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LIFE INSURANCE AS ASSETS AVAILABLE TO CREDITORS OF THE INSURED DURING HIS LIFETIME UNDER THE LAW OF NORTH DAKOTA

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Two sections of the 1943 Revised Code of North Dakota must be examined as a prelude to any discussion of the topic at hand.

Section 26-1017 provides:[1]

"The surrender value of any policy of life insurance which, upon the death of the insured, would be payable to the wife or children or any relative of the insured, dependent, or likely to be dependent, upon him for support, shall be exempt absolutely from the claims of creditors of the insured. No creditor of the insured, and no court or officer of a court acting for any such creditors, shall have the right under any circumstances to elect for the insured to have such policy of insurance surrendered or in any wise converted into money, and no such policy of life insurance or property right therein belonging to the holder, and no value thereof, shall be subject to seizure under any process of any court under any circumstances."[1a]

Section 26-1018 provides:[2]

"The avails of a life insurance policy or of a contract payable by any mutual aid or benevolent society, when made payable to the deceased, to the personal representative of the deceased, to his heirs, or to his estate, shall not be subject to the debts of the decedent upon the death of such insured or member of such society except by special contract. . ."[2a]

At the outset, it should be noted that the discussion involves the second section by indirection only. We are primarily concerned with the first section, which purports to exempt the proceeds of the policy from the creditors of the insured during his lifetime.[3] It must appear

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[1] N. D. Laws 1915 c. 173, s. 1; N. D. COMP. LAWS ANN. (SUPP. 1925), s. 878a; N. D. REV. CODE (1943), s. 26-1017.

[1](a) The original bill was introduced in the Senate. *Englund*, S. B. 103. The following amendment was proposed by the judiciary committee: "If the premium is paid by any person with intent to defraud his creditors, an amount equal to the premiums so paid, with interest thereon, shall inure to their benefit. . ." The amendment failed to carry the House. For form of amendment, see SEN. JOUR. (1915) p. 226.

[2] N. D. REV. CODE (1895), s. 6385; *amended* N. D. Laws 1897, c. 111, s. 24; N.D. REV. CODE (1899), s. 6385; N. D. REV. CODE (1905), S. 8083; N. D. COMP. LAWS ANN. (1913), s. 8719; *amended* N. D. Laws 1927, c. 225, s. 1; and again in N. D. Laws 1929, c. 149, s. 1; N. D. REV. CODE (1943), S. 26-1018.

[2](a) A brief discussion of this section will be found in 18 BAR BRIEFS, STATE BAR ASS'N OF N. DAK., p. 102 (Jan. 1942). As originally enacted this statute read: "The avails of a life insurance policy or of a contract payable by any mutual aid or benevolent society upon the death of a member of such society are not subjcet to the debts of the decedent except by special contract, but in other respects shall be inventoried and disposed of like other property." N. D. REV. CODE (1895), s. 6385. See discussion in *Jorgensen v. DeViney*, 57 N. D. 63, 74; 222 N. W. 464, 468 (1928); *Farmer's State Bank v. Smith*, 36 N. D. 225, 233; 162 N. W. 302, 304 (1917).

[3] N. D. CONST. art. XVII, s. 208, provides: "The right of the debtor to enjoy the comforts and necessaries of life shall be recognized by wholesome laws, exempting from forced sale to all heads of families a homestead, the value of which shall be limited and defined by law; and a reasonable amount of personal property; the kind and value shall be fixed by law . . ." In the opinion of one writer: "The exemption laws of today are almost everywhere vicious. They extend a protection beyond reason, which is easily done away with by the honest debtor by incumbering his exemptions, and therefore they destroy their own effect. To the dishonest debtor they furnish opportunity for moral fraud on his creditors within the law." John H. Lewis, *Principles of Exemption Laws*, (1928) 2 DAK. LAW REV. 140, 145.

It has been suggested that laws exempting the proceeds of life insurance permit the man who owns no property to acquire a homestead. GLENN, FRAUDULENT CONVEYANCES AND PREFERENCES (Rev. ed. 1940), s. 175, p. 317. To be effective, such protection should cover the proceeds in the hands of the beneficiary. N. D. LAWS 1913, c. 191, s. 21; N. D. COMP. LAWS ANN. (1913), s. 5078; N. D. REV. CODE (1943), s.26-1222; covers the beneficiary in fraternal benefit policies. Held constitutional in *Brown v. Steckler*, 40 N. D. 113, 1 A.L.R. 753, 168 N. W. 670 (1918).

at once from a careful analysis of this section that ambiguity of expression leaves much to the good judgment of the court. For example, the term "life insurance" must be defined. Is an annuity contract "life insurance"?[4] Would accrued dividends;[5] endowment provisions, where the judgment debtor survives the life insurance term;[6] disability payments;[7] or the cash value, where an election is made to cash in the policy,[8] be protected?

What does the statute mean by the expression "would be payable"? Is it necessary to specifically designate the beneficiary falling within the class protected under the statute? The problem is illustrated by assuming a case where the insured has a wife, child, or dependent relative living, but has designated his estate as beneficiary. In such a case "would be payable" is open to two possible constructions. First, it might mean that the beneficiary must be designated. Second, it might mean that any policy which upon death of the insured might fall under the second section if no change in statute thereafter occurred, is within the protection of the first section. Since the presumed intention of the legislature was to protect the wife, child, or dependent relative by

[4] It is commonly accepted that annuity contracts are not insurance. For an illustrative case see *In re Walsh*, 19 F. Supp. 567 (D.Ct. Minn., 1937). At page 575, the court states: ". . . a savings plan annuity contract, in which the insurance feature is nothing more than the return of the cash surrender value, does not come within the purview of the statute in question."

Statutes requiring the filing of insurance forms have been held not to apply to annuity contracts. *Hall v. Metropolitan Life Insurance Co.*, 146 Or. 32, 28 P.2d 875 (1934); *Rishel v. Pacific Mut. Life Ins. Co.*, 78 F2d 881 (C.C.A. 10th, 1935). The question is frequently raised in tax cases. *Daniel v. Life Ins. Co. of Va.*, 102 S.W.2d 256 (Tex. Civ. App. 1937) (Foreign company held not subject to occupation tax on annuity premiums); *Old Colony Trust Co. v. Comm. Int. Rev.*, 102 F2d 380 (C.C.A. 1st, 1939) (annuity fund properly included in gross taxable estate, and not excluded to extent of $40,000 as "Insurance"). However, annuity contracts frequently combine life insurance features. Compare cases in note 6, *infra.*

[5] Dividends represent earnings, and the insured is given various options, among which are included the privilege of receiving them in cash, or applying them upon premiums, adding them to the principal amount payable to the beneficiary on death, or perhaps applying them upon additional paid-up insurance. Dividends would seem to be exempt under the broad language of our statute. But see *New York Plumbers' Specialties Co., Inc. v. Stein*, 136 Misc. 703, 240 N.Y.S. 834 (1930), where dividends payable to insured were recovered in supplementary proceedings. But if the insured exercises an option that will benefit the beneficiary, the result is otherwise. *Radnik Realty Corp. v. Moseyeff*, 147 Misc. 618, 263 N.Y.S. 440 (1933). *Cf. Bethards v. Metropolitan Life Ins. Co.*, 287 Ill. App. 7, 4 N.E. 2d 257 (1936). Holding dividends not to be within an exemption statute, see *Ellison v. Straw*, 119 Wis. 502, 97 N.W. 168 (1903). The Wisconsin court suggests that there is no "legislative intent. . . to screen the husband in building up for himself a fund beyond the reach of his creditors." The court continues: "Life insurance is one thing, investment is another, but the ingenuity of the life insurance companies in formulating contracts which confuse the distinction has been active for generations. Pure life insurance has become rare . . . Life insurance is a promise to pay a certain sum upon the death of the assured . . . Doubtless the amount so payable may be augumented by accumulation of excessive premiums and their earnings in the hands of the company without destroying the essential character of the contract. When, however, we find, as frequently, a promise to repay a sum made up from a portion of the premiums and their earnings at a date certain in the lifetime of the assured, we have only a contract such as a savings bank may as well make." *Id.* at 97 N.W. 170.

[6] The modern trend is contra to *Talcott v. Field*, 34 Neb. 611, 52 N. W. 400 (1892); followed in *Bank of Brule v. Harper*, 141 Neb. 616, 4 N.W.2d 400 (1942). While the investment feature is prominent in the modern policy, and may play a part where regulatory problems are involved, as in *Marsh v. Bowan*, 335 Pa. 305, 6 Atl. 2d 781 (1939); the tendency is to disregard the property rights of the insured when the rights of a beneficiary are under consideration. See note in 19 A.L.R. 654-664; VANCE INSURANCE (2d ed. 1930), p. 547. As indicated by the court in *Briggs v. McCullough*, 36 Cal. 542, 550 (1869), "The term 'life insurance' is not alone applicable to an insurance for the full term of one's life. On the contrary, it may be for a term of years, or until the assured shall arrive at a certain age." Speaking of the annuity feature, the court went on to say: "It is only a new and additional element in the contract not inconsistent with its other, which is its chief constituent part, to wit: the undertaking to pay on the death of the assured within the specified term." *Id.* at 551. *In accord*: *Drysch v. Prudential Ins. Co. of America*, 287 Ill. App. 68, 4 N. E. 2d 530 (1936) (garnishment action); *but see Scobie v. Connor*, 94 Misc. 429, 157 N.Y.S. 567 (1916).

[7] Disability payments, like dividends, might be considered as no concern of the beneficiary, since payable to the insured. In fact, the creditor's case is much stronger here. See discussion by *Isadore H. Cohen, Execution Process and Life Insurance*, (1939) 39 COL. LAW REV. 139, at pp. 154 and 161. To the effect that disability benefits are included in the term "cash surrender" value, see *Bank of Greenwood v. Rawls*, 117 Fla. 381, 158 So. 173 (1934); *contra, Commissioner of Banks v. Yelverton*, 204 N. C. 441, 168 S. E. 505 (1933). In the latter case the court permitted the debtor to select the $300 due him each month as part of the $500 personal property exemption allowed by statute. The matter is better handled by a separate exemption statute. See Cohen, *op. cit. supra*, p. 161, n. 1. *Cf. Edgar A. Levy Leasing Co. v. Wishner*, 147 Misc. 288, 265 N.Y.S. 184 (1933); *Preston v. Martin*, 69 S. W. 2d 472 (Tex. Civ. App. 1934).

[8] Early cases in New York permitted creditors to reach the cash surrender value, altho no election to surrender the policy had been made by the insured. *Cavagnaro v. Thompson*, 78

exempting the proceeds during the life of the insured, the second view seems most reasonable.[9]

Whether or not the statute is constructed as covering only designated beneficiaries, the question still arises, should the court take the words of the act literally or treat the statute as a blanket exemption? Thus, if a wife is independently wealthy, will the legal duty of the husband to support raise a presumption—contrary to the facts—that she is "likely to be dependent" within the meaning of the statute? Is a mother "likely to be dependent" upon the son whose life is insured for her benefit? If we assume that the mother is living with a solvent husband who carries $100,000.00 of insurance for her benefit, what then? What of the bachelor without relatives or dependents of any kind, who either names his estate as beneficiary, or has specified a beneficiary with the usual alternative provision designating his estate in case the beneficiary does not survive.[10]

The answer to these, and many other questions that may arise in the future depends in part upon the meaning of the second section. If the latter is an outright exemption statute exempting the proceeds of any policy that falls within its terms, before death as well as after, the reason for enactment of the first section would be hard to explain. It is possible that the legislature felt that some doubt existed as to present exemption in favor of the insured, and hence it was necessary to supplement the second section by enacting the first, thus making it clear that the exemption was intended to protect dependents related by blood or marriage.[11] At any rate, our law is clear on the point that the second

Misc. Rep. 687, 138 N.Y.S. 819 (Sup. Ct. 1912); *Clark v. Shaw*, 91 Misc. Rep. 245, 154 N.Y.S. 1101 (Co. Ct. 1915); *Hall v. Hess*, 97 Misc. Rep. 331, 161 N.Y.S. 418 (Sup. Ct. 1916); *Ecker v. Myer*, 118 Misc. Rep. 356, 194 N.Y.S. 320 (City Ct., N. Y. 1922), 118 Misc. Rep. 443, 194 N.Y.S. 654, *rev'd on point of practice*, 19 Misc. Rep. 375, 196 N.Y.S. 268 (Sup. Ct. 1922). The theory adopted by these cases is based upon the reserved power to change the beneficiary at will. The decisions indicate that such dominion is inconsistent with property in the beneficiary, and the policy constitutes assets of the insured available to his creditors in supplementary proceedings. The customary practice was to apply for appointment of a receiver who took possession of the policy. It would appear proper to conclude that the receiver had title and hence could exercise all options, including the power to change the beneficiary and cash in the policy. The New York decisions indicate that his title is not limited to the cash value. *Reynolds v Aetna Life Ins. Co.*, 160 N. Y. 635, 55 N. E. 305 (1899). However, in later cases the court changed its view. In *Maurice v. Travellers Ins. Co.*, 121 Misc. 427, 201 N.Y.S. 369 (Sup. Ct. 1923), the receiver sued the company directly. In dismissing the complaint, the court intimated that a court of equity had no power to order the insured to exercise his options under the contract, and in the absence of such an order, the receiver could recover nothing. The view of the court seems due to faulty reasoning. The policy is property, and if title passed, the receiver had power to exercise all options under the contract. Further, a court of equity has inherent power to order the necessary transfer. In the particular case the beneficiary ultimately recovered the policy, no appeal being taken by the receiver. *Gershman v. Berliner*, 214 App. Div. 196, 211 N.Y.S. 881 (1925). The trend in other jurisdictions is in accord with the last two cases. *Murphy v Casey*, 150 Minn. 107, 184 N. W. 783 (1921); *Shurszberg v. Prudential Ins. Co.*, 15 N. J. Misc. 423, 192 Atl. 451 (1936); and note in 57 A.L.R. 695 (1928). Before election by insured to surrender the policy, the cash value is not subject to garnishment, *Bethards v. Metropolitan Life Ins. Co.*, 287 Ill. App. 7, 4 N. E. 2d 257 (1936); *First Nat. Bank of Burkbarnett v. Friend*, 23 S. W. 2d 482 (Tex. Civ. App. 1929); nor can it be reached by creditor's bill, *Fidelity Coal Co. v. Diamond*, 322 Ill. App. 229, 54 N. E. 2d 240 (1944); *Contra*: *Anthracite Ins. Co. v. Sears*, 109 Mass. 383 (1872). In *Crossman v. Rauch*, 263 N. Y. 264, 188 N. E. 748 (1934), *rev'g.* 238 App. Div. 299, 264 N.Y.S. 111 (Sup. Ct. 1933), income paid out under an insurance trust was held not subject to garnishment under special statute.

[9] No case has reached the Supreme Court in which an attempt was made to secure the cash surrender value before death of the insured. The statute was mentioned in passing by only two cases. *Re Coughlin*, 53 N. D. 188, 205 N. W. 14 (1925); *Jorgensen v. DeViney*, 57 N. D. 63, 222 N.W. 464 (1928). Both decisions speak of the second section as an exemption statute; that it is not within section 208 of our Constitution, see *Farmers' State Bank v. Smith*, 36 N. D. 225, 162 N. W. 302 (1917). The construction contended for seems to be the one accepted in Tennessee. *Wright v. Wright*, 100 Tenn. 313, 45 S. W. 672 (1898).

[10] *Wright v. Wright*, 100 Tenn. 313, 45 S. W. 672 (1898).

[11] "There is nothing in section 8719. . . indicating any intention . . . to control the terms of a life insurance contract, or to restrict the right of the insured during his lifetime to dispose of the same or the avails thereof . . . The statute by its express terms, purports to become effective only upon the death of the insured. It does not even purport to exempt insurance policies of the kind therein described or the cash surrender value thereof from the claims of creditors during the lifetime of the insured. In fact, the legislature subsequently deemed it necessary to enact another statute to accomplish this purpose." Christianson, J., in *Jorgensen v. DeViney*, 57 N. D. 63, 80, 222 N. W. 464, 470 (1928).

section is an exemption only to the estate of the insured and our court has taken the position that the constitutional prohibition of unlimited exemptions has no application to an exemption after death.[12]

The problem of reaching the policy or its proceeds cannot be disposed of without first considering the nature of the insurance contract and the nature of the beneficiaries' interest therein. A cannot take B's property to satisfy the debt of another. If the insurance contract creates a vested property right in the beneficiary, creditors cannot reach the policy or its value to satisfy the debt of the insured. Thus, the American view that where no power to change the beneficiary is reserved, the latter has a vested interest that constitutes property in the contract itself, carries the logical implication that no exemption statute is necessary to protect the rights of the beneficiary.[13]

That such a result did not satisfy the needs of insurer and insured, is clearly evidenced by the modern practice of reserving power to change the beneficiary, together with other options common to modern insurance contracts, all exercisable without the consent of any existing beneficiary.[14] The new relationship clearly indicated an intent to reserve all property rights to the insured, and consistent with that view are the cases which hold that the cause of action is in the insured, rather than the beneficiary, in case of anticipatory breach by the insurer.[15] But once the rights of a creditor are involved the courts resort to either of two principles to protect the beneficiary; some courts adopt the view that exemption statutes indicate a rule of public policy that prevents recovery under any type of legal process during the lifetime of the insured;[16] a few jurisdictions resort to the vested interest rule despite reservation of the power to change.[17] Either position seems difficult to justify. But even so the creditor's problem is not solved. He must seek legal process that will reduce this asset to possession. Can he resort to garnishment, attachment, execution, creditor's bill, or supplementary proceedings?[18] The cases indicate that his chance of success under any of these is very slim. In the field of the fraudulent conveyance his rights are equally doubtful in the absence of legislation.[19]

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[12] *Farmers State Bank v. Smith*, 36 N. D. 225, 162 N. W. 302 (1917).

[13] VANCE, INSURANCE (2d ed. 1930), sec. 144, 145, pp. 542-3; 7 COOLEY, BRIEFS ON INSURANCE (2d ed. 1928), 6399.

[14] The various views are summarized in *Davis v. Modern Industrial Bank*, 279 N. Y. 405, 18 N. E. 2d 639, 135 A.L.R. 1035 (1939): "The first view is that the insured takes no rights in the policy during the life of the beneficiary; that he has merely the power to divest the named beneficiary of his rights and to vest those rights in a new beneficiary. . . The second view is that the insured, by reserving the right to change the beneficiary and to assign the policy, retains the beneficial ownership of the policy during life, and that the naming of a beneficiary constitutes only an instruction to the company to pay at his death to the person named unless such instruction is changed by the insured. Under this view of the law the beneficiary has a mere expectancy or vested interest subject to be divested or an inchoate right depending entirely upon the will of the insured." Hubbs, Judge, *id.* 18 N. E. 2d at 641, 135 A.L.R. at 1037. The second view is said to represent the great weight of authority. 46 C.J.S., s. 1173, p. 62; 29 AM. JUR., S. 1276, p. 952; 2 COOLEY, BRIEFS ON INSURANCE, (2d ed. 1928) p. 1805; *Rasmussen v. Mutual Life Ins. Co.*, 70 N. D. 295, 298, 293 N. W. 805, 807 (1940).

[15] 29 AM. JUR. s. 313, p. 286; 46 C.J.S. s. 1266, p. 289; 48 A.L.R. 110; 107 A.L.R. 1235.

[16] See *Murphy v. Casey*, 150 Minn. 107, 184 N. W. 783 (1921); *Shurszberg v. Prudential Ins. Co.*, 15 N. J. Misc. 423, 192 Atl. 451 (1936), *cited supra*, note 8.

[17] See cases cited in note 8. 46 C.J.S., s. 1179, p. 86; 37 C.J., s. 354, p. 588; and *Nat. Bank of Commerce v. Appel Clothing Co.*, 35 Col. 149, 83 Pac. 965 (1905).

[18] *Attachment*: 6 C.J., s. 377, p. 206; 7 C.J.S., s. 80, p. 255; 4 AM. JUR., s. 304, p. 746. *Execution*: 23 C.J., s. 48, p. 327; 33 C.J.S., s. 30, p. 160; 21 AM. JUR., s. 405, p. 202; Annotations in 44 A.L.R. 1189, 57 A.L.R. 695; FREEMAN, EXECUTIONS (3d ed. ....) sec. 112, p. 434. *Supplementary Proceedings*: 23 C. J., s. 939, p. 882; 33 C.J.S. S. 350, p. 655; 21 AM. JUR., s. 690, p. 327. *Garnishment*: 28 C.J., sec. 208, pp. 165-66; 38 C.J.S., s. 110 (c), p. 317; 4 AM. JUR., s. 293, p. 740.

[19] Fraudulent conveyances are beyond the scope of this brief comment, but see the excellent discussion by Isadore H. Cohen, *The Fraudulent Transfer of Life Insurance Policies*, (1940) 88 U. PA. LAW REV. 771, Recovery is sometimes limited to the cash surrender value. *First Wis. Nat. Bank of Milwaukee v. Roehling*, 224 Wis. 316, 269 N. W. 677 (1936), *rehearing denied* 224 Wis. 316, 272 N. W. 664 (1936); *Equitable Life Ins. Society of U. S. v. Hitchcock*, 270

Finally, is the statute constitutional? Our court has never passed on this question in relation to the section under discussion.[20] Since the statute itself purports to be an exemption to the insured during his lifetime, the question must be answered at some time in the future.

Unfortunately, any discussion of these problems is complicated by a judicial tendency to emote rather than reason when the supposed rights of a beneficiary are at stake.[21] The courts are distinctly opposed to any onslaught on the fortress of insurance. Little or no authority can be cited from other jurisdictions to support the right of a creditor to insurance proceeds during the lifetime of the insured.[22] The writer feels, however, that current decisions on this subject constitute judicial legislation which has removed assets bordering on astronomical proportions beyond the reach of creditors.[23] A critical analysis of our statutory and case law seems both timely and proper.

The problem is high-lighted when we consider the case of a will. Let us assume that the husband and father invests in a well selected group of stocks and bonds. He drafts a will which sets up a trust after his death for the benefit of his wife and children. Here we have the essence of the insurance contract with power reserved to change the beneficiary at will, or to surrender the policy and demand the cash value. Yet in the case of the policy the assets are exempt under our liberal statute; while in the other case creditors can reach those assets not covered by other exemption laws. Indeed, it cannot be said that one form of transaction shows more of intent to benefit the wife and children than the other. In fact the free use of the policy as collateral in modern business indicates that it is primarily a savings device in many cases, and the real purpose is to benefit the insured during his lifetime.[24]

Stated concisely, then, the two sections under consideration carry the following implications. The first section purports to cover all policies, whether made payable to members of the class covered in the act, by name or as a class; or payable to the estate of one who has a

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Mich. 72, 258 N. W. 214 (1935); commented on in WIS. LAW REV. (1946) 329, by H. Keith Frey, *Creditor Versus Widow on Life Insurance Proceeds.*

"Most authorities hold that the head of a family may rightfully devote a portion of his earnings to insuring his life, thereby making reasonable provision for his family after death, without being held to have intended to hinder, delay, or defraud his creditors, even though he may have been insolvent at the time of procuring the insurance. . ." 24 AM. JUR., s. 87, p. 237. The decision in *Washington Central Bank v. Hume*, 128 U. S. 195, 32 L. Ed. 370, 9 S. Ct. 41 (1888), that the creditor must prove that the insurance company participated in the fraud, seems indefensible in view of the fact that the beneficiary is a donee. *Contra*: *Merchant's & Miners' Transportation Co. v. Borland*, 53 N. J. Eq. 282, 31 Atl. 272 (1895). While no fraudulent conveyance results from the transfer of exempt property, a different problem is posed where premiums come out of the debtor's estate. See Williston, *Can An Insolvent Debtor Insure His Life For The Benefit Of His Wife?* (1891), 25 AM. LAW REV. 185, 193.

[20] If the statute under consideration is applied to past debts it would impair the obligation of contract clause in the Federal Constitution. This would be true even though the policy was taken out after passage of the act, provided the debt existed prior thereto. *Bank of Minden v. Clement*, 256 U. S. 126, 65 L. Ed. 857, 41 S. Ct. 408 (1921); *W. B. Worthen Co. v. Thomas*, 292 U. S. 426, 78 L. Ed. 1344, 93 A.L.R. 173, 54 S. Ct. 816 (1934). This principle has been applied by state courts. *Skinner v. Holt*, 9 S.D. 427, 69 N.W. 595 (1896); *Trust Co. v. Fay*, 14 Wash. 536, 45 Pac. 153 (1896); *Rice v. Smith*, 72 Miss. 42, 16 So. 417 (1894). But compare the language in *How v. How*, 61 Minn. 217, 63 N.W. 627 (1895), *modifying* 61 N.W. 456 (1894). "On a motion for reargument it was suggested for the first time that . . . the statute merely attempted to exempt from her creditors a gift to the debtor, that she parted with no consideration for this gift, and her creditors are in no way injured . . . that without the aid of this statute, by the intervention of a trustee, the donor could have given her the benefit of this fund exempt from seizure by her creditors . . ." *Id.* 63 N.W. 627.

Exemption provisions in state constitutions have been liberally construed in Washington and California. *Holden v. Stratton*, 198 U.S. 202, 49 L.Ed. 1018, 25 S. Ct. 656 (1905).

[21] See Cohen, *op. cit. supra*, note 19, at pp. 140, 171.

[22] But see references in note 17, *supra*.

[23] Much has been written on the subject; for a critical analysis, see two articles by Cohen: *Execution Process and Life Insurance* (1939) 39 COL. LAW REV. 139; *The Fraudulent Transfer of Life Insurance Policies*, (1940) 88 U. PA. L. REV. 771.

[24] See cases cited in notes 4, 5, 6.

wife, children, or dependent relatives living at the moment the creditor seeks to realize on the policy.[25]

It seems reasonable that the statute should not be construed to cover any of the beneficiaries within the classes named in the statute unless they are "dependent," in fact, upon the insured. A holding to the contrary could not be classed as the exemption of "a reasonable amount of personal property" within section 208 of our constitution. Further, it would seem to be an unjustifiable extension of the language used in the statute.[26] In the absence of express legislation, one having a mere expectancy has no standing either from the legal or moral standpoint, as against the rights of creditors.[27] Since our court has recognized that the exemption under the second section does not create a vested right in the beneficiary,[28] and the control of the insured over the policy is limited only by the express terms of the contract, it would be reasonable to conclude from the language used in the first section, that the legislature was vesting in the courts, discretionary power to prevent abuse of a liberal exemption. Viewed from that standpoint, most constitutional objections would disappear. The only objection remaining would be technical—since the constitution states that the "kind and value shall be fixed by law"—would the act so interpreted be an illegal delegation of legislative powers?

The case of the bachelor without dependent relatives does not fall within the spirit of the law. The bulk of exemptions are allowed only to the head of the family as defined by law. The purpose is to protect dependents, not the insured.[29]

The act probably does cover a policy payable to a beneficiary outside the classes protected in the statute. However, two situations are possible and must be distinguished. As already indicated, if no power to change is reserved, under the vested interest rule creditors of the insured are helpless.[30] Where the power to change is reserved, we are faced with the proposition that by exercising the power to change the beneficiary the policy may be brought at once under the protection of the statute. Of course, it might be contended, that the diligent creditor could secure a restraining order,[31] and if we concede that the cash surrender value can be reached by supplementary proceedings, this seems entirely logical. It must be admitted that if the insured effects the change before the creditor can act, the statute will protect him unless the change constitutes a fraudulent conveyance.[32] The better view supports a holding that a change of beneficiary by an insolvent, at least where the policy has a cash surrender value, is a fraudulent conveyance and can be set aside in equity.[33]

The second section, as we have seen, has no operation until the death of the insured.[34] This being true, those policies not within the

[25] The statute has not been judicially construed on this point.

[26] But see the specious argument advanced in the *How* case, cited *supra* note 20. It might be noted that trust analogies fail here for lack of a trust res. Rather, we are dealing with a contract, and third party rights thereunder.

[27] Even the interest of the wife was given little consideration in the early cases. *Supra*, note 8.

[28] *Supra*, note 11.

[29] *Supra*, note 10.

[30] VANCE, *op. cit. supra* note 13.

[31] N. D. REV. CODE (1943), SS. 28-2512, 32-1001. *Hall v. Hess*, 27 Misc. 331, 161, N.Y.S. 418 (Sup. Ct. 1916).

[32] Note 19, *supra*

[33] See references, first paragraph note 19, *supra*.

[34] Note 11, *supra*.

protection of the first section should be subject to legal process. A policy of insurance is personal property within the meaning of the statute defining property subject to execution.[35] The immediate objection to use of this process is that no debt is due.[36] But that would seem to be no obstacle. Promissory notes not yet due may be levied upon and must be sold unless the purchaser or creditor is willing to receive them at par.[37] While it is true that few cases will ever arise when an insurance policy would be accepted at par by a creditor, because premiums must be kept up to realize anything—yet if a twenty year pay contract has but a short time to run it would be readily salable and an excellent investment.[38] Nor is the requirement of an insurable interest any objection to such a procedure.[39]

On the other hand, the true value of the ordinary life policy is fairly represented by its cash surrender value—an asset that should be readily available to creditors[40] in the absence of exemption. If a man has $10,000 in his pocket, surely a court can order him to reach into that pocket and pay the non-exempt portion to a creditor. That seems a fair statement of the problem here. If the creditor seeks to reach the cash surrender value his first step might be to secure a lien by actual levy.[41] Such a lien should preserve the rights of the creditor should the debtor die unexpectedly. Having secured his lien, the creditor will probably resort to supplementary proceedings at the foot of the judg-

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[35] N. D. REV. CODE (1943), s. 28-2108 provides: "All goods, chattels, moneys, and other property, both real and personal, or any interest therein, of the judgment debtor not exempt by law, and all property and rights of property seized and held under attachment in the action are subject to execution. Shares and interests in any corporation or company, and debts and credits, and all other property, both real and personal, and any interest in real or personal property, and all other property not capable of manual delivery, may be taken on execution . ."

That the policy may be assigned and transferred by will, see *Talcott v. Bailey*, 54 N.D. 19, 208 N.W. 549 (1926). The insured clearly has an interest in personal property when he owns a policy on his life with power to assign or change the beneficiary at will. *Anthracite Ins. Co. v. Sears*, 109 Mass. 383 (1872); *Industrial Loan & Investment Co. v. Mo. State Life Ins. Co.*, 222 Mo. App. 1228, 3 S.W. 2d 1046 (1928).

[36] See 21 AM. JUR., s. 405, p. 202; *Boisseau v. Bass' Adm'r*, 100 Va. 207, 40 S.E. 647 (1902) (insured could not collect until twenty year endowment period elapsed); most of the early cases involved policies with no cash surrender value provision. *Day v. New Eng. Mut. Life Ins. Co.*, 111 Pa. 507, 4 Atl. 748, 56 Am. Rep. 297 (1886).

[37] *Johnson v. Dahlquist*, 130 Wash. 29, 225 Pac. 817 (1924), and authorities cited therein; *Industrial Loan & Investment Co. v. Mo. State Life Ins. Co.*, 222 Mo. App. 1228, 3 S.W. 2d. 1046 (1928).

[38] N. D. REV. CODE (1943), s. 28-2114 provides:

"Money levied on may be appropriated without being advertised or sold. The same may be done with judgments, drafts, promissory notes, or other papers of like character, if the judgment creditor will receive them at their par value, and an assignment thereof by the officer shall have the same effect as if made by the execution debtor."

The implication is that if not receivable at par these instruments must be sold by the sheriff. But an undefined rule of public policy might prevent a public sale of an insurance policy. The rule is ennunciated by the court in *Industrial Loan & Investment Co. v. Mo. State Life Ins. Co.*, cited *supra*, note 35: "We are firmly convinced, however, that a life insurance policy cannot be bartered and sold as a chattel at a public sale on execution. Our statute does not contemplate that property of such character may be sold. The creditor has no right to collect more than his debt, and no person purchasing at a sale, if such were permitted, could acquire a greater right than the creditor might have . . . If policies of insurance of this character could be sold to any person who might desire to speculate therein, it would result in interminable litigation and confusion and likewise would seem to be against public policy." *Id.* 3 N.W. 2d at 1049.

[39] N. D. REV. CODE (1943), S. 26-0212.

[40] But the creditor is limited by the terms of the contract. If the policy has no cash surrender value, and public policy prevents barter or sale, the only procedure would be to levy, thus securing a lien which could only be realized on after death. It should be noted that not all modern policies give an option to the insured to take the cash value at any time. Such a right generally arises only after a premium is in default. However, the policies do have a loan value, they can be assigned, and are frequently pledged as collateral, hence it should follow that a lien could be secured by levy of execution, and if this occurs while a premium is in default, or shortly before a default occurs, the problem of realization should be solved. *Anthracite Ins. Co. v. Sears*, 109 Mass. 383 (1872); *Industrial Loan & Investment Co. v. Mo. State Life Ins. Co.*, 222 Mo. App. 1228, 3 S.W. 2d 1046 (1928).

[41] But the weight of authority does not sustain this view. However, the prevailing view appears to be based upon earlier cases which dealth with policies having no cash surrender value, or were decided in jurisdictions which followed the common law rule that choses in action could not be reached by execution. Compare the practice in New York (cases cited *supra*, note 8), with the practice in Virginia (cast cited *supra*, note 36).

ment,[42] asking the court to appoint a receiver, and directing the receiver to make the necessary transfer.[43] Of course, supplementary proceedings at the foot of the judgment, based upon a return of execution unsatisfied, constitute the logical remedy where the creditor cannot reach the policy under regular process. If the court considers our statute inadequate to handle these situations, then a creditor's bill in aid of execution should be an available remedy.[44] In the writer's opinion, cases to the contrary are based not upon a lack of power, but upon a judicial determination not to use it. Since we have no judicial authority in this state to prevent such a construction of our procedural statutes, it is to be hoped that the views expressed above will be given effect.[45]

Coming to the question of policy, and it seems clear that this is a legislative and not a judicial question, it appears to the writer that the act as it now stands is not adequate. If the purpose is to protect the widow and dependents, it fails to achieve its end because no bar is placed upon her creditors whether existing prior to the death of the insured or subsequent thereto. Even a partial bar covering creditors whose claims arose prior to the death of the insured, would be better than no bar at all. It is further suggested that the term "life insurance" be defined. While the language used is broad, it would not seem to cover annuity contracts, and some doubt might exist as to single premium endowment policies. It should cover disability benefits and define the amount exempt. The act contains no provisions as to premiums paid in fraud of creditors, or fraudulent assignments. It is not at all clear that the rejection of a clause covering premiums paid in fraud of creditors grew out of an understanding by the legislators that such a clause was unnecessary, or showed an intent that the premiums should not be recoverable in such a case. In view of our recent enactment of the Uniform Fraudulent Conveyances Act, this statute should contain provisions covering the rights of a defrauded creditor. The amount of insurance exempt under law should be limited as required by the constitution. To complete the picture, if any doubt exists as to the availability of legal process to reach the proceeds of a non-exempt policy, and to make it clear that a creditor need not wait until the death of the insured, a clause should be inserted, either in the exemption statute, or in the provisions governing supplementary proceedings, specifically covering the case of an insurance policy. The act might well make special provision for the case of the policy that exceeds the exemption. Provision might be made to keep the creditor's lien alive until the policy matures, or for a court order compelling a surrender and issuance of a new policy for the exempt amount where policy provisions permit. Certainly the subject of insurance exemptions is worthy of consideration by the Legislative Research Committee. The New York

[42] "We are of the opinion that when an insurance policy is attached . . . it should be placed in the hands of a receiver . . . or, if no receiver be appointed, then the attaching officer should perform such duties and collect the amount due . . . as he would a note or other obligation." *Industrial Loan & Investment Co., v. Mo. State Life Ins. Co.*, 222 Mo. App. 1228, 3 S.W. 2d 1046 (1928), *cited supra*, note 40.

[43] Supplementary proceedings are commonly used. See references in note 18, *supra*; and the practice in New York, cases cited in note 8, *supra*.

[44] 15 C. J., s. 79, p. 1404; 21 C.J.S., s. 21; p. 1068; *Anthracite Ins. Co., v. Sears*, 109 Mass. 383 (1872).

[45] Compare the attitude of the court in *O'Connor v. McManus*, 71 N.D. 88, 299 N.W. 22 (1941).

statute has served as a model for many states, and is set out below.[46] With one modification, setting out the amount of exempt insurance to comply with our constitution, it might well serve as a working model for the amendment of our own statute.

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[46] N. Y. Ins. Law s. 166 provides:

"Exemption of proceeds and avails of certain insurance and annuity contracts. 1. If any 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, by assignment, change of beneficiary or otherwise, to a third person, such third person beneficiary, assignee or payee 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. If any policy of insurance has been or shall be effected by any person upon the life of another person in favor of the person effecting the same or made payable, by assignment, change of beneficiary or 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 wife of the insured, she shall be entitled to the proceeds and avails of such policy as against her own creditors, trustees in bankruptcy and receivers in state and federal courts. If any policy of insurance has been or shall be effected by any person on the life of another person in favor of a third person beneficiary, or made payable, by assignment, change of beneficiary or otherwise, to a third person, such third person beneficiary, assignee or payee 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 and of the person effecting the insurance. The term "proceeds and avails" shall include death benefits, cash surrender and loan values, premiums waived, and dividends, whether used in reduction of the premiums or in whatsoever manner used or applied, excepting only where the debtor has, subsequent to the issuance of the policy, actually elected to receive the dividends in cash. The person insured in a case under the first sentence of this subsection, or the person effecting the insurance other than the wife of the insured in a case under the second sentence, and the person effecting the insurance under the third sentence thereof, or the executor or administrator of any such persons, or a person entitled to the proceeds or avails of such policy in trust for such persons shall not be deemed a third person beneficiary, assignee or payee. A policy shall be deemed payable to a third person beneficiary if and to the extent that, a facility-of-payment clause or similar clause, in the policy permits the insurer to discharge its obligation after the death of the person insured by paying the death benefits to a third person as herein defined. The provisions of this section shall be applicable whether or not the right is reserved in any such policy to change the beneficiary therein designated, 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.

"2. No money or other benefits payable or allowable under any policy or insurance against disability arising from accidental injury or bodily infirmity or ailment of the person insured, shall be liable to execution for the purpose of satisfying any debt or liability of the insured, whether incurred before or after the commencement of the disability, except as provided in subsection four, and except further that (a) with respect to debts or liabilities incurred for necessaries furnished the insured after the commencement of disability, the exemption shall not include any income payment benefits payable as a result of any disability of the insured, and (b) with respect to all other debts or liabilities incurred after the commencement of disability of the insured, the exemption of income payment benefits payable as a result of any disability of the insured shall not at any time exceed payment at rate of four hundred dollars per month for the period of such disability. When a policy provides for lump sum payment because of a dismemberment or other specific loss of insured, such payment shall be exempt from execution of insured's creditors. The provisions of this subsection shall not affect the assignability of any benefit otherwise assignable.

"3. The benefits, rights, privileges and options which, under any annuity contract heretofore or hereafter issued are due or prospectively due the annuitant, who paid the consideration for the annuity contract, shall not be subject to execution nor shall the annuitant be compelled to exercise any such rights, powers or options contained in said annuity contract, nor shall creditors be allowed to interfere with or terminate the contract, except (a) as provided in subsection four and except (b) that 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 four hundred dollars per month for the length of time represented by such installments, and that such periodic payment shall be subject to garnishee execution to the same extent as are wages and salaries, . . ; and (c) that if the total benefits presently due and payable to any annuitant under all annuity contracts under which he is an annuitant, shall at any time exceed payment at the rate of four hundred dollars per month, then under the provisions of the civil practice act, the court may order such annuitant to pay to a judgment creditor or apply on the judgment, in installments, such portion of such excess benefits, as to the court may appear just and proper, after due regard for the reasonable requirements of the judgment debtor and his family, if dependent upon him, as well as any payments required to be made by the annuitant to other creditors under prior court orders. The benefits, rights, privileges or options accruing under such contract to a beneficiary or assignee shall not be transferrable nor subject to commutation, and if the benefits are payable periodically or at stated times, the same exemptions and exceptions contained herein for the annuitant, shall apply with respect to such beneficiary or assignee.

"An annuity contract within the meaning of this section shall be any obligation to pay certain sums at stated times, during life or lives, or for a specified term or terms, issued for a valuable consideration, regardless of whether or not such sums are payable to one or more persons, jointly or otherwise, but does not include payments under a life insurance policy at stated times during life or lives, or for a specified term or terms.

"4. Every assignment or change of beneficiary, or other transfer, shall be valid, except in cases of transfer with actual intent to hinder, delay or defraud creditors, as such actual intent is defined by article 10 of the debtor and creditor law (UNIFORM FRAUDULENT CONVEYANCES ACT, N. D. REV. CODE (1943) SS 13-1201, to 13-0211; in case of transfer with

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