

# THE FUTURE OF BANKRUPTCY EXEMPTIONS IN NORTH CAROLINA: EXPANDING DEBTORS' ABILITY TO EXEMPT THE EITC

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## INTRODUCTION

The North Carolina legislature has the opportunity to improve the lives of debtors in this state. To reflect the changing opinions towards bankruptcy, North Carolina is equipped to create a new state exemptions statute for the first time in over twenty years. In fact, the United States Bankruptcy Court for the Middle District of North Carolina suggests that “such concerns *must* be addressed by the North Carolina General Assembly.”<sup>1</sup>

In bankruptcy proceedings, a debtor’s right to exempt certain assets from the estate is deemed necessary for the debtor to support their family and ensure financial rehabilitation.<sup>2</sup> Debtors may exempt the value of their homes, vehicles, and even personal property such as clothes or jewelry.<sup>3</sup> Some states have taken a broader approach to what a debtor may exempt by allowing a debtor

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1. *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1, \*9 (Bankr. M.D.N.C. Aug. 9, 2024) (emphasis added) (“While the Court is sympathetic to the Debtors’ broader policy arguments regarding the importance of the EIC or ACTC to low-income workers and their children, such concerns must be addressed by the North Carolina General Assembly.”).

2. Douglas E. Deutsch, Note, *Exemption Reform: Examining the Proposals*, 3 AM. BANKR. INST. L. REV. 207, 207 (1995).

3. *Id.* at 208.

to exempt public assistance, like the Earned Income Tax Credit (“EITC”).<sup>4</sup>

States’ ability to create exemptions in bankruptcy is based on the presumption that states are best suited to define property rights.<sup>5</sup> However, some commentators suggest that the expansion of state exemptions disadvantages creditors, resulting in higher interest rates for consumers, thus creating more harm than good.<sup>6</sup> However, the expansion of state exemptions works to keep states in touch with changing attitudes towards bankruptcy, and ensures debtors truly have a “fresh start.”

Part I of this Note will discuss the guiding bankruptcy policies at work in the background of all bankruptcy proceedings. Part II of this Note will describe the history and purpose of the EITC, and how it can be exempt in bankruptcy. Part III of this Note will discuss *In re Quevedo*, a recent Middle District of North Carolina opinion, and what influence it may have on the North Carolina legislature.

Finally, Part IV of this Note will analyze the benefits and downfalls of state exemptions for the debtor, society, and the bankruptcy system. This Note argues that the North Carolina legislature should amend N.C. Gen. Stat. § 1C-1601 to create a provision that exempts “[t]he debtor’s right to receive an earned income tax credit under the federal tax laws and any moneys that are traceable to a payment of an earned income tax credit under the federal tax laws.”<sup>7</sup> This would thereby create an explicit exemption for federal earned income tax credits. By doing so, the North Carolina legislature is creating change that is reflective of a general shift in attitudes towards bankruptcy and feelings towards “dishonest” debtors.

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4. See *In re Quevedo*, 2024 WL 3754885, at \*8.

5. See Tristan G. Axelrod, *Defending State Exemptions in Bankruptcy*, 27 LOY. CONSUMER L. REV. 284, 285 (2015) (explaining the bankruptcy system is based on “centuries-old traditions” that state law is more competent in defining property rights).

6. See, e.g., Deutsch, *supra* note 2, at 208; Richard Posner, *Posner [Chicago]: The Bankruptcy Reform Act*, JURISTNEWS (Mar. 27, 2005, at 7:11 CT), <https://www.jurist.org/commentary/2005/03/posner-chicago-bankruptcy-reform-act> (“[T]he most important effect that [BAPCPA] is likely to have . . . is to reduce interest rates.”).

7. OR. REV. STAT. § 18.345(1)(n) (2025).

## BACKGROUND

## I. THE BANKRUPTCY “ESTATE” AND A DEBTOR’S “FRESH START”

When a debtor files a bankruptcy petition, the Bankruptcy Code creates authority for “all legal or equitable interests”<sup>8</sup> of the debtor to be preserved together in “a separate legal entity . . . .”<sup>9</sup> This creates what is known as the bankruptcy estate, which is used to “pay[] distributions to creditors therefrom.”<sup>10</sup> Section 541 prescribes a broad scope to determine what is part of the estate.<sup>11</sup> Generally, property of the estate includes “all kinds of property, tangible and intangible, causes of action, and all other forms of property.”<sup>12</sup> The Bankruptcy Code determines what is property of the estate,<sup>13</sup> but states are left to determine what interest a debtor has in a specific property.<sup>14</sup> Courts often turn to the relevant state’s property, marriage, or tax laws to determine this interest.<sup>15</sup> Whether an asset is exempt turns on the debtor’s property interests; thus, state property law should control.<sup>16</sup> The type of property system the state has upon dissolution of marriage may also be used to guide a court’s analysis;<sup>17</sup> only nine states are community property states, while the other forty-one states, North Carolina included, are common law states.<sup>18</sup>

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8. 11 U.S.C. § 541(a)(1).

9. Axelrod, *supra* note 5, at 289.

10. *Id.*

11. 5 COLLIER ON BANKRUPTCY ¶ 541.03 (Richard Levin & Henry J. Sommer eds., 16th ed. 2026).

12. *Id.*

13. *See* 11 U.S.C. § 541.

14. *See id.*; *see also* *Butner v. United States*, 440 U.S. 48, 54–55 (1979) (“Congress has generally left the determination of property rights in the assets of a bankrupt’s estate to state law. . . . Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.”).

15. *See generally In re McInerney*, 609 B.R. 497, 503 (Bankr. N.D. Ill. 2019) (explaining that bankruptcy courts turn to various areas of law when assessing parties’ property rights).

16. *Id.*

17. *See, e.g., Butner*, 440 U.S. at 54–55; *In re Carlson*, 394 B.R. 491, 495 (B.A.P. 8th Cir. 2008) (noting that a state being a community property or tenancy by the entirety state may lead courts to cite other areas of law, like marriage dissolution, compared to non-community property systems).

18. Tanza Loudenback & Jake Safane, *Community Property States: Understanding Marital Property Rights*, BUS. INSIDER (Oct. 31, 2024, at 12:39 ET), <https://www.businessinsider.com/personal-finance/investing/which-states-are-community-property-states-in-divorce>.

A. *Using Exemptions to Keep Certain Assets Out of the Estate*

Individuals may file for bankruptcy with their spouses, thereby becoming joint debtors, but they each still maintain separate estates.<sup>19</sup> In an effort to keep some assets from the reach of creditors, debtors have the ability to claim some assets as exempt from the estate.<sup>20</sup> Just as joint debtors maintain a separate estate, each qualifies for their own exemptions.<sup>21</sup> For individuals who find themselves in a position where they need to file for bankruptcy, “the right to protect property ‘exempt’ from turnover in bankruptcy may be second in importance only to the right to file at all.”<sup>22</sup>

The Federal Bankruptcy Code provides a list of exemptions that the debtor may use.<sup>23</sup> For example, New Mexico gives debtors the option to choose between the federal list of exemptions or the state’s list of exemptions.<sup>24</sup> However, states may instead choose to “opt out” of the federal exemptions.<sup>25</sup> These thirty “opt-out” states, North Carolina included, require debtors to follow the state exemptions only.<sup>26</sup>

B. *A Fresh Start*

There are several different social policies for having exemptions in place. Alan Resnick, a former bankruptcy professor at the Maurice A. Deane School of Law at Hofstra University, describes five social policies that are furthered by allowing exemptions:

- (1) providing property needed for the debtor’s physical survival;
- (2) protecting the debtor’s dignity, culture and religious identity;

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19. 11 U.S.C. § 302(a).

20. *Id.* § 522(b)(1); see Deutsch, *supra* note 2, at 208 (“[E]xempt property is excluded from the pool of assets distributed in satisfaction of debtor’s obligations.”).

21. 11 U.S.C. § 522(m); see, e.g., Cheeseman v. Nachman, 656 F.2d 60, 62 (4th Cir. 1981) (“Section 522(m) permits each debtor in a joint case to exempt property from his estate.”).

22. Jennifer E. Spreng, *When “Welfare” Becomes “Work Support”: Exempting Earned Income Tax Credit Payments in Consumer Bankruptcy*, 78 AM. BANKR. L.J. 279, 301 (2004).

23. See 11 U.S.C. § 522(d) (listing the federal bankruptcy exemptions); *id.* § 522(b)(1) (describing how debtors may choose between the federal or state exemptions, if the state allows it).

24. Cara O’Neill, *Filing for Bankruptcy in New Mexico (NM)*, Nolo (Nov. 13, 2025), <https://www.nolo.com/legal-encyclopedia/how-to-file-bankruptcy-in-new-mexico.html>.

25. See, e.g., 11 U.S.C. § 522(b)(1) (allowing states to “opt-out” of federal exemptions).

26. *Bankruptcy Exemption Laws: 50-State Survey*, JUSTIA (Sep. 2022), <https://www.justia.com/bankruptcy/exemptions/bankruptcy-exemptions-50-state-survey>; see N.C. GEN. STAT. ANN. § 1C-1601(f) (West 2013) (stating North Carolina state exemptions apply instead of the federal exemptions).

- (3) ensuring the financial rehabilitation of the debtor;
- (4) ensuring that the debtor's family does not become impoverished; and
- (5) shifting the burden of providing for the debtor and family from society to the creditor.<sup>27</sup>

These social policies support the notion that the fundamental goal of bankruptcy is to give debtors a “fresh start.”<sup>28</sup> A fresh start, in the bankruptcy context, allows debtors to free themselves from “burdensome debts”<sup>29</sup> and start anew. The Supreme Court has emphasized the importance of this goal: “[I]t gives to the honest but unfortunate debtor . . . a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt.”<sup>30</sup> Commentators suggest that some state exemptions reflect the importance of a fresh start for debtors; others urge that some exemptions do little to advance this goal.<sup>31</sup> The commentators in the latter group argue that some states prioritize paying creditors by allowing such small exemption amounts that the exempting effects are insignificant for debtors.<sup>32</sup> While a debtor's fresh start is fundamental to the bankruptcy system, it does not go unchecked. Rather, the policy reasons behind the debtor's fresh start are balanced against the best interests of the estate, and, thus,

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27. Deutsch, *supra* note 2, at 207–08 (citing Alan N. Resnick, *Prudent Planning or Fraudulent Transfer? The Use of Nonexempt Assets to Purchase or Improve Exempt Property on the Eve of Bankruptcy*, 31 RUTGERS L. REV. 615, 621 (1978)).

28. *Process - Bankruptcy Basics*, U.S. CTS., <https://www.uscourts.gov/court-programs/bankruptcy/bankruptcy-basics/process-bankruptcy-basics> (last visited Oct. 18, 2025).

29. *Id.*

30. *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934) (citing *Stellwagen v. Clum*, 245 U.S. 605, 617 (1918)); *see also Williams v. U.S. Fidelity & Guaranty Co.*, 236 U.S. 549, 554 (“One of the primary purposes of the Bankruptcy Act is to ‘relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.’”).

31. *Compare* MICHAEL BEST & CAROLYN CARTER, NAT’L CONSUMER L. CTR., NO FRESH START 2023: WILL STATES LET DEBT COLLECTORS PUSH FAMILIES INTO POVERTY AS ECONOMIC UNCERTAINTY LOOMS? 4 (2023), [https://www.nclc.org/wp-content/uploads/2024/03/2023\\_Report\\_No-Fresh-Start.pdf](https://www.nclc.org/wp-content/uploads/2024/03/2023_Report_No-Fresh-Start.pdf) (explaining states like New Mexico, North Dakota, and Washington have recently moved from a grade of C to B for providing more protections to debtors through increasing exemptions amounts or types as compiled in a report by the National Consumer Law Center), *with id.* (explaining states like Georgia, Kentucky, Michigan, New Jersey, and Utah are the worst “rated” states for providing protections to debtors as compiled in a report by the National Consumer Law Center). This report goes on to say that the exemption laws in these states show indifference to debtors by allowing creditors to seize assets like wages, the home, the family car, and household goods.

32. *See Axelrod, supra* note 5, at 287 n.12 (listing several sources that have analyzed exemption statutes in multiple states with dollar limits so low that assets cannot be adequately protected to any significant degree).

creditors.<sup>33</sup> The limiting of debtors' access to exemptions, by setting dollar caps or disallowing certain items from being exempt, balances these conflicting interests.<sup>34</sup>

### C. Criticisms of Exemptions

Those against increasing the types or amount of exemptions argue that creditors are injured and consumers bear the brunt of this injury.<sup>35</sup> While exemptions do prevent a creditor's total recovery,<sup>36</sup> some argue that these losses are then "passed on to other consumers via higher interest rates and lower credit availability."<sup>37</sup> Most of the literature on this phenomenon was written in the mid-to-late 1990s.<sup>38</sup> However, some research from the same time period suggests that high levels of exemptions do not increase mortgage rates.<sup>39</sup> In fact, research from the mid-2000s attempted to settle these conflicting results and found that exemptions should not, and do not, play a role in credit-granting decisions or credit availability.<sup>40</sup>

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33. See, e.g., 11 U.S.C. § 704 (explaining that the trustee must perform two essential tasks: first, ensure debtor has a "fresh start," and second, maximize the values of assets for the estate and to pay creditors); see also Deutsch, *supra* note 2, at 213 (suggesting this equitable balance between the interests of the debtor and creditors "should be used to determine the propriety of a given exemption").

34. Deutsch, *supra* note 2, at 212-13 ("Since exemptions are not without limitation, there is some implicit recognition that interests other than a debtor's fresh start are to be considered in determining exemption policy. The most important interests are, naturally, those of the creditor and consumer. If discharge were granted with all, or almost all assets exempted, the creditor would be forced to pass on enormous costs to the consuming public.").

35. *Id.* at 208-09.

36. *Id.* at 208.

37. *Id.*; see, e.g., *id.* at 208 n.11 (suggesting these losses from not making a total recovery may be passed on to others through higher costs).

38. See, e.g., Deutsch, *supra* note 2 (arguing increased exemptions will lead to higher interest rates for borrowers); Reint Gropp, John Karl Scholz & Michelle J. White, *Personal Bankruptcy and Credit Supply and Demand*, 112 Q. J. ECON. 217, 220 (1997) (using data from 1983 to suggest that "interest rates on automobile loans are higher for low-asset households in states with higher bankruptcy exemptions . . .").

39. Jeremy Berkowitz & Richard Hynes, *Bankruptcy Exemptions and the Market for Mortgage Loans*, 42 U. CHI. J. L. & ECON. 809, 809 (1999) ("Using both household-level data and state-level data, we show that in the 1990s high exemption levels have not tended to increase mortgage rates or increase the probability of being denied a mortgage.").

40. See Souphala Chomsisengphet & Ronel Elul, *Bankruptcy Exemptions, Credit History, and the Mortgage Market*, 59 J. OF URB. ECON. 171, 172 (2006) ("Our theoretical predictions and empirical results also stand in contrast to recent work on the effect of bankruptcy exemptions on the availability of mortgage credit, in particular Berkowitz and Hynes [] and Lin and White[] . . . While the previous literature models exemptions as directly affecting the mortgage market, we argue that they are actually irrelevant to the mortgage underwriting decision.").

Critics also argue that some exemptions are not strict enough, which encourages abuse by debtors.<sup>41</sup> The passing of the Bankruptcy Abuse Prevention and Consumer Protection Act (“BAPCPA”) of 2005 seemed to indicate that these worries were more widespread than had previously been understood.<sup>42</sup> Commentators have criticized BAPCPA for misdirecting reform towards a non-issue;<sup>43</sup> meanwhile, there has been no concerning statistical evidence that debtors abuse bankruptcy at all.<sup>44</sup> Rather, some in the bankruptcy world believed the more pressing issue was the potentially negative effects of BAPCPA for women and children.<sup>45</sup> For example, Massachusetts senator and bankruptcy expert, Elizabeth Warren, argued that the proposed legislation would prioritize the rights of institutional lenders over mothers in the collection of child support payments.<sup>46</sup>

## II. EITC AND HOW IT HELPS DEBTORS HAVE A FRESH START

As previously highlighted, debtors utilize exemptions to protect assets from the reach of creditors.<sup>47</sup> These various assets are seen as necessary for the debtor to maintain economic security and general well-being.<sup>48</sup> The types and amounts of assets that could be exempt have varied throughout time. In the early years of the United States

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41. See Axelrod, *supra* note 5, at 286–87 (explaining that this is a common complaint by scholars and creditors’ lobbyists). Yet, some scholars speak overly broad about these debtor “abuses” without a specific account of how often this abuse happens. See, e.g., Deutsch, *supra* note 2, at 229 (“Almost all of the exemption reform proposals would help curb some form of bankruptcy abuse.”).

42. See H.R. REP. NO. 109-31, at 2–8 (2005) (explaining how this act reforms bankruptcy practices and standards with a lens towards targeting abuse of the system).

43. See Melissa B. Jacoby, *Negotiating Bankruptcy Legislation Through the News Media*, 41 HOUS. L. REV. 1091, 1132 (2004) (describing the news coverage at the time by the *New York Times* as being very critical of the reform because “the bill inflexibly ‘cracks down’ on ordinary debtors but does ‘next to nothing’ about the bankruptcies of Burt Reynolds and Bowie Kuhn. . . . [T]he *New York Times* distinguished the bill’s gentle treatment of the ‘well heeled’ from its harsh treatment of ‘unsophisticated debtors.’”).

44. Axelrod, *supra* note 5, at 324 (citing multiple studies that showed there is “no statistically significant abuse of bankruptcy and exemption laws by any citizens, rich or poor”); see generally *id.* at 308 n.141 (“More cynically, one might argue that lenders saw no real risk of abuse; rather, that they acknowledged bankruptcy filings as profit loss and exercised their lobbying power to maximize profit.”).

45. See, e.g., Jacoby, *supra* note 43, at 1136 (describing how media coverage prior to 2005 began framing bankruptcy issues as women’s and children’s issues).

46. Elizabeth Warren, Editorial, *Bankrupt? Pay Your Child Support First*, N.Y. TIMES, Apr. 27, 1998, at A15.

47. Deutsch, *supra* note 2, at 207.

48. See Axelrod, *supra* note 5, at 306 (explaining that exempting these assets protects a debtor’s “economic and social life”).

bankruptcy system, exempt items included “small value items, like clothes, and household and kitchen furniture.”<sup>49</sup> Now, exempt assets could include the value of a house, life insurance, alimony payments, and, in a few states, wages.<sup>50</sup> Exempting more assets and increasing exemption values signifies a shift in bankruptcy practice to reflect the increasingly difficult financial situation that modern debtors find themselves in.<sup>51</sup> This shift is evidenced by the fact that “the vast majority of bankruptcy filings were by middle and lower-class families unlikely to own real estate free of significant mortgage obligations.”<sup>52</sup>

Enacted in 1975, the EITC originated in the tax system as a public benefit received in the form of a “refundable” tax credit.<sup>53</sup> The refundable nature of the EITC means “if a taxpayer’s EITC is greater than what they owe in income taxes, they can receive the difference [] as a tax refund . . . .”<sup>54</sup> The credit was founded as temporary relief during a time of high inflation, encouraging the government to act to support struggling families.<sup>55</sup> Although originally intended to be a temporary measure, the program proved necessary and has remained in place as an essential piece to the “work support system.”<sup>56</sup> These targeted payments differ from other federal programs, which provide public benefits for families with little to no income, because receiving the EITC is contingent upon earned income from work.<sup>57</sup> Now, the established role of the program is “to provide benefits from the public to poor families in order to fight poverty in ways that will create incentives for at least one parent in those families to earn income through work and minimize disincentives to work.”<sup>58</sup>

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49. Deutsch, *supra* note 2, at 208.

50. *Id.*

51. See, e.g., BEST & CARTER, *supra* note 31, at 42 (“The growing wealth gap, the high volume of collection lawsuits filed around the country, and the soaring costs of necessities are all straining families to the breaking point and will make them increasingly vulnerable to seizure of essential wages and property.”).

52. Axelrod, *supra* note 5, at 324–25.

53. Tax Reduction Act of 1975, Pub. L. No. 94-12, 89 Stat. 26 (codified as amended in scattered sections of 26 U.S.C.); see Spreng, *supra* note 22, at 281–82 (explaining the origins of the EITC).

54. MARGOT L. CRANDALL-HOLLYCK ET AL., CONG. RSCH. SERV., R43805, THE EARNED INCOME TAX CREDIT (EITC): HOW IT WORKS AND WHO RECEIVES IT 12 (2023).

55. See *id.* at 15 (explaining the EITC’s initial, temporary status); see also Spreng, *supra* note 22, at 282 (stating that families in the 1970s were struggling with “rising food and energy prices”).

56. Spreng, *supra* note 22, at 282.

57. *Id.* at 281.

58. *Id.* at 282.

The EITC is intended to assist low-income workers and their families, usually those with children.<sup>59</sup> However, even individuals without qualifying children may receive the credit, and “taxpayers with children may receive the EITC even with income well above the poverty level.”<sup>60</sup> In line with its intended purpose, “the largest EITC benefits are focused on low-income earners near the poverty line . . .”<sup>61</sup> In 2024, census data showed that EITC benefits “lifted about 4.4 million people above the poverty line, including 2.3 million children . . .”<sup>62</sup> In the taxable year 2022, a family with children receiving an average EITC of \$3,338<sup>63</sup> was likely to spend most of the money on basic necessities, like food.<sup>64</sup>

Courts generally hold that tax refunds are the property of the estate;<sup>65</sup> likewise, earned income and child tax credits are also included in the estate.<sup>66</sup> The treatment of whether these tax credits count as exempt property in bankruptcy proceedings varies largely by the type of tax credit, the state, the court, and the applicable exemption.<sup>67</sup> Some scholars urge state legislatures to enact broad

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59. See CRANDALL-HOLLICK ET AL., *supra* note 54, at 1.

60. *Id.* at 21 (“When filing taxes for 2025 (due in April 2026), working families with children that have annual incomes below about \$50,434 to \$68,675 (depending on marital status and number of dependent children) may be eligible for the federal EITC.”)

61. *Id.* at 22.

62. CTR. ON BUDGET & POL’Y PRIORITIES, THE EARNED INCOME TAX CREDIT 2 (2025), <https://www.cbpp.org/sites/default/files/atoms/files/policybasics-eitc.pdf>.

63. *Id.* at 1.

64. See SAM WAXMAN, ARLOC SHERMAN & KRIS COX, CTR. ON BUDGET & POL’Y PRIORITIES, INCOME SUPPORT ASSOCIATED WITH IMPROVED HEALTH OUTCOMES FOR CHILDREN, MANY STUDIES SHOW: REFUNDABLE TAX CREDITS AMONG PROGRAMS THAT BOOST INCOME 5 (2021), <https://www.cbpp.org/sites/default/files/5-27-21tax.pdf> (“Another [study] reviewed how families spend their once-yearly EITC refunds, finding that households eligible for the credit spent more on healthy items including fresh fruit and vegetables, meat and poultry, and dairy products during the months when most refunds are paid.”)

65. See, e.g., *Kokoszka v. Belford*, 417 U.S. 642, 648 (1974) (holding the income tax refund is property of the bankruptcy estate).

66. See, e.g., *Johnston v. Hazlett* (*In re Johnston*), 209 F.3d 611, 613 (6th Cir. 2000) (holding the earned income credit of the debtor was properly decided as property of the bankruptcy estate); see also *Wood v. Jones* (*In re Montgomery*), 224 F.3d 1193, 1195 (10th Cir. 2000) (“Given that EICs are to be treated as tax refunds, and that contingent interests are to be included in the bankruptcy estate, we agree with the BAP and the overwhelming weight of authority that a debtor’s EIC for a tax year . . . is property of the estate . . .”); but see *BEST & CARTER*, *supra* note 31, at 44 (providing their support for “federal safety net payments” to be excluded from the bankruptcy estate as a whole).

67. Compare *In re Hardy*, 787 F.3d 1189, 1193 (8th Cir. 2015) (allowing ACTC to be exempt under a Missouri “public assistance benefits” exemption), and *In re Murphy*, 99 B.R. 370, 371 (Bankr. S.D. Ohio 1989) (finding the EITC exempt under an Ohio “poor relief payments” exemption statute), with *In re Rutter*, 204 B.R. 57 (Bankr. D. Or. 1997) (holding EITC was not public-assistance benefits under an Oregon law), and *In re Arthur*, No. 10-

“public assistance” exemption statutes, arguing the EITC would fit squarely within the definition of public assistance.<sup>68</sup> Meanwhile, some state legislatures have enacted statutes that explicitly exempt the EITC.<sup>69</sup> Courts have generally urged the legislature to weigh in on such determinations, one way or another.<sup>70</sup>

### III. AN ISSUE OF FIRST IMPRESSION

In 2024, the United States Bankruptcy Court for the Middle District of North Carolina decided a case, *In re Quevedo*, that could persuade the North Carolina legislature to rethink the state’s exemptions.<sup>71</sup> Upon filing a petition for Chapter 7 bankruptcy on November 14, 2023, the Debtors appropriately filed their 2023 joint federal and state income tax returns.<sup>72</sup> The Debtors’ refund was expected to be \$10,035 from the federal tax return and \$1,490 from the state tax return.<sup>73</sup> The male Debtor, being the sole income earner from employment with the U.S. military, had \$2,391 of the refund attributed to his W-2 federal withholdings.<sup>74</sup> The remaining refund amount is attributed to two federal tax credits due to the Debtors having two dependent children.<sup>75</sup> Specifically, \$4,444 is for the EITC, and \$3,200 was for the Additional Child Tax Credit (“ACTC”).<sup>76</sup> There was also a Virginia tax refund of \$1,490 from the male Debtor’s W-2 state withholdings.<sup>77</sup>

As a reflection of their 2023 federal and state tax refunds, each Debtor filed their own amended property exemptions.<sup>78</sup> In doing so, the Debtors attempted to claim their tax refunds as exempt under

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00463-als7, 2010 WL 4674450, at \*4 (Bankr. S.D. Iowa Oct. 20, 2010) (finding a scholarship credit not exempt under an Iowa public-assistance benefit exemption).

68. Spreng, *supra* note 22, at 312.

69. *Id.* at 302, 338 n.133.

70. See, e.g., *In re Medina*, No. 22-10233-j7, 2022 Bankr. LEXIS 3562, at \*14 (Bankr. D.N.M. Dec. 16, 2022) (“[T]he decision whether to permit a debtor in bankruptcy to protect a sufficient amount of her tax refunds/EITC to make such home repairs is a decision for the legislature.”).

71. *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1 (Bankr. M.D.N.C. Aug. 9, 2024).

72. Trustee’s Objection to Amended Exemptions at 1–2, *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1 (Bankr. M.D.N.C. Aug. 9, 2024), Dkt. No. 28.

73. *Id.* at 2.

74. *Id.*

75. *Id.*

76. *Id.* This Note does not address the ACTC or propose legislative amendments; future scholarship could expand on this issue.

77. *Id.*

78. Debtor’s Claim for Property Exemptions Amended, *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1 (Bankr. M.D.N.C. Aug. 9, 2024), Dkt. No. 25.

N.C. Gen. Stat. § 1C-1601(a)(12) or 1C-1601(a)(2).<sup>79</sup> The male Debtor could exempt only \$110.57 of the refund attributable to him; the female Debtor had \$4,995 available for her to exempt from the portion of the refund.<sup>80</sup>

This matter was brought before the Bankruptcy Court for the Middle District of North Carolina on the Chapter 7 Trustee's ("Trustee") objection<sup>81</sup> to the Debtors' filing of amended property exemptions for their Chapter 7 petition.<sup>82</sup> The Trustee's main objections were that the Debtors could not claim the 2023 tax refunds as exempt under N.C. Gen. Stat. § 1C-1601(a)(12), and only the male Debtor could claim a small portion of the refund as exempt under N.C. Gen. Stat. § 1C-1601(a)(2).<sup>83</sup> This would leave the female Debtor unable to claim any part of their joint tax refund as exempt.<sup>84</sup> Both issues presented in this case, "allocation of joint tax refunds and the potential exemptibility of those refunds as support payments under § 1C-1601(a)(12) . . ." were issues of first impression for this district.<sup>85</sup>

The first issue involves the court's interpretation of N.C. Gen. Stat. § 1C-1601(a)(12). Although the court construed the child support exemption statute in a way most favorable to the debtor,<sup>86</sup> it did not read the statute as so expansive to include the EITC.<sup>87</sup> For support, the court acknowledged that the Exemption Revision Committee, which was cited as being the main supporter of such

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79. Brief in Response to Trustee's Objection to Amended Exemptions at 1-2, *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1 (Bankr. M.D.N.C. Aug. 9, 2024), Dkt. No. 42; *see also* N.C. GEN. STAT. ANN. § 1C-1601(a)(12) (West 2013) (allowing debtors to exempt "[a]limony, support, separate maintenance, and child support payments . . ."); *id.* § 1C-1601(a)(2) (allowing debtors to exempt "[t]he debtor's aggregate interest in any property, not to exceed five thousand dollars (\$5,000) in value of any unused . . ." portion from their real property exemption).

80. Trustee's Objection to Amended Exemptions, *supra* note 72, at 3.

81. *Id.*; Debtor's Claim for Property Exemptions Amended, *supra* note 78.

82. Trustee's Objection to Amended Exemptions, *supra* note 72; Debtor's Claim for Property Exemptions Amended, *supra* note 78; *see also In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*2-3 (Bankr. M.D.N.C. Aug. 9, 2024) (describing the various arguments of the Trustee, the Debtors, and the Bankruptcy Administrator).

83. Trustee's Objection to Amended Exemptions, *supra* note 72, at 3.

84. *Id.*

85. *In re Quevedo*, 2024 WL 3754885, at \*3. The Fourth Circuit Court of Appeals has not previously considered this topic either.

86. *Id.* at \*6 ("In the case of ambiguity, '[i]f it is possible to construe an exemption statute in ways that are both favorable and unfavorable to a debtor, then the favorable method should be chosen.'") (quoting *In re Man*, 428 B.R. 644, 653 (Bankr. M.D.N.C. 2010)).

87. *Id.* at \*9 ("Based on the statute's language, construction, and the circumstances surrounding its adoption, the Court concludes that EIC and ACTC are not exempted from the claims of creditors as support payments under § 1C-1601(a)(12).")

legislation, “focused exclusively on child support and alimony in its commentary and specifically modeled the language of what became subdivision (12) on Oklahoma’s analogous statute . . . .”<sup>88</sup> Further, the court found Oklahoma had contemplated a similar case where that court was asked to determine if the child support statute could be read to include an earned income credit.<sup>89</sup> The District Court for the Northern District of Oklahoma similarly reasoned that “[o]nly by wrenching the term support wholly out of its statutory context is it possible to include federal income tax credits within its scope.”<sup>90</sup>

The second issue concerns the proper allocation of tax refunds between joint debtors under North Carolina’s wildcard exemption.<sup>91</sup> There are different approaches to deciding the proper ownership of tax refunds between debtors who jointly file their taxes. The Bankruptcy Administrator advocated for the “Separate Filings Rule,”<sup>92</sup> the Trustee argued for the “Withholding Rule,”<sup>93</sup> and the Debtors argued that the “50/50 Rule”<sup>94</sup> would result in the most equitable outcome for the female debtor.<sup>95</sup> The court found that the Separate Filings Rule would be “the proper method for allocating the 2023 state and federal tax refunds between the two Debtors in this

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88. *Id.* at \*8; *see also* 31 OKLA. STAT. § 1(19) (2024) (serving as the cited, model statute for which North Carolina adopted language from).

89. *In re Quevedo*, 2024 WL 3754885, at \*8 (citing *Kirtley v. George*, No. 97-CV-40-K(J), 1997 WL 33311019, at \*1, \*6 (N.D. Okla. Aug. 7, 1997)).

90. *Kirtley*, 1997 WL 33311019, at \*5 (quoting *In re Fraire*, 1997 WL 45465, at \*3 (D. Kan. Jan. 2, 1997)).

91. *In re Quevedo*, 2024 WL 3754885, at \*9 (summarizing case law that establishes tax refunds may be claimed as exempt under “wildcard” statutes).

92. Brief in Response to Trustee’s Objection to Amended Exemptions at 8, *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1 (Bankr. M.D.N.C. Aug. 9, 2024), Dkt. No. 42 (stating this rule determines how much of the tax return is attributable to each spouse, as if each had filed separately instead).

93. *In re McInerney*, 609 B.R. 497, 505 (Bankr. N.D. Ill. 2019) (“[T]he refund is allocated between spouses in proportion to their respective tax withholdings during the relevant tax year.”).

94. *Id.* at 507 (describing the rule as splitting a joint tax refund equally between the spouses).

95. *Compare In re Nevins*, 564 B.R. 151, 155 (Bankr. D.N.H. 2016) (noting that reliance on laws of marital dissolution and equitable distribution, of which the 50/50 Rule purports to represent, is misguided because they are misaligned with bankruptcy policies), *and In re Crowson*, 431 B.R. 484, 489 (B.A.P. 10th Cir. 2010) (finding that the Withholding Rule that was adopted by the BAP in *In re Klienfeldt* “is the appropriate method where a joint tax return consists *solely* of returns from withholdings made by one spouse and does not involve any tax credits or other credits” (emphasis added)), *with In re Duarte*, 492 B.R. 100, 109 (Bankr. E.D.N.Y. 2011) (clarifying that the Separate Filings Rule accurately protects the true legal and separate interests to the tax refund while taking into account income earned, credits, and taxes withheld).

joint case . . .”<sup>96</sup> Thus, the court also held that this method would be used in future cases when the parties cannot agree on the proper allocation of a joint tax refund.<sup>97</sup>

From an onlooker’s perspective, it would appear that this court was asked to read between the lines of statutes and step into the shoes of the North Carolina legislature to decide if a debtor could exempt an asset that was earned from being a hard-working individual with an income below, or near, the poverty line. As will be discussed in-depth, *infra*, this court prioritized North Carolina’s law of separate property interests in marriage and incorporation of “Internal Revenue Code sections into North Carolina tax law.”<sup>98</sup> The Separate Filings Rule is consistent with separate property interests, while also accounting for income earned, credits, and taxes withheld in a tax return.<sup>99</sup>

Beyond the scope of this Note, but worth mentioning, is the inherent contradiction in married filing jointly spouses having, by default, joint and several liability for a tax deficiency,<sup>100</sup> but the right to any overpayment in the form of a refund is not shared jointly in bankruptcy.<sup>101</sup> Specifically, bankruptcy courts have differed as to whether a non-income producing spouse would be entitled to a portion of a refund comprised of credits.<sup>102</sup> The policy concern that arises from such contradiction is the non-monetary contributions of the non-income-producing spouse being valued less than the other spouse’s earned income.<sup>103</sup> The underlying implication of this issue

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96. *In re Quevedo*, 2024 WL 3754885, at \*13.

97. *Id.*

98. *Id.* at \*11.

99. *In re Duarte*, 492 B.R. at 109.

100. See 26 U.S.C. § 6013(d)(3).

101. See, e.g., *In re Aldrich*, 250 B.R. 907, 912 (Bankr. W.D. Tenn. 2000) (“[T]he [non-earning] spouse’s liability would be joint in the event taxes were left unpaid. Thus, the right to a tax refund here should be joint.”); see also Response to Trustee’s Objection to Exemptions at 4, *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*1 (Bankr. M.D.N.C. Aug. 9, 2024) Dkt. No. 34 (“The Trustee has not explained why tax liabilities and tax refunds should be treated differently by this Court.”).

102. Compare *In re Griffin*, 1 B.R. 653 (M.D. Tenn. 1979) (denying the non-income producing wife a portion of the refund), and *In re Colbert*, 5 B.R. 646 (Bankr. S.D. Ohio 1980) (denying the non-income producing wife a portion of the refund), with *Hundley v. Marsh*, 459 Mass. 78 (2011) (permitting the non-income producing wife a portion of the refund).

103. See *Aldrich*, 250 B.R. at 912 (stating that it is not equitable to “completely ignore the substantial contributions of a non-income producing homemaker, who performs valuable but economically uncompensated services for the family”).

is that denying a portion of a refund to the “non-income producing homemaker” will continue disproportionately affecting women.<sup>104</sup>

In a similar case, the New Mexico Bankruptcy Court in *In re Medina* held that the debtor could not exempt the EITC under the New Mexico Public Assistance Act.<sup>105</sup> There was not a statute that explicitly exempted the EITC, and there were no other applicable exemptions.<sup>106</sup> The debtor in that case believed that her entire tax refund would be exempt, including the \$3,861 attributable to her EITC.<sup>107</sup> Preparing for the New Mexico summer heat, the debtor used her refund money to fix the “air conditioner and hot water heater” in the family home.<sup>108</sup> The debtor made an argument that she was spending the money on “reasonable and necessary expenses,” which should make it exempt.<sup>109</sup> With their sympathies, the court rejected this argument, and concluded that “the decision whether to permit a debtor in bankruptcy to protect a sufficient amount of her tax refunds/EITC to make such home repairs is a *decision for the legislature*.”<sup>110</sup>

#### IV. ARGUMENTS FOR EXEMPTING THE EITC IN NORTH CAROLINA

Lawmakers in North Carolina could help debtors have a legitimate “fresh start” in bankruptcy and resolve the issues described in Part I of this Note. Section A of this Part describes how exempting the EITC would comport with North Carolina state law and the legislature’s intent behind having exemptions in this state. Section B addresses the concerns with creating more exemptions, as described in Section C of Part I.

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104. See generally 26 U.S.C. § 6013(d)(3) (demonstrating that most cases analyze allocation of a refund for a non-income producing wife more often than a non-income producing husband); see also *supra* notes 71–85 and accompanying text (describing the main case of this Note that analyzed a non-income producing wife).

105. No. 22-10233-j7, 2022 Bankr. LEXIS 3562, at \*14 (Bankr. D.N.M. Dec. 16, 2022).

106. *Id.*

107. *Id.* at \*1–2.

108. *Id.* at \*3 (confirming that the debtor made the repairs by the end of April 2022).

109. *Id.* at \*15.

110. *Id.* (emphasis added).

A. *Creating an Exemption Statute for the EITC Aligns with North Carolina Law, Past Legislative Intent, and Values of Protecting Low-Income Families*

i. North Carolina Property Law Permits the EITC to be Exempt

As previously discussed, creating exemptions is a task largely undertaken by states.<sup>111</sup> This is due to state law defining the rights a debtor has in property that is exempt from the estate.<sup>112</sup>

North Carolina is a non-community property state, meaning “a spouse has no vested interest in property held by the other spouse until (1) the filing of a divorce action, or (2) the death of the other spouse.”<sup>113</sup> In marriage, North Carolina values the separate interests of spouses; upon dissolution of the marriage, North Carolina utilizes equitable distribution.<sup>114</sup> These values of separate property interests should also be upheld in bankruptcy proceedings where jointly filing spouses remain together.<sup>115</sup>

Courts have held that tax refunds and credits are property of the estate, and they can only be kept out of the estate through state exemptions.<sup>116</sup> As the Bankruptcy Court for the Middle District of North Carolina recently held, the EITC cannot be exempt under N.C. Gen. Stat. § 1C-1601(a)(12), or the child support exemption.<sup>117</sup> In North Carolina, the exemption statute currently most applicable to exempt the EITC is the wildcard exemption.<sup>118</sup> However, as exhibited by this recent case, joint debtors still face uncertainty as to whether

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111. See, e.g., 11 U.S.C. § 522(b)(1) (allowing states to “opt-out” of federal exemptions).

112. See *Butner v. U.S.*, 440 U.S. 48, 54–55 (1979) (“Congress has generally left the determination of property rights in the assets of a bankrupt’s estate to state law. . . . Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.”).

113. *Common-Law State*, BLACK’S LAW DICTIONARY (12th ed. 2024); but see *Community-Property State*, BLACK’S LAW DICTIONARY (12th ed. 2024) (defining this as “[a] state in which spouses hold property that is acquired during marriage . . . as community property”).

114. N.C. GEN. STAT. § 50-20(c) (2013).

115. See *In re Nevins*, 564 B.R. 151, 155 (Bankr. D.N.H. 2016) (explaining that “relying on marital dissolution concepts [is] at odds with policies underpinning the Bankruptcy Code”); see also *Hundley v. Marsh*, 459 Mass. 78, 84 (2011) (noting that policies behind equitable distribution in divorce proceedings do not align with policies behind allocation of property interests in bankruptcy).

116. *Supra* text accompanying note 20.

117. *In re Quevedo*, No. 23-80195, 2024 WL 3754885, at \*9 (Bankr. M.D.N.C. Aug. 9, 2024).

118. N.C. GEN. STAT. § 1C-1601(a)(2) (2013).

the full amount of the credit, as attributable to each debtor, may be exempt.<sup>119</sup>

ii. Allowing the EITC to be Exempt Comports with Past Legislative Intent

Faced with uncertainty in the already uncertain world of filing for bankruptcy, the North Carolina legislature could ease debtors' worries and provide much-needed clarity for the courts by creating an EITC exemption statute. Further, the legislature could rest assured it is following closely with the intent of the legislature when it first amended North Carolina Exemptions in 2005.<sup>120</sup>

Before this amendment, the Bankruptcy Section Council of the North Carolina Bar Association ("NCBA") formed an Exemption Revision Committee ("ERC") in 2002 out of growing concerns that "the real and practical values of North Carolina's exemptions ha[d] diminished greatly . . . ."<sup>121</sup> The ERC then released a report with several recommendations for the North Carolina legislature to rethink exemption types and dollar limits to reflect the needs of citizens at that time.<sup>122</sup> The language proposed for the new exemptions remained the same from the ERC's report to the day it was enacted as law.<sup>123</sup> Thus, while the report is not formal legislative history, "the commentary to a statutory provision can be helpful in discerning legislative intent."<sup>124</sup>

On September 14, 2005, the North Carolina House of Representatives implemented new exemption statutes and an overall increase in exemption values.<sup>125</sup> This was the first time that N.C. Gen. Stat. § 1C-1601 had been updated since 1991.<sup>126</sup> The 2005 amendments "fulfill[ed] important public policies . . . [meant] to

119. *In re Quevedo*, 2024 WL 3754885, at \*13.

120. H.B. 1176, 147th Gen. Assem., Reg. Sess. (N.C. 2005); *see also infra* notes 125–30 and accompanying text.

121. THE BANKR. SECTION OF THE N.C. BAR ASS'N, REP. OF THE EXEMPTION REVISION COMM.: ON REVISIONS TO N.C.'S LAWS WITH REGARD TO EXEMPTIONS 92, 94 (2004) [hereinafter REPORT OF ERC] (on file with author).

122. *Id.* at 97.

123. *Id.* at 104 (explaining how the proposed language for the child support exemption was adopted exactly as proposed).

124. *In re Quevedo*, 2024 WL 3754885, at \*7 (citing *Parsons v. Jefferson-Pilot Corp.*, 426 S.E.2d 685, 689 (N.C. 1993)).

125. H.B. 1176, 147th Gen. Assem., Reg. Sess. (N.C. 2005); *see also* UNIV. OF N.C. CHAPEL HILL SCH. OF GOV'T., NORTH CAROLINA LEGISLATION 73 (Martha H. Harris ed., 2005) (summarizing the new exemptions as including child support/alimony, qualified college savings plans, and retirement benefits from other states).

126. REPORT OF ERC, *supra* note 121, at 97.

protect property necessary for a debtor's fresh start and for the support of a debtor and his/her family, and to ensure that a debtor [wa]s able to [] recover or maintain status as a productive member of economy and of society."<sup>127</sup> This report can help to discern the North Carolina legislature's intent,<sup>128</sup> and it is reasonable to assume the legislature supported the advancement of these policies by choosing to adopt the report's suggestions. Consistent with the social policies that Professor Resnick articulated,<sup>129</sup> the public policies stated in the report are likely not met with the current state of exemptions in North Carolina. Remaining largely untouched since 2005, N.C. Gen. Stat. § 1C-1601 is once again in need of improvement for "the real and practical values of North Carolina's exemptions have diminished greatly . . . ." <sup>130</sup> The legislature could begin the much-needed revisions by creating an explicit EITC exemption.

iii. The N.C. Legislature Could Enact an EITC Exemption Similar to How it Enacted Medicaid Expansion

The North Carolina legislature has prevailed over divisive issues before, with Medicaid expansion being the most recent issue to gain near-unanimous bipartisan support in the House and Senate.<sup>131</sup> Officially launched on December 1, 2023, this "monumental achievement"<sup>132</sup> would provide "an estimated 600,000 low-income residents across the state access to health insurance."<sup>133</sup> While thirty-nine states chose to expand Medicaid before North Carolina, the path that North Carolina took was unique due to the strong bipartisan legislative vote that was comprised of many former opponents of extending coverage.<sup>134</sup> When analyzing media

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127. *Id.* at 6.

128. *In re Quevedo*, 2024 WL 3754885, at \*7 (citing *Parsons*, 426 S.E.2d at 689).

129. *Supra* text accompanying note 27.

130. REPORT OF ERC, *supra* note 121, at 94.

131. Jade Little & Adam Searing, *Bipartisan Medicaid Expansion Efforts in North Carolina: How Politicians Formerly Opposed to Expansion Are Framing Their New Support*, CTR. FOR CHILD. & FAMS. (CCF) OF THE GEO. UNIV. MCCOURT SCH. OF PUB. POL'Y (Sep. 8, 2022), <https://ccf.georgetown.edu/2022/09/08/bipartisan-medicaid-expansion-efforts-in-north-carolina-how-politicians-formerly-opposed-to-expansion-are-framing-their-new-support>.

132. Jaymie Baxley, *Medicaid expansion for North Carolina will go into effect on Dec. 1*, N.C. HEALTH NEWS (Sep. 27, 2023), <https://www.northcarolinahealthnews.org/2023/09/27/expansion-starting-in-december>.

133. Jaymie Baxley, *Medicaid expansion in N.C. launches today, here are answers to some common questions*, N.C. HEALTH NEWS (Dec. 1, 2023), <https://www.northcarolinahealthnews.org/2023/12/01/medicaid-expansion-faq>.

134. *Id.*

coverage of this issue, researchers found that former opponents of the expansion focused on a few themes when explaining the change in their positions: one theme being that “Medicaid expansion will help North Carolina’s working poor parents.”<sup>135</sup> Phil Berger, the Republican Senate leader, recalled a story that helped change his mind about “a single mom with two kids, making around \$25,000 a year, who’d [have been] considered too wealthy to qualify for Medicaid, unless expansion [was] approved.”<sup>136</sup> Similarly, the sentiment of wanting to help working, low-income parents is the entire purpose of the EITC.<sup>137</sup> Thus, it seems likely that if the legislature introduced a proposed EITC exemption for North Carolina debtors, it would garner bipartisan support as this exemption would help North Carolina’s working poor parents.

*B. Concerns with Adding a New Exemption, Like the EITC, Can Be Properly Accounted For*

Some scholars and credit lenders often voice two concerns for either adding new exemptions or increasing the value of existing exemptions: first, it results in increased interest rates for creditors and consumers alike; and second, exemptions inevitably lead to abuse of the system by the “dishonest” debtor.<sup>138</sup> Both of these “concerns” should give pause, for the probability that either occurs on the scale that they’re claimed to is not fully supported.

i. First Concern: Increased Interest Rates

The first concern, increased interest rates being correlated with more allowable exempt property, originated in the mid to late 1990s from research, which relied on hypotheses and data from 1983.<sup>139</sup> One author proposed that higher exemptions would lead to higher interest rates for consumers,<sup>140</sup> and the other made a connection

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135. Little & Searing, *supra* note 131.

136. *Id.* (quoting Will Doran, *Medicaid expansion approved by NC Senate in near-unanimous votes*, NEWS & OBSERVER (June 2, 2022, at 2:47 ET), <https://www.newsobserver.com/news/politics-government/state-politics/article262038887.html>).

137. See N.C. DEP’T OF REVENUE, 2007 TAX LAW CHANGES \*3 (2007), <https://www.ncdor.gov/documents/laws-and-decisions/north-carolina-2007-tax-law-changes/open> (establishing a State Earned Income Tax Credit modeled on federal EITC, which provides refundable tax credits benefitting low-income working taxpayers).

138. See Robert Rector & Jamie Bryan Hall, *Reforming the Earned Income Tax Credit and Additional Child Tax Credit to End Waste, Fraud, and Abuse and Strengthen Marriage*, HERITAGE FOUND. BACKGROUNDER, Nov. 2016, at 1, 3–5.

139. Berkowitz & Hynes, *supra* note 39 and accompanying text.

140. Deutsch, *supra* note 2, at 209 (emphasis added).

between higher interest rates on automobile loans and states with increased exemptions.<sup>141</sup> In both, the authors failed to include just how many variables contribute to fluctuating interest rates.<sup>142</sup> Not only is this often-cited research lacking a new perspective with current numbers, but contrasting research also came out at the same time.<sup>143</sup> This contrasting research found that “high exemption levels have not tended to increase mortgage rates or the probability of being denied a mortgage.”<sup>144</sup>

What this concern lacks most is the emphasis placed on fairness to the creditor. In consumer bankruptcy, creditors have substantially more bargaining power than the average debtor.<sup>145</sup> Creditors are typically more savvy and can adjust their lending practices to account for losses; meanwhile, debtors’ usual course of action is to file for bankruptcy and liquidate their assets.<sup>146</sup> Moreso, creditors are armed with knowledge of and personal experience with “state and federal debtor-creditor laws.”<sup>147</sup> This is exemplified in the crucial role that creditor lenders played in the creation and subsequent enactment of the BAPCPA.<sup>148</sup>

#### ii. Second Concern: The “Dishonest” Debtor

The second concern is especially harmful because it perpetuates false stereotypes of the “dishonest” debtor who schemes the bankruptcy system and leaves creditors penniless.<sup>149</sup> The worry that these types of debtors will abuse the system is difficult to conceive when most individuals decide against filing for bankruptcy since the filing fee is over \$1,000.<sup>150</sup> Between 2008 and 2018, “the number of consumer bankruptcies filed each year has ranged from about

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141. Gropp, Scholz & White, *supra* note 38.

142. See, e.g., Reem Heakal, *Understanding What Drives Fluctuations in Interest Rates*, INVESTOPEDIA (Nov. 2, 2025), <https://www.investopedia.com/insights/forces-behind-interest-rates> (listing various reasons for why interest rates increase or decrease, and how it is also dependent on the individual borrower).

143. Berkowitz & Hynes, *supra* note 39, at 109 and accompanying text.

144. *Id.*

145. Axelrod, *supra* note 5, at 311 n.162 (limiting the scope of the article to fairness to debtors, not creditors).

146. *Id.*

147. *Id.*

148. See, e.g., Jacoby, *supra* note 43.

149. Paul Kiel, *When You Can't Afford to Go Bankrupt*, PROPUBLICA (Mar. 2, 2018), <https://www.propublica.org/article/when-you-cannot-afford-to-go-bankrupt>.

150. *Id.* (“Scores of people considering bankruptcy told me the same thing again and again: If they had \$1,000 to pay an attorney, then they probably wouldn’t need to file in the first place.”).

800,000 to 1.5 million.”<sup>151</sup> However, this number does not accurately reflect how dire most individuals’ financial situation is when “[m]ore than a third of Americans said they couldn’t cover a sudden \$400 expense with cash or cash equivalents.”<sup>152</sup> What was revealed to Paul Kiel through interviews with those struggling with debt was simply put: “People are too broke to go bankrupt. Filing costs money, as does hiring an attorney, which is the best way to make sure you actually get debt relief.”<sup>153</sup> There are many reasons why an individual would or would not file for bankruptcy, but it’s evident that the first step—paying the filing fees and attorney’s fees—is the first barrier.<sup>154</sup>

Moreover, those who do make the difficult decision<sup>155</sup> to file for bankruptcy are usually “middle- and lower-class families unlikely to own real estate free of significant mortgage obligations.”<sup>156</sup> As previously stated, there have also been multiple studies that concluded that abuse of bankruptcy and exemption laws does not occur at the high rates some authors make it out to be.<sup>157</sup>

### CONCLUSION

It is past due for North Carolina to update exemptions by creating new exemptions and increasing the value that may be exempt. The last time the legislature undertook this crucial work, in furtherance of “fundamental public policies,” was in 2005. Over twenty years later, many debtors are still struggling. While North Carolina does have in place many exemptions that serve as important safety measures to protect debtors and their families,<sup>158</sup> there is always room for improvement.

The first step in the right direction would be implementing an EITC exemption statute. Other states have done just that when presented with cases that encouraged the legislature to act;<sup>159</sup> the

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151. *Id.*

152. Aaron McDade, *Here’s How Many Americans Can’t Afford a \$400 Emergency—The Numbers May Shock You*, INVESTOPEDIA (Sep. 22, 2025), <https://www.investopedia.com/here-s-how-many-americans-can-t-afford-a-usd400-emergency-the-numbers-may-shock-you-11814788>.

153. Kiel, *supra* note 149.

154. *Id.*

155. Axelrod, *supra* note 5, at 305 (stating bankruptcy was seen as “moral and financial” failure and individuals may buy into this outlook).

156. *Id.* at 325.

157. *Id.* at 324.

158. *See, e.g.*, BEST & CARTER, *supra* note 31, at 11 (stating North Carolina protects debtors’ wages by banning wage seizure).

159. *See* N.M. STAT. ANN. § 42-10-1(A)(7) (2023) (making exempt “refundable federal and state tax credits” in response to *In re* Medina).

same opportunity now presents itself in *In re Quevedo*. As it has once before with the child support statute,<sup>160</sup> the North Carolina legislature could find inspiration from Oklahoma's EITC exemption statute: "Any amount received pursuant to the federal earned income tax credit."<sup>161</sup> For more explicit statutory language, the legislature could follow Oregon's statute which exempts: "[t]he debtor's right to receive an earned income tax credit under the federal tax laws and any moneys that are traceable to a payment of an earned income tax credit under the federal tax laws."<sup>162</sup>

Worth emphasizing is this quote from the late Judge TeSelle of the United States Bankruptcy Court for the Western District of Oklahoma in 1997, which necessitates repeating nearly thirty years later:

To put this case in perspective, one need only step back and note we are dealing here with "poor, but honest" debtors for whom the government has enacted laws intended to relieve their extreme poverty ... It is difficult to understand why more effort is not expended by other counsel, the trustees, and the courts to permit impoverished debtors to keep their earned income credit rather than expending time, effort and legal skills in trying to take the earned income credit away from such debtors.<sup>163</sup>

Perhaps Judge TeSelle's words will not fall upon deaf ears and need not be repeated in another thirty years.

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160. *Supra* note 88 and accompanying text.

161. OKLA. STAT. tit. 31, § 1(23) (2009).

162. OR. REV. STAT. § 18.345(1)(n) (2017).

163. *In re Barnett*, 214 B.R. 632, 634 (Bankr. W.D. Okla. 1997).

