

# In the United States Bankruptcy Court

## for the Northern District of Iowa

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RAYMOND ALTON ODEGARD  
BEULAH ELVINA ODEGARD

Bankruptcy No. 96-22839-D

*Debtor(s).*

Chapter 7

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### ORDER RE: TRUSTEE'S OBJECTION TO EXEMPTION AND MOTION FOR TURNOVER

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The matter before the Court is Trustee's Objection to Exemption and Motion for Turnover involving two prepaid burial contracts claimed exempt by Debtors. Trustee objects to exemption and moves for turnover of the funds. Debtors and Trustee have agreed to submission of this matter on the written briefs and arguments of the parties. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(B).

#### STATEMENT OF THE CASE

Debtors Raymond and Beulah Odegard jointly filed a voluntary petition under Chapter 7 of the Bankruptcy Code on November 7, 1996. Their Schedule B-Personal Property, and Schedule C-Property Claimed as Exempt, each as amended December 12, 1996, lists two "Burial trust accounts payable for burial upon death of Beulah Odegard." These two accounts have a total market value of \$ 3,562.06 and are listed as property of Mrs. Odegard. The funds are held in trust by the Waukon State Bank, Waukon, Iowa, and accumulate interest. The funds are claimed as exempt on Debtors' amended Schedule C under 11 U.S.C. § 541(c)(2). Trustee objects to exemption.

The two accounts are based upon 1) an "Agreement" (Agreement) and 2) a "Contract" (Contract) made at two separate times, on different forms. Each of these contracts was made between Martin Funeral Home (Martin) and Beulah Odegard (Debtor), with Debtor as beneficiary of the funeral services to be rendered and as the party who signed each contract as purchaser. Each contract is denominated as "irrevocable." The Agreement was entered into on August 9th, 1988, and was accompanied by Debtor's deposit of \$2,500.00 into an escrow account at Waukon State Bank "to be held in escrow by said bank for the purpose of applying towards a burial of the first party [Beulah Odegard] upon his/her death." The interest earned by this deposit was paid to Debtor as earned until August 18, 1992, at which time Debtor instructed the bank in writing to allow the interest to "be added to Burial Agreement and irrevocably added to the value of Burial agreement."

The Contract was signed on October 29, 1996, nine days before Debtors' bankruptcy petition was filed. Debtor deposited \$685.68 with Martin to be placed "in trust . . . until the death of Beneficiary." These funds were to be deposited by Martin at Waukon State Bank where they would accumulate interest, and were to be used "to provide for the future funeral service for Beulah Odegard." The Contract contains a section entitled "DEFAULT BY PURCHASER/BENEFICIARY-- CANCELLATION CHARGE," which reads in part as follows:

**CANCELLATION CHARGE.** Upon default by the Purchaser/Beneficiary, this Contract shall be deemed cancelled and MARTIN FUNERAL HOME Shall Retain \$100.00 of the original amount deposited, as a cancellation charge. The balance and accrued interest thereon, shall be refunded.

Except for the use of another funeral service provider upon the death of the beneficiary, the Contract does not define default.

### **PROPERTY OF THE ESTATE**

Debtor bases her argument on 11 U.S.C. § 541(c)(2) which provides:

A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable non-bankruptcy law is enforceable in a case under this title.

Debtor relies exclusively on this Code section to assert that the Burial Trust Certificates are not property of the bankruptcy estate. Debtor relies heavily on the term "irrevocable" in each contract to allow for their protection under § 541(c)(2) as irrevocable trusts. She equates "irrevocable" to a restriction on transfer. A casual reading of § 541(c)(2) appears to entitle a debtor to exclude any interest in a plan or trust that contains a transfer restriction enforceable under any applicable non-bankruptcy law from the bankruptcy estate. Patterson v. Shumate, 112 S. Ct. 2242, 2246 (1992). House and Senate reports accompanying the Bankruptcy Reform Act of 1978 reflect congressional intent to include state spendthrift trust law within the meaning of "applicable non-bankruptcy law." Id. at 2248. However, § 541(c)(2) has been interpreted to apply exclusively to a narrow variety of trust, the spendthrift trust. In In re Brown, 86 B.R. 944 (N.D. Ind. 1988) the court made the following analysis of the provisions of 11 U.S.C. § 541.

Eleven U.S.C. § 541 is a broadly inclusive statute defining property of a bankruptcy estate. The scope of § 541(a) is particularly "broad and all embracing." In re Miller, 16 B.R. 790, 791 (Bankr. D.Md. 1982). But for a specific, narrowly construed exception set forth in § 541(c)(2), an interest of a debtor will become property of the bankruptcy estate despite any agreement to the contrary which attempts to restrict transfer. 11 U.S.C. § 541 (c)(1)(A). Under subsection (2), however, "[a] restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable non-bankruptcy law is enforceable in a case under this title." 11 U.S.C. § 541(c)(2). The law is clear that this provision was intended by Congress to specifically preserve "restrictions on transfer of a spendthrift trust." In re Miller at 791, quoting H.Rep. No. 95-595, 95th Cong., 1st Sess. 369 (1977); (citations omitted). . . . As a general rule, a beneficiary's interest in a spendthrift trust is excluded from his bankruptcy estate if state law and the trust so provide.

Brown, 86 B.R. at 946.

Trustee argues the contracts in this case are not spendthrift trusts under applicable state law, and that § 541(c)(2) is not applicable to them. Trustee asserts they remain part of the bankruptcy estate under the "broad and all embracing" § 541(a).

### **SPENDTHRIFT TRUSTS**

Iowa law generally recognizes and upholds the validity of spendthrift trusts. In re Dodge, 281 N.W.2d 447, 450 (Iowa 1979). These trusts have specific characteristics as briefly summarized in In re Schwartz, 58 B.R. 606 ( Bankr. N.D. Iowa 1984):

Spendthrift trusts are trusts created to maintain a designated beneficiary and to insulate the fund from claims of the beneficiary's creditors. Generally, a settlor cannot make a spendthrift trust for [settlor's] own benefit.

Id. at 607 (citations omitted). "In Iowa, a spendthrift trust may not be established by the beneficiary." In re Holst, 192 B.R. 194, 198 (Bankr. N.D. Iowa 1996), aff'd. 197 B.R. 856 (N.D. Iowa 1996); Hanson v. Minette, 461 N.W.2d 592, 595 (Iowa 1990); see also Humphrey v. Buckley, (In re Swanson), 873 F.2d 1121, 1124 (8th Cir. 1989) (same under Minnesota law). When a trust does not qualify as a spendthrift trust under state law, its restriction on alienation is ineffective under state law. Holst, 192 B.R. at 198.

Trustee argues that the contracts are "self-settled trusts" which do not qualify as spendthrift trusts under Iowa law. Debtor was both the purchaser and beneficiary of each of the two contracts, having signed each one. Since these contracts were self-settled by Debtor, they do not qualify as enforceable spendthrift trusts under Iowa law. A restriction placed on the transfer of a beneficial interest of the debtor is not enforceable under Iowa law. They are not protected under § 541(c)(2) as Debtor contends. Such protection requires enforceability under applicable non-bankruptcy law and absent such § 541(c)(2) protection, these two contracts remain part of Debtors' bankruptcy estate.

#### **EXEMPTION UNDER IOWA CODE**

Iowa Code sec. 627.6 identifies specific items of a debtor's property which are exempt from inclusion in the bankruptcy estate of a debtor. A burial plot is listed as exempt under Iowa Code sec. 627.6(4) which reads: "An interment space or an interest in a public or private burying ground, not exceeding one acre for any defendant." The Iowa Code is silent concerning an exemption for burial expenses or funeral service costs. The absence of any mention by the Legislature of these costs, whether prepaid or not, establishes an intent to exclude them as exempt. The contracts here make no reference to the provision of an interment space of any kind. They refer only to funeral goods and services, and are not exempt under Iowa Code sec. 627.6(4).

#### **MOTION FOR TURNOVER**

Debtor's argument bases her claim of inalienability on the use of the term irrevocable in these contracts. Inalienability, as relied upon by Debtor, is a characteristic peculiar to the spendthrift trust. As previously decided, these contracts are not spendthrift trusts. Since they do not meet the requirements of spendthrift trusts, they are not inalienable as Debtor claims. These contracts are vulnerable to the claims of creditors. "When a settlor creates for her own benefit a spendthrift trust . . . creditors may reach assets of the trust estate." In re Tunink, No. 93-50528XS, slip op. at 5 (Bankr. N.D. Iowa April 22, 1994). The funds are therefore not exempt and are to be turned over to Trustee for administration.

#### **VALUE TO THE ESTATE**

The Contract includes a cancellation clause which provides for a cancellation charge upon default of \$100.00, with the balance to be refunded. The only explanation of default in the contract is described in the following sentence: "Default includes the procurement of funeral services for the Beneficiary

after death from a person or entity other than MARTIN FUNERAL HOME." The wording of this sentence indicates other events also constitute a default. Cancellation of the contract by the Trustee on behalf of the bankruptcy estate qualifies as such a default, triggering the refund of the balance after the cancellation charge. Martin earns nothing until it performs the services specified in the contracts. Therefore, all funds in the account, except the \$100 default penalty, are assets of the bankruptcy estate.

The Agreement contains no cancellation or default provision. It states that the escrowed monies are not earned until the service is performed for Debtor. With no provision in the Agreement for default or cancellation, all funds presently held in this account are assets of the bankruptcy estate.

**WHEREFORE**, Trustee's Objection to Exemption and Motion for Turnover is SUSTAINED.

**FURTHER**, the two burial contracts are not spendthrift trusts and are not exempt. They are property of the estate.

**FURTHER**, the funds in the Waukon State Bank covered by the two burial contracts are to be turned over to Trustee for disposition as assets of the estate subject to the default provision addressed in this opinion.

**SO ORDERED** this 8th day of July, 1997.

Paul J. Kilburg  
U.S. Bankruptcy Judge