GIVING CREDIT WHERE THIS CREDIT'S DUE:

KANSAS' BANKRUPTCY-SPECIFIC EXEMPTION OF THE EARNED INCOME TAX CREDIT PASSES THE CONSTITUTIONAL TEST

*Andréa Horvath**

I. INTRODUCTION

Praised by President Reagan as "the best antipoverty, the best pro-family, the best job creation measure to come out of Congress,"[1] the Earned Income Tax Credit reduces poverty by encouraging eligible individuals to work, and by providing low-income families with much-needed financial assistance.[2] Unlike a tax refund, which generates a refund based on the amount of taxes overpaid through withholding of wages, the Earned Income Tax Credit operates independently of the amount of tax owed and functions more like a grant based on an individual's income level and number of dependent children.[3] Between 1989 and 2006, around half of all U.S. taxpayers with children claimed the Earned Income Tax Credit at least once.[4] However, more than half of those who claimed the Earned Income Tax Credit during these years did so only for one to two years at a time.[5] In this way, the Earned

* J.D. Candidate 2015, University of Kansas School of Law; B.A. (Psychology) 2009, University of Kansas. This article would not have been possible without the support of several important people along the way. To begin, thank you to Professor Stephen Ware for sharing his knowledge of bankruptcy law and guidance during this writing process. Additional thanks to Mr. Ed Nazar, who was more of a mentor than an employer, and whose enthusiasm for and interest in bankruptcy law was both inspiring and contagious. Finally, my deepest gratitude goes to my parents, Jay and Brenda Horvath, and my fiancée, Chuck Smith. I am incredibly grateful for their encouragement, unconditional love, and never-ending confidence in me.

1. Shai Akabas & Matt Graham, *The Earned Income Tax Credit: Facts, Statistics, and Context*, BIPARTISAN POLICY CTR. (June 12, 2013), http://bipartisanpolicy.org/blog/earned-income-tax-credit-facts-statistics-and-context/.

2. Jimmy Charite et al., *Earned Income Tax Credit Promotes Work, Encourages Children's Success at School, Research Finds*, CTR. ON BUDGET AND POLICY PRIORITIES 8 (Apr. 9, 2013), http://www.cbpp.org/files/6-26-12tax.pdf.

3. *In re* Brown, 186 B.R. 224, 226 (Bankr. W.D. Ky. 1995).

4. Charite, *supra* note 2, at 10.

5. Tim Dowd & John B. Harowitz, *Income Mobility and the Earned Income Tax Credit: Short-Term Safety Net or Long-Term Income Support*, PUB. FIN. REVIEW, 29 (Sept. 2011),

Income Tax Credit has acted as a temporary safety net for many families in need during difficult financial times.[6] In 2011, about 220,000 Kansas families received the federal Earned Income Tax Credit.[7] That same year, the Kansas Legislature passed Senate Bill No. 12, later codified as Kan. Stat. Ann. § 60-2315, which exempted the Earned Income Tax Credit for debtors in bankruptcy.[8]

The general purpose behind exemption statutes is to ensure that the debtor is not left destitute without any property after creditors exercise their collection efforts through the available remedies under state law.[9] Most state exemption statutes designate certain property of the debtor to be exempt from seizure by creditors outside of bankruptcy.[10] Where the state has opted-out of the federal bankruptcy exemption scheme in 11 U.S.C. § 522, these same state property exemptions continue to apply to debtors in bankruptcy.[11] Therefore, Kan. Stat. Ann. § 60-2315's exemption for only those debtors in bankruptcy creates an unusual result, because typical state exemption statutes are written to apply to all debtors, not just those in bankruptcy.[12]

The legislative history of Kan. Stat. Ann. § 60-2315 indicates that it was passed to help low income Kansans "maintain and improve their lives."[13] Prior to its enactment, the Earned Income Tax Credit portion of a debtor's tax refund, together with the rest of the refund, was frequently and routinely seized by his or her bankruptcy trustee as part of the debtor's bankruptcy estate.[14] In the administration of Chapter 7 bankruptcy cases, a debtor's total tax refund, a portion of which for eligible individuals would be comprised of the Earned Income Tax Credit, would often go to pay the bankruptcy trustee's fees and other creditors of the debtor.[15] In response to this practice, the Kansas Legislature enacted Kan. Stat. Ann. § 60-2315, because it found that such a forfeiture of the tax credit to the bankruptcy estate was "counterproductive to the debtor's ability to recover, making it more likely that the debtor will come

---

http://cms.bsu.edu/Academics/CollegesandDepartments/MCOB/Programs/Depts/Economics/FacultyResearch/-/media/WWW/DepartmentalContent/MillerCollegeofBusiness/Econ/research/FacultyPapers/horowitz2011pfr.ashx.

6. *Id.* at 30.

7. Quiana Torres Flores, *Tax Credits for Working Families: Earned Income Tax Credit*, NAT'L CONFERENCE OF STATE LEGISLATURES, Table 2 (Sept. 2011), http://www.ncsl.org/issues-research/labor/earned-income-tax-credits-for-working-families.aspx.

8. S.B. No. 12, 2011 Kan. Sess. Laws 94 (codified as KAN. STAT. ANN. § 60-2315 (2012)).

9. LYNN M. LOPUCKI & ELIZABETH WARREN, SECURED CREDIT: A SYSTEMS APPROACH 15 (7th ed. 2012).

10. *Id.*

11. *See* 11 U.S.C. § 522(b)(3) (2012); *see also* discussion *infra* Part II.C.

12. LOPUCKI & WARREN, *supra* note 9, at 93.

13. *Minutes of the House Judiciary Committee*, 2011 Reg. Sess., Attach. No. 5 (Kan. Jan. 26, 2010) (testimony presented to House Judiciary Committee by Sen. John Vratil), *available at* http://www.kanfocus.com/Minutes/Senate_Judiciary_01_26_10.pdf.

14. *See* Dalie Jiminez, *The Distribution of Assets in Consumer Chapter 7 Bankruptcy Cases*, 83 AM. BANKR. L.J. 795, 812 (2009).

15. *See id.*

to require state services."[16] In addition to Kansas, four other states also expressly exempt a debtor's Earned Income Tax Credit.[17]

Kansas is an opt-out state with regard to bankruptcy exemptions, meaning that in Kansas, general state property exemption statutes dictate what exemptions a debtor can claim when he or she files bankruptcy within the state.[18] That being the case, one may ask what the problem is with Kansas choosing to exempt the Earned Income Tax Credit. The issue lies with the fact that Kansas' exemption statute exempts the Earned Income Tax Credit *only* for debtors in bankruptcy, unlike the traditional property exemption that exempts property from all creditor attachment prior to bankruptcy.[19] This difference amounts to much more than just an administrative technicality; it raises constitutional questions and has led to frequent litigation and disagreement among courts in states with similar bankruptcy-specific exemptions.[20] Once explored, however, it becomes clear that the issues that plague many bankruptcy-specific exemptions do not threaten the exemption of the Earned Income Tax Credit for Kansas debtors in bankruptcy.[21] Consequently, the importance of keeping the funds from the Earned Income Tax Credit in the hands of those recipients who need it most should move to the forefront of this discussion.

This article argues that many state-enacted bankruptcy-specific exemptions may be unconstitutional for two reasons: first, because they likely do not meet the constitutional standard of "uniform laws on the subject of bankruptcies;" and second, they may be preempted if they conflict with one or more sections of the Bankruptcy Code. Importantly, Kan. Stat. Ann. § 60-

16. *Minutes*, *supra* note 13.

17. Colorado, Oregon, Indiana, Florida and Kansas have expressly exempted the Earned Income Credit. COLO. REV. STAT. § 13-54-102(1)(o) (2004); FLA. STAT. 222.25 (2004); OR. REV. STAT. § 18.345(1)(n) (2003); IND. CODE ANN. § 34-55-10-2(c)(11) (2011); KAN. STAT. ANN. § 60-2315 (2011).

18. *See* 11 U.S.C. § 522(b)(3) (2012). *See also infra* Part II.C for further explanation of the history of the opt-out provision and the effects of a state's choice on its debtors in bankruptcy.

19. *See, e.g.*, KAN. STAT. ANN. § 60-2313(a)(5) (1999). This statute exempts a debtor's crime victim compensation award, preventing a creditor from being able to execute upon that particular asset to repay a debt. The statute reads as follows: "Exemptions from legal process. (a) Except to the extent otherwise provided by law, every person residing in this state shall have exempt from seizure and sale upon any attachment, execution or other process issued from any court in this state: …(5) Any crime victims compensation award exempt from process pursuant to K.S.A. 74-7313 and amendments thereto."

20. Most courts have found that bankruptcy-specific exemptions are constitutional. *See, e.g.*, *In re* Peveich, 574 F.3d 248, 252 (4th Cir. 2009); *In re* Shumaker, 124 B.R. 820, 827 (Bankr. D. Mont. 1991) (finding bankruptcy-specific exemptions do not violate uniformity within the Bankruptcy Clause). A few courts have found that bankruptcy-specific exemptions are unconstitutional. *See In re* Kanter, 505 F.2d 228, 231 (9th Cir. 1974); *In re* Regevig, 379 B.R. 736, 737 (Bankr. N.D. Ariz. 2008); *In re* Cross, 255 B.R. 25, 34–35 (Bankr. N.D. Ind. 2000). However, the current trend among appellate courts has found bankruptcy-specific exemptions are constitutional. *See, e.g.*, *In re* Schafer, 455 B.R. 590, 606 (B.A.P. 6th Cir. 2011), *rev'd*, 689 F.3d 601 (6th Cir. 2012).

21. *See infra* Part IV.

2315 survives either constitutional test, due to the unique nature of the exemption itself.

Part II of this article begins with the history of the Bankruptcy Clause, examines the Supreme Court's interpretation of "uniformity," particularly as it relates to Congress' ability to recognize and incorporate state laws into its national bankruptcy scheme, and discusses Congress' enactment of section 522 of the Bankruptcy Code. Part III focuses on how uniformity, other constitutional provisions like the Contract Clause, and Congressional intent may impose certain pre-emptive limitations on a state's ability to pass its own bankruptcy-specific exemptions. Part IV discusses what makes Kan. Stat. Ann. § 60-2315 unique from a constitutional standpoint and explains why it does not suffer the same fate as other bankruptcy-specific exemptions. Finally, Part V concludes that enacting an exemption of the Earned Income Tax Credit for debtors in bankruptcy is not only constitutional, but also good policy, and urges other states and Congress to follow suit.

II. FROM THE BANKRUPTCY CLAUSE TO THE CURRENT BANKRUPTCY CODE: UNIFORM LAWS AND THE OPT OUT PROVISION OF SECTION 522

The Constitution gives Congress the power to "establish. . .uniform Laws on the subject of Bankruptcies throughout the United States."[22] As is discussed in detail in Part II of this article, 11 U.S.C. § 522 of the Bankruptcy Code outlines a federal exemption scheme for debtors in bankruptcy, but also gives states a couple of choices with regard to their debtors' exemptions.[23] A state can allow its residents to choose between the federal exemption scheme and its own existing state property exemptions, or it can opt-out of the federal exemption scheme altogether, which imposes upon its residents the state's existing property exemptions as their only option.[24] Each state can have very different exemptions, and further inconsistency results when states pass bankruptcy-specific exemptions.[25] With so many scenarios facing a debtor and his choice of exemptions, and even further differences imposed by state law, one may be left with a few questions. What could the constitutional language of 'uniform laws' possibly mean? Whatever requirement this language imposes, how can the current system meet any potential test? Some of these questions have faced courts since the time that the Constitution was ratified,[26]

22. U.S. CONST. art. I, § 8, cl. 4.

23. 11 U.S.C. § 522 (2012).

24. *See id.* Kansas has chosen the latter, meaning that Kansas debtors elect exemptions from state statutes.

25. *See, e.g.*, *In re* Wilson, 446 B.R. 555, 560–61 (Bankr. M.D. Fla. 2011) (discussing the "wildcard exemption" of FLA. CONST. ART. X, § 4(a)(2)); *see also* Lawrence Ponoroff, *Constitutional Limitations on State-Enacted Bankruptcy Exemption Legislation and the Long Overdue Case for Uniformity*, 88 AM. BANKR. L.J. 353, 359–60 (2014) (mentioning that thirty-four states have chosen to opt-out of the Code's exemption scheme, and, as early as 1980, several of those states began enacting bankruptcy-specific exemption statutes).

26. For further discussion of this question, *see generally* Hon. William Houston Brown,

and unfortunately, the Supreme Court has not directly decided either the constitutionality of the opt-out provision of section 522(b) or bankruptcy-specific exemptions.[27] To understand the potential limits on the most current Bankruptcy Act's exemption scheme, it is necessary to at least briefly examine its history.

A. A Brief History: What Inspired the Framers to Call for Uniform Laws?

To quote Justice Thurgood Marshall, the "scanty history of the [Bankruptcy] Clause" leaves those who attempt to analyze its purpose and meaning stuck with a difficult task.[28] To the extent that we can rely on the context in which the Bankruptcy Clause was drafted to provide guidance as to its meaning, it is best to begin with a look back at the treatment of debtors in England before the American Revolution.[29] The English system pre-dating that of the United States' system for dealing with debtors in bankruptcy was one of harsh penalties, including imprisonment and punishment by death.[30] The early years of the United States' legal system was not much better in this respect, and in both England and the American Colonies, debtors were sometimes treated more harshly than common criminals.[31] To make matters worse, legal processes for debtors varied widely by state.[32] This presented problems for enforcement of insolvency laws between states, and a grant of discharge of debt in one state would often still result in the debtor's imprisonment in another.[33] In the *Federalist Papers*, Alexander Hamilton and James Madison expressed views that a federal system of bankruptcy laws would best accomplish uniformity in treatment of debtors between states.[34]

The Constitution's Bankruptcy Clause was written, at least in part, to combat the harshness and inconsistency in bankruptcy laws between states where the differences in treatment caused debtors to suffer injustice.[35] To achieve this goal, the framers drafted the Bankruptcy Clause's broad grant of

---

Political and Ethical Considerations of Exemption Limitations: The "Opt-Out" as Child of the First and Parent of the Second, 71 AM. BANKR. L.J. 149 (1997).

27. *In re* Westby, 473 B.R. 392, 407 (Bankr. D. Kan. 2012), *aff'd*, 486 B.R. 509 (10th Cir. B.A.P. 2013).

28. Ry. Labor Execs.' Ass'n v. Gibbons, 455 U.S. 457, 474 (1982) (Marshall, J., concurring).

29. *See* Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 362 (2006) ("It is appropriate to presume that the Framers of the Constitution were familiar with the contemporary legal context when they adopted the Bankruptcy Clause . . . .").

30. Hanover Nat'l Bank v. Moyses, 186 U.S. 181, 187 (1902).

31. *See Katz*, 546 U.S. at 365.

32. *See id.*

33. *See id.* at 363–65 ("The only consistency among debt laws in the eighteenth century was that every colony, and later every state, permitted imprisonment for debt—most on mesne process, and all on execution of a judgment.").

34. *See* THE FEDERALIST NOS. 32 (Alexander Hamilton), 42 (James Madison), *available at* http://www2.hn.psu.edu/faculty/jmanis/poldocs/fed-papers.pdf.

35. *Katz*, 546 U.S. at 363 (quoting Ry. Labor Execs.' Ass'n v. Gibbons, 455 U.S. 457, 472 (1982)).

power to Congress, directing it to "pass uniform laws on the subject of bankruptcies."[36] In addition, they drafted the Contract Clause, which prohibited the States from passing any legislation that impairs the obligation of contracts.[37] Working together, these Clauses empower Congress to discharge debt and impair contracts of debtors in the fifty states, and thus carry out the primary purpose of bankruptcy law.[38] Importantly, for determining the constitutionality of bankruptcy-specific exemptions, these clauses indicate that Congress, and Congress alone, may pass laws that affect the contracts of a debtor upon filing of bankruptcy.[39] As a result, limitations on a state's power to pass bankruptcy-specific exemptions may not stem solely from the Bankruptcy Clause's uniformity requirement, but instead from the interaction between the Bankruptcy Clause and the Contract Clause.[40]

B. The Moyses Standard of Uniformity And a Discussion of the Contract Clause

In 1902, the Supreme Court in *Hanover Nat'l Bank v. Moyses* had the task of reviewing the constitutionality of the Bankruptcy Act of 1898.[41] The Act did not provide a federal exemption scheme, and instead left the determination of bankruptcy exemptions to state law.[42] The specific issue the Court faced was whether Congress had the power to recognize state law exemptions within its national bankruptcy system, or whether the uniformity requirement of the Bankruptcy Clause of the Constitution prohibited that result.[43] Seeking to derive the meaning of uniformity within the Bankruptcy Clause, the *Moyses* Court began by looking at the context in which the Clause was written.[44] The Court considered the applicability of both the Bankruptcy Clause and the Contract Clause to the concept of uniformity, and ultimately found that a system that incorporated state law was permissible under the Constitution.[45] In support of its holding, the Court reasoned "that uniformity is geographical and not personal," so the presence of different results in different cases was not determinative.[46] The *Moyses* Court's interpretation of the Bankruptcy Clause

36. U.S. CONST. art. I, § 8, cl. 4.

37. U.S. CONST. art. I, § 10, cl. 1.

38. *See* Blake Rohrbacher, *More Equal Than Others: Defending Property-Contract Parity in Bankruptcy*, 114 YALE L.J. 1099, 1114 (2005).

39. *See supra* Part III.A for an explanation of the interaction between the Contract Clause and the Bankruptcy Clause of the Constitution and the effect those provisions have on the constitutionality of bankruptcy-specific exemptions.

40. *See* Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 265 (1929); *but see In re* Schafer, 689 F.3d 601, 610 (6th Cir. 2012).

41. Hanover Nat'l Bank v. Moyses, 186 U.S. 181 (1902).

42. Joseph Lamport, *The Preemption of Bankruptcy-Only Exemptions*, 6 CARDOZO L. REV. 583, 591 (1985) (discussing the Bankruptcy Act of 1898).

43. *Moyses*, 186 U.S. at 181.

44. *Id.* at 185–90.

45. *Id.*

46. *Id.* at 188.

acknowledges that a creditor and debtor contract around the existing laws of the state. Where a creditor whose debtor has not filed for bankruptcy could execute upon the same property as the trustee could within bankruptcy, then the creditor receives the full benefit of the laws as expected, and the outcome is constitutionally uniform.[47]

In upholding the Bankruptcy Act of 1898, the *Moyses* Court acknowledged that incorporation of state exemption statutes may provide different results in different states for debtors in bankruptcy, yet that would not necessarily be inconsistent with a uniform national bankruptcy Act.[48] The Court held that where states exempt property from execution though their exemption statutes, Congress' incorporation of those statutes into a federal scheme would not violate uniformity because all contracts are made under existing state law, taking exemption laws into consideration.[49] The outcome remains "just" and "uniform" where this effect remains consistent, such that a creditor may execute on the same property both outside of bankruptcy as its representative, the trustee, could within bankruptcy.[50] The *Moyses* Court concluded "[a] rule which operates to this effect throughout the United States is uniform within the meaning of that term, as used in the Constitution."[51]

In the years following *Moyses*, the Supreme Court interpreted the meaning and effect of the Bankruptcy Clause, and its uniformity requirement, to determine what constitutional limits "uniformity" places on Congress' ability to enact legislation directed at more localized, non-nationwide problems.[52] In

47. *Id.* at 188–90 ("[I]n the constitutional sense, uniform throughout the United States, when the trustee takes in each State whatever would have been available to the creditors if the bankrupt law had not been passed. The general operation of the law is uniform although it may result in certain particulars differently in different States.").

48. *Id.* at 188.

49. *Id.* at 189–90.

50. *Id.* ("This is not unjust, as every debt is contracted with reference to the rights of the parties thereto under existing exemption laws, and no creditor can reasonably complain if he gets his full share of all that the law, for the time being, places at the disposal of creditors . . . . It is quite proper, therefore, to confine [the Bankruptcy Code's] operation to such property as other legal process could reach. A rule which operates to this effect throughout the United States is uniform within the meaning of that term, as used in the Constitution."). This was also the finding of the Sixth Circuit Bankruptcy Appellate Panel in *In re* Schafer, 455 B.R. 590, 606 (B.A.P. 6th Cir. 2011), *rev'd*, 689 F.3d 601 (6th Cir. 2012). The case has since been overruled by the Circuit Court of Appeals for the Sixth Circuit.

51. *Id.* at 190; *but see In re* Schafer, 689 F.3d 601, 610 (6th Cir. 2012), *cert. denied sub nom.* Richardson v. Schafer, 133 S. Ct. 1244 (2013) (interpreting *Moyses* as holding that variations among states do not violate uniformity and not that the trustee in bankruptcy must have access to the same property as a judgment creditor outside of bankruptcy).

52. *See* Blanchette v. Conn. Gen. Ins. Corps., 419 U.S. 102 (1974); *see also* Ry. Labor Execs.' Ass'n v. Gibbons, 455 U.S. 457 (1982). The "railroad cases," as they are commonly known, dealt with the ability of Congress to address a particular problem in the administration of bankruptcies of major railroads. The consistency in these cases is that the Court found that if Congress passes a separate bankruptcy Act to address a particular type of debtor it must apply uniformly to all debtors in that class. Where the Act of Congress applies only to one debtor, then it is a private Act and that would violate the uniformity requirement.

1974, the Court expressly held that the Clause's 'uniformity' language does not operate as a restraint on Congress, which forces it to enact one set of rules where it sees a need for more localized rules.[53] The *Blanchette* Court made clear that Congress may enact legislation that proposes different solutions in different regions in the United States without violating the uniformity provision.[54] In 1982, the Supreme Court struck down a law for violating the uniformity requirement, finding that although a law can be uniform to constitutional standards, where it recognizes the different rules in different states, a law is not uniform if it imposes a rule of bankruptcy on just one bankrupt railroad.[55] To date, this is the only case in which the Supreme Court struck down a federal enactment for its failure to comply with the Bankruptcy Clause's uniformity requirement.

The most recent cases interpreting "uniformity" and its potential limitations on Congress' power to legislate bankruptcy laws provide that Congress' constitutional power to enact "uniform laws on the subject of bankruptcies" does not require Congress to pass one set of bankruptcy laws applicable to all.[56] These cases are not entirely on point regarding Congress' ability to recognize state exemption statutes within its national bankruptcy Code, however, and *Moyses* remains the best authority for analyzing the constitutionality of state-enacted bankruptcy-specific legislation. Taken as a whole, the Supreme Court's Bankruptcy Clause precedent addresses at least two primary functions of the Clause: (1) as a broad grant of legislative power to Congress to combat issues surrounding inconsistency in insolvency laws,[57] implying a limit on a state's power to pass laws conflicting with federal bankruptcy laws,[58] and (2) as a limit on Congress' power to pass non-uniform bankruptcy legislation,[59] arguably implying a limit on Congress' power to recognize some non-uniform state laws in its federal scheme to the extent that the state laws would violate minimal standards of "uniformity."[60]

53. *Blanchette*, 419 U.S. at 159 ("[T]he uniformity clause was not intended 'to hobble Congress by forcing it into nationwide enactments to deal with conditions calling for remedy only in certain regions.'").

54. *Id.* ("The uniformity provision does not deny Congress power to take into account differences that exist between different parts of the country, and to fashion legislation to resolve geographically isolated problems. 'The problem dealt with (under the Bankruptcy Clause) may present significant variations in different parts of the country.'").

55. *See Ry. Labor*, 455 U.S. at 473.

56. *Blanchette*, 419 U.S. at 160.

57. *See* Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 377 n.13 (2006).

58. *See* Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 265 (1929).

59. *See Ry. Labor*, 455 U.S. at 473.

60. *See In re* Pontius, 421 B.R. 814, 822 (Bankr. W.D. Mich. 2009), *abrogated by In re* Schafer, 689 F.3d 601 (6th Cir. 2012); *see also* Randolph J. Haines, Federalism Principles in Bankruptcy After Katz, 15 AM. BANKR. INST. L. REV. 135, 147 (2007).

C. The Opt-Out Provision in Section 522 and Congressional Intent to Leave Room for the States

If the Supreme Court granted certiorari today to determine whether a state's bankruptcy-specific exemption is preempted by the Bankruptcy Code, it would first need to analyze the constitutionality of Congress' opt-out portion of 11 U.S.C. § 522.[61] The history of this provision and the context in which it was passed help to explain Congress' choice to incorporate an opt-out provision as the solution to the question of which exemption scheme would govern: state law or federal law. In an exercise of its power to establish uniform laws, Congress passed the current version of the federal Bankruptcy Code in 1978.[62] This national bankruptcy system is designed to balance two competing goals:[63] give "the honest but unfortunate debtor" a "fresh start"[64] and provide a fair distribution to his creditors.[65] One important mechanism for affording a debtor a fresh start is through exemptions.[66] Exemptions prevent certain essential items from being subject to attachment by creditors, and in bankruptcy, they shield the assets from liquidation and distribution to creditors.[67] The current federal Bankruptcy Code allows states, if they so choose, to opt-out of the federal list of exemptions and apply their own state exemption statutes to the bankrupt debtors within their borders.[68] Kansas has chosen to opt-out, and as a result, debtors in Kansas who file for bankruptcy under the federal Bankruptcy Code use Kansas' property exemptions in lieu of the federal list.[69]

Since the first attempts to establish a federal bankruptcy scheme, the question of whether state or federal exemptions should apply has been hotly

61. *See In re* Neiheisel, 32 B.R. 146, 148–65 (Bankr. D. Utah 1983) (discussing the legislative history of the opt-out compromise of 11 U.S.C. § 522).

62. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978).

63. Elizabeth Warren, *Reforming Consumer Bankruptcy Law: Four Proposal: A Principled Approach to Consumer Bankruptcy*, 71 AM. BANKR. L.J. 483, 483 (1997).

64. *See* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934) (holding a purpose of bankruptcy is to give an "honest but unfortunate debtor who surrenders for distribution the property which he owns at the time of bankruptcy, a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt").

65. *See* Howard Delivery Serv., Inc. v. Zurich Am. Ins. Co., 547 U.S. 651, 655 (2006); *see also* Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 363–64 (2006) ("Critical features of every bankruptcy proceeding are the exercise of exclusive jurisdiction over all of the debtor's property, the equitable distribution of that property among the debtor's creditors, and the ultimate discharge that gives the debtor a 'fresh start' by releasing him, her, or it from further liability for old debts.").

66. *See* Wells M. Engledow, *Cleaning up the Pigsty: Approaching a Consensus on Exemption Laws*, 74 AM. BANKR. L.J. 275, 278–79 (2000) (discussing the purpose of exemption laws and their importance to a debtor's ability to achieve a 'fresh start').

67. *See, e.g.*, Michael Terry Hertz, *Bankruptcy Code Exemptions: Notes on the Effect of State Law*, 54 AM. BANKR L.J. 339, 339 (1980).

68. 11 U.S.C. § 522(b)(1) (2012).

69. *See* KAN. STAT. ANN. § 60-2312. The federal list of exemptions can be found at 11 U.S.C. § 522 (2012).

contested.[70] The Bankruptcy Act of 1800 only permitted a debtor to exempt proceeds from "wearing apparel, and the necessary wearing apparel of the wife and children and necessary beds and bedding of such bankrupt."[71] It did not allow a debtor to supplement this short list of exemptions with existing state exemption laws.[72] This exclusive federal list was likely the result of the Framers' discussions of the importance of a national system of bankruptcy laws.[73] In his writings as part of *The Federalist No. 10*, James Madison wrote the following about the need for a uniform national bankruptcy scheme:

> Those who hold and those who are without property have ever formed distinct interests in society. Those who are creditors, and those who are debtors, fall under a like discrimination. . . . The regulation of these various and interfering interests forms the principal task of modern legislation, and involves the spirit of party and faction in the necessary and ordinary operations of government. . . . It is a question to which the creditors are parties on one side and the debtors on the other. Justice ought to hold the balance between them.[74]

It was not until many years later, in 1867, that Congress decided to incorporate state exemption laws into the operation of the federal bankruptcy scheme.[75]

In 1978, Congress' decision to incorporate a "hybrid approach" was made as a compromise of the two alternatives.[76] When debates took place over the proper treatment of section 522, the version of the Bankruptcy Act existing at that time was the Bankruptcy Act of 1898.[77] This Act did not contain a federal bankruptcy exemption scheme and instead left the question of what exemptions apply to a debtor in bankruptcy to existing state exemption laws.[78] As Congress looked to enact a new version of the federal Bankruptcy Code in 1978, the Senate supported maintaining this system that would allow for state law to govern the issue of exemptions.[79] In contrast, the House supported the Framers' original position during the discussion surrounding which exemption scheme to enact in 1978.[80] It was thought that a federal exemption scheme that

70. Richard Lombino, *Uniformity of Exemptions: Assessing the Commission's Proposals*, 6 AM. BANKR. INST. L. REV. 177, 179 (1998).

71. Edward Stechschulte, *The (Un)Constitutionality of State-Enacted Bankruptcy-Specific Exemptions: Using Ohio Revised Code Section 2329.66(A)(18) as a Mechanism for Analysis*, 40 U. TOL. L. REV. 761, 768 (2009) (quoting the Bankruptcy Act of 1800).

72. *Id.*

73. *Id.* at 767–68; THE FEDERALIST NOS. 10, 42 (James Madison), *available at* http://www2.hn.psu.edu/faculty/jmanis/poldocs/fed-papers.pdf.

74. *Id.*

75. Lamport, *supra* note 42, at 591–92 (summarizing the Bankruptcy Act of 1867).

76. *See generally* Brown, *supra* note 26.

77. *Id.* at 158.

78. Lamport, *supra* note 42, at 591 (discussing the Bankruptcy Act of 1898).

79. *Id.* (discussing S. 2266, 95th Cong., 2d Sess., 123 Cong. Rec. 36,091 (1977)).

80. *Id.* at 590–99 (discussing the history of the compromise in the enactment of 11 U.S.C. § 522).

did not account for existing state exemptions was the best way to avoid the problems that were caused by inconsistencies in the bankruptcy law.[81]

It is not surprising that the House and the Senate each expressed a conflicting view when one looks at the conflicted history of the compromise. In preparing for the enactment of the Bankruptcy Code of 1978, Congress formed the Commission on the Bankruptcy Laws of the United States.[82] The Commission favored a national bankruptcy scheme that would provide its own uniform federal list of exemptions as the exclusive list available to debtors who file under the federal code, thereby removing any link between state exemption statutes and exemptions available to debtors in bankruptcy.[83] Contrary to this recommendation, the National Conference of Bankruptcy Judges were in support of a scheme that would recognize existing state law exemptions applied to debtors filing bankruptcy in that state.[84]

The compromise found in section 522's opt-out provision grew out of this debate. Although the Supreme Court has not specifically addressed whether this opt-out compromise is constitutional, it has found that even though recognition of state laws within the operation of the Bankruptcy Code may lead to different results in different states, that disparity does not render the Bankruptcy Code unconstitutionally non-uniform.[85] Thus, it can be said that Congress' power to establish a national system of bankruptcy laws includes a right to recognize state exemption laws within that system.[86] Congress was within its power to leave room in its federal scheme for existing states' exemption statutes to apply to debtors in bankruptcy.[87] It is also likely within Congress' power to allow states to make a choice as to whether the federal scheme or the state scheme should apply to debtors in bankruptcy within that

81. THE FEDERALIST NO. 42 (James Madison), *available at* http://www2.hn.psu.edu/faculty/jmanis/poldocs/fed-papers.pdf.

82. The commission was formed in 1970. *See* Brown, *supra* note 26, at 159 (citing Act of July 24, 1970, Pub. L. No. 91-354, 84 Stat. 468).

83. *See id.* (citing COMM'N ON THE BANKR. LAWS OF THE U.S., REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, at 171 (1973)).

84. Lamport, *supra* note 42, at 595.

85. Stellwagen v. Clum, 245 U.S. 605, 613 (1918); *but see* Owen v. Owen, 500 U.S. 305, 308–12 (1991). In *Owen*, the Court was not asked to review the constitutionality of the opt-out provision of 11 U.S.C. § 522(b), and was instead reviewing states' lien avoidance provisions and their operation within the Bankruptcy Code. However, in dicta, Justice Scalia wrote, "If a State opts out, then its debtors are limited to the exemptions provided by state law. Nothing in [§ 522] (or elsewhere in the Code) limits a State's power to restrict the scope of its exemptions; indeed, it could theoretically accord no exemptions at all." The author argues that, not only is this non-binding dicta, but Justice Scalia's conclusion here is incorrect due to its apparent conflict with Congressional intent for the Bankruptcy Code, i.e. its purposes. Where a state decides to abolish all exemptions, the balance of the two competing purposes of the Bankruptcy Code is frustrated, and the state's statute that elects to opt-out of the federal exemption scheme would be preempted. *See In re* Cross, 255 B.R. 25, 34–35 (Bankr. N.D. Ind. 2000).

86. *See* Hanover Nat'l Bank v. Moyses, 186 U.S. 181, 190 (1902).

87. *Id.*

state's borders.[88] Conceding the likely constitutionality of Congress' opt-out provisions does not end the inquiry, however, because Congress cannot legislate around limitations imposed on it by the Constitution.

III. WHAT, IF ANY, LIMITATIONS DO CONGRESSIONAL INTENT AND UNIFORMITY PLACE ON THE STATES?

Even if one presumes the constitutionality of Congress' opt-out provision in § 522, the next question becomes whether a state's enactment may go too far, either rendering it unconstitutional for violating uniformity or preempted for falling outside of Congressional intent when it enacted § 522.

A. Most states' bankruptcy-specific exemptions conflict with the Bankruptcy Clause's uniformity requirement and the Contract Clause.

Many courts that have looked at the uniformity clause in the context of state-enacted bankruptcy-specific exemptions have ended their inquiry upon finding that the uniformity requirement is a limitation on Congress and not the states.[89] Although the cases interpreting the Constitution's uniformity requirement primarily looked at its potential limits on *Congress'* power to incorporate state law,[90] those same decisions may also be instructive on possible limits on state legislation.[91] When the interaction between the Bankruptcy Clause and the Contract Clause[92] is examined more closely, it

88. *See id.* at 188.

89. *See In re* Cross, 255 B.R. 25, 31 n.2 (Bankr. N.D. Ind. 2000). In Cross, the court said the following in a footnote regarding the proper analysis of constitutional limits on a state's ability to pass bankruptcy laws:

> Saying that the Uniformity Clause does not apply to the states is not the same as saying that they are free to enact bankruptcy legislation. There are limitations on the states' ability to do so. Yet those limitations do not come from the Uniformity Clause. Instead, they arise out of other provisions of the Constitution, such as Article I, section 10, clause 1, which prohibits states from impairing contracts, and the Supremacy Clause of Article VI, clause 2. *See Gibbons,* 455 U.S. at 472 n.14, 102 S. Ct. at 1178 n.14 . . . . In reaching this conclusion, the court recognizes that there are decisions, based upon the Uniformity Clause, invalidating state exemption laws that apply only in the event of bankruptcy . . . . The court believes that the issue is more appropriately analyzed under the Supremacy Clause.

See also In re Applebaum, 422 B.R. 684, 692 (B.A.P. 9th Cir. 2009); *In re* Earned Income Tax Credit Exemption Constitutional Challenge Cases, 477 B.R. 791, 800 (Bankr. D. Kan. 2012), *aff'd sub nom. In re* Lea, No. 11-11131, 2013 WL 4431267, at *6 (D. Kan. Aug. 16, 2013).

90. *But see* Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 265–68 (1929). In *Pinkus*, the Court discussed uniformity as a possible justification for invalidating a state statute that interfered with the federal bankruptcy act's discharge provisions. After the Court's discussion of how the state statute conflicted with Congress' power to pass uniform bankruptcy laws, it ultimately invalidated the statute under the Supremacy Clause.

91. *See, e.g.*, *Moyses*, 186 U.S. 181 (1902); Ry. Labor Execs.' Ass'n v. Gibbons, 455 U.S. 457 (1982).

92. U.S. CONST. art. I, § 10, cl. 1.

raises serious questions about the constitutionality of many states' bankruptcy-specific exemptions.[93]

The power given to Congress by the Constitution is distinct from that which was reserved for the states because Congress alone may pass "bankruptcy laws."[94] Historically, a bankruptcy law has the power to discharge debt, and thus release a debtor from contractual liability to a creditor.[95] A state could not do this, because states were forbidden from passing laws that interfered with contractual rights.[96] The Constitution prohibits states from making or enforcing bankruptcy laws if those laws impair the obligation of contracts or conflict with the Bankruptcy Code.[97] In *Railway Labor Executives' Assn. v. Gibbons,* the Court tied the Contract Clause into its discussion of the meaning of "uniformity" in a footnote, saying,

> The Framers' intent to achieve uniformity among the Nation's bankruptcy laws is also reflected in the Contract Clause. Apart from and independently of the Supremacy Clause, the Contract Clause prohibits the States from enacting debtor relief laws which discharge the debtor from his obligations, unless the law operates prospectively.[98]

Therefore, a state's bankruptcy-specific exemption is invalid to the extent it does not meet this constitutional test of uniformity.

Although the more recent *Railway* Court articulated a broad interpretation of the uniformity requirement regarding Congress' power to legislate on the subject of bankruptcy laws to affect a particular evil it had observed,[99] it is consistent with the holding in *Moyses*.[100] The Bankruptcy Clause may function as an indirect limit on state legislation, or at least as a limit on Congress' ability to incorporate certain state legislation into its overall bankruptcy scheme.[101] Ultimately, the Constitution gave Congress broad power to enact uniform laws, including the power to change the rules for creditors in bankruptcy.[102] The states, however, have no such power.[103]

---

93. U.S. CONST. art. I, § 8, cl. 4.

94. *Moyses*, 186 U.S. at 188. The Court discussed how a state cannot legislate on the subject of bankruptcy, meaning to discharge debt or impair contracts of a debtor, but mere recognition of a state's pre-existing exemptions by Congress is permissible.

95. *Id.*

96. Sturges v. Crowninshield, 17 U.S. 122, 193–94 (1819); Ogden v. Saunders, 25 U.S. 213, 257 (1827).

97. Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 263–64 (1929).

98. Ry. Labor Execs.' Ass'n v. Gibbons, 455 U.S. 457, 472 n.14 (1982) (internal citations omitted).

99. *See id.* at 473–75 (Marshall, J., concurring).

100. *See id.* at 472 n.14 (1982); *see also Moyses*, 186 U.S. at 189–90.

101. *See Ry. Labor*, 455 U.S. at 472 n.14. The *Railway* Court affirmed this discussion from *Moyses* in a footnote where it addressed the constitutional meaning of "uniform laws."

102. *See* Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 377 n.13 (2006).

103. *Moyses*, 186 U.S. at 188.

B. Bankruptcy-specific Exemptions May Also Violate the Supremacy Clause.

The Supremacy Clause invalidates state laws that frustrate "the full effectiveness of federal law."[104] To determine whether a particular state enactment is preempted under the Supremacy Clause, a court must conduct a two-step analysis, beginning with a construction of the federal and state statutes. [105] Where the two statutes conflict, the Supremacy Clause dictates that the federal law is supreme.[106]

The precise meaning of section 522 depends upon Congressional intent, which is necessarily limited by the scope of Congress' bankruptcy power under the Constitution.[107] Congress' power under the Bankruptcy Clause allowed distribution of a debtor's property for the benefit of his creditors, and it allowed Congress to discharge a debtor from his contractual obligations.[108] While supreme, Congress' power to legislate in the area of bankruptcies was not exclusive.[109] After the Constitution was ratified, the states retained much of their power to pass laws on the subject of bankruptcies, subject to important limitations.[110] State laws could not conflict with federal bankruptcy laws, once a federal scheme was enacted.[111] In addition, the state's law could not impair any contracts between the parties to the bankruptcy.[112] In this way, the Contracts Clause affected states' ability to legislate on the subject of bankruptcies even before Congress passed a national bankruptcy act.[113] After the enactment of a national bankruptcy act, the states' power to legislate on the subject was further diminished.[114]

A particular state's bankruptcy-specific exemption may be preempted if it conflicts with a goal of the Bankruptcy Code, or it may also be unconstitutional if its incorporation exceeds the scope of the Bankruptcy

104. Perez v. Campbell, 402 U.S. 637, 652 (1971).

105. *Perez*, 402 U.S. at 644.

106. *Id.* at 652.

107. *See id.* at 648–49.

108. *Moyses*, 186 U.S. at 186.

109. *See* Sturges v. Crowninshield, 17 U.S. 122, 193–94 (1819).

110. *Moyses*, 186 U.S. at 187

111. Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 265 (1929)("States may not pass or enforce laws to interfere with or complement the Bankruptcy Act or to provide additional or auxiliary regulations"); *see also In re* Pontius, 421 B.R. 814, 823 (Bankr. W.D. Mich. 2009), *abrogated by In re* Schafer, 689 F.3d 601 (6th Cir. 2012).

112. *See* Ry. Labor Execs.' Ass'n v. Gibbons, 455 U.S. 457, 472 n.14 (1982). In this footnote, Justice Rehnquist wrote, "The Framers' intent to achieve uniformity among the Nation's bankruptcy laws is also reflected in the Contract Clause." The Court says this is a separate analysis than the one found under the Supremacy Clause. It is unclear, however, whether this would amount to a violation under the Bankruptcy Clause for lack of uniformity or under the Contract Clause. Either way, it is an analysis that the Supreme Court has recognized as a constitutional limitation on states.

113. *Moyses*, 186 U.S. at 187; *Sturges*, 17 U.S. at 193–94; *Ry. Labor*, 455 U.S. at 472 n.14.

114. *Moyses*, 186 U.S. at 187.

Clause.[115] Although Congress may recognize a state's existing exemption laws in its federal bankruptcy scheme, states do not have unlimited power to enact legislation that will apply to debtors in bankruptcy.[116] Some courts have drawn a distinction between a state's power to merely "forbid" application of the federal bankruptcy exemption scheme and a more expansive power to enact bankruptcy laws.[117] Those courts have acknowledged that, at most, states have the power to exercise the former, but not the latter. The court in *In re Wallace* provides the following helpful illustration of this limitation:

> Put differently, it is within Congress' discretion under the Bankruptcy Clause to decide what is to be the set of exemptions available to debtors seeking bankruptcy relief. Congress can create its own scheme. It can establish more than one scheme. It can reference state law for purposes of defining the scheme it has chosen. For that matter, Congress could reference the laws of Kazakstan [sic] to define the bankruptcy exemption scheme if it were to so choose. What Congress cannot do under the Constitution is delegate to Kazakstan, [sic] to the states, or to any other entity the power to actually decide what is to be the appropriate scheme. That power is reserved under the Constitution for the exclusive exercise of Congress.[118]

Therefore, a state that purports to do more than merely elect to disregard the federal exemption scheme cannot rely on broad Congressional intent in section 522(b)(2) to justify its action because such action necessarily exceeds Congressional intent.

As stated in *Moyses*, Congress may not recognize a state law that gives a bankruptcy trustee access to less property than an unsecured creditor would have had prior to its debtor filing bankruptcy.[119] To do so would produce a result in violation of the Bankruptcy Clause of the Constitution.[120] Thus, it

115. Lawrence Ponoroff, *supra* note 25, at 379–80; s*ee* Butner v. United States, 440 U.S. 48, 56 (1979); Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 376 n.13 (2006) ("As our holding today demonstrates, Congress has the power to enact bankruptcy laws the purpose and effect of which are to ensure uniformity in treatment of state and private creditors."); *Sturges*, 17 U.S. at 193–94 (opinion for the Court by Marshall, C. J.) ("The peculiar terms of the grant certainly deserve notice. Congress is not authorized merely to pass laws, the operation of which shall be uniform, but to *establish* uniform laws on the subject throughout the United States.").

116. *See In re* Kanter, 505 F.2d 228, 230 (9th Cir. 1974); *see also In re* Regevig, 389 B.R. 736, 740 (Bankr. D. Ariz. 2008).

117. *See In re* Cross, 255 B.R. 25, 34 n.5 (Bankr. N.D. Ind. 2000) ("[T]he power to forbid is not the same thing as having been given the power to create. Thus, in giving states the ability to opt out of the federal bankruptcy exemptions Congress did not give them the authority to create bankruptcy exemptions. Instead, what the opt-out represents is a Congressional willingness to recognize the generally available exemptions that states have created for their own purposes in bankruptcy proceedings.").

118. *In re* Wallace, 347 B.R. 626, 635 (Bankr. W.D. Mich. 2006), *abrogated by In re* Schafer, 689 F.3d 601 (6th Cir. 2012).

119. Hanover Nat'l Bank v. Moyses, 186 U.S. 181, 188–90 (1902).

120. *In re* Pontius, 421 B.R. 814, 822 (Bankr. W.D. Mich. 2009), *abrogated by In re* Schafer, 689 F.3d 601 (6th Cir. 2012) ("[A]ll other bankruptcy specific state exemption schemes,

could not have been within the contemplation of Congress when it enacted section 522's opt-out provision to allow states to enact such a law.[121] Accordingly, bankruptcy-specific exemptions conflict with section 522 because they were not, nor could they constitutionally be, within Congressional intent when it left room to recognize state exemptions. They fall outside the permissible scope of Congressional intent, as confined by the Bankruptcy Clause.[122]

The list of federal exemptions in section 522 suggests that Congress believed these exemptions maintained a proper balance between the interests of the debtor and his creditors in bankruptcy, and a state's exemption scheme should not stray too far from the federal model.[123] In dicta in *Owen v. Owen*, Justice Scalia expressed a view of the all-inclusiveness of the opt-out provision where a state's decision to opt-out could give the state free reign on any exemption scheme it wished to pass.[124] If this is taken to be true, then it would represent the view that the federal exemptions provided in section 522 are not meant to serve as an authoritative or even suggestive example of what states must provide to maintain a sufficient balance of debtor and creditor interests in bankruptcy.[125] It is unlikely Congress intended this result.

One can imagine a state's exemption list so different or so far removed from the federal list that it would not maintain debtor-creditor balance to the extent intended by Congress.[126] For example, under the approach proposed by *Owen*, an opt-out state could theoretically enact a statute saying that none of the state's debtor exemptions apply to a debtor in bankruptcy. A state exemption scheme to this effect would frustrate the purpose of the Bankruptcy Code.[127] Similarly, a state exemption statute that exempted all or nearly all of its debtors' property upon filing of a bankruptcy, leaving no meaningful distribution for creditors in the state, would also likely frustrate the purpose of the Bankruptcy Code. The Indiana bankruptcy court applied this rationale in *In re Cross*, invalidating the state's bankruptcy-specific exemption because it stood as an obstacle to the full objectives of the Bankruptcy Code.[128] This is

---

accomplish[] the opposite result. Their very purpose is to ensure that the bankruptcy trustee does not take whatever property 'would have been available to the creditor' outside of bankruptcy." (emphasis removed)). For further discussion of how KAN. STAT. ANN. § 60-2315 manages to avoid this conflict, *see infra* Part IV.

121. This reasoning was articulated by the Bankruptcy Court in *In re Pontius,* a case that has since been overruled by the Sixth Circuit, but this article argues it is the reason that most bankruptcy-specific exemptions are likely preempted. *See In re* Pontius, 421 B.R. at 821–23 (Bankr. W.D. Mich. 2009), *abrogated by In re* Schafer, 689 F.3d 601 (6th Cir. 2012).

122. *See Moyses*, 186 U.S. at 189–90.

123. *In re* Cross, 255 B.R. 25, 34–35 (Bankr. N.D. Ind. 2000).

124. Owen v. Owen, 500 U.S. 305, 309–12 (1991). *See* discussion *supra* note 85.

125. *Id.* at 309–12. Importantly, the issue before the Court in *Owen* was not the constitutionality of the opt-out provision, so these statements are not likely binding.

126. *In re* Cross, 255 B.R. at 34–35.

127. *Id.*

128. *Id.* at 33–36 (holding that Indiana's bankruptcy specific exemption was void on

just another example of how a state's exemption scheme may frustrate the purpose of section 522, rendering it preempted.[129]

IV. EXEMPTING THE EARNED INCOME CREDIT IS BOTH CONSTITUTIONAL AND GOOD POLICY

A. Kan. Stat. Ann. § 60-2315 Passes Constitutional Tests

The Earned Income Tax Credit exemption does not run into the same constitutional problems as the typical bankruptcy-specific exemption for two reasons. First, it is possible that the Earned Income Tax Credit is "public assistance" and is therefore already exempt by Kansas' law from execution by creditors outside of bankruptcy.[130] As part of its federal exemption scheme, Congress allows debtors the "right to receive" certain public assistance benefits, including unemployment compensation and Social Security benefits in section 522(d)(10)(A).[131] Many states, including Kansas,[132] have enacted similarly worded exemption statutes to protect certain payments of "public assistance."[133] Whether these exemptions of "local public assistance benefits" include the right to receive the Earned Income Tax Credit has been reviewed by a number of bankruptcy courts.[134] Some have found that the Earned Income Tax Credit is a form of public assistance, and that legislators likely intended the funds from the credit to go to the hands of a debtor, as opposed to the debtor's bankruptcy estate.[135] Other courts, including the Tenth Circuit Court of Appeals and the Tenth Circuit Bankruptcy Appellate Panel, have found instead that the credit is more analogous to a debtor's tax refund, which becomes property of the bankruptcy estate when a debtor who is entitled to receive the credit files for bankruptcy.[136] Whether the Earned Income Tax Credit is within a state's exemption for "public assistance" may depend on the purpose and history of the credit as a replacement program for traditional

preemption grounds, using the preemption language in Perez v. Campbell, 402 U.S. 637, 644 (1971)).

129. *Id.* at 35.

130. KAN. STAT. ANN. § 60-2313(a)(2). For further explanation of the arguments for and against classifying the Earned Income Tax Credit as "public assistance" for exemption purposes, *see generally* Jennifer E. Spreng, *When 'Welfare' Becomes 'Work Support': Exempting Earned Income Tax Credit Payments in Consumer Bankruptcy*, 78 AM. BANKR. L.J. 279 (2004).

131. 11 U.S.C. § 522(d)(10)(A) (2006).

132. *See* KAN. STAT. ANN. § 60-2313(a)(2) (2003); KAN. STAT. ANN. § 39-717(c) (2003).

133. *See, e.g.*, ALA. CODE § 38-4-8 (1975) ("All amounts paid or payable as public assistance to needy persons shall be exempt . . . and in the case of bankruptcy, shall not pass to the trustee or other person acting on behalf of the creditors of the recipient of public assistance.").

134. *See, e.g.*, *In re* Brasher, 253 B.R. 484, 486–87 (M.D. Ala. 2000).

135. *See In re* Longstreet, 246 B.R. 611 (Bankr. S.D. Iowa 2000); *see also In re* Brown, 186 B.R. 224 (Bankr. W.D. Ky. 1995).

136. *See, e.g.*, *In re* Whitmer, 228 B.R. 841, 844 (Bankr. W.D. Va. 1998); *see also In re* Montgomery, 224 F.3d 1193, 1195 (10th Cir. 2000); *In re* Trudeau, 237 B.R. 803, 807 (10th Cir. B.A.P. 1999).

welfare payments and the particular wording of the state statute or statutes in question.[137]

A second reason that Kan. Stat. Ann. § 60-2315 avoids the constitutional issues faced by most state bankruptcy-specific exemption statutes is that it does not alter the outcome between a creditor trying to seize the Earned Income Credit from a debtor out of bankruptcy and the trustee attempting to seize the Earned Income Tax Credit from a debtor in bankruptcy.[138] This outcome was discussed by Judge Nugent in a recent case brought by several Kansas trustees challenging the validity of the state's bankruptcy-specific exemption statute.[139] The statute exempts the debtor's "right to receive" the Earned Income Credit, and the debtor's "right to receive" the Earned Income Credit is already unavailable to creditors looking to obtain the credit; the creditor has no rights to the credit before it reaches the hands of the debtor.[140] "A creditor of a non-bankruptcy Kansas debtor outside of bankruptcy could only attach the proceeds of the EIC in the hands of the debtor once she had received them."[141] Such a creditor cannot garnish the IRS or Kansas Department of Revenue.[142] This consistency in treatment of the exempted property both in and outside of bankruptcy is key. The uniformity test of the Bankruptcy Clause and preemption issues arising from conflict with the Bankruptcy Code that plague many bankruptcy-specific statutes do not invalidate a state bankruptcy-specific exemption that has the same result for a debtor and creditor relationship both before and after a bankruptcy filing.[143]

B. Why Congress and Other States Should Follow Kansas' Lead and Exempt the EITC.

The Earned Income Tax Credit is widely regarded as "the largest federal anti-poverty program in the Untied States."[144] In passing the exemption in Kan. Stat. Ann. § 60-2315, the Kansas legislature stayed well within the limits

137. Spreng, *supra* note 130, at 314–34.

138. Recall, this is the rule provided for uniformity in Hanover Nat'l Bank v. Moyses. *See also In re* Earned Income Tax Credit Exemption Constitutional Challenge Cases, 477 B.R. 791, 800 (2012).

139. *In re Earned Income Tax Credit*, 477 B.R. at 800.

140. *See id.*; *see also* Brockelman v. Brockelman, 478 F. Supp. 141 (D. Kan. 1979).

141. *In re Earned Income Tax Credit*, 477 B.R. at 800.

142. *Id.* ("[I]t is by no means clear that a Kansas creditor of a non-bankrupt debtor would receive any more of the EIC benefit than would a trustee . . . . Thus, unlike [other bankruptcy-specific exemptions], these trustees will receive exactly what a creditor outside of bankruptcy in Kansas would receive from the debtor's 'right to receive' the EIC: nothing. Geographical uniformity as articulated in *Moyses* is thus served."); *see also Brockelman*, 478 F. Supp. at 143–45.

143. *See, e.g.*, 11 U.S.C. § 303; 11 U.S.C. § 544; *see also In re* Westby, 473 B.R. 392, 416–19 (Bankr. D. Kan. 2012), *aff'd*, 486 B.R. 509 (10th Cir. B.A.P. 2013) (discussing Trustees' claims that § 60-2315 conflicts with particular provisions of the Bankruptcy Code).

144. *See In re* Murray, 506 B.R. 129, 134 (B.A.P. 10th Cir. 2014); *see also* Sara S. Greene, *The Broken Safety Net: A Study of Earned Income Tax Credit Recipients and a Proposal for Repair*, 88 N.Y.U. L. REV. 515, 515–88 (2013).

of Congressional intent when Congress decided to leave room for the states to opt-out of the federal exemption scheme and pass their own exemption statutes based on local needs and goals.[145] Although the federal exemption system does not expressly exempt Earned Income Credits, Kansas has realized the importance of the exemption for a particular class of debtors, and has legislated to protect this valuable asset from bankruptcy trustees and creditors, ensuring it goes to the eligible families that are in financial need.[146] After the enactment of Kan. Stat. Ann. 60-2315 in 2011, several Kansas trustees brought challenges to the statute's constitutionality.[147] So far, Kansas courts have agreed in all cases to date that the state's bankruptcy-specific exemption of the Earned Income Tax Credit is constitutional.[148]

The Kansas Legislature recognized the Earned Income Tax Credit as a form of public assistance that would serve as a work-encouraging replacement of the traditional welfare system. It sought to ensure that those families that needed money most and those that work and earn an income retain the right to receive the money from the tax credit.[149] Further, the Earned Income Tax Credit can amount to up to one-fourth of an eligible recipient's total annual income.[150] Such a dramatic impact on needy families should not be ignored. Both Congress and those states that have not yet done so,[151] should enact an exemption of the Earned Income Tax Credit to keep this payment of public assistance where it belongs: with working families who need it.

V. CONCLUSION

Due to the importance of the Earned Income Tax Credit for families in Kansas, the Kansas Legislature passed Kan. Stat. Ann. § 60-2315, exempting this tax credit from the bankruptcy estate for Kansans in bankruptcy. Although bankruptcy-specific exemption statutes in other states have inspired countless challenges by trustees in the last couple of decades, an exemption of the Earned Income Tax Credit does not encounter the same constitutional issues of uniformity and preemption.

The most recent Supreme Court cases addressing the uniformity requirement of the Bankruptcy Clause have interpreted the Framers' call for

145. *See* discussion *supra* Part III.

146. *Minutes*, *supra* note 13.

147. KHI News Service, *Court Upholds Bankruptcy Exemption For Earned Income Tax Credit*, KAN. HEALTH INST. (April 6, 2012), http://www.khi.org/news/2012/apr/06/court-upholds-bankruptcy-exemption-earned-income-t/.

148. *See, e.g.*, *In re* Westby, 473 B.R. 392, 422 (Bankr. D. Kan. 2012), *aff'd*, 486 B.R. 509 (10th Cir. B.A.P. 2013); *In re* Earned Income Tax Credit, 477 B.R. 791, 807 (Bankr. D. Kan. 2012).

149. *In re Earned Income Tax Credit*, 477 B.R. at 794.

150. Spreng, *supra* note 130, at 283–84.

151. Those states are Colorado, Oregon, Florida and Kansas. COLO. REV. STAT. § 13-54-102(1)(o) (2004); FLA. STAT. § 222.25 (2004); OR. REV. STAT. § 18.345(1)(n) (2003); KAN. STAT. ANN. § 60-2315 (2011).

"uniform laws" as a minimal standard. However, even if one looks at the clearer, stricter standard articulated in *Hanover Nat'l Bank v. Moyses*, the bankruptcy-specific exemption of the Earned Income Tax Credit passes the test, because a creditor cannot expect to execute on the tax credit of a debtor either in or outside of bankruptcy. Further, the Earned Income Credit bankruptcy-specific exemption is not preempted because it does not conflict with any provisions of the United States Bankruptcy Code. In support of these conclusions, Kansas courts have reviewed the constitutionality of this statute and held that the exemption of the Earned Income Tax Credit for debtors in bankruptcy is constitutional.[152] Those states that have not yet enacted specific statutes exempting the Earned Income Tax Credit should follow Kansas' lead, confident that their enactments would pass constitutional scrutiny.

152. *In re* Westby, 473 B.R. 392, 421 (Bankr. D. Kan. 2012), *aff'd*, 486 B.R. 509 (10th Cir. B.A.P. 2013); *In re Earned Income Tax Credit*, 477 B.R. at 800.