

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF ALABAMA

In Re

NATASHA B. BUNN

Case No. 02-17303-MAM-7

Debtor.

**ORDER OVERRULING TRUSTEE'S OBJECTION AND FINDING THAT
DEBTOR'S INTEREST IN A \$12,500 ANNUITY PAYMENT IS EXEMPT
PROPERTY OF THE ESTATE UNDER 11 U.S.C. §522(b)**

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This matter is before the Court on the trustee's objection to Natasha Bunn's \$12,500 claimed exemption in a litigation settlement annuity under which she is the beneficiary. The Court has jurisdiction to hear this matter pursuant to 28 U.S.C. §§ 157 and 1334 and the Order of Reference of the District Court. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2) and the Court has authority to enter a final order. For the reasons indicated below, the Court finds that the trustee's objection to Natasha Bunn's claimed exemption is overruled because Bunn's interest in the \$12,500 annuity payment is exempt property of the estate under 11 U.S.C. §522(b).

FACTS

Natasha Bunn's father, George A. Bowman, was killed in an automobile accident on Airport Boulevard in Mobile, Alabama on May 9, 1981 when the car he was driving collided with a City of Mobile truck. Subsequently, Natasha Bunn's mother, Sharon H. Bowman, filed a lawsuit on behalf of her deceased husband's estate against the City of Mobile in the Circuit Court of Mobile County, Alabama. On March 15, 1985 the circuit court entered an order that

awarded \$10,000 to Sharon Bowman and provided for a structured settlement for the benefit of George Bowman's two children, Natasha Bunn and John Bowman.

The structured settlement provided for a total of five lump sum payments to each child. The first payment to Natasha Bunn was scheduled for April 1, 1997 and the last payment was scheduled for April 1, 2004. The first four lump sum payments were to be in the amount of \$4,500 each and the fifth lump sum payment was to be in the amount of \$12,500.

A "structured single premium immediate single life annuity" was purchased to effectuate the structured settlement. It is unclear whether the City of Mobile or Bunn's mother, Sharon Bowman, entered into a contract with Federal Home Life Insurance Company on February 19, 1985 to purchase the annuity. Bunn testified that her mother "put up" the annuity to further Bunn's education. The contract lists Home Insurance Company as the owner, Natasha Bowman (now Natasha Bunn) as the annuitant, and the estate of Natasha Bowman as the beneficiary.

The structured payments under the annuity contract are in the same amounts as listed in the structured settlement. The distribution schedule is also the same under the annuity contract. The cover page of the annuity contract states that the "annuity payments shall continue if the Annuitant dies prior to the expiration of any Guaranteed Period until the final payment in the Guaranteed Period." The "description of benefits" section of the contract states that the lump sum payments are "all guaranteed, no life contingencies." The "general provisions" section of the contract states that it is assignable.

Natasha Bunn filed a chapter 7 bankruptcy case on December 27, 2002. She has already received the first four annuity payments in the amount of \$4,500 each. Bunn is due to receive the fifth annuity payment in the amount of \$12,500 on April 1, 2004. In her schedules, Bunn

listed the \$12,500 annuity payment as personal property with a current market value of \$12,500; she then claimed it as exempt under Ala. Code §19-3-1. The trustee filed an objection to Bunn's claimed exemption.

The Court held a hearing on the trustee's objection on March 18, 2003. Bunn and the trustee disagree regarding the application of 11 U.S.C. §541 and Ala. Code §19-3-1 in this case. Bunn argues that the annuity payment is not property of her estate under §541. She analogizes her right to receive the annuity payment to a debtor's interest in an inheritance. The trustee argues that the lump sum annuity payment is property of Bunn's estate under §541 that is not exempt under §541(c)(2) because it is not eligible for exemption under Ala. Code § 19-3-1.

LAW

The Court must consider the following issues to determine if Natasha Bunn may exempt an annuity payment in her chapter 7 bankruptcy case:

1. Is the annuity payment property of the estate under 11 U.S.C. §541(a)(1)?
2. If so, may the annuity payment be excluded from property of the estate under 11 U.S.C. §541(c)(2)?
3. If the annuity payment is property of the estate, is it exempt under 11 U.S.C. §522(b)?

1.

Is the Annuity Payment Property of the Estate Under 11 U.S.C. §541?

Natasha Bunn claims that the annuity payment she is due to receive on April 1, 2004 is not property of the estate in her chapter 7 bankruptcy case. Whether a debtor's interest in property becomes property of the estate is governed by 11 U.S.C. §541. Section 541(a)(1) broadly defines property of the estate to include "all legal or equitable interests of the debtor in property as of the commencement of the case." *In re Powell*, 223 B.R. 225, 232-33 (Bankr. N.D.

Ala. 1998). Section 541(c)(2) provides an exception to the “otherwise broad definition of ‘property of the estate’ contained in §541(a)(1) of the Code. *Patterson v. Shumate*, 504 U.S. 753, 757 (1992). The Court will discuss §541(a)(1) first and then §541(c)(2).

11 U.S.C. §541(a)(1) 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:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

Section 541(a)(1) of the Code brings into the property of the estate all legal or equitable *interests* of the debtor in property. *Meehan v. Wallace (In re Meehan)*. 102 F.3d 1209, 1210 (11th Cir. 1997). The interest does not have to be a complete (100%) interest nor an ownership interest. *See In re Williams*, 197 B.R. 398, 402 (Bankr. M.D. Ga. 1996) (holding that “every conceivable interest of the debtor, future, nonpossessory, contingent, speculative, and derivative, is within the reach of §541”) (quoting *In re Yonikus*, 996 F.2d 866, 869 (7th Cir. 1993).

In the schedules filed in her bankruptcy case, Bunn listed the annuity payment she is due to receive on April 1, 2004 as personal property. At her hearing, Bunn argued that the annuity contract is not property of the estate for two reasons. First, Bunn stated that she is not the owner of the annuity because it lists Home Insurance Company as the owner on the contract. Second, Bunn stated that the trustee may not recover the \$12,500 annuity payment from her because at this time she only has the right to receive the annuity payment on April 1, 2004.

Bunn is correct that the annuity contract lists Home Insurance Company as the owner of the annuity. More importantly though, the annuity contract lists Natasha Bunn as the annuitant and the estate of Natasha Bunn as the beneficiary. The contract states that Home Insurance Company may only change the beneficiary if the beneficiary gives it written permission to do so.

No testimony or evidence was presented to indicate that Bunn has given Home Insurance Company written permission to change the beneficiary under the contract. Therefore, Bunn's right to receive the \$12,500 annuity payment under the annuity contract is not impeded by the contract listing Home Insurance Company as the owner.

Bunn is also correct that at this time, she only has the right to receive the \$12,500 annuity payment on April 1, 2004. She does not have access to the money. However, Bunn's absolute right to receive the \$12,500 annuity payment under contract makes it property of the estate. The cover page of the annuity contract states that the "annuity payments shall continue if the Annuitant dies prior to the expiration of any Guaranteed Period until the final payment in the Guaranteed Period." The "description of benefits" section of the contract states that the lump sum payments are "all guaranteed, no life contingencies." Additionally, the "general provisions" section of the annuity contract gives Bunn the right to assign the annuity. Therefore, the Court finds that Bunn has a "legal or equitable interest" in the \$12,500 annuity payment, which makes it property of the estate under §541(a)(1). *In re Wiley*, 184 B.R. 759, 765 (Bankr. N.D. Iowa 1995).

2.

If So, May the Annuity Payment Be Excluded From Property of the Estate Under 11 U.S.C. §541(c)(2)?

Although the Court has found that Bunn's interest in the annuity payment makes it property of the estate under §541(a)(1), she may still exclude her interest in the payment from property of the estate if she meets the requirements of §541(c)(2). Section 541(c)(2) provides:

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

The United States Supreme Court has held that “[t]he natural reading of [541(c)(2)] entitles a debtor to exclude from property of the estate any interest in a plan or trust that contains a transfer restriction enforceable under any relevant nonbankruptcy law.” *Patterson v. Shumate*, 504 U.S. 753, 758 (1992). It defined the term “applicable nonbankruptcy law” in §541(c)(2) to include both federal and state law. *Id.*

Based on the United States Supreme Court’s analysis of §541(c)(2) in *Shumate*, this Court finds that Bunn must meet a three prong test to exclude her interest in the annuity payment from property of the estate. She must show that 1) she has a beneficial interest in a trust; 2) the transfer of her interest is restricted; and 3) the restriction is enforceable under applicable federal or state law. *See In re Schuster*, 256 B.R. 701, 703 (Bankr. D. N.J. 2000). Bunn carries the burden of proof to show that her interest in the annuity payment should be excluded from property of the estate under §541(c)(2). *See In re Lowenschuss*, 202 B.R. 305, 313 (Bankr. D. Nev. 1996) (finding that “[d]ebtors have the burden of proof to demonstrate by a preponderance of the evidence that their retirement plans contain enforceable anti-alienation restrictions that would permit them to be excluded from the bankruptcy estate under 541(c)(2)”).

The Court will not discuss each prong that Bunn must prove to show that her interest in the annuity payment should be excluded from property of estate under §541(c)(2) because the second requirement is not met. Bunn’s annuity does not contain a transfer restriction; instead, it specifically states that it is assignable in the “general provisions” section of the contract. Therefore, the Court finds that Bunn may not exclude her interest in the annuity payment from property of the estate under §541(c)(1). Her interest in the annuity payment is property of the estate under §541(a)(1).

3.

If the Annuity Payment is Property of the Estate, Is It Exempt Under 11 U.S.C. §522(b)?

Although Bunn’s interest in the annuity payment is nonexcludeable property of the estate under §541(a)(1), she may be able to exempt her interest under 11 U.S.C. §522(b), which provides:

(b) Notwithstanding section 541 of this title, an individual debtor may exempt from property of the estate the property listed in either paragraph (1) or, in the alternative, paragraph (2) of this subsection. In joint cases filed under section 302 of this title and individual cases filed under section 301 or 303 of this title by or against debtors who are husband and wife, and whose estates are ordered to be jointly administered under Rule 1015(b) of the Federal Rules of Bankruptcy Procedure, one debtor may not elect to exempt property listed in paragraph (1) and the other debtor elect to exempt property listed in paragraph (2) of this subsection. If the parties cannot agree on the alternative to be elected, they shall be deemed to elect paragraph (1), where such election is permitted under the law of the jurisdiction where the case is filed. Such property is--

(1) property that is specified under subsection (d) of this section, unless the State law that is applicable to the debtor under paragraph (2)(A) of this subsection specifically does not so authorize; or, in the alternative,

(2)(A) any property that is exempt under Federal law, other than subsection (d) of this section, or State or local law that is applicable on the date of the filing of the petition at the place in which the debtor's domicile has been located for the 180 days immediately preceding the date of the filing of the petition, or for a longer portion of such 180-day period than in any other place; and

(B) any interest in property in which the debtor had, immediately before the commencement of the case, an interest as a tenant by the entirety or joint tenant to the extent that such interest as a tenant by the entirety or joint tenant is exempt from process under applicable nonbankruptcy law.

“Under 11 U.S.C. §522(b), a debtor may choose between the federal exemptions provided by §522(d) and those provided under state law, unless state law ‘vetoes’ the debtor’s option to choose the federal exemptions.” *In re Wiley*, 184 B.R. 759, 765 (Bankr. N.D. Iowa 1995) (citing to *In re Huebner*, 986 F.2d 122, 1224 (8th Cir. 1993)). Alabama is an “opt-out” state that has “vetoed” its debtors’ option to choose the federal exemptions, therefore, the only exemptions a debtor may claim under §522(b) in Alabama are the state exemptions. *Dionne v.*

Harless (In re Harless), 187 B.R. 719, 726-27 (Bankr. N.D. Ala. 1995). Bunn cites to Ala. Code §19-3-1 as the source of her exemption. It provides in relevant part:

(b) QUALIFIED TRUST UNDER THE INTERNAL REVENUE CODE.

(1) PROHIBITION ON ASSIGNMENT. -- Any benefits provided under a plan which includes a trust that constitutes a "qualified trust" may not be assigned or alienated, voluntarily or involuntarily, and shall be exempt from the operation of any bankruptcy or insolvency laws under 11 U.S.C. s 522(b), as from time to time amended. This subdivision may not be waived by a participant or beneficiary of any qualified plan.

....

(4) INTERPRETATION. -- The provisions of this section shall be interpreted so as to provide restrictions on alienation and assignment to the extent, and only to the extent, the same are required for a trust within the definition of "qualified trust" herein to be a "qualified trust" under the applicable provisions of the Code, notwithstanding any attempted assignment or alienation in violation of Section 401(a) or other applicable provisions of the Code. It is intended that this section will constitute "a restriction of the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law" for purposes of Section 541(c)(2) of the Federal Bankruptcy Code, 11 U.S.C. s 541(c)(2), as from time to time amended. This section shall further be construed as a "state spendthrift trust law." It is further intended for this section to provide an exemption from creditors' claims within 11 U.S.C. s 522.

....

d. "Qualified trust" means a "qualified trust" as such term is used in section 401(a) of the Code, and includes any trust that would not be qualified but for this section. A "qualified trust" includes, without limitations, any trust that has received a favorable determination letter from the Internal Revenue Service of the United States Department of Treasury to the effect that such trust is, or will be upon the satisfaction of certain administrative conditions, a "qualified trust" under Section 401(a) of the Code. "Qualified trust" also includes:

1. A "retirement annuity" described in Section 404(a)(2) of the Code, including a retirement annuity that would not satisfy the requirements of Section 404(a)(2) of the Code but for this section;

2. An annuity described in Section 403(b) of the Code, including an annuity that would not satisfy the requirements of Section 403(b) of the Code but for this section;

3. An individual retirement plan described in Section 7701(a)(37) of the Code, including an individual retirement plan that would not satisfy the requirements of Section 7701(a)(37) of the Code but for this section;

4. A retirement bond described in Section 409 of the Code, as in effect prior to January 1, 1984, including a retirement bond that would not satisfy the requirements of Section 409 of the Code but for this section;

5. A governmental plan described in Section 414(d) of the Code;

6. A church plan described in Section 414(e) of the Code; and
7. A tax credit employee stock ownership plan described in Section 409 of the Code, including a tax credit employee stock ownership plan that would not satisfy the requirements of Section 409 of the Code but for this section.

Alabama Code §19-3-1 defines the term “qualified trust” to include “both ‘ERISA-qualified’ plans *and* other tax-preferred retirement assets which are not ‘ERISA-qualified’ and for which the Internal Revenue Code requires no transfer restriction.” *In re Harless* at 724. It also includes “any trust that has received a favorable determination letter from the Internal Revenue Service of the United States Department of Treasury to the effect that such trust is, or will be upon the satisfaction of certain administrative conditions, a ‘qualified trust’ under Section 401(a) of the Code.” Ala. Code §19-3-1(d).

The Court finds that Bunn’s annuity contract does not satisfy the definition of “qualified trust” as that term is defined in Ala. Code §19-3-1. Bunn’s annuity contract states that it was set up as a “litigation settlement annuity” rather than as a individual retirement account (IRA) or any other type of employee annuity plan under the Internal Revenue Code. No evidence or testimony was presented to indicate that Bunn’s annuity received a “favorable determination letter” from the IRS. Therefore, Bunn may not exempt her interest in the annuity payment under Ala. Code §19-3-1.

Although Ala. Code §19-3-1 is the only state law exemption cited by Bunn, the trustee submitted a case into evidence that considered whether Ala. Code §27-14-32 exempts annuity contracts from property of the estate. *Turner v. Dees (In re Dees)*, 155 B.R. 238 (Bankr. S.D. Ala. 1992). The *Dees* court found that Ala. Code §27-14-32 allows for a \$250 monthly exemption on annuity contracts; however, because no Alabama court had published an opinion on the application of the statute at that time, the debtor’s motion for summary judgment was denied and the matter was set for hearing. *Id.* at 240-41. This Court could find only two cases in

which Ala. Code §27-14-32 has been cited since the *Dees* decision and neither case provides any insight into its application. See *In re Poffenbarger*, 281 B.R. 379, 392 (Bankr. S.D. Ala. 2002); *In re Darby*, 212 B.R. 382, 383-84 (Bankr. M.D. Ala. 1997).

The Court will consider on its own motion whether Bunn may exempt her interest in the annuity payment pursuant to Ala Code §27-14-32, which provides in relevant part:

(a) The benefits, rights, privileges and options which under any annuity contract, heretofore or hereafter issued, are due or prospectively due the annuitant shall not be subject to execution, nor shall the annuitant be compelled to exercise any such rights, powers or options, nor shall creditors be allowed to interfere with or terminate the contract, except:

(1) As to amounts paid for or as premium on any such annuity with intent to defraud creditors, with interest thereon, and of which the creditor has given the insurer written notice at its home office prior to the making of the payments to the annuitant out of which the creditor seeks to recover. Any such notice shall specify the amount claimed, or such facts as will enable the insurer to ascertain such amount, and shall set forth such facts as will enable the insurer to ascertain the insurance or annuity contract, the person insured or annuitant and the payments sought to be avoided on the ground of fraud;

(2) The total exemption of benefits presently due and payable to any annuitant periodically or at stated times under all annuity contracts under which he is an annuitant shall not at any time exceed \$250.00 per month for the length of time represented by such installments, and such periodic payments in excess of \$250.00 per month shall be subject to garnishment;

....

Alabama Code §27-14-32 does not define the term “annuity” or “annuity contract.” It simply provides a limited exemption for annuity benefits from seizure by creditors. See *In re Darby* at 384 (finding that “[c]hapter 14 of the Alabama Code does not define the terms ‘annuity contract’ or ‘annuity’”). The Court could not find any Alabama code section or case law that defines the term “annuity” or “annuity contract.” However, *Black’s Law Dictionary* 88 (7th ed. 1999) gives four broad definitions of “annuity,” one of which is “[a] fixed sum of money payable periodically.” The 11th Circuit Court of Appeals upheld a similarly broad definition of an “annuity” under Florida law in a case it certified to the Supreme Court of Florida. *LeCroy v. McCollam* (*In re McCollam*), 986 F.2d 436, 438 (11th Cir. 1993).

In *McCollam*, the Supreme Court of Florida stated that an annuity “[i]n its broader sense . . . designates a fixed sum . . . payable periodically, at aliquot parts of a year, at stated intervals, and not necessarily annually.” *Leroy v. McCollam (In re McCollam)*, 612 So.2d 572, 574 (Fla. 1993) (citing to *In re Gefen*, 35 B.R. 368, 371 (Bankr. S.D. Fla. 1984) (quoting *In re Talbert*, 15 B.R. 536, 537 (Bankr. W.D. La. 1981)). The 11th Circuit Court of Appeals upheld the definition of “annuity” under Florida law as promulgated by the Supreme Court of Florida. *In re McCollam*, 986 F.2d at 438. This Court now adopts the same definition of “annuity” as used in *McCollam*.

Bunn’s “annuity contract” describes itself as a “structured single premium immediate single life annuity.” Under the contract, Bunn has already received four lump sum payments in the amount of \$4,500 each. Bunn received the first \$4,500 lump sum payment on April 1, 1997. She received the second payment on April 1, 1998, the third payment on April 1, 1999, and the fourth payment on April 1, 2000. She is due to receive a fifth lump sum payment of \$12,500 on April 1, 2004.

The Court finds that Bunn’s contract is an “annuity.” The payments to Bunn are fixed sums payable periodically. Even though the last payment is larger than the previous four payments, the period of time between the fourth and fifth payment is also larger. Additionally, the contract requires the payments to be made periodically, which is all that is required under the Court’s “annuity” definition.

Alabama Code §27-14-32(a) provides for a broad exemption of annuity benefits, subject to two exceptions that may be relevant in this case. The first exception is found in Ala. Code §27-14-32(a)(1). Pursuant to that section, creditors may recover amounts paid as premiums on annuity contracts entered into with the intent to defraud creditors. In this case, no evidence or

testimony was presented that indicates Bunn's annuity contract was entered into "with intent to defraud creditors." Ala. Code §27-14-32(a)(1). Bunn testified that her mother "put up" the annuity to further Bunn's education. Moreover, the annuity contract with Federal Home Life Insurance Company was entered into on February 19, 1985; almost fifteen years before Bunn filed her chapter 7 bankruptcy case. The Court finds that the annuity contract was not entered into with the intent to defraud Bunn's creditors; therefore, Bunn's creditors may not recover any amounts paid as premium in the annuity contract.

The second exception to Ala. Code §27-14-32's broad exemption of annuity benefits is found in Ala. Code §27-14-32(a)(2). Pursuant to that section, "[t]he total exemption of benefits presently due and payable to any annuitant periodically or at stated times under all annuity contracts under which he is an annuitant shall not at any time exceed \$250.00 per month for the length of time represented by such installments, and such periodic payments in excess of \$250.00 per month shall be subject to garnishment." Ala. Code §27-14-32(a)(2). Bunn's annuity contract is payable in five lump sum installments. Bunn was not scheduled to receive any annuity payments when she filed her petition on December 27, 2002. She is due to receive the fifth lump sum payment of \$12,500 pursuant to the annuity contract on April 1, 2004.

The Court is not aware of any case law regarding the application of Ala. Code §27-14-32(a)(2) to lump sum annuity payments. However, the Court was able to find a Wyoming case in which the court considered the application of Wyoming's state annuity exemption statute, Wyo. Stat. §26-15-132, which is very similar to Ala. Code §27-14-32(a)(2). *Norwest Bank Wyoming Casper, N.A. v. Pancratz (In re Pancratz)*, 175 B.R. 85 (D. Wyo. 1994). Like Alabama's annuity exemption statute, Wyo. Stat. §26-15-132 contains an exception to its broad

exemption of annuity benefits that limits the total exemption of benefits “presently due and payable” to a specific dollar amount per month.

In *Pancratz*, the district court affirmed a bankruptcy court decision largely exempting two annuity contracts held by the debtors. *Id.* The bankruptcy court found that “just as the petition date determine[s] the rights of the debtors to claim exemptions, so does the petition date determine the rights of the estate in property. The estate succeeds only to the rights in the annuity contract that the debtors had on the date of the petition.” *Id.* at 93. The bankruptcy court then held that the debtors’ first annuity contract was entirely exempt because “no payments were ‘presently due and payable’ on the petition date” and it held that the debtors’ second annuity contract was exempt as to all payments except for the \$1,969.74 monthly annuity payment that was “presently due and payable” on the petition date. *Id.* at 92.

This is a case of first impression in this Court. There is no Alabama case law regarding the application of Ala. Code §27-14-32(a)(2) to lump sum annuity payments. However, the Court finds the reasoning of the *Pancratz* court persuasive in its application of a Wyoming statute that is very similar to Ala. Code §27-14-32(a)(2). Therefore, this Court adopts the *Pancratz* court’s application of Wyo. Stat. §26-15-132 to determine the meaning of the phrase “presently due and payable” under Ala. Code §27-14-32(a)(2).

Bunn is scheduled to receive the fifth lump sum payment under her annuity contract on April 1, 2004. The fifth payment was not “presently due and payable” to Bunn when she filed her petition on December 27, 2002. The only interest Bunn had in the fifth annuity payment when she filed her petition was the right to receive it on April 1, 2004. Therefore, the Court finds that Ala. Code §27-14-32(a)(2) does not provide any exception to Ala. Code §27-14-32(a)’s broad exemption of Bunn’s annuity benefits because no annuity payments were

“presently due and payable” to Bunn when she filed her petition. Accordingly, Bunn’s interest in the \$12,500 annuity payment is entirely exempt property of the estate under 11 U.S.C. §522(b).

It is ORDERED that the trustee’s objection to Natasha Bunn’s \$12,500 claimed exemption in a lump sum annuity payment is overruled because Bunn’s interest in the \$12,500 annuity payment she is due to receive on April 1, 2004 is exempt property of the estate under 11 U.S.C. §522(b).

Dated: March 31, 2003


MARGARET A. MAHONEY
U.S. BANKRUPTCY JUDGE