# RECENT CASES

**Bankruptcy—Insurance—Trustee's Right to Benefits under Disability Policy—[United States].**—The bankrupt insured his life, making his wife the beneficiary and reserving the right to change the beneficiary. Attached to the life policy was a supplementary contract which provided that if the insured should become totally disabled, he was to receive a monthly annuity. In this contract also, the insured retained the right to change the beneficiary. Prior to the bankruptcy, the bankrupt became totally disabled and began to receive monthly payments on the disability insurance. The trustee conceded that the life policy was exempt under the Tennessee statute (Tenn. Code § 8456 (1932)) but contended that the obligation of the insurance company to make future disability payments passed to the trustee. The Circuit Court of Appeals gave judgment for the trustee. On appeal, *held*, affirmed. *Legge v. St. Johns*, 56 Sup. Ct. 336 (1935).

Section 70(a)(5) of the Bankruptcy Act, 32 Stat. 800 (1903), 11 U.S.C.A. 110 (1927), vests in the trustee the title to "property which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him. Provided, when any bankrupt shall have any insurance policy which has a cash surrender value payable to himself, his estate, or personal representatives, he may, within thirty days after the cash surrender value has been ascertained and stated to the trustee by the company issuing the same, pay or secure to the trustee the sum so ascertained and stated, and continue to hold, own, and carry such policy free from the claims of the creditors participating in the distribution of his estate under the bankruptcy proceedings, otherwise the policy shall pass to the trustee as assets; . . . ." The obligation of the insurance company to make disability payments, having arisen before the filing of the petition, was held to be property which the bankrupt "could by any means have transferred or which might have been levied upon," and so passed to the trustee. *Accord: In re Matschke*, 193 Fed. 284 (D.C. N.Y. 1912); *In re Kern*, 8 F. Supp. 246 (D.C. N.Y. 1934). Similarly, an annuity on which the annuitant has made all payments before the petition in bankruptcy has always been held to pass to the trustee as property vested in the bankrupt. *In re Burtis*, 188 Fed. 527 (D.C. N.Y. 1911). Rights under the disability policy are like any other rights, acquired by the bankrupt before bankruptcy, to receive payment thereafter; and such rights pass to the trustee even though the amount be indefinite. *In re Wright*, 157 Fed. 544 (C.C.A. 2d 1907) (contract to receive commissions on renewal for a term of years after bankruptcy); *In re Evans*, 253 Fed. 276 (D.C. Tenn. 1918) (wages earned before the petition to be paid thereafter). Even contingent remainders that are transferable under state law are considered property falling within § 70(a) (5). *Clowe v. Seavey*, 208 N.Y. 496, 102 N.E. 521 (1913). But expectancies do not pass to the trustee. *In re Baker*, 13 F. (2d) 707 (C.C.A. 6th 1926).

In the principal case, the bankrupt contended that his disability policy fell within the proviso of § 70(a) (5) and that since it had no cash surrender value, no interest in it ever passed to the trustee. Decisions of the Supreme Court have established the rule that the proviso of § 70(a) (5) standing alone is the only source of the trustee's rights to a bankrupt's life insurance; that the trustee gets no title to life policies but is entitled only to the cash surrender value thereof. *Burlingham v. Crouse*, 228 U.S. 459 (1913). An earlier view was *contra*, 3 Remington, Bankruptcy § 1243 (3d ed. 1923). The bankrupt insisted that his disability policy was like life insurance in this respect and indeed the proviso is not in terms limited to life insurance. But in previous cases the Supreme Court had interpreted the proviso as limiting the rights of creditors to the cash surrender value solely for the purpose of giving protection to the bankrupt's dependents after his death. *Burlingham v. Crouse*, 228 U.S. 459 (1913). In the instant case the court declined to find in the proviso any protection for the insured or his dependents during his life.

The bankrupt next argued that the disability policy was merely supplemental to his contract of life insurance and was so integrated with and dependent on the latter that it took on the character of the life policy. This theory of integration has been used to bring disability insurance within state statutes exempting life insurance. *Baranovich v. Horwatt*, 113 Pa. 467, 173 Atl. 676 (1934). But these decisions are illustrations of a very liberal construction of state statutes (see *infra*) treating exemptions for the benefit of a debtor and have no parallel in previous decisions construing § 70(a) (5). It seems that the court in the instant case was correct in holding that the two kinds of insurance were two distinct contracts. The disability policy could have elapsed without terminating the life policy; and the hazards of each were different.

Under § 6 of the Bankruptcy Act, bankruptcy courts must apply state exemption statutes. *Holden v. Stratton*, 198 U.S. 202 (1905). Most states have insurance exemption statutes. Some of these expressly exempt matured disability policies. Section 55B, N.Y. Ins. Laws, c. 626 (1934); Pa. Pub. L. 276 (40 P.S. § 766). The Tennessee statute fails to do so expressly but exempts *annuities* made for the "benefit of, or assigned to the wife and/or children or dependent relatives" of the insured whether or not the insured reserved the right to change the beneficiary. Tenn. Code 1932 § 8458. The court in the instant case held that the policy was not within this statute because the insured, rather than his wife or dependents, was the beneficiary. This result shows a narrow interpretation of the statute. Under the statute which reads "whether or not the right to change the . . . . beneficiary is reserved," if the insured had named his wife as beneficiary, he would have retained the policy even though he reserved the right to change the beneficiary. See Glenn, Fraudulent Conveyances § 181 (1931). And he could have changed the beneficiary to himself after bankruptcy. See *In re Vaughn*, 2 F. Supp. 385 (D.C. Fla. 1932). Therefore, where as in the instant case the right to change is retained, it should make no difference who is named beneficiary. *Cf. Houston v. Maddux*, 178 Ill. 377, 53 N.E. 599, 602 (1899). The court properly considered the matured disability policy an annuity. The typical annuity arises from an investment by the annuitant of a certain sum until a fixed future date from which time the annuitant receives monthly payments until his death. A disability policy is an annuity which differs from the typical only in the fact that part of its value (that above the premiums) arises from the insured's becoming disabled. Since the difference only makes the disability policy less harmful to creditors, the legislature could not have intended to exclude such a policy. A Tennessee appellate court has held that disability benefits under a health insurance policy are not exempt because disability insurance is not life insurance. *Cravens v. Robbins*, 8 Tenn. App. 435 (1928). But in that case no reference was made to that section of the statute which exempts annuities. And the Tennessee Supreme Court has been liberal in construing its exemption statutes. *Rose v. Wortham*, 95 Tenn. 505, 32 S.W. 458 (1895). See *In re Stansell*, 8 F. (2d) 363 (D.C. Tenn. 1925).

The statutes of most states exempt only life insurance. But most courts under these statutes have exempted not only the proceeds of the insurance on the insured's death but also the cash surrender value of the policy during his life even though the statutes are ambiguous. *In re Stansell*, 8 F. (2d) 363 (D.C. Tenn. 1925); *In re Phillips*, 7 F. Supp. 807 (D.C. Pa. 1934); *Contra*, *In re Grant*, 21 F. (2d) 88 (D.C. Wis. 1927). In these jurisdictions there is some probability that the life insurance exemption will be stretched to include disability insurance because (1) disability deprives the insured of the capacity to earn a living which is detrimental to himself, his dependents and the community; (2) by exempting the cash surrender value of life policies, these courts have already construed these statutes as making available to the insured a sum of money free from the claims of his creditors; (3) exemption statutes are to be construed liberally (*Hickman v. Hanover*, 33 F. (2d) 873 (C.C.A. 4th 1929)); (4) disability insurance, in the form of a supplementary contract to a life policy might be considered so integrated with the life policy that the disability insurance takes on the character of life insurance. *Baranovich v. Horwatt*, 113 Pa. 467, 173 Atl. 676 (1934). But see *contra*, *Cravens v. Robbins*, 8 Tenn. App. 435 (1928); *Chattanooga Sewer Pipe Works v. Dumler*, 153 Miss. 276, 120 So. 450 (1929); *Baxter v. Old Nat'l City Bank*, 46 Ohio App. 533, 189 N.E. 514 (1933).

In many endowment policies the insured pays premiums until a certain date at which time he becomes the beneficiary of an annuity; and if he dies before that time a third person gets only the amount of premiums paid in plus interest. Such contracts are not life insurance, but investments (Vance, Insurance 153 (2d ed. 1930)) and have been held not to come within a statute exempting only life insurance. *Moskowitz v. Davis*, 68 F. (2d) 818 (C.C.A. 6th 1934). But where an endowment policy provided that on the death of the insured before the endowment matured, the beneficiary was to get a stated sum irrespective of the amount of premiums paid in by the insured, the policy was held to be life insurance and so within the exemption statute. *In re Weick*, 2 F. (2d) 647 (C.C.A. 6th 1924). The cash surrender value of such a policy is greater than that on a straight life policy because premiums paid are building up a future annuity. This excess represents an investment which, if standing alone, would go to creditors under *Moskowitz v. Davis*, *supra*. If the mere fact that the investment feature is combined with a life insurance feature will exempt an annuity, certainly a matured disability policy which is incidental to a life policy should be exempt. But see *Baxter v. Old Nat'l Bank*, 46 Ohio App. 533, 189 N.E. 514, 517 (1933) (same statute but analogy not raised).

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Business Trusts—Liability of Trust Estate on *Ultra Vires* Contracts—Unjust Enrichment—[Massachusetts].—The plaintiff, under a contract with one of two trustees, installed the plumbing in an apartment building belonging to a business trust. The co-trustee authorized the construction work but did not sign the contract. The contracting trustee failed to insert a clause exempting himself from personal liability as directed by the recorded trust instrument. When the contracting trustee became insolvent, the plaintiff sued in equity to reach the trust estate. *Held*, recovery denied;