IN THE SUPREME COURT
STATE OF FLORIDA

Case No. 79,495

Certified Question from
the United States Court of Appeals
for the Eleventh Circuit
(NO. 90-5733)

In re PAULA L. McCOLLAM,

Debtor.

THOMAS E. LeCROY,

Plaintiff-Appellant,

v.

PAULA L. McCOLLAM,

Defendant-Appellee.

INITIAL BRIEF OF PLAINTIFF-APPELLANT

STEARNS WEAVER MILLER WEISSLER
ALHADEFF & SITTERSON, P.A.
150 West Flagler Street
2200 Museum Tower Building
Miami, Florida 33130
Telephone: (305) 789-3200

ATTORNEYS FOR PLAINTIFF-APPELLANT

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INTRODUCTION

This case originated in the United States Bankruptcy Court for the Southern District of Florida and is before this Court because the United States Court of Appeals for the Eleventh Circuit certified the following question:

> Whether, as a matter of law, an annuity contract which is established in lieu of a creditor paying a debtor a lump sum presently owed is exempt from creditor claims in bankruptcy under Fla. Stat. § 222.14.

The Bankruptcy Court and the District Court allowed their focus on the existence of the annuity contract to mask the underlying obligation, and they concluded that the annuity prevailed.

The Eleventh Circuit reviewed the overall substance of the arrangement (a structured settlement funded by an annuity), questioned the lower courts' reliance on a particular Florida bankruptcy court decision, noted that in addition to the right to receive the annuity payments the bankruptcy debtor retained the right to collect from the original obligor, and suggested that courts in other jurisdictions had approached the matter more appropriately by recognizing that the arrangement was nothing more than an account receivable, (A copy of the Eleventh Circuit's opinion is attached hereto as Exhibit A.)

STATEMENT OF THE CASE

Course of Proceedinqs and Dispositions Below.

Appellee (the "Debtor") filed a Chapter 7 petition in bankruptcy on July 11, 1989, in the United States Bankruptcy Court, Southern District of Florida (R1-1-45)[1/], and on Schedule B-4 listed among her claimed exempt property "Travelers Indemnity Co. annuity, exempt pursuant to Florida Statute 222.14." (R1-1-60). Appellant (the "Creditor") filed an Objection to Exemption (dated September 12, 1989) (R1-1-32; Item 2 of Record Excerpts). The bankruptcy court issued an Order on Objection to Exemption (dated January 31, 1990) (Rl-1-8; Item 4 of Record Excerpts) upholding the Debtor's claimed exemption. The Creditor timely filed a Notice of Appeal (Rl-1-1). The United States District Court, Southern District of Florida, thereafter entered an Order Dismissing Appeal (dated July 31, 1990) (Rl-8-1; Item 5 of Record Excerpts), affirming the bankruptcy court's ruling. The Creditor timely filed a Notice of Appeal (R1-10-1). The United States Court of Appeals for the Eleventh Circuit thereafter issued an opinion certifying a question to the Florida Supreme Court (Exhibit A hereto).

Statement of the Facts and Nature of the Case.

The Debtor was a party (along with others) to a General Release and Settlement Agreement dated July 9, 1985 (the "Settlement") under which Travelers Insurance Company became

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[1/] References are to the record as transmitted to the United States Court of Appeals for the Eleventh Circuit and to the Record Excerpts filed therein along with Appellant's Brief.

obligated to pay to the Debtor certain sums of money. The Settlement was an arrangement commonly referred to as a "structured settlement" that resolved claims for damages by the Debtor (the surviving child of her father) against various third parties for the death of her father. A copy of the Settlement is attached to the Objection to Exemption as Exhibit A (Rl-1-32; Item 2 of Record Excerpts).

Under paragraph 6 of the Settlement, Travelers remains directly responsible for the sums to be paid to the Debtor, but has purchased an annuity contract as security for the payment of such sums. (The Creditor's claim did not exist at the time that the annuity was issued, and there is not any allegation of fraud in connection with the purchase of the annuity.) On her bankruptcy schedules, the Debtor did not list among her assets the debt from Travelers and instead listed only the annuity. Moreover, the Debtor listed the annuity as an exempt asset (the debt itself from Travelers could not have been claimed as exempt). The Creditor objected to the listing of the collateral for the debt as an exempt asset (and the failure to list the debt itself as an asset).

The Bankruptcy Court upheld the claimed exemption, and the District Court affirmed that ruling on appeal. The Court of Appeals for the Eleventh Circuit certified the following question to this Court:

> Whether, as a matter of law, an annuity contract which is established in lieu of a creditor paying a debtor a lump sum presently owed is exempt from creditor claims in bankruptcy under Fla. Stat. § 222.14.

SUMMARY OF ARGUMENT

Travelers Insurance Company owes the Debtor a debt, which is an account receivable (i.e., an asset) in her hands and could not be exempted from the claims of her creditors, The payment of the debt is secured by an annuity. By allowing the Debtor to claim the annuity (and the payments thereunder) as exempt property in her bankruptcy case, the bankruptcy court effectively made the debt from Travelers exempt.

Courts in jurisdictions other than Florida have held that under similar circumstances and similar statutes, annuities that merely serve to provide the funds to pay a structured settlement should not be exempt from the claims of creditors of the beneficiary of the annuity. The annuity is merely an adjunct to the Travelers debt, does not exist but for that debt, and should not be permitted to remove from the bankruptcy trustee's control (and the general creditors' claims) a valuable asset.

The annuity and the payments thereunder should not be exempt because the Travelers debt itself is not exempt.

ARGUMENT

The Debtor takes the simplistic approach that because she is receiving payments under an annuity (regardless of the reason for the existence of the annuity) and because Florida law (§ 222.14) provides an exemption from the claims of creditors for "the proceeds of annuity contracts issued to citizens or residents of the state ...", she is entitled to exempt from her bankruptcy estate the annuity purchased by Travelers and the payments thereunder. The problem with this approach is that it also leads the Debtor to gloss over an asset: her claim against Travelers.

In the beginning, there was a debt owed by Travelers Insurance Company to Paula Lea McCollam, and without the existence of that debt, there never would have been an annuity.[2/] This essential fact undermines the arguments of the Debtor (Ms. McCollam), who would prefer to ignore the debt from Travelers and instead insist that the annuity has a life of its own.

a. The Florida Bankruptcy Court (In re Benedict)

The Debtor relies on In re Benedict, 88 B.R. 387 (Bankr. M.D. Fla. 1988), and the companion case at 88 B.R. 390 (Bankr. M.D. Fla. 1988), which also dealt with an annuity issued in connection with a structured settlement. The Creditor does not argue that the

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[2/] The Settlement provides that "(6) TRAVELERS INSURANCE COMPANY a/k/a TRAVELERS INDEMNITY COMPANY shall at all times remain directly responsible for the payment of all sums and obligations contained within this Agreement. As security for said installment payments ... TRAVELERS ... shall purchase an annuity contract ...." Travelers is the applicant and owner of the annuity. The Debtor may nominate and change beneficiaries.

Bsnedict cases did not consider generally the same issues that are before the Court here. The Creditor's point is that the Benedict cases were incorrectly decided because the court there overlooked the central fact that is being stressed here: the annuity is merely a means to secure a steady stream of payments of a debt.

The Benedict court let the tail wag the dog by focusing its attention solely on the payment structure of the annuity and not recognizing the existence of the original debt. That error should not be repeated, and for that reason the Benedict cases should not be followed.

The Eleventh Circuit noted that the Benedict court reasoned "summarily", In re McCollam, 955 F.2d 678, 680 (11th Cir. 1992), and suggested that "[a] Florida court may find the reasoning in In re Benedict unpersuasive." Id. The Eleventh Circuit also observed that "courts in jurisdictions other than Florida have held that statutes similar to Fla. Stat. § 222.14 do not exempt annuity contracts established in settlement of a debt." Id. at 678.

b. Courts in Jurisdictions Other than Florida

In re Young, 806 F.2d 1303 (5th Cir. 1986), is cited by the Eleventh Circuit as similar to the present case and as an example of a court that looked behind the form of the annuity to determine the substance of the arrangement. In Young, the debtor was an attorney who had represented parties in an action that eventually resulted in a structured settlement. The settlement included a provision for the payment of his fees over time, and the payments were supplied by an annuity that was purchased by the obligor.

As in the present situation, the debtor in Young claimed the annuity payments to be exempt under a Louisiana statute (La. Rev. Stat. Ann. § 20:33) that stated "[t]he following shall be exempt from all liability for any debt except alimony and child support: (1) All pensions, all proceeds of and payments under annuity policies or plans, ..." and under a related Louisiana statute (La. Rev. Stat. Ann. § 22:647(B)). Refusing to undertake a blind, literal reading of the statutes, the Young court instead held that "[w]hile the payments Debtor claims to be exempt are, strictly speaking, an 'annuity', they are also accounts receivable. We must, therefore, pierce the veil of this arrangement to determine its true nature." 806 F.2d at 1306.

The Young court found guidance in a Pennsylvania decision, Commonwealth v. Beisel, 338 Pa. 519, 13 A.2d 419 (1940), and quoted the following language regarding annuities (which the Eleventh Circuit felt merited quotation in its opinion too):

> Its determining characteristic is that the annuitant has an interest only in the payments themselves and not in any principal fund or source from which they may be derived. The purchaser of an annuity surrenders all right and title in and to the money he pays for it. On the other hand, where a debtor agrees to pay his creditor in installments at regular intervals, the debt or principal sum itself is due to the creditor although payable only in the manner agreed upon; it is an account receivable in which he has a property interest. Therefore, installment payments of a debt, or payments of interest on a debt, do not constitute an annuity.

13 A.2d at 421; Young, 806 F.2d at 1307; McCollam, 955 F.2d at 680-81. The Eleventh Circuit also quoted the admonition of the Young

court that "[i]t is the substance of the arrangement rather than the label affixed to it that determines whether the payments are exempt under Louisiana statutes as proceeds from an annuity, or accounts receivable, and part of the bankruptcy estate." Young, 806 F.2d at 1307; McCollam, 955 F.2d at 680.

The Young court made one further point that should be noted. The debtor in Young could have accepted the total amount of his fees in one lump payment, paid the appropriate taxes thereon, and used the balance to purchase an annuity, which clearly would have been exempt. He instead chose to delay the payment and receive it in installments, very likely for tax reasons. In doing so, he retained the right to pursue the original obligor (which purchased the annuity) for any payments not made under the annuity, and the settlement agreement (as in the present situation) provided that payments under the annuity would merely discharge proportionately the underlying debt, but would not affect the debtor's right to pursue the obligor for the remaining balance. "Retaining such a right renders the so-called annuity, in substance, nothing more than an account receivable, and not exempt from the bankruptcy estate." 806 F.2d at 1307.

Three additional cases, two from Ohio and one from North Dakota, reinforce the logic of Young and give added strength to the Creditor's argument in the present situation. In In re Simon, 71 B.R. 65 (Bankr. N.D. Ohio 1987), the court considered an annuity purchased to fund a structured settlement. In analyzing the statute (O.R.C. § 2329.66(A)(10)(b)) under which the debtor claimed

the annuity as exempt, the Simon court noted that the statute dealt with:

> retirement, unemployment compensation, alimony, disability payments and things of that nature. ... Notably, the sources of the listed exempt payments are chiefly an employer, former spouse, or a governmental entity. Consequently, an examination of the provision leads to the inference that an annuity which is merely in settlement of a tort suit was not contemplated by the drafters. It appears they were concerned mainly with annuities as used in retirement and disability planning.

Id. at 66. The Simon court ruled that the annuity was not exempt.

Significantly, when the Florida legislature amended § 222.14 in 1978 to include the provision for "the proceeds of annuity contracts issued to citizens or residents of the state", the scope of Chapter 222, Florida Statutes, covered homestead, personal property, wages of the head of a family, proceeds of a life insurance policy, cash surrender value of life insurance policies, wages or unemployment compensation payments due a deceased employee, and disability income benefits. Chapter 222, Fla. Stat. (1977). These topics overlap to a large extent the items of retirement and disability planning covered by the Ohio exemption statute considered by the court in Simon. Similarly, in expanding the exemption statute, the Florida legislature evidenced no intent to include annuities that serve to fund settlements of tort suits in addition to annuities that serve as retirement instruments.

The placement of the annuity exemption language amidst an exemption statute regarding the cash surrender value of life insurance policies suggests that the Florida legislature considered

the two matters (annuity contracts and insurance policies) to be related. Moreover, in the sequence of topics covered by Chapter 222 prior to the addition of the annuity exemption, two successive sections (§ 222.13 and § 222.14) pertained respectively to the proceeds of and cash surrender value of life insurance policies. Reference to the other portions of Chapter 222 in pari materia is not only proper, Davies v. Bossert, 449 So. 2d 418, 420 (Fla. 1984), but also required, Radio Tel. Communs., Inc., v. Southeastern Tel. Co., 170 So. 2d 577, 580 (Fla. 1965) ("it is our duty to give effect to the legislative intent; and if a literal interpretation leads to an unreasonable result, plainly at variance with the purpose of the legislation as a whole, we must examine the matter further."); State v. Webb, 398 So. 2d 820, 824 (Fla. 1981) ("It is a fundamental rule of statutory construction that legislative intent is the polestar by which the court must be guided, and this intent must be given effect even though it may contradict the strict letter of the statute."); Sutherland Stat Const §§ 46.05 and 46.07 (5th ed.).

The result of such analysis is a conclusion that the Florida legislature intended the annuity exemption to be a companion to another form of retirement instrument: the cash surrender value of a life insurance policy. The staff report and staff analysis regarding the House and Senate bills confirm that this was the legislature's intention. Staff Analysis and Economic Statement (dated January 10, 1978) to Senate Bill No. 163; Judiciary Committee Staff Report (undated) to House Bill No. 153.

Armed with the reasoning of the Young and Simon decisions, the court in In re Johnson, 108 B.R. 240 (Bankr. D.N.D. 1989), likewise found that an annuity that funded a structured settlement could not be exempted. The statute (N.D. Cent. code § 28-22-03.1(3))[3/] included "annuity policies" among the listed items, but the Johnson court determined that the statute covered "instruments [that] are mainly concerned with retirement or death. Therefore, it is reasonable to infer that the North Dakota legislature intended for 'annuities' in the context of retirement instruments be exempted, not annuities based upon tort settlements." Id. at 242.

Moreover, the Johnson court quoted the language from Young (quoting in turn the language from Beisel) regarding the distinction between an annuity and an account receivable, adopted the focus of Young on the "substance of the arrangement rather than the label affixed to it", Id. at 243, pointed out that the debtor would have the right to collect from the insurance company in the event that the annuity contract went into default, and contrasted the situation to what would have been the case had the debtor opted for a lump sum settlement rather than a stream of payments funded by an annuity. All of these factors exist in the present situation.

Finally, the court in In re Rhinebolt, 131 B.R. 973 (Bankr. S.D. Ohio 1991), recited the reasoning of Young, Simon, and Johnson

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[3/] Unlike the Ohio statute, which refers to annuities in connection with illness, age, disability, and similar factors, the North Dakota statute (along with the Louisiana and Florida statutes) does not qualify the term "annuity" with any such limitations.

and referred to those decisions as "persuasive authorities" for denying the claimed exemption of yet another annuity "set up simply to provide a method by which to fund the settlement of the Debtor's tort lawsuit." Id. at 977. The Ohio statute in question was the same one considered by the Simon court, and the court in Rhinebolt likewise looked to the context of the statute and the substance of the arrangement to determine whether the annuity should be allowed to be exempted. The court denied the exemption and also refused to permit a literal reading of another related exemption statute to yield a result that "would distort the purpose of the statute." Id. at 978.

c. Summary

The Eleventh Circuit indicated that "it is appropriate for the highest court of Florida to determine whether the intent of the legislature is to exempt from the claims of creditors in bankruptcy annuities in the nature of retirement instruments, or all debts structured as annuities, including those that derive from personal injury settlements." 955 F.2d at 681 (footnote omitted).[4/]

While the exact language of the statutes in the Young, Simon (and Rhinebolt), and Johnson cases differed, each of those courts approached the analysis identically. Each indicated that a blind,

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[4/] The exemption for the proceeds of annuity contracts was added to § 222.14, Fla. Stat., by Chapter 78-76, § 1, Laws of Florida, effective July 1, 1978. See Staff Analysis and Economic Statement (dated January 10, 1978) to Senate Bill No. 163; Judiciary Committee Staff Report (undated) to House Bill No. 153.

literal reading of the statute was insufficient. Each noted that the annuity in question did not have an independent existence, but instead came into being only because of a structured settlement that remained an obligation of the purchaser of the annuity. Each concluded that the relevant legislature could not have intended to include such annuities within the scope of the enacted exemption statute.

The decisions in Young, Simon, Johnson, and Rhinebolt illustrate why the annuity in the present situation should not be exempt under § 222.14, Fla. Stat. The debt owed *to* the Debtor by Travelers is property of her bankruptcy estate and should have been listed on her bankruptcy schedules. The fact that an annuity provides a source of payments for that debt should not make the debt and the annuity and the payments thereunder exempt from the claims of general unsecured creditors of the Debtor's bankruptcy estate. Any ruling to the contrary would only invite substantial abuses of the exemption statute through the funding of all manner of obligations by annuities, which the recipients would blithely argue made the entire debt immune from the claims of creditors.

CONCLUSION

Creditor requests the Court to answer the certified question[5/] in the negative and to hold that an annuity contract that is established in lieu of a party's paying another party a lump sum currently owed is not exempt from creditor claims in bankruptcy under Fla. Stat. § 222.14.

In the event that the Court feels compelled to rephrase the certified question or otherwise distinguish among cases that could collectively fit within the question as certified, Creditor requests the Court to rule that an annuity that merely serves to fund payments due under a structured settlement is not exempt from creditor claims under Fla. Stat. § 222.14.

[5/] The precise language of the certified question is "whether, as a matter of law, an annuity contract which is established in lieu of a creditor paying a debtor a lump sum presently owed is exempt from creditor claims in bankruptcy under Fla. Stat. § 222.14." (emphasis supplied) Since creditors do not pay debtors, and instead the reverse is true, the Eleventh Circuit presumably meant to ask something along the lines of "whether, as a mater of law, an annuity contract which is established in lieu of an entity paying a party (who subsequently becomes a debtor in bankruptcy) a lump sum ...."

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Initial Brief of Plaintiff-Appellant was *mailed* this 7th *day* of May, 1992, to the following persons:

LESLIE GERN CLOYD, ESQ.
P.O. Drawer 3948
West Palm Beach, FL 33402

ANDREA A. RUFF, ESQ.
1205 Mt. Vernon Street
Orlando, FL 32803-5464

NORMAN L. HULL, ESQ.
'Russell& Hull, P.A.
537 North Magnolia Avenue
P.O. Box 2751
Orlando, FL 32802

STEARNS WEAVER MILLER WEISSLER
ALHADEFF & SITTERSON, P.A.
Attorneys for Appellant LeCroy
150 West Flagler Street
2200 Museum Tower Building
Miami, Florida 33130
Telephone: (305) 789-3200

By: Theodore A. Jewell
THEODORE A. JEWELL
Fla. Bar No. 260681