
In the United States Bankruptcy Court
for the
Southern District of Georgia
Savannah Division

In the matter of:)
)
JOSEPH McHOLLAND) Chapter 13 Case
NADA LEE McHOLLAND) Number 91-41691
)
)
Debtors)

ORDER ON DEBTORS' PROPOSED MODIFICATION AFTER CONFIRMATION

The Debtors' Chapter 13 plan in the above-captioned case was confirmed on January 14, 1992. It provided for payments of \$450.00 semi-monthly, a sum sufficient to pay all secured and unsecured creditors in full. On June 24, 1992, Debtors filed a proposed modification to reduce his monthly contributions to the plan to \$450.00 per month which would have resulted in a substantial reduction in the unsecured dividend. When the proposed modification was considered on July 30, 1992, the Debtor revealed that he had been terminated from his job and was receiving severance pay but had no continuing ability to pay the case for the balance of the plan unless he obtained gainful employment. The court ordered a further modification be filed.

On November 25, 1992, the Debtors filed a "Disclosure and Request for Instructions" which revealed that the employer which had terminated him had also liquidated the pension or retirement plan in which the Debtor participated and forwarded proceeds in

the amount of \$30,620.43 to the Debtor. The Debtor further revealed that if the funds were used for any purpose other than a "rollover" into a qualified pension plan the Debtor would sustain serious adverse tax consequences. Accordingly, Debtor sought court authorization to reinvest the entire sum in a retirement account.

On January 7, 1993, a hearing to consider the Debtors' request for instructions was held and continued in order for the Debtors and the Trustee to attempt to work out a suitable compromise to the Trustee's objection to the Debtor's request that he be allowed to rollover the retirement funds. Thereafter, on January 28, 1993, a consent order was submitted by the Debtor and the Trustee which provided that the proceeds of the retirement account constituted property of the estate. The order further provided that in order to assist the Debtor in avoiding adverse tax consequences that the properties could be reinvested so long as Debtors' case continued to pay a 100% dividend and so long as the monies reinvested were subject to recapture by the Trustee if the plan failed or went into default.

Subsequently the Debtor filed a Petition for Modification on May 4, 1993, setting forth that following confirmation of his plan he had been through a divorce, lost his employment, sold his house, and continued to be unable to find employment. He sought modification of the plan to delete the provisions allowing the Trustee to encroach upon the rollover retirement proceeds in the event of default and to delete the requirement that the

plan pay 100% to all creditors. The Trustee objected to the modification, arguing under principles of *res judicata*, and under the authority of Patterson v. Shumate, 119 L.Ed.2d 519 (1992), that the funds constituted estate property and would have to be distributed to creditors in order for the plan to be confirmable.

Based on the evidence and the argument of counsel I sustain the Trustee's objection. It is undisputed that the Debtor has been unable to become re-employed at a level commensurate with his education and experience. It is further undisputed that the retirement plan in which the Debtor participated at his former place of employment was liquidated and the funds held in that retirement plan came into the unrestricted possession of the Debtor.

As a result the holding in Patterson v. Shumate [that funds held in an ERISA qualified plan containing anti-alienation provisions are not property of the estate] is inapplicable and by inference supports a finding that property in a plan which contains no anti-alienation provisions is estate property under 11 U.S.C. Section 541. Furthermore, the Debtor's position is adversely controlled by the decision of Velis v. Kardanis, 949 F.2d 78 (3rd Cir. 1991). In the Kardanis case the court ruled that even property in a pension plan containing an anti-alienation provision becomes property of the estate when it is withdrawn and reinvested by the debtor because after withdrawal the debtor no longer had available the anti-alienation protections.

Debtor attempts to distinguish the Kardanis case by pointing out that the

only reason the funds were remitted to the Debtor was that his employer terminated the plan and the monies were forwarded to the Debtor. The Debtor further argues that in the absence of his bankruptcy and because of the adverse tax consequences of using the funds he would have reinvested them in a retirement account and that it is inequitable for him to suffer the penalty that will or may occur if these funds are now applied by the Trustee to the payment of his debts inasmuch as he did not receive the funds as a result of his voluntary act as did the debtor in Kardanis. While I have the greatest sympathy with the Debtor's argument, I have concluded that the result does not change simply by virtue of the fact that the withdrawal of the funds was something beyond the control of the Debtor. In both the Kardanis case and in this case the funds were in the debtor's hands and were not subject to any restriction as to how they might be used. The Debtor clearly would have reinvested them in a retirement plan to avoid adverse tax consequences had he been operating in his best economic self interest. Nevertheless he was free to use the money for any purpose he desired if he were willing to suffer the adverse tax consequences and it is, under Kardanis, the Debtor's ability to choose and the fact that the monies were not subject to any legal restriction as to the manner in which he did use them that brings them into his estate.

Accordingly, I find under both Kardanis and Patterson that the monies deposited pursuant to the terms of the January 28, 1993, order of this court constitute property of the estate. Debtor has claimed no exemption in those funds and at the time of confirmation the general unsecured claims in his case totalled \$25,855.91. As a result, pursuant to the provisions of 11 U.S.C. Section 1325(a)(4), in order for the modification to

be confirmed unsecured creditors must receive 100 cents on the dollar. Accordingly, confirmation of the modified plan must be and is denied.

This leaves as the sole remaining issue the Trustee's Motion to Dismiss in which the Trustee sets forth that the case is approximately \$2,150.00 delinquent and that no payment has been received since February. The Debtor testified that his sole source of income is \$250.00 per month as an apartment complex caretaker. Although he does receive free room, this income is clearly insufficient to fund his plan which requires payment of \$450.00 semi-monthly.

Pursuant to the provisions of the January, 1993, order, the Trustee may encroach upon the account and unless she proceeds to do so, there can be no justification for allowing this case to continue to pend. Unfortunately, the encroachment in the account will likely result in the same adverse tax consequences to the Debtor as were contemplated in the earlier portion of this order at least until the time he reaches the age of 59 and one-half.

Accordingly, I decline to rule on the Motion to Dismiss and direct the Clerk to send notice of a continued hearing on that motion during the September, 1993, term of court. In the interim, the Trustee and Debtor's counsel are directed to investigate further to determine precisely when the Trustee might encroach upon the retirement account without adverse tax consequences in light of the Debtor's current age. If the period of deferral on said encroachment is not unduly excessive in the eyes of the Trustee, creditors, or the court,

the court will entertain a moratorium on payments. While the moratorium may serve to delay creditors in their receipt of funds, avoidance of the adverse consequences may result in a greater distribution to those creditors in the final analysis. For that reason I will permit the Trustee and Debtor's counsel additional time to analyze the desirability of encroaching on the retirement fund at this point. This will also serve to permit Debtor additional time in which to find gainful employment with which his plan can be funded.

Lamar W. Davis, Jr.
United States Bankruptcy Judge

Dated at Savannah, Georgia

This ___ day of August, 1993.