UNITED STATES DISTRICT COURT
DISTRICT OF SOUTH DAKOTA
SOUTHERN DIVISION

In Re: MELVIN DEAN VAN DENTOP, Debtor.	CIV 97-4057 MEMORANDUM OPINION
MELVIN DEAN VAN DENTOP, Appellant, -vs- RICK YARNALL, Chapter 7 Trustee, Appellee.	

Introduction

Pending before the Court is a bankruptcy appeal brought by Debtor Melvin Dean VanDentop against Trustee Rick Yarnall. Debtor appeals from a bankruptcy court order sustaining Trustee's Objection to an exemption declared by the Debtor. Bankr. Doc. 30. For the following reasons this Court affirms the decision of the bankruptcy court.

Background

Debtor VanDentop filed for Chapter 7 bankruptcy on November 13, 1995. On the same day, immediately before filing for bankruptcy, Debtor issued a check for $2200.00 written to Life

Investors Insurance Company of America as repayment of a loan taken against Debtor's policy.[1] The check was hand delivered by the Debtor to the agency office on November 13, 1995, but the check did not clear Debtor's account until November 22, 1995. According to Life Investors, the check had to clear before the company would consider the loan paid. Had Debtor died prior to the clearing of the check, the insurance company would have paid the value of the policy as calculated without the additional funds.[2]

As part of his filing, the Debtor listed $300.00 in his schedules as the amount in his account on the day of filing; however, the Debtor's actual balance was $3,679.83. In his schedules Debtor claimed a number of exemptions including an exemption under S.D.C.L. § 58-12-4 of $ 3,350.00 in cash value in the policy with Life Investors. Trustee Yarnell filed an objection claiming that the value of the property claimed exempt exceeded permissible allowance of $2,000.00 under S.D.C.L. § 43-45-4. Trustee calculated that Debtor actually had total personal property in the amount of $5539.83 which Trustee believed Debtor was trying to exempt. Debtor responded by arguing that on the date he filed bankruptcy his checking account had only $304.74 after deducting amounts owed on outstanding checks.

The Trustee claims that under Barnhill v. Johnson 112 S.Ct. 1386 (1992) (the court looks to the date that a check was honored under 11 U.S.C. § 547 (b) to determine whether an avoidable preference was made on or within 90 days of the date of filing a bankruptcy), the date honored must control the date of the transfer of funds; therefore, the money that was on the Debtor's account as of November 13 remains part of the Debtor's estate. Debtor claims that this money is exempt because Debtor was permitted to take non-exempt funds and convert them to exempt funds under Federal Savings and Loan Ins., Corp. v. Holt, 894 F.2d 1005 (8th Cir. 1990) (debtor may convert non-exempt assets into exempt assets on the eve of bankruptcy). Since the

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[1]According to the Debtor $200.00 of this amount was to be paid for additional coverage, but the information provided to the bankruptcy court by the appellant does not specify that $200.00 was a new payment.

[2]Debtor objects to the bankruptcy court's use of an out-of-court statement made by a representative from the insurance company to determine the facts in this case. It is clear from the record that the Debtor himself filed the material to which he now objects. He did not state any objection to this material in the proceedings below nor does he properly state an objection to the material now.

life insurance policy qualifies for exemption, the Debtor claims that the funds are not subject to the Barnhill "date honored" rule.

To resolve the issue the bankruptcy court posed the following two questions:

1. May the Debtor declare the Life Investors policy exempt where the loan repayment check to Life Investors had not cleared before the petition date?
2. May the Trustee recover from Debtor for the checks that were written pre-petition but cashed post-petition?

The bankruptcy court answered both questions in the negative. First, the bankruptcy court concluded that the Debtor was not converting non-exempt assets into exempt assets on the eve of bankruptcy but rather was repaying a debt owed for a loan. The court supported this conclusion by citing evidence that had Debtor died immediately after the delivery of the check, the company would have paid the benefits under the policy minus the loan balance. Once the check was honored, the Debtor would be eligible for full benefits. Thus, the bankruptcy court concluded, this was a debt repayment not the creation of exempt property.

Next, the bankruptcy court considered whether the relevant $2200.00 in the account on the filing date was the property of the Debtor estate or the insurance company. Based on the rule in Barnhill the court concluded that the honored date should control; therefore, the assets that were in the account on the date of filing are still to be regarded as part of the Debtor's estate.

Finally, the court concluded that the Debtor had no obligation to recover the assets from the insurance company or other post-filing transferees. Consequently, the Trustee will only have a cause of action against these third parties to recover the assets that rightfully belong to the Debtor estate. On appeal, Debtor argues that the bankruptcy court erred in ruling that the date of honor should be used when considering whether a post-petition transaction occurred and in concluding that the funds transferred to Life Investors remained in the Debtor's estate on the date of filing.

Discussion

On an appeal, a district court may affirm, modify, or reverse a judgment, order, or decree of a bankruptcy court or remand to the bankruptcy court with instructions for further

proceedings. A district court may set aside a bankruptcy court's findings of fact only if clearly erroneous. In contrast, a bankruptcy court's legal conclusions are subject to plenary review. In re Apex Oil, 884 F.2d 343, 348 (8th Cir. 1989); Wegner v. Grunewaldt, 821 F.2d 1317, 1320 (8th Cir. 1987); In re Spirit Holding Co., Inc., 124 B.R. 891 (E.D. Mo. 1997).

Under S.D.C.L. § 58-12-4 a debtor may exempt "[t]he proceeds of a policy of life or health insurance to the total amount of twenty thousand dollars . . . ." Further, it is well established that "[d]ebtors are permitted to exempt a certain amount of their personal assets to facilitate a 'fresh start.' They may make full use of exemptions, and can even convert nonexempt property to exempt property on the eve of bankruptcy." Armstrong v. Lindberg (In re Lindberg), 735 F.2d 1087, 1090 (8th Cir. 1984) (citing H.R. Rep. 595, 95th Cong. 1st Sess. 361, reprinted in 1978 U.S. Code Cong. & Ad. News 5787, 5963, 6317). It is clear from the facts that Debtor attempted to take advantage of the state law exemption for life insurance on the eve of bankruptcy by repaying the loan he had taken against his policy. The question for the Court is whether he was successful in doing so. On these facts, the Court concludes that he was not.

The amount of the exemptions under state law to which a debtor is entitled is determined based upon the condition of the Debtors estate on the date of filing for Bankruptcy. See Armstrong v. Peterson, 897 F.2d 935 (8th Cir. 1990); In Re May, 194 B.R. 853, 855 (Bank. D.S.D. 1996); 11 U.S.C. § 541 ("The commencement of a case . . . creates an estate" which includes "interests of the debtor in property as of the commencement of the case.") In this instance, on the date of filing, the check written to Life Investors for $2200.00 had not yet cleared, and Debtor had $3,679.83 in his checking account.

The Debtor urges the Court to adopt a date of delivery rule as articulated in Kroh Bros. Dev. Co. v. Continental Constr. Eng'r, Inc. (In re Kroh Bros.), 930 F.2d 648 (8th Cir. 1991), in this context. Under 11 U.S.C. § 547 (b) payments made to creditors on or within 90 days of filing for bankruptcy are considered avoidable preferences with some exceptions as described in the statute in section (c). If the payment is considered an avoidable preference under 547 (b) the date that the check is honored is used to determine whether it falls within the 90 days under the Supreme Court's decision in Barnhill. In Kroh the Eighth Circuit concluded that under the exception to the avoidable preference found in § 547(c)(4) the date of delivery of a check should be used to determine when a pre-petition preference has taken place so that creditors will be

encouraged to continue to deal with troubled businesses.

The bankruptcy court correctly found that in this case the distinct policy considerations favor the application of the date of honor rule in the post-petition transfer context. To begin with, as the bankruptcy court pointed out, if the date of honor were used for pre-petition preference purposes but the date of delivery were used for post-petition transfers, checks written pre-petition but honored post-petition would not be subject to avoidance under § 547(b) or § 549 (a). Cf. Steege v. A.T. &T. (In re Superior Toy & Mfg. Co.), 183 B.R. 826, 837 (Bankr. N.D. Ill. 1995); see also Maurer v. Hedback (In re Maurer), 140 B.R. 744 (D. Minn. 1992) (equity is promoted where checks written by Debtor prior to filing that were honored after filing remained part of the estate). Further, there is substantial authority for proposition that checks written to pay pre-filing debt that are honored post-filing are to be regarded as post-petition transfers. See, e.g., Clendenen v. Van Dyk Oil Co. (In re By-Rite Distrib., Inc.), 89 B.R. 906 (D. Utah 1988); Shanor v. Chappell & Barlow (In re Bellamah Community Dev.), 139 B.R. 29 (Bankr. D. N.M. 1992); In re Lange, 110 B.R. 907 (Bankr. D. Minn. 1990).

> Post-petition transfers are governed by 11 U.S.C. § 549 which provides in part:
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> (a) Except as provided in subsection (b) and (c) of this section, the trustee may avoid a transfer of property of the estate — (1) that occurs after the commencement of the case; and (2) (B) that is not authorized under this title or by the court.

The determination of whether a post-petition transfer occurred under 11 U.S.C. § 549(a) turns on whether (1) there was a transfer (2) of estate property (3) after commencement of the bankruptcy (4) which was not authorized under the bankruptcy code or approved by the court. Section 101 (54) of the bankruptcy code defines a transfer as "every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing or parting with property or with an interest in property." Disbursement of funds from a checking account qualifies as a transfer under this definition. Clendenen v. Van Dyk Oil Co. (In re By-Rite Distrib., Inc.), 89 B.R. 906 (D. Utah 1988).

Under South Dakota law, "[a] check or other draft does not of itself operate as an assignment of funds in the hands of the drawee available for its payment . . . ." S.D.C.L § 57A-3-408. See also Clendenen, 89 B.R. 906, 909-910 (applying state law to determine whether a transfer of funds from a checking account is complete at the time of delivery or time of honoring). Since a check is not an assignment of someone's funds but only represents an order upon a bank

to pay a specified sum to the order of a certain person, the Court must look to when the checks were paid to determine whether the funds remained in the estate. See In re Wilson, 56 B.R. 74, 76 (Bankr. E.D. Tenn. 1985) (noting that a number of things can prevent the transfer of funds once a check has been written including notice of the bank customer's death or bankruptcy, the customer's stop payment, or an intervening legal process). Accordingly, at the time the check to Life Investors was paid, property of the estate was used to pay a pre-petition debt.

Conclusion

In view of the foregoing discussion, the decision of the bankruptcy court will be affirmed. Therefore,

IT IS ORDERED:

that the decision of the bankruptcy court is affirmed.

Dated this 9th day of September, 1998.

BY THE COURT:

Lawrence L. Piersol
United States District Judge

ATTEST:
JOSEPH HAAS, CLERK
BY: Sharon Soucy
DEPUTY
(SEAL)

FILED

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CLERK

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SOUTHERN DIVISION

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	*	JUDGMENT
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In accordance with the Opinion entered September 9, 1998 by the Court,

IT IS ORDERED, ADJUDGED, AND DECREED:

that the decision of the Bankruptcy Court is affirmed.

Dated this 11th day of September, 1998.

BY THE COURT:

Lawrence L. Piersol
United States District Judge

ATTEST:
JOSEPH HAAS, CLERK

BY: Sharon Sure
DEPUTY

(SEAL)