

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF IOWA**

In the Matter of:

Steven Robert Gates,

Debtor

Case No. 11-03226-als7

Chapter 7

**MEMORANDUM OF DECISION
(date entered on docket: March 9, 2012)**

BACKGROUND

The matter before the Court is the Chapter 7 trustee's ("Trustee") timely filed objection to the Debtor's claim of exemptions in two insurance policies. Calculation of the Debtor's exempt interest in the value of these policies is the only issue to be resolved. At a telephonic hearing, the parties stated that there were no factual disputes and no legal precedent on the issue. By agreement, the matter is fully submitted based solely on the hearing record and the filed documents. Jurisdiction for this core proceeding is pursuant to 28 U.S.C. sections 157 and 1334. For the reasons stated herein the Trustee's Objection to Exemptions is overruled.

DISCUSSION

Steven R. Gates ("Debtor") filed a voluntary chapter 7 proceeding on August 10, 2011. Schedule B-9 identified two life insurance policies: Guardian Life valued at \$31,695 and Lafayette Life valued at \$262,108. The policies designate the Debtor's spouse as the beneficiary. These policies were claimed as exempt on Schedule C in the respective amounts of \$4,029 and \$10,293. Annual premiums on these policies have consistently been paid in

advance. Premium payments have remained constant since the purchase of the original policies, except for a reduction in the amount paid on the Lafayette policy starting in March 2010.

In framing their arguments, the parties rely on two concepts: “gross cash value” and “net cash value.” The insurance contract, which would presumably provide definitions for these terms, was not provided to the Court. Based upon the exhibits and the arguments made at the time of hearing, the following characterizations of these terms are adopted for purposes of this ruling. Gross Cash Value is the total value of the policy without any reduction to reflect outstanding loans existing against the policy. Net Cash Value is the cash amount payable to the insured after deducting all outstanding policy obligations (commonly referred to as cash surrender value).

Iowa has opted out of the federal exemption provisions and its residents must utilize state law exemptions in bankruptcy. See Iowa Code § 627.10 (2011). Iowa law provides for an exemption in insurance policies by stating in relevant part:

The interest of an individual in any accrued dividend or interest, loan or cash surrender value of, or any other interest in a life insurance policy owned by the individual if the beneficiary of the policy is the individual's spouse, child, or dependent. However, the amount of the exemption shall not exceed ten thousand dollars in the aggregate of any interest or value in insurance acquired within two years of the date execution is issued or exemptions are claimed, or for additions within the same time period to a prior existing policy which additions are in excess of the amount necessary to fund the amount of face value coverage of the policies for the two-year period.

Iowa Code § 627.6(6) (2011) (“Statute”). At issue in this proceeding is the method by which any increase in value during the two year time period is calculated. The policy values

for this time period are summarized below.

GUARDIAN	8/10/2009	8/10/2010	8/10/2011	Increase/(Decrease)
GROSS CASH VALUE	\$10,271	\$20,700	\$31,695	\$21,424
POLICY LOAN(S)	\$0.00	\$20,667	\$27,666	
NET CASH VALUE	\$10,271	\$33	\$4,028	(\$6,243)

LAFAYETTE	8/10/2009	8/10/2010	8/10/2011	Increase/(Decrease)
GROSS CASH VALUE	\$217,411	243,188	\$263,183	\$45,772
POLICY LOAN(S)	\$156,987	\$217,133	\$226,421	
NET CASH VALUE	\$60,424	\$26,055	\$36,762	(\$23,662)

The Trustee argues that the change in the total Gross Cash Value is the proper measure to determine whether there has been an increase beyond the \$10,000 limitation contained in the statute. Under this theory, because the Gross Cash Value of the Debtor's policies increased by the aggregate amount of \$67,196.00 within the two years prior to filing, the Debtor would be limited to claiming \$10,000 of this total increase as exempt. The remaining balance of the aggregate increase of \$57,195.20 would not be exempt and could be administered by the Trustee.

The Debtor counters by asserting that the value of the exemption is more appropriately calculated by comparing the aggregate Net Cash Values under the policies as of August 10, 2009 and August 10, 2011. Utilizing this formula represents the Debtor's interest in the actual cash values available under the policies. By way of example, under the facts of this case, the Debtor's exemption in the Guardian policy is initially established at \$10,271 and in the Lafayette policy at

\$60,242 for an aggregate total of \$70,513. Only if the Net Cash Value increased by more than \$10,000 above this initial aggregate total as of August 20, 2011 would the statutory restriction be applicable to his exemption claim. Because this did not occur, the Debtor argues that he is entitled to claim the total Net Cash Values under both policies as exempt.

Determining the intent and purpose of a law begins with general principles of statutory construction. See Iowa Comprehensive Petroleum Underground Storage Tank Fund Bd. v. Mobil Oil Corp., 606 N.W.2d 359, 363 (Iowa 2000). It is well settled that legislative intent is based upon the plain language used in a statute. See In re Fowler, 784 N.W.2d 184, 187 (Iowa 2010); Benjegerdes v. Reindl (In re Reindl), 671 N.W. 2d 466, 469 (Iowa 2003). “The court is not at liberty to read into the statute provisions which the legislature did not see fit to incorporate, nor may it enlarge the scope of its provisions by an unwarranted interpretation of the language used.” Moulton v. Iowa Emp’t Sec. Comm’n, 34 N.W.2d 211, 216 (Iowa 1948). This exercise requires evaluating the statute as a whole instead of focusing on “isolated words or phrases.” In re Conservatorship of Alessio, 803 N.W. 2d 656, 661 (Iowa 2011). The issue presented in this case also requires the Court to be mindful of the proposition that Iowa exemption statutes are liberally construed in favor of a debtor to confer the intended benefit. See Frudden Lumber Co. v. Clifton, 183 N.W.2d 201, 203 (Iowa 1971).

Recorded legislative history may also assist in discerning legislative intent. In 1988, the Iowa Legislature passed House File 649, which amended the Statute to its current form. 1988 Iowa Acts ch. 1255 § 7. Before the amendment, Iowa Code section 627.6(6) read “[a]ny unmaturred life insurance policy owned by the debtor, other than a credit life insurance contract.” Iowa Code § 627.6(6) (1987). This prior version of the statute did not restrict the value or dollar amount of insurance that could be claimed as exempt. Looking to the original House File 649,

as produced by the Committee on Judiciary and Law Enforcement, there was a brief explanation paragraph in the original bill. H.F. 649 Explanation, 72d Gen. Assemb., Reg. Sess. (Iowa 1988). The explanation merely recites the content of the bill, and sheds no light on the legislative intent for the issue raised in this proceeding. Also contained in the record of amendments to the bill is a suggestion for a study committee to research abuse of bankruptcy exemptions. H.F. 649 Proposed Amendment H-6061, 72d Gen. Assemb., Reg. Sess. (Iowa 1988). Lastly, the legislature deemed this bill of “immediate importance” and declared that it should be effective upon enactment. 1988 Iowa Acts ch. 1255 § 10. All of this information combined depicts a legislature that was concerned about the abuse of the unlimited insurance exemption available to individuals under Iowa law, and the amendment was passed to curb the ability of an individual to obtain an unlimited amount of life insurance from the disposition of non-exempt assets prior to a bankruptcy filing or potential creditor execution. It is with this additional background that the facts of this case and the Statute are analyzed.

The first sentence of the Statute identifies and grants the exemption as follows:

The interest of an individual in any accrued dividend or interest, loan or cash surrender value of, or any other interest in a life insurance policy owned by the individual if the beneficiary of the policy is the individual's spouse, child, or dependent.

Iowa Code § 627.6(6) (2011) (emphasis added). This language clearly allows an individual holding an “interest” in one of the enumerated items, or even more broadly stated “any other interest” in a life insurance policy as exempt. An “interest” can generally be described as a right, share, or claim to property, and in this instance, would arise under the contract that created and governs the insurance policy. The term ‘interest’ is not defined in the Bankruptcy Code but has been interpreted as being limited to an equity interest in a debtor.” William L. Norton, Jr.,

Norton Bankr. L. & Prac. 3d Dictionary of Bankr. Terms § I115 (2012). This description implies that value can only be calculated after allowing for payment of liabilities that may exist against the property subject to an ownership interest. There is no question that under any definition, the Statute permits an expansive range of interests in life insurance policies to be protected from creditors' claims.

The Statute, in its second sentence, addresses the value of any interest in an insurance policy that may be claimed as exempt. The primary disagreement between the parties arises under the language of this section. The law states in relevant part that:

the amount of the exemption shall not exceed ten thousand dollars in the aggregate of any interest or value in insurance acquired within two years of the date . . . exemptions are claimed.

Iowa Code § 627.6(6) (2011).¹ The amount of the exemption cannot exceed an increase of more than \$10,000 in one of two alternatives – “any interest” or “any value” in insurance during the two year time period.

The Trustee focuses on the word “value” in this portion of the Statute, reasoning that if the legislature had intended for the cash surrender value (or as used here Net Cash Value) of the policy to be considered in calculating the \$10,000 limitation, the Legislature could have included those exact words in the Statute. The word “value” as it appears in this sentence of the Statute is not modified by any other terms. It is equally plausible to conclude that the legislature specifically excluded the use of the terms “face value,” “total value” or “gross cash value” in drafting this provision. Because none of these options can be read into the Statute this argument must be rejected. The term “interest,” contrary to the generic use of the term “value,” has been specifically defined by the Statute for purposes of the exemption claim. When interpreting a

¹ The parties agree that use of the word “aggregate” requires the dollar restriction to be applied against all policies owned by the Debtor at the time of his bankruptcy filing.

statute, use of a more specific or identified term is generally preferred over the use of a more general or generic alternative. See Oyens Feed & Supply, Inc. v. Primebank, 808 N.W.2d 186, 2011 WL 6849603, at *8 (Iowa Dec. 30, 2011) (“To the extent there is a conflict or ambiguity between specific and general statutes, the provisions of specific statutes control.”) (citations omitted). See also Westinghouse Credit Corp. v. Crotts, 98 N.W.2d 843, 845-46 (Iowa 1959) (discussing whether cash surrender value of life insurance contract is exempt from creditor claims).

Because the legislature described the types of “interest” that may be claimed as exempt, there is no reason to ignore or deviate from the earlier characterization of that word as used in the Statute. Cash surrender value is an interest that can be claimed as exempt, and as such can constitute the basis for computing whether such an interest increased by more than \$10,000 within the prior two years.

The Trustee urges that any determination of the claimed exemption be independent from a determination of whether there may be any actual cash value available for administration by the bankruptcy estate. While this may represent a technically correct procedure, it does not promote judicial economy or efficient case administration. In any bankruptcy proceeding, all individual debtors must file Schedule C – Property Claimed as Exempt.² This form requires a debtor to state the value of a claimed exemption and then provide the current total value of the property. These two values need not be identical.³ A comparison of how value is stated on Schedule C when claimed under other Iowa exemption statutes is helpful in interpreting the Statute at issue in this case.

² B6C (Official Form 6C) (4/10) Schedule C – Property Claimed as Exempt

³ As noted on the Debtor’s filings, his interest in the insurance policies identified on Schedule B – Personal Property (B6B (Official form 6B 12/07) are much higher than the values claimed as exempt on Schedule C.

Iowa Code section 627.6(9) allows an individual to exempt an “interest in one motor vehicle, not to exceed in value seven thousand dollars.” Iowa Code § 627.6(9) (2011). In practice, and according to the official bankruptcy forms, the amount claimed as exempt on Schedule C is a debtor’s equity in the vehicle which is determined after allowing for any unpaid liens. For example, if an individual listed a vehicle valued at \$20,000 with a valid secured loan against it in the amount of \$15,000, the individual’s stated exemption value would be calculated as \$5,000. Iowa Code section 561.16 permits an individual to claim a homestead interest as exempt. Iowa Code § (2011). Similar to Iowa Code section 627.6(9), the exemption is claimed in the equity remaining in the homestead after allowance for any mortgages against the property. Applying a different standard to compute a debtor’s exemption in a life insurance policy is not justified under the Statute. As a general proposition, it is common for an insurer to require application of the Gross Cash Value available under a policy to satisfy outstanding loans prior to paying the resulting Net Cash Value to the insured. See 5 Lee R. Russ, Couch on Insurance § 80:45 (2011). To suggest that another manner of calculation should be utilized, would permit the Trustee to calculate a value under the policy that would be higher than any “interest” available to the Debtor.

IT IS THEREFORE ORDERED that under the facts of this case, the Trustee’s Objection to the Debtor’s Claim of Exemption is overruled.

/s/ Anita L. Shodeen
Anita L. Shodeen
U.S. Bankruptcy Judge

Parties receiving this Memorandum of Decision from the Clerk of Court:
Electronic Filers in this Chapter Case
Others: S. Gates, Debtor