UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF NEW YORK

In re:

CASE NO. 00-20130

JIMMIE C. HICKSON and
LEOLA HICKSON,

Debtors. **DECISION & ORDER**

BACKGROUND

On January 21, 2000, Jimmie Hickson and Leola Hickson (the "Debtors") filed a petition initiating a Chapter 7 case. On the Schedules and Statements required to be filed by Section 521 and Rule 1007, the Debtors: (1) indicated that Jimmie Hickson was the owner of a whole life insurance policy with Prudential that named Leola Hickson as the beneficiary and had a cash surrender value of $7,609.67 (the "Jimmie Hickson Policy"); (2) indicated that Leola Hickson was the owner of a whole life insurance policy with Prudential that named Jimmie Hickson as the beneficiary and had a cash surrender value of $3,543.55 (the "Leola Hickson Policy"); and (3) claimed on Schedule C the cash surrender values of the Jimmie and Leola Hickson Policies as exempt pursuant to Section 5205 of the New York Civil Practice Law and Rules (the "CPLR").

On March 6, 2000, the Chapter 7 trustee (the "Trustee")filed an Objection to the Debtors' claims that the cash surrender values of the Jimmie and Leola Hickson Policies were exempt.

On April 13, 2000, the Debtors filed amended Schedules which: (1) indicated that the cash surrender value of the Leola Hickson Policy was only $1,483.83; and (2) claimed on Schedule C the cash surrender values of the Jimmie and Leola Hickson Policies as exempt pursuant to Section 3212

of the New York Insurance Law (the "Insurance Law"), CPLR Section 5205 and Section 283(2) of the New York Debtor and Creditor Law (the "DCL").

On March 13, 2000, the Trustee filed a motion (the "Turnover Motion") which alleged that: (1) the Trustee had demanded that the Debtors turnover to him the cash surrender values of the Jimmie and Leola Hickson Policies, however, they had refused to do so; and (2) he was entitled to the cash surrender values in accordance with the decision of Bankruptcy Judge Michael J. Kaplan in *In Re Mata*, 244 B.R. 580 (Bankr. W.D.N.Y. 1999) ("*Mata*").

On April 24, 2000, the Debtors filed: (1) the Affidavit of Jimmie Hickson which alleged in connection with the Jimmie Hickson Policy that: (a) pursuant to the terms of the Policy, since he had been on disability for the last ten years from a work-related injury, Prudential was paying the premiums; (b) Prudential had advised him that because of the disability mode of the Policy, its cash surrender value could not be withdrawn; (c) Prudential had further advised him that as the owner of the Policy only he could obtain a loan against it or any cash surrender value, Leola Hickson, as the current beneficiary, had no right to obtain a loan against the Policy or its cash surrender value, and as the owner of the Policy he could change the beneficiary at any time; (2) the Affidavit of Leola Hickson which alleged in connection with the Leola Hickson Policy that Prudential had advised her that she was the only one who could obtain a loan against the Policy or its cash surrender value, Jimmie Hickson, as the current beneficiary, had no right to obtain a loan against the Policy or its cash surrender value, and as the owner of the Policy she could change the beneficiary at any time; and (3) a Memorandum of Law which alleged that: (a) the Jimmie and Leola Hickson Policies were exempt pursuant to Section 3212(b)(1) of the Insurance Law; (b) Jimmie and Leola Hickson, as the

beneficiary of their spouse's Policy, had only contingent, inchoate rights in the Policy prior to the Joint Debtor/Owner's death, and no current right to any of the "proceeds and avails" of the Policy as they are defined in Section 3212(a)(1) of the Insurance Law; (c) it was clearly the intention of the New York State Legislature to make all financial interests in life insurance policies exempt from the creditors and trustees of both the owners and beneficiaries of the policies; (d) in furtherance of the clear intention of the New York State Legislature, even though the Insurance Law did not specifically provide for such an exemption, State and Federal courts, including the New York Court of Appeals in *Chatham Phoenix National Bank v. Grosney*, 251 N.Y. 189 (1929) ("Chatham"), have broadly interpreted the Insurance Law and found an exemption as to the creditors and trustees of a spouse beneficiary of a life insurance policy; and (e) for various equitable reasons, and as a matter of public policy, the Debtors should be allowed to retain all of their interests in the Jimmie and Leola Hickson Policies.

DISCUSSION

I. Summary of Decision

The Turnover Motion is denied.

The cash surrender value of each Joint Debtor/Owner's policy is exempt as to their Trustee and their bankruptcy estate pursuant to Section 3212(b)(1) of the Insurance Law as long as a third party is the beneficiary.[1] Furthermore, because of the prohibition set forth in Section 3212(b)(5) of

[1] New York law is clear that the Section 3212(b)(1) exemption only applies if there is a third party beneficiary. See e.g. *In re Adas*, 335 N.Y.S.2d 128 (Surr. Ct. 1972); *Brandt v. Godfrey*, 32 N.Y.S.2d 400 (Sup. Ct. 1941), *aff'd* 35 N.Y.S.2d 713 (1942); *Stoudt v. Guaranty Trust Co. of New York, et al.*, 271 N.Y.S. 409 (Sup. Ct. 1933); *Lion Credit Union v. Gutman*, 265 N.Y.S. 479 (City Ct. N.Y. County 1932); *Beigel v. Windschauer*, 274 N.Y.S. 850 (City Ct. Bronx County 1934).

the Insurance Law, neither the Trustee nor the Bankruptcy Court can require that either Joint Debtor/Owner take the steps required to obtain a loan or the cash surrender value of their Policy, or turn the Policy over to the Trustee so that he may obtain a loan or the cash surrender value.[2]

Although, for the purposes of the allowance of an exemption pursuant to Section 3212(b)(1) of the Insurance Law, each Joint Debtor/Beneficiary has a superior right in the proceeds and avails of the respective Policy as against the Joint Debtor/Owner's creditors and trustee, they have only contingent non-vested rights in the Policy itself. Although there is nothing that this Court is aware of in the law, including the Insurance Law, which would make any cash surrender or loan proceeds that are in the possession of the Joint Debtor/Beneficiary exempt, the Trustee of the Joint Debtor/Beneficiary has no ability to obtain such proceeds or avails that are not in existence at the time of the filing of a joint petition, the date used to determine the availability of an exemption.

II. Relevant Statutes

Section 282 of the DCL allows a New York debtor to exempt insurance policies and annuity contracts and the proceeds and avails thereof as provided in Section 3212 of the Insurance Law ("Section 3212"). Section 3212 provides in part that:

> (a)(1) The term "proceeds and avails," in reference to policies of life insurance, includes death benefits, accelerated payments of the death benefit or accelerated payment of a special surrender value, cash surrender and loan values, premiums waived, and dividends, whether used in reduction of premiums or in whatever manner used or applied, except where the

[2] See generally, *Schwartz v. Seldon*, 153 F.2d 334 (2d Cir. 1945); *Rowen v. Commissioner of Internal Revenue*, 215 F.2d 641 (2d Cir. 1954).

> debtor has, after insurance of the policy, elected to receive the dividends in cash.
>
> (b)(1) If a policy of insurance has been or shall be effected by any person on his own life in favor of a third person beneficiary, or made payable otherwise to a third person, such third person shall be entitled to the proceeds and avails of such policy as against the creditors, personal representatives, trustees in bankruptcy and receivers in state and federal courts of the person effecting the insurance.
>
> (b)(5) This section shall be applicable whether or not the right is reserved in any such policy to change the designated beneficiary and whether or not the policy is made payable to the person whose life is insured if the beneficiary, assignee or payee shall predecease such person; and no person shall be compelled to exercise any rights, powers, options or privileges under such policy.

III. Rights of the Trustee as the Trustee of Debtor Owner of a Policy

Although the cash surrender value of the Jimmie and Leola Hickson Policies may initially be an asset of the bankruptcy estate of the Joint Debtor/Owner of the Policy pursuant to Section 541: (1) Section 3212(a)(1) includes the cash surrender value in the definition of proceeds and avails; and (2) Section 3212(b)(1), which is inartfully drafted and made applicable in bankruptcy by Section 282 of the DCL, essentially exempts such proceeds and avails in bankruptcy by giving the beneficiary of the Policy a superior right in the proceeds as against the Trustee of the Joint Debtor/Owner and their bankruptcy estate. See *In re Rundlett*, 153 B.R. 126 (Bankr. S.D.N.Y. 1993).

In addition, even though each Joint Debtor/Owner has the right at any time to: (1) change the beneficiary of the Policy, including making their probate estate the beneficiary; or (2) surrender the

Policy and obtain its cash surrender value, Section 3212(b)(5) prevents the Joint Debtor/Owner from being compelled to exercise any rights or powers including any steps which, if taken, would: (a) remove the Policy from the provisions of Section 3212(b)(1); or (b) make the cash surrender value immediately available to the respective beneficiary as against the Joint Debtor/Owner's creditors and Trustee. See generally, *In re Messinger*, 29 F.2d 158, 160 (2d Cir. 1928), *cert. denied* Sub Nom, 279 U.S. 855 (1929) ("*Messinger*").

Furthermore, to allow a bankruptcy trustee of a Joint Debtor/Owner to directly obtain a loan or any cash surrender proceeds would be contrary to the clear purpose of the statute, which is to provide for the Joint Debtor/Owner's beneficiary after the Joint Debtor/Owner's death.

IV. Rights of the Trustee as the Trustee of a Debtor Spouse Beneficiary

Since the Joint Debtor/Owner of the Jimmie and Leola Hickson Policies has the right at any time to change the beneficiary of their Policy, the current Joint Debtor/Beneficiary does not have a vested interest in the Policy. They only possess a contingent and inchoate right and interest in the Policy prior to the death of the Joint Debtor/Owner. See *In re Greenberg*, 271 F. 258 (2d Cir. 1921).

Although it is clear from a reading of the Statute and relevant case law that there would be no exemption as against the creditors and Trustee of the Joint Debtor/Beneficiary if the cash surrender value proceeds were immediately available to the Joint Debtor/Beneficiary or in their possession, the Trustee of the Joint Debtor/Beneficiary has no greater rights or abilities than the Joint Debtor/Beneficiary to obtain any cash surrender value. In this case the Trustee does not assert that, as the Trustee of either Joint Debtor/Beneficiary, he has a contractual right to demand that Prudential or the Joint Debtor/Owner obtain or pay over the cash surrender value of the respective Policy.

Therefore, although such cash surrender value proceeds would not be exempt in hands of a Joint Debtor/Beneficiary, because the rights of the Joint Debtor/Beneficiary are contingent, their Trustee has no ability to obtain those cash surrender value proceeds.[3]

Even though a Joint Debtor/Beneficiary's interest in the Joint Debtor/Owner's policy may be contingent at the time of the filing of the petition, should the Joint Debtor/Owner pass away within one hundred eighty days of the filing of the joint petition, Section 541(a)(5)(C) makes the proceeds of the Policy an asset of the bankruptcy estate of Joint Debtor/Beneficiary. In that event, the proceeds would be available for administration and distribution.[4]

V. Overview

Although their decisions did not involve the rights of a bankruptcy trustee in a case filed jointly by the Joint Debtor/Owner and the Joint Debtor/Beneficiary of a life insurance policy, New York courts have consistently held that where such individuals are joint judgment debtors, the

---

[3] See e.g., *In re Judson*, 199 F. 702 (S.D.N.Y. 1911); *In re Hogan*, 194 F. 846 (7th Cir. 1912); *In re McDonnell*, 101 F. 239 (N.D. Iowa 1900).

[4] Section 541(a)(5)(C) provides:

> (a) The commencement of a case under section 301, 302 or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:
>
> > (5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date—
> >
> > > (C) as beneficiary of a life insurance policy or of a death benefit plan.

11 U.S.C. § 541(a)(5)(C) (2000).

judgment creditor cannot reach the loan or cash surrender value of a Hickson-type life insurance policy. See *Kaufman v. New York Life Insurance Co., Inc.,* 299 N.Y.S.2d 269 (N.Y.A.D. 1st Dept. 1969); *Dellefield v. Block,* 40 F.Supp 616, 617 (S.D.N.Y. 1941); and *Joint Venture Acquisition v. Misra,* 1992 W.L. 212352 (S.D.N.Y. 1992). I agree with the assertion of the Debtors that when Section 3212 is applied in a joint bankruptcy case, the creditors of the husband or wife should not have a greater interest in such policies than they would if the same husband and wife had a joint judgment entered and enforced against them under New York Law.[5]

I also agree with the Debtors' assertion that: (1) there is no logical or policy reason for the New York State Legislature to have specifically provided that the proceeds and avails of an insurance policy as described in part of Section 3212(b)(2), a policy taken out by one spouse on the life of the other spouse where the spouse taking out the policy is the owner and also the beneficiary, and, therefore, possesses all of the incidents of ownership, is exempt from the creditors, trustees and representatives of both of the spouses,[6] but not to have specifically provided that the proceeds and avails of Hickson-type policy where the spouse is the beneficiary is exempt from the creditors,

---

[5] Would such a contrary result induce a collection attorney enforcing a State Court judgment against both spouses to file involuntary bankruptcy petitions against each spouse and then move to substantively consolidate the cases in order to each the cash value of a Hickson-type policy?

[6] Insurance Law Section 3212(b)(2) provides that:

> (b)(2) If a policy of insurance has been or shall be effected upon the life of another person in favor of the person effecting the same or made payable otherwise to such person, the latter shall be entitled to the proceeds and avails of such policy as against the creditors, personal representatives, trustees in bankruptcy and receivers in state and federal courts of the person insured. If the person effecting such insurance shall be the spouse of the insured, he or she shall be entitled to the proceeds and avails of such policy as against his or her own creditors, trustees in bankruptcy and receivers in state and federal courts.

New York State Insurance Law § 3212(b)(2) (2000).

trustees and representatives of both of the spouses; and (2) the proper inference to be drawn from the failure of the Legislature in this regard, is that the proceeds and avails of these policies would not be exempt from the creditors, representatives and trustees of the beneficiary. It seems to this Court that a Hickson-type policy is the most common form of life insurance policy that individuals take out to protect their spouse and family and, therefore, the New York State Legislature intended for it to be exempt in bankruptcy.

CONCLUSION

The Trustee's Turnover Motion is denied.

IT IS SO ORDERED.

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

Dated: August 14, 2000