



WRNewswire

An AALU Washington Report

Tuesday, 20 January 2015

WRN# 15.1.20

The *WRNewswire* is created exclusively for AALU Members by insurance experts led by Steve Leimberg, Lawrence Brody and Linas Sudzius. *WRNewswire* #15.01.20 was written by Linas Sudzius of [Advanced Underwriting Consultants](#).

TOPIC: Life Insurance Death Proceeds Made Available to Beneficiary's Creditors in Chapter 13 Bankruptcy

CITES: *In Re: Evans*, No. 10–05397–8–DMW, 2015 WL 77722 (Bankr. E D NC, Jan. 5, 2015); [11 U.S.C. Section 541](#); [11 U.S.C. Section 1306](#); [11 U.S.C. Section 1329](#).

SUMMARY: Lee Evans and his wife Kimberly Evans filed a joint Chapter 13 bankruptcy petition in North Carolina in 2010. The bankruptcy court approved the Evanses' original plan to pay their secured creditor and partly repay unsecured creditors. The court also approved a plan modification in 2013.

Kimberly Evans died in 2014, leaving a nearly \$170,000 net life insurance death benefit payable to Lee. Lee argued that the death proceeds were exempt from the claims of the bankruptcy creditors. However, the bankruptcy trustee disagreed.

The bankruptcy court ruled in favor of the trustee, making the insurance proceeds available to pay Lee's unsecured creditors.

RELEVANCE: We have written about cases where the parties argued about the availability of life insurance death proceeds to pay creditors in bankruptcy previously in *WRNewswires* #14.09.26 and #14.05.30. Where the beneficiary of the policy proceeds is in the middle of a bankruptcy proceeding, the courts usually rule that the death proceeds are available to satisfy creditors. The *Evans* decision is consistent with that general rule.

When an insured client is seeking to protect the death proceeds from a beneficiary's creditors, an agent should be prepared to discuss alternative beneficiary designations—perhaps naming a spendthrift trust as the policy beneficiary—to achieve the desired results.

FACTS: Kimberly and Lee purchased two life insurance policies in July, 1995. According to Lee's bankruptcy schedules, the Evanses paid \$281.00 per month in life insurance premiums for the two policies.

Beginning in 1999, Kimberly suffered severe intestinal and stomach problems. Treatment for Kimberly's condition ultimately led to the discovery and diagnosis of

breast cancer around 2007. Kimberly underwent treatment for the cancer, including chemotherapy, radiation, and surgery. Following the diagnosis, the Evanses generated no income in 2008 and 2009. In the year of the bankruptcy petition, Kimberly worked from home part-time, assisting Mr. Evans with his home repair business.

Kimberly and Lee Evans filed a joint petition under Chapter 13 of the United States Bankruptcy Code on July 7, 2010. Under a Chapter 13 bankruptcy, debtors generally agree to a monthly payment plan that is designed to satisfy the claims of their creditors, in whole or in part, over a three to five year period. The court must approve their plan based on the status of creditors and the debtors' available income and assets.

The bankruptcy trustee conducted a meeting of the creditors on August 2, 2010, at which time the Evanses stated that Kimberly was "disabled" but did not elaborate.

The bankruptcy court confirmed the Evanses' Chapter 13 plan on December 20, 2010. Their general unsecured claims totaled \$110,265.36, and the plan provided for a 1% dividend to those creditors. Subsequent to the plan's confirmation, one of Kimberly's doctors told her that she had approximately two years to live.

The Chapter 13 plan was modified on April 19, 2013 to accommodate a mortgage modification with the Evanses' mortgage bank. The modification resulted in an increase in the projected dividend to unsecured creditors, from 1% to 2.3%. There is no record suggesting that in the process of negotiating the plan modification that the Evanses informed the trustee of Kimberly's health prognosis.

Kimberly died on April 23, 2014. The following month Lee filed a notice with the court stating that he was a beneficiary under Kimberly's life insurance policy and was entitled to receive a death benefit. The gross value of the insurance payout was \$200,000.00. After payment of a policy loan and funeral home expenses, the net benefit payable to Lee was \$169,796.29.

The trustee filed a motion to require Lee to use the policy's death benefit to pay his own unsecured debts and also to pay the joint debts of himself and his late wife.

The court observed that life insurance proceeds received during a Chapter 13 bankruptcy proceeding are usually included in the bankruptcy estate under Bankruptcy Code Sections 541 and 1306.

The court went on to say that in order for the trustee's motion to be approved, Section 1329 of the Bankruptcy Code required that that the debtor must have experienced a substantial and unanticipated post-confirmation change in his financial condition.

Lee argued that Kimberly was in a terminal condition *during* the Chapter 13 process, and that the trustee should have anticipated her death, *i.e.*, that any potential claim against the policy proceeds should have been made *prior* to the Chapter 13 plan confirmation. If the change in financial condition were *anticipated*, the new circumstance would not meet the requirements of Section 1329, and the death proceeds would not be part of the bankruptcy estate.

RESULT: The court refused to impose a duty on the trustee to anticipate Kimberly's death. Nothing in the bankruptcy record made explicit that Kimberly was in a terminal

condition. While Lee argued that the trustee should have inferred Kimberly's condition, the court said such an evaluation was outside the scope of a bankruptcy trustee's normal duties.

The court ruled that the life insurance proceeds would be made available to pay the unsecured creditors of Lee and to pay the unsecured debts for which he was jointly liable with Kimberly.

The court also ruled that the proceeds were not available to pay Kimberly's sole unsecured debts. North Carolina law specifically protects the death proceeds of insurance on a decedent's life from the claims of the *decedent's* creditors where the policy is payable to a spouse.

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