IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF IOWA

In the Matter of:

Sharon A. Arthur, Case No. 10-00463-als7

Debtor Chapter 7

In the Matter of:

Corey L. McKillip, Case No. 09-04332-als7
Jamie L. McKillip,

Debtor Chapter 7

MEMORANDUM OF DECISION
(date entered on docket: October 20, 2010)

COURSE OF PROCEEDINGS

These proceedings are before the Court upon the trustees' timely objections to the Debtors' amended claims of exemption in tax refunds and tax credits. Telephonic hearings were held related to the issues raised and a briefing schedule was established. The matters are now fully submitted. Identical legal issues are raised in each of the filings captioned above. The Court addresses the disputed matters in each case in this single ruling.

The court has jurisdiction of this core proceeding pursuant to 28 U.S.C. sections 157(b)(1) and 1334. The following findings and conclusions of law are entered by the Court pursuant to Federal Rules of Bankruptcy Procedure 7052 and 9014.

BACKGROUND

Sharon A. Arthur, Case Number 10-00463-als7

Sharon A. Arthur ("Arthur" or "Debtor(s)") filed a voluntary chapter 7 proceeding on February 11, 2010. On Schedule B, line 18, a possible tax refund in the amount of $1,000 was set forth, and claimed as exempt in the same value on Schedule C of the filing. Copies of Arthur's 2009 federal and state income tax returns were provided to Wesley B. Huisinga ("Trustee") post-filing. The returns set forth refunds owing to the Debtor in the amount of $10,544 and $979 from the Internal Revenue Service and Iowa Department of Revenue respectively. A request for turnover of non-exempt refunds in the amount of $9,123 was made upon the Debtor(s) by the Trustee. On March 24, 2010, prior to complying with the Trustee's payment request, the Debtor(s) filed amended Schedules B and C. Amended schedule B identified a tax refund valued at $11,523. Amended schedule C claims tax refunds valued at $7,842 as exempt pursuant to Iowa Code section 627.6(10). Tax credits valued at $1,400, which arise under the Making Work Pay Credit and Hope Scholarship Credit are additionally claimed as exempt pursuant to Iowa Code section 627.6(8)(a). Having reviewed Arthur's pay advice and amended Schedule C the Trustee filed a timely objection to the claim of exemptions in the tax refunds and accrued wages which exceeded the amount of $2,221.77, and requested turnover of the tax credits.

Corey L. and Jamie L. McKillip, Case Number 09-4332-als7

Corey L. and Jamie L. McKillip ("McKillips" or "Debtor(s)") filed a voluntary chapter 7 proceeding on September 3, 2009. On Schedule B, line 18, estimated accrued wages in the amount of $1,500 was set forth and claimed as exempt in the same value on

Schedule C of the filing. On May 17, 2010, the Debtor(s) amended the original Schedule B to set forth accrued state and federal income tax refunds in the amount of $5,511.75. Amended Schedule C claims a pro-rated portion of tax refunds as exempt pursuant to Iowa Code section 627.6(10). Schedules B and C were also amended to identify a Make Work Pay Credit in the amount of $539.18 and claim this asset as exempt pursuant to Iowa Code section 627.6(8)(a). Burton H. Fagan ("Trustee") filed a timely objection to the amended claims of exemption.

DISCUSSION

Iowa has opted out of the federal exemption provisions and its residents must utilize state law exemptions in bankruptcy. See Iowa Code § 627.10 (2010). The exemption challenges in this proceeding are based upon two statutory provisions found at Iowa Code Chapter 627.

ACCRUED WAGE and TAX REFUND EXEMPTION

Pursuant to Iowa Code section 627.6(10) a debtor is permitted to claim an exemption in wages and tax refunds as follows:

> In the event of a bankruptcy proceeding, the debtor's interest in accrued wages and in state and federal tax refunds as of the date of filing of the petition in bankruptcy, not to exceed one thousand dollars in the aggregate. This exemption is in addition to the limitations contained in sections 642.21 and 537.5105.

(2010). This exemption provision references two Iowa statutes that restrict the amount of wages that may be garnished. "[D]isposable earnings of an individual are exempt from garnishment to the extent provided by the federal Consumer Credit Protection Act" ("CCPA"). Iowa Code § 642.21 (2010) (citation omitted). Without reference to the CCPA, Iowa Code section 537.5105(2) (2010) limits the amount of disposable earnings

which may be garnished on a weekly basis. Two terms are germane in discerning the character of the funds that are subject to the garnishment limitations. "Earnings" are defined as: "compensation paid or payable for personal services, whether denominated as wages, salary, commission, bonus or otherwise, and includes periodic payments pursuant to a pension or retirement program." Id. § 642.21(3)(a).[1] "Disposable earnings" are defined as "that part of the earnings of an individual remaining after the deduction from those earnings of amounts required by law to be withheld [or assigned]." Id. §§ 642.21(3)(b), 537.5105(1)(a). In the context of bankruptcy proceeding, applying these two garnishment provisions results in an increase in the total value of accrued wages that a debtor may claim as exempt. See In re Irish, 311 B.R. 63 (B.A.P. 8th Cir. 2004).

At issue in this case is whether tax refunds are earnings or disposable earnings for purposes of applying Iowa Code section 627.6(10) (2010). The United States Supreme Court has held that tax refunds are not earnings for purposes of expanding a claim of exemption in bankruptcy based upon the limitations imposed upon wage garnishment. See Kokoszka v. Belford, 417 U.S. 642 (1974). The opinion stated that "earnings" and "disposable earnings" were limited to "periodic payments of compensation and [do] not pertain to every asset that is traceable in some way to such compensation." Id. at 651 (quoting In re Kokoszka, 479 F.2d 990, 997 (2nd Cir. 1973)).

The Debtors argue that the provisions of the CCPA are not relevant to an interpretation of the Iowa exemption and garnishment statute. I disagree. The definitions of the state and federal act are substantially similar, if not identical. Further, the weight

[1] Iowa's statutory definition of earnings is identical to that of the federal statute. See 15 U.S.C. § 1672(a) (2010).

of authority, applying both federal and state laws, have declined to recognize tax refunds as earnings which are subject to garnishment limitations in the context of a bankruptcy proceeding. See, e.g., In re Annis, 232 F.3d 749 (10th Cir. 2000); In re Sebastian, No. 08-60340-7, 2008 WL 5063084 (Bankr. D. Mont. Nov. 5, 2008); In re Lancaster, 161 B.R. 308 (Bankr. S.D. Fla. 1993); In re Miles, 153 B.R. 72 (Bankr. N.D. Okla. 1993); In re Orndoff, 100 B.R. 516 (Bankr. E.D. Calif. 1989); In re Traux, 104 B.R. 471 (Bankr. M.D. Fla 1989); In re Verill, 17 B.R. 652 (Bankr. D. Md. 1982).

In Iowa, exemptions are liberally construed in favor of a debtor to confer the intended benefit. See Frudden Lumber Co. v. Clifton, 183 N.W.2d 201, 203 (Iowa 1971). However, in its analysis the Court must also be mindful of the rules governing statutory construction. See Kokoszka v. Belford, 417 U.S. at 646, 650, 651. It is well settled that the language of a statute is given its plain meaning to initially determine the legislative intent. See In re Detention of Fowler, 784 N.W.2d 184, 187 (Iowa 2010); In re Reindl, 671 N.W. 2d 466, 469 (Iowa 2003). "The court is not at liberty to read into the statute provisions which the legislature did not see fit to incorporate, nor may it enlarge the scope of its provisions by an unwarranted interpretation of the language used." In re Irish, 311 B.R. at 68 (quoting Moulton v. Iowa Emp't Sec. Comm'n., 34 N.W.2d 211, 216 (1948)). Accepting the Debtors' argument would result in the application of the garnishment limitation simply because the term "tax refunds" is present in Iowa Code section 627.6(9), not because the tax refunds represent earnings that are subject to

garnishment restrictions.[2] This conclusion would enlarge the exemption beyond the statute's plain meaning and legislative intent.

Based upon the relevant statutory language, and persuasive authority, tax refunds do not qualify for the protections afforded by the garnishment provisions identified in Iowa's exemption statute.

TAX CREDITS

The Making Work Pay and Hope Scholarship tax credits were claimed as exempt under Iowa Code section 627.6(8)(a) (2010) which applies to social security benefits, unemployment compensation or "any public assistance benefit." The character of a public assistance benefit entitled to exempt status under Iowa law was addressed in detail in the case of In re Longstreet, 246 B.R. 611 (Bankr. S.D. Iowa 2000). In reaching its determination that an Earned Income Tax Credit ("EIC") was exempt the Court analyzed the statute and focused on the term "public assistance" which is defined as: "government aid to the needy, blind, aged, or disabled persons and to dependent children." Id. at 615. The Court further distinguished EIC and other types of tax credits.

> [EIC] differs from other traditional "tax credits" in that some eligible filers need not have paid or owed taxes during the year for which they qualify for the credit. [26. U.S.C. § 32 (1994)]. Thus the EIC goes beyond mere tax relief to become, in essence, a grant. The credit was "enacted to reduce the disincentive to work caused by the imposition of Social Security taxes on earned income (welfare payments are not similarly taxed), to stimulate the economy by funneling funds to persons likely to spend the money immediately, and to provide relief for low-income families hurt by rising food and energy prices." Sorenson v. Secretary of the Treasury of the United States, 475 U.S. 851, 864 (1986) (internal citation omitted). Since an EIC is

[2] The Eighth Circuit has been consistent in stating that a tax refund that results from voluntary withholdings in excess of the mandated minimum amounts are not protected as disposable earnings. See Gherig v. Shreves, 491 F.2d 688, 671 (8th Cir. 1974) (citing In re Wetteroff, 453 F.2d 544 (8th Cir. 1972)).

> available even when no tax is owing, the property in issue may be construed as a government aid payment.

Id. at 614.

Pursuant to federal law, the Making Work Pay tax credit ("MWP") is a component of the American Recovery and Reinvestment Act of 2009 ("Act"). Hearings before Congress were clear that this credit was made available to stimulate the economy and spending. See, e.g., January Employment Data: Hearing Before S. Joint Economic Comm., 110th Cong. (2009) (statement of Carolyn Maloney, Chair, Senate Joint Economic Comm.) (stating that the tax cut was made in hopes that the families would spend the money to stimulate local economies). Payments made under the stimulus programs were not implemented with the goal of providing government aid to low income individuals. Clearly, the receipt of funds, made available under a variety of stimulus programs, were helpful to many individuals and families, however, this consequence was not the primary focus of the Act. It is also noteworthy that to qualify for MWP, an individual must have been employed, but must not have annual income exceeding $95,000.[3] Due to its origins under the Act and its stated purposes, along with the broad application to all income levels, MWP is not easily classified as a form of government aid to the needy. Guided by the analysis of the Court in In re Longstreet, supra, the Making Work Pay is not exempt as a public assistance benefit.

The Hope Scholarship Credit was established in 1997 and provides non-refundable credits related to qualifying undergraduate college educational expenses. This tax credit is only available to those individuals that owe taxes, and is not available to those taxpayers earning more than $80,000 annually. This tax credit may only be

[3] The tax credit was established at 6.2% and capped at $400 per individual. The tax credit was reduced to 4.2% for individuals earning between $75,000 and $95,000 annually.

claimed twice by any individual taxpayer. See 26 U.S.C. § 25A (2010). Based upon these restrictions, it is apparent that this category of tax credit was not intended to be an ongoing source of assistance. Only one bankruptcy court appears to have addressed this specific tax credit and determined that it is exempt as a public assistance benefit. See In re Crampton, 249 B.R. 215, 217-218 (Bankr. D. Idaho 2000). In reaching this conclusion, the Crampton court stated that the Hope Scholarship Credit "was intended to encourage taxpayers' education generally. It was not intended to help the poor." Id. at 218. Given the circumstances surrounding receipt of the Hope Scholarship tax credit, it is not exempt as a public assistance benefit.

Based upon the foregoing it is hereby ORDERED that

1. Arthur and McKillips' objections to the Trustees' Objections are overruled and the Trustees' Objections to Exemptions are sustained.
2. Arthur shall remit non-exempt funds in the amount of $10,930.25 to her Trustee for administration.

/s/ Anita L. Shodeen
Anita L. Shodeen
U.S. Bankruptcy Judge

Parties receiving this Memorandum of Decision from the Clerk of Court:
Electronic Filers in these Chapter Cases