

UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re:

CASE NO. 06-22149

ALLAN DOUGLAS SAUNDERS and
MICHELE MARIE SAUNDERS,

Debtors.

DECISION & ORDER

BACKGROUND

On November 3, 2006, Allan Douglas Saunders ("Allan Saunders") and Michele Marie Saunders ("Michele Saunders") (collectively, the "Debtors") filed a voluntary joint petition initiating a Chapter 7 case, and Kenneth W. Gordon, Esq. (the "Trustee") was appointed as their Chapter 7 Trustee.

On the Schedules and Statements required to be filed by Section 521 and Rule 1007, the Debtors: (1) indicated on Schedule B, Item #9, that Allan Saunders was the owner of a term life insurance policy for \$105,000.00 that had no value even before deducting any secured claim or exemption and Michele Saunders was the owner of a term life insurance policy for \$50,000.00 that had no value even before deducting any secured claim or exemption; and (2) claimed the scheduled term life insurance policies as exempt under New York Insurance Law Section 3212.

On December 8, 2006, the Trustee filed an Objection (the "Objection to Exemptions") to the Debtors' claimed exemptions for

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their life insurance policies, and on February 20, 2007, he commenced an Adversary Proceeding (the "Turnover Proceeding") against the Debtors and Gary R. Acker ("Acker"), an insurance agent, which requested that the Court enter an order compelling the defendants to turn over to him the cash value of life insurance policies of Allan Saunders (\$16,849.14) and the cash value of the life insurance policy of Michele Saunders (\$4,093.89), for a total of \$20,943.03.¹

On March 2, 2007, the Debtors filed a motion (the "Severance Motion") which requested that the Court enter an order: (1) overruling the Objection to Exemptions; or (2) in the alternative, pursuant to Rule 1015(b), directing the separate and independent administrations of the estates of Allan Saunders and Michele Saunders.

The Severance Motion asserted that: (1) although the Debtors' case was being jointly administered by the Bankruptcy Court Clerk's Office and the Trustee, no order of joint administration had

¹ Although the Debtors scheduled only one policy each, it appears that the Debtor, Allan Saunders, owned several policies. In addition, the Debtors scheduled their policies as term life insurance policies. Such policies would not have any cash value, so the Court can only conclude that the policies are in fact whole life insurance policies.

actually been entered by the Court pursuant to Rule 1015(b);² (2) if the Court exercised its discretion to require the separate, rather than joint, administrations of the estates of Allan Saunders and Michele Saunders, the Decisions of the United States District Court for the Western District of New York (the "District Court") in *Teufel v. Schlant*, 2002 U.S. Dist. LEXIS 27930 (W.D.N.Y. 2002) ("*Teufel*"), and *Wornick v. Gaffney (In re Wornick)*, 2006 U.S. Dist. LEXIS 85327 (W.D.N.Y. 2006) ("*Wornick*"), would not apply, and the whole life insurance policies owned by each of the Debtors, as well as any cash surrender values available on any of those policies would be exempt from the reach of the creditors of each of the Debtors and the Trustee; (3) each policy as well as any available cash surrender value owned by Allan Saunders or Michele Saunders was exempt under New York Insurance Law Section 3212 as against

² Rule 1015(b) provides that:

(b) Cases involving two or more related debtors.

If a joint petition or two or more petitions are pending in the same court by or against (1) a husband and wife, or (2) a partnership and one or more of its general partners, or (3) two or more general partners, or (4) a debtor and an affiliate, the court may order a joint administration of the estates. Prior to entering an order the court shall give consideration to protecting creditors of different estates against potential conflicts of interest. An order directing joint administration of individual cases of a husband and wife shall, if one spouse has elected the exemptions under § 522(b)(1) of the Code and the other has elected the exemptions under § 522(b)(2), fix a reasonable time within which either may amend the election so that both shall have elected the same exemptions. The order shall notify the debtors that unless they elect the same exemptions within the time fixed by the court, they will be deemed to have elected the exemptions provided by § 522(b)(1).

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their creditors and their Trustee, and only each individual Debtor, as the owner of a policy, could surrender their owned policy and obtain the cash surrender value, as provided for by New York Insurance Law Section 4221; (4) although there was no specific exemption under New York Insurance Law Section 3212 for their interests as beneficiaries in the policies owned by their spouse, each Debtor had no right to surrender any policy owned by their spouse for which they were the mere beneficiary, so they could not obtain any available cash value, and, notwithstanding the *Teufel* and *Wornick* Decisions, neither their creditors nor their Trustee had any greater powers than they did to accomplish that; and (5) *Teufel* appeared to incorrectly assume that a joint petition filed by a husband and wife resulted in the automatic consolidation of the two separate estates, notwithstanding the absence of an order being entered to that effect under Rule 1015(b), when it held that all of the interests in reciprocal life insurance policies of spouses merge in a jointly held Chapter 7 case and the Trustee can obtain the cash surrender value of any reciprocal policy for distribution to the creditors of the beneficiary of the policy.

On April 16, 2007, the Trustee interposed a "Response" to the Severance Motion, which asserted that: (1) the Trustee objected to the Debtors' claims of exemptions in their reciprocal life insurance policies as well as any available cash surrender value

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based upon the *Teufel* and *Wornick* Decisions, and he filed the Turnover Proceeding to obtain the cash surrender value of the policies from the Debtors in accordance with those Decisions; (2) based upon the *Teufel* and *Wornick* Decisions, the Court should deny the Severance Motion, sustain the Objection to Exemptions and enter judgment in the Turnover Proceeding against the Debtors; (3) the *Teufel* and *Wornick* Decisions were intended to and did eliminate any conflict in the decisions of the Bankruptcy Courts for the Western District of New York with respect to the treatment of reciprocal whole life insurance policies when a joint Chapter 7 petition is filed by a husband and wife in the Western District of New York; (4) by the agreement of the Bankruptcy Judges of the Western District of New York, the Bankruptcy Court for the Western District of New York, Rochester Division, is bound by the *Teufel* and *Wornick* Decisions; (5) notwithstanding the Debtors' allegations that many of the issues it raised in the Severance Motion were not directly considered by the District Court in the *Teufel* and *Wornick* Decisions, in fact all of the Debtors' arguments were made either in the published conflicting Bankruptcy Court Decisions that were filed before the *Teufel* and *Wornick* Decisions, or in the *Teufel* and *Wornick* Decisions themselves, and they were all by necessity considered and decided by the District Court; (6) subsequent to the *Teufel* and *Wornick* Decisions, the Debtors, a husband and wife with

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reciprocal whole life insurance policies, elected to file a joint Chapter 7 petition, which they knew would be jointly administered, as all such cases have been in the Bankruptcy Court for the Western District of New York prior to and subsequent to the *Teufel* and *Wornick* Decisions, even though no specific order is ever entered under Rule 1015(b) with respect to the administration of the case; and (7) there is no provision in the Code or Rules for the severance of a joint case commenced by the voluntary petition of a husband and wife.

DISCUSSION

The Decisions in *Teufel* and *Wornick* hold that in the Chapter 7 case of a husband and wife who elected to file a joint petition, New York Insurance Law Section 3212 does not insulate the cash value of a whole life insurance policy owned by one spouse that names the other spouse as the beneficiary from distribution to the creditors of the beneficiary spouse.

By the agreement of the Bankruptcy Judges for the Western District of New York, this Court is bound by the *Teufel* and *Wornick* Decisions, so that the Severance Motion, to the extent that it requests an order determining that the Trustee cannot obtain the cash surrender value of the reciprocal whole life insurance policies because they are exempt both as to the creditors of the

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respective Debtor/owner and the respective Debtor/beneficiary, and thus the Trustee, is in all respects denied for the reasons set forth in the *Teufel* and *Wornick* Decisions.

The *Teufel* and *Wornick* Decisions were made in Chapter 7 cases voluntarily commenced by a joint petition filed by a husband and wife in the Western District of New York. To the extent that this Court has any discretion under Rule 1015(b) to enter an order of joint administration or severance that would result in an administration that would be the equivalent of the Debtors having filed separate Chapter 7 cases, I decline to exercise any such discretion in view of the *Teufel* and *Wornick* Decisions.

If spouses who own reciprocal whole life insurance policies and voluntarily file a joint Chapter 7 petition can avoid the holdings in the *Teufel* and *Wornick* Decisions by simply moving post-petition for an order that would create two separate estates as if they each filed a separate Chapter 7 petition, that procedure should be determined by the District Court to be appropriate and a proper exercise of discretion by a Bankruptcy Judge in this District.³

³A number of Decisions filed before and after the *Teufel* and *Wornick* Decisions, such as *In re Rundlett*, 142 B.R. 649 (Bankr. S.D.N.Y. 1992), *aff'd* 153 B.R. 126 (Bankr. S.D.N.Y. 1993), and even the *Teufel* Decision itself, have indicated how spouses can do appropriate pre-bankruptcy planning to avoid the results in the *Teufel* and *Wornick* Decisions. This includes filing two separate Chapter 7 petitions.

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CONCLUSION

The Severance Motion is in all respects denied. The Objection to Exemptions is in all respects sustained. However, the Turnover Proceeding shall be held in abeyance pending the appeal of this Decision & Order which this Court considers final on the issues decided.

IT IS SO ORDERED.

/s/
HON. JOHN C. NINFO, II
U.S. BANKRUPTCY JUDGE

Dated: May 18, 2007