and any of his dependents." Here, the payments to Ms. Hoyles do not come directly from the Voluntary Incentive Separation Fund established by Congress, and are not being made on account of her own pay or length of service or separation from the military. Instead, they come directly from Mr. Hoyles, after he receives his payments, under the Separation Agreement and the state court

dissolution decree. Moreover, the federal statute expressly provides that Mr. Hoyles is not permitted to transfer his "right to receive payments." *Cf.* 10 U.S.C. § 1408, Uniformed Services Former Spouses' Protection Act (as an exception to the prohibition on alienation of retirement pay, statute provides for method of direct payment of military disposable retired pay, as defined, to former spouse, who obtains a direct interest in payments through state court orders analogous to Qualified Domestic Relations Orders in the context of ERISA); *In re Satterwhite,* 271 B.R. 378 (Bankr. W.D. Mo. 2002). Unlike Mr. Hoyles, Ms. Hoyles does not herself have any separate interest in the Fund and did not acquire one in the dissolution.

There are no Ohio cases on the issue of whether derivative acquisition of the right to payments constitute payments "under" the plan or contract within the meaning of the exemption statute. Another bankruptcy court has construed this issue under Section 2329.66(A)(10)(b) in the context of payments due from a spouse's profit sharing pension plan. In *In re Mabrey,* 51 B.R. 383 (Bankr. S.D. Ohio 1985), debtor was awarded in a divorce decree an interest in her ex-spouse's profit sharing plan through his employment. The bankruptcy court sustained the Chapter 7 trustee's objection to the exemption, holding that the exemption is personal to the person whose employment and length of service gave rise to the interest.

Another bankruptcy court, in construing Illinois exemption law, distinguished and criticized *Mabrey*. *In re Lummer,* 219 B.R. 510, 512 (Bankr. S. D. Ill. 1998). In *Lummer,* the debtor was awarded a share of her husband's military retirement pay through a divorce decree. The award was made pursuant to the Uniformed Services Former Spouses' Protection Act, such that the debtor spouse received payments directly from the federal government. Construing the applicable Illinois exemption statute, which is analogous

to but worded somewhat differently than Ohio Rev. Code § 2329.66(A)(10)(b), the bankruptcy court held that the debtor's interest was exempt because the "statute is drawn broadly and is devoid of any suggestion that its scope excludes debtors who have come into their pension rights derivatively." As correctly noted by the Illinois bankruptcy court in *Lummer*, *Mabrey* was decided before the Supreme Court decision in *Patterson v. Shumate*, 504 U.S. 753 (1992), which held that ERISA constitutes applicable nonbankruptcy law for purposes of exclusion of certain trust interests from bankruptcy estates under 11 U.S.C, § 541(c)(2). This court agrees that *Mabrey* would be decided differently today, because the exemption issue would never be addressed in the first place. As to ERISA-qualified retirement plan interests, which *Mabrey* appeared to involve, *Patterson* now excludes them from the estate before even reaching the exemption issue. However, the holding that the rights established by Ohio Rev. Code § 2329.66(A)(10)(b) are not applicable to debtors who receive their retirement benefits only derivatively through a divorce decree is still valid to the extent that the property interest in issue is not derived from an ERISA-qualified plan and trust. This court finds that *Mabrey* is still persuasive authority on that point, and agrees with its reasoning. On the other hand, *Lummer* is distinguishable, as the property interest in issue involved payments directly from the federal government to the debtor spouse after the divorce, not from the debtor's ex- husband as is occurring in this case.

In opposition to this court's interpretation of Ohio Rev. Code § 2329.66(A)(10), Ms. Hoyles might point to cases involving debtor interests in former spouses' ERISA-qualified pension plans. Recent case law in that context holds that ERISA-qualified plan interests derived through a divorce decree and not through a debtor's own employment are nevertheless excluded as property of the debtor's bankruptcy estate under 11 U.S.C. § 541(c)(2) and the holding of *Patterson v. Shumate*. *See Nelson v. Ramette (In re Nelson)*, 322 F.3d 541, 544 (8th Cir. 2003) (citing 29 U.S.C. § 1056(d)(3)(J) and (K)); *In re Hthiy*, 283 B.R. 447 (Bankr. E.D. Mich. 2002). *Contra In re Hageman*, 260 B.R. 852 (Bankr. S.D. Ohio 2001). Where the property interest in issue is in an ERISA-qualified plan and trust, the plain language of ERISA provides that an alternate payee under a qualified domestic relations order ("QDRO") issued by a state domestic relations court is considered a beneficiary of the plan. *See Nelson*, 322 F.3d at 544 (citing 29

U.S.C. § 1056(d)(3)(J) and (K)). Thus, a spouse's right to receive benefits paid by an ERISA-qualified pension plan arises as a beneficiary under the plan itself. *Cf. Satterwhite*, 271 B.R. at 380 (debtor ex-spouse's interest in military retirement payments is excluded from property of the estate by 11 U.S.C. § 541(c)(2)); *In re Seddon*, 255 B.R. 815, 817 (Bankr. W.D. N.C. 2000)(debtor's interest in her former spouse's federal civil service retirement system award is a proprietary interest in the retirement plan itself, not merely a derivative right to receive payments from the plan, excluded by 11 U.S.C. § 541(c)(2)).[2]

In contrast, notwithstanding the Ohio Supreme Court's characterization of VSI payments as retirement pay, Ms. Hoyles' right to receive payments from Mr. Hoyles on account of his interest in the VSI arises solely under the state court's judgment adopting the terms of the Separation Agreement. Unlike benefits under an ERISA-qualified plan subject to a QDRO, Debtor's right does not arise "under any

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[2] Debtor has not argued that the payments should be excluded from property of the estate under 11 U.S.C. § 5451(c)(2), an argument that would find some support in cases such as *Satterwhite* and *Seddon*. While *Satterwhite* and *Seddon* are distinguishable in that the debtors in both cases had a direct property interest in the plan in issue, this court does not agree with their holdings insofar as application of 11 U.S.C. § 541(c)(2) and *Patterson v. Shumate.* They seem to be examples of a growing genre of cases that unaccountably obviate the plain statutory requirement of § 541(c)(2) that the debtor have an interest in a trust. *See In re Barnes*, 264 B.R. 415, 421-429 (Bankr. E.D. Mich. 2001) and cases cited therein. Neither of the federal retirement programs involved in *Satterwhite* and *Seddon* appear to involve any trust, just restrictions on alienation. This court agrees with the thoughtful and thorough analysis in *Barnes* that "at least in the 'non-ERISA' context, § 541(c)(2) applies only to trust interests." *Id*. at 429. The Sixth Circuit has also delineated the requirement of an interest in a trust in applying § 541(c)(2) to exclude retirement interests from the bankruptcy estate, suggesting to this court that these cases would be decided differently in this circuit. *See Taunt v. General Retirement System of the City of Detroit (In re Wilcox)*, 233 F.3d 899, 904 (6th Cir. 2000)(indicating that the first step in the three part inquiry under § 541(c)(2) is the determination as to whether "the debtor has a beneficial interest in a trust."). Even if Ms. Hoyles had a direct interest in the Fund, which she does not, there is nothing in the federal statute creating the VSI that appears to establish a trust or make the Fund the corpus of a trust such that it could be argued the interest is not property of the estate in the first instance.

pension, annuity, or similar plan or contract." *See Anderson v. Seaver (In re Anderson)*, 269 B.R. 27 (B.A.P. 8th Cir. 2001)(court finds under Minnesota exemption statute that debtor's interest in his former spouse's individual retirement account, obtained under a QDRO, was not exempt). Ms. Hoyles does not have a proprietary interest in and does not receive payments from the Fund itself, but merely a derivative right to receive payments from her ex-husband as a participant in the Fund. As such, § 2329.66(A)(10)(b) does not exempt Mr. Hoyles' payments to Ms. Hoyles on account of his participation in the VSI.[3]

A separate order in accordance with this memorandum of decision will be entered by the court.

/s/ Mary Ann Whipple
Mary Ann Whipple
United States Bankruptcy Judge

[3] As a result of the court's decision that the payments are not within scope of Ohio Rev. Code § 2329.66(A)(10)(b), the court need not address whether the payments are reasonably necessary for the support of Ms. Hoyles.