

# Excluding Life and Insurance Benefits from Insolvent Estates: A Comparative Study of South Africa, England and Wales, and the United States of America

Z Mabe\* and E Mbiriri\*\*

Online ISSN  
1727-3781

**P·E·R**

Pioneer in peer-reviewed,  
open access online law publications

## Authors

Zingapi Mabe  
Edith Mbiriri

## Affiliation

University of Pretoria,  
South Africa  
University of South Africa

## Email

zingapi.mabe@up.ac.za  
mbirie@unisa.ac.za

## Date Submitted

15 June 2023

## Date Revised

7 March 2024

## Date Accepted

18 April 2024

## Date Published

16 October 2024

## Editor

Prof C Rautenbach

## Journal Editor

Prof W Erlank

## How to cite this contribution

Mabe Z Mbiriri E "Excluding Life and Insurance Benefits from Insolvent Estates: A Comparative Study of South Africa, England and Wales, and the United States of America" *PER / PELJ* 2024(27) - DOI  
<http://dx.doi.org/10.17159/1727-3781/2024/v27i0a16330>

## Copyright



## DOI

<http://dx.doi.org/10.17159/1727-3781/2024/v27i0a16330>

## Abstract

In South Africa, two principles apply to the exclusion of certain assets from an insolvent estate. First is the common-law principle that even the desperate insolvent is entitled to the basic necessities of life. Hence his entitlement to keep certain assets and to protect assets belonging to third parties. Secondly, the "creditor advantage" principle requires the trustee of the insolvent estate to collect assets to benefit the creditors of the estate. One of the assets excluded from the insolvent estate is the life and disability insurance policy benefits of the insolvent. These benefits are excluded, however, only if the beneficiary is the insolvent and the exclusion will not apply where the beneficiary is a third party such as a solvent spouse. However, section 21 of the *Insolvency Act* 24 of 1936 vests the assets of the solvent spouse in the trustee of the insolvent estate upon the latter's sequestration. This vesting is out of sync with the principle aimed at protecting assets belonging to third parties. In England and Wales a trust is created to protect the insurance policy benefits of a spouse or child of the bankrupt but does not extend to any other third party. In the United States of America the proceeds of a life insurance policy benefit will form part of the estate if the bankrupt owned it before the bankruptcy began or if the debtor acquired or became entitled to it within 180 days after the filing date. Where the debtor nominated a third party as the beneficiary of an unmatured policy, the power of appointment becomes part of the estate of the debtor. As the nominated third party acquires only an inchoate expectation, the third party's expectation of that unmatured life insurance policy benefit forms part of the bankrupt estate. This paper compares the treatment of life and disability insurance benefits in insolvent estates in South Africa with the position in England and Wales and the United States of America to establish whether there are lessons to be learnt which may assist in modelling an insolvency law process for South Africa which will consider the affected members of society.

## Keywords

Life insurance policy; benefits; insolvent estate; third parties; exclusion; vesting; trustee; insured.

.....

## 1 Introduction

In South Africa the sequestration of an insolvent person vests all his<sup>1</sup> assets in the trustee of the insolvent estate to benefit the creditors of the estate.<sup>2</sup> The vesting of these assets is driven by the principle of creditor advantage,<sup>3</sup> which forms the cornerstone of South African insolvency law. This principle requires the trustee of the estate to collect as many assets from the debtor and from any person who is in possession of assets belonging to the debtor, to benefit the creditors of the estate.<sup>4</sup> This entails that if, through the process of sequestration, it appears that the creditors of the estate would receive a better dividend outside of sequestration, the court may refuse to grant the sequestration order.<sup>5</sup>

However, in collecting these assets the trustee may come across assets that belong to third parties. As all the assets in the debtor's possession upon his sequestration vest in the trustee, assets in the debtor's possession belonging to third parties also vest in the trustee of the insolvent estate.<sup>6</sup> Therefore, there are stakeholders other than the insolvent debtor and creditor who are affected by sequestration proceedings and whose interests demand protection. Katz AJ in *SA Restructuring and Insolvency Practitioners Association*<sup>7</sup> stated that, although the law of insolvency is generally concerned with protecting the rights and interests of creditors, insolvency is necessarily and appropriately shifting from being a creditor-

---

\* Zingapi Mabe. LLB LLM PhD. Senior Lecturer, Faculty of Law, University of Pretoria (Hatfield Campus), South Africa. Email: zingapi.mabe@up.ac.za. ORCID ID: <https://orcid.org/0000-0002-4106-2385>. Google scholar ID: <https://scholar.google.com/citations?user=-HDhaUEAAAAJ&hl=en>.

\*\* Edith Mbiriri. LLB, LLM. Lecturer, Faculty of Law, University of South Africa (Pretoria Campus) South Africa. E-mail: mbirie@unisa.ac.za. ORCID ID: <https://orcid.org/0000-0002-2762-824X>.

<sup>1</sup> For the purpose of convenience, where relevant the male and/or female genders will be used interchangeably. No discrimination is implied or intended.

<sup>2</sup> Sections 20(2)(a) and (b) of the *Insolvency Act* 24 of 1936 (hereafter the *Insolvency Act* or Act). See Evans 2011 *PELJ* 39; *Warricker v Liberty Life Association of Africa Ltd* 2003 6 SA 272 (W) (hereafter *Warricker v Liberty Life*) para 9.

<sup>3</sup> Sections 6(1), 10(c) and 12(1)(c) of the *Insolvency Act*. See generally Loubser 1997 *SA Merc LJ* 327.

<sup>4</sup> Bertelsmann *et al Mars: Law of Insolvency* 80-82, 152-155, and, generally, ch 15. Evans and Borraine 2005 *De Jure* 268; Evans 2011 *PELJ* 39.

<sup>5</sup> Bertelsmann *et al Mars: Law of Insolvency* 80-82, 152-155.

<sup>6</sup> Whenever an insolvent has acquired possession of property which is claimed by the trustee, it is deemed to belong to the insolvent estate unless the contrary is proved. See s 24(2) of the *Insolvency Act*; Smith, Van der Linde and Calitz *Hockly's Law of Insolvency* para 5.2.

<sup>7</sup> *South African Restructuring and Insolvency Practitioners Association v Minister of Justice and Constitutional Development* 2015 2 SA 430 (WCC) para 24 (hereafter *SA Restructuring and Insolvency Practitioners Association*).

driven regime to focusing on the interests of other stakeholders involved in and affected by insolvency proceedings.<sup>8</sup>

Certain assets, however, are excluded from the insolvent estate.<sup>9</sup> One of these is insurance policy benefits in terms of section 63 of the *Long-Term Insurance Act*.<sup>10</sup> Section 63 provides for the exclusion and protection from the insolvent estate of life and other insurance policy benefits which the insolvent insured took out for his benefit and which are payable to him. These policy benefits are wholly excluded from the insolvent estate and do not vest in the trustee.<sup>11</sup>

This exclusion of certain assets from the insolvent estate derives from the common-law principle that even the desperate insolvent is entitled to the basic necessities of life.<sup>12</sup> He is consequently entitled to retain certain assets.<sup>13</sup> This common-law principle is not only aimed at protecting the insolvent's dignity and basic necessities of life, but it appears to also support the need to protect assets belonging to third parties.<sup>14</sup>

The trustee of an insolvent estate is therefore driven by two policies. Firstly, that of protecting certain assets from the insolvent estate for the benefit of the insolvent and third parties (where applicable); and secondly, that of collecting the maximum amount in assets to benefit creditors of the estate.<sup>15</sup>

In South Africa third parties are further protected in the case of insurance policy benefits by the creation of a contract for the benefit of a third party. This entails that where a person has effected life or disability insurance on his life but for the benefit of a third person, in which case section 63 above would not apply, a contract for the benefit of that third person will be created.<sup>16</sup>

---

<sup>8</sup> Also see World Bank *Report on the Treatment of the Insolvency of Natural Persons* (hereafter the World Bank Report) para 76.

<sup>9</sup> See generally, ss 82(6), 23(9), 23(7) and 23(8) of the *Insolvency Act*, Bertelsmann *et al Mars: Law of Insolvency* 212-221.

<sup>10</sup> Section 63 of the *Long-Term Insurance Act* 52 of 1998 (hereafter the LTIA) as amended by the *Financial Services Laws General Amendment Act* 45 of 2013 (hereafter the *Financial Services Laws General Amendment Act*), which came into effect on 28 February 2014 and as amended by the *Insurance Act* 18 of 2017, which came into effect on 1 July 2018 (hereafter the *Insurance Act*).

<sup>11</sup> Since the amendment of the LTIA in 2014, s 63 does not vest any portion of the proceeds of the insurance policy benefit in the trustee of the insolvent estate.

<sup>12</sup> *Ex parte Kroese* 2015 1 SA 405 (NWM) para 67.

<sup>13</sup> Evans 2011 *PELJ* 40; Evans *Critical Analysis of Problem Areas* 251.

<sup>14</sup> Evans 2011 *PELJ* 40.

<sup>15</sup> Also see the public interest policy under the aims of a good modern insolvency law as promulgated by the Cork Review Committee *Review Committee Report* (the Cork Report) para 198.

<sup>16</sup> Evans and Borraine 2005 *De Jure* 270-273; Evans *Critical Analysis of Problem Areas* 281; *Pieterse v Shrobbree*; *Shrobbree v Love* 2005 1 SA 309 (SCA) para 8 (hereafter *Pieterse v Shrobbree*); *Warricker v Liberty Life* para 10. In insurance law these

However, neither the common-law policy of exclusion mentioned above nor the contract for the benefit of a third party appears to protect the assets of the solvent spouse, who is also a third party, which vest in the trustee of the insolvent estate upon the sequestration of the estate of his spouse in terms of section 21 of the *Insolvency Act*.

In England and Wales the assets of the bankrupt also vest in the trustee of the bankrupt estate upon his appointment<sup>17</sup> and as in South Africa certain assets are excluded from the insolvent estate.<sup>18</sup> Similarly life and ill-health insurance policies vest in the trustee of the bankrupt estate<sup>19</sup> and are termed "vesting assets".<sup>20</sup> However, section 11 of the *Married Women's Property Act*<sup>21</sup> by exception excludes a life policy from the bankrupt estate where the beneficiary of the policy is a spouse or child of the bankrupt. This section does not, however, protect insurance policy benefits taken out by the bankrupt for the benefit of someone other than his spouse or child.<sup>22</sup>

In the United States of America, all prepetition property becomes the property of the estate<sup>23</sup> and the trustee is obliged to sell and use the proceeds to pay creditors of the estate.<sup>24</sup> However, this does not apply to exempt property.<sup>25</sup> As a general rule, property that an individual debtor acquires after a Chapter 7 filing does not form part of the bankrupt estate and the bankrupt is entitled to keep such property.<sup>26</sup> However, the *Bankruptcy Code*<sup>27</sup> allows for the proceeds of a life insurance policy to form part of the estate if the bankrupt debtor owned the property before the bankruptcy filing or if he acquired or became entitled to acquire the property within 180 days after the date of the petition.

---

contracts are described as "third party contracts". See Reinecke, Van Niekerk and Nienaber *South African Insurance Law* 423.

<sup>17</sup> Section 306 of the *Insolvency Act*, 1986 (IA 1986) as amended by the *Insolvency Act*, 2000 and the *Enterprise Act*, 2002. See also Floyd, Brumby and Knight *Personal Insolvency* para 6-27; Fletcher *Law of Insolvency* para 8-002.

<sup>18</sup> Section 283(2) of the IA 1986.

<sup>19</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 168; Insolvency Service date unknown <https://bit.ly/3hOBcdG>; Fletcher *Law of Insolvency* para 8-037.

<sup>20</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 168.

<sup>21</sup> Section 11 of the *Married Women's Property Act*, 1882 (hereafter MWPA). Certain words in s 11 were repealed by the *Law Reform (Married Women and Tortfeasors) Act*, 1935 (c 30), *Statute Law (Repeals) Act*, 1969 (c 52) and certain words were replaced by the *Law Reform (Married Women and Tortfeasors) Act*, 1935 (c 30).

<sup>22</sup> Clarke *Law of Insurance Contracts* para 5-4A.

<sup>23</sup> Section 541(a)(1) of the *Bankruptcy Code* (*Bankruptcy Reform Act* of 1978) (hereafter the *Bankruptcy Code* or Code).

<sup>24</sup> Sections 704(a) and 726 of the Code.

<sup>25</sup> Ferriell and Janger *Understanding Bankruptcy* 204.

<sup>26</sup> Ferriell and Janger *Understanding Bankruptcy* 204.

<sup>27</sup> Section 541(a)(5)(C) of the Code.

In this article the treatment of life and other insurance policy benefits in insolvent estates and the effect on third parties in South Africa will be compared with the position in England and Wales and the United States of America.

The English and the American jurisdictions have been chosen for comparison because they are seen to be at the forefront of the shift from a creditor-friendly bankruptcy system to a more debtor-friendly system that considers the interests not only of the creditors and debtors but also all other affected stakeholders.<sup>28</sup> For instance, one of the goals of bankruptcy, as proposed by the World Bank Report,<sup>29</sup> is to provide a fresh start to the honest but unfortunate debtor. Both these jurisdictions have advanced in developing their insolvency laws in this regard. Therefore, a brief discussion of their bankruptcy system as regards the vesting of insurance policy benefits in the bankrupt estate and the effect on third parties will be beneficial in establishing whether there are lessons to be learnt in the treatment of insurance benefits in insolvent estates in South Africa. This may also assist in modelling a sequestration process in South Africa that takes account of the affected members of society.

This discussion opens with an analysis of South Africa's *Long-Term Insurance Act* (LTIA) and its effect on the assets belonging to third parties. The English position followed by the American bankruptcy system is then considered to show how they treat life and ill-health insurance benefits on insolvency. The discussion will conclude with a summary of findings and recommendations regarding the South African position.

## 2 The *Long-Term Insurance Act*

As indicated, the exclusion of life and other insurance from the insolvent estate in South Africa is directed by section 63 of the LTIA. Section 63 reads:

### 63. Protection of policy benefits under certain long-term policies.

- (1) Subject to subsections (2), (3) and (4), the policy benefits provided or to be provided to a person under one or more -
  - (a) in respect of a registered insurer, assistance, life, disability or health policies; or
  - (b) in the case of a licensed insurer, policies written under the risk, fund risk, credit life, funeral, life annuities, individual investment or income drawdown class of life insurance business as set out in Table 1 of Schedule 2 of the Insurance Act,  
  
in which that person or the spouse of that person is the life insured and which has or have been in force for at least three

---

<sup>28</sup> World Bank Report para 76.

<sup>29</sup> World Bank Report paras 398 and 454.

- years (or the assets acquired exclusively with those policy benefits) shall, other than for a debt secured by the policy -
- (i) during his or her lifetime, not be liable to be attached or subjected to execution under a judgment of a court or form part of his or her insolvent estate; or
  - (ii) upon his or her death, if he or she is survived by a spouse, child, stepchild or parent, not be available for the purpose of the payment of his or her debts.
- (2) The protection contemplated in subsection (1) shall apply to policy benefits and assets acquired solely with the policy benefits, for a period of five years from the date on which the policy benefits were provided.
  - (3) Policy benefits are only protected as provided in -
    - (a) subsection (1)(b), if they devolve upon the spouse, child, stepchild or parent of the person referred to in subsection (1) in the event of that person's death; and
    - (b) subsection (1)(a) and (b), if the person claiming such protection is able to prove on a balance of probabilities that the protection is afforded to him or her under this section.
  - (4) Policy benefits are protected as provided for in subsection (1)(a) and (b), unless it can be shown that the policy in question was taken out with the intention to defraud creditors.

Section 63 protects life, disability and other insurance policy benefits payable to the insolvent from falling into his insolvent estate. It applies in circumstances where the insolvent or his spouse is the life insured, and where the policy has been in existence for at least three years.<sup>30</sup> Section 63 protects those insurance benefits payable to the insolvent while he is still alive, as well as those payable after his death.<sup>31</sup>

However, where the policy was taken out with the intent to defraud creditors of the insolvent estate, section 63(4) provides that any benefit arising from a policy that can be shown to have been taken out to defraud creditors will not be protected by section 63. This provision is one of the additions to section 63 which resulted from the amendment of the section in February 2014. It appears to be aimed at ensuring that beneficiaries do not receive monies that should be used to satisfy the claims of creditors.<sup>32</sup>

Before the amendment of section 63, only R50 000 of the insurance benefit payable to the insolvent was excluded from the insolvent estate,<sup>33</sup> leaving

---

<sup>30</sup> Section 63(1) of the LTIA. See Meskin *et al Insolvency Law* para 5.3.2.1; Bertelsmann *et al Mars: Law of Insolvency* 215.

<sup>31</sup> Section 63(1)(b) of the LTIA. Bertelsmann *et al Mars: Law of Insolvency* 215.

<sup>32</sup> Mabe 2015 *THRHR* para 2.2.2.

<sup>33</sup> Section 63(2)(b) of the LTIA before the 2014 amendment. Also see Meskin *et al Insolvency Law* para 5.3.2.1; Bertelsmann *et al Mars: Law of Insolvency* 215.

the balance of the policy benefit (if any) to satisfy creditors' claims.<sup>34</sup> Currently the entire benefit is excluded from the insolvent estate, leaving nothing for the creditors of the estate.<sup>35</sup>

Section 63 applies to any insolvent person and does not distinguish between marriages in community of property<sup>36</sup> and those that are out of community of property.<sup>37</sup> Further, this protection or exclusion of insurance benefits applies only where the insolvent is the beneficiary of the insurance policy and does not apply where the beneficiary is a third party.<sup>38</sup> In this regard, a third party includes amongst others the spouse<sup>39</sup> of the insolvent to whom he is married out of community of property.<sup>40</sup>

Where the insolvent policyholder nominates a third party as a beneficiary of his insurance policy benefit, a contract for the benefit of a third party is created.<sup>41</sup> On acceptance of the benefit by the third party, that policy benefit is paid directly to the third party to the exclusion of the creditors of the insolvent estate.<sup>42</sup> Although the contract for the benefit of a third party appears to protect the third party in this scenario, it does not protect the policy benefit from falling into the insolvent estate of the third party. This would be the case where A (a third party) is a beneficiary of an insurance policy effected by B, who has subsequently been declared insolvent. It emerges that A, too, is insolvent. When A accepts the insurance policy benefit from B, that benefit will fall into his (A's) insolvent estate.<sup>43</sup>

On the other hand, where the third party is a solvent spouse, a contract for the benefit of a third party will still be created, and on acceptance of the

---

<sup>34</sup> *Shroobree v Van Rooyen* 2004 1 SA 226 (SE) 230-231; Meskin *et al Insolvency Law* para 5.3.2.1 B.

<sup>35</sup> The current s 63(2) of the LTIA no longer makes a reference to the R50 000. Mabe 2015 *THRHR* para 2.2.1; Bertelsmann *et al Mars: Law of Insolvency* 215.

<sup>36</sup> Where there is a joint estate and the spouses are jointly referred to as the "insolvent debtors". Smith, Van der Linde and Calitz *Hockly's Law of Insolvency* para 5.2. For a consideration of whether the trustees of an insolvent joint estate are entitled to claim the proceeds of a life insurance policy that was paid to the surviving insolvent husband who was married in community of property to his late wife, see *Wentzel v Discovery Life Limited: In Re Botha v Wentzel* 2021 6 SA 437 (SCA), although the court in this case failed to analyse the circumstances under which s 63 applies and consequently could not realise that s 63 applied to the facts in this case. Also see Mabe and Mbiriri 2022 *PELJ* and Roestoff and Borraine 2022 *THRHR*.

<sup>37</sup> Where there are separate estates belonging to the insolvent spouse and the solvent spouse.

<sup>38</sup> Bertelsmann *et al Mars: Law of Insolvency* 215.

<sup>39</sup> Hereafter the "solvent spouse".

<sup>40</sup> Bertelsmann *et al Mars: Law of Insolvency* 215.

<sup>41</sup> Evans and Borraine 2005 *De Jure* 270; Evans *Critical Analysis of Problem Areas* 281; *Pieterse v Shroobree* para 8; *Warricker v Liberty Life* para 10.

<sup>42</sup> *Pieterse v Shroobree* para 12.

<sup>43</sup> See *Wessels v De Jager* 2000 4 SA 924 (SCA) 928, where the insolvent repudiated the insurance policy for fear of its falling into his insolvent estate.



benefit it will be paid to him directly. However, section 21 of the Insolvency Act provides for the vesting of the assets of the solvent spouse together with those of the insolvent spouse in the trustee of the insolvent estate upon the sequestration of the insolvent spouse.<sup>44</sup> This means that although the solvent spouse has an estate separate from that of the insolvent, his assets also vest in the trustee of the insolvent estate.<sup>45</sup>

Now, section 63 of the LTIA and the common-law policy of exclusion in the context of life and other insurance policies, only protect assets belonging to an insolvent person. As indicated earlier, they do not protect assets belonging to the solvent spouse which have vested in the trustee of the insolvent estate in terms of section 21 of the *Insolvency Act*. It may consequently happen that the proceeds of an insurance policy payable to a solvent spouse may also vest in the insolvent estate as per section 21 of the *Insolvency Act*.<sup>46</sup> If that is the correct position, it means not only that the solvent spouse is not sufficiently protected by insolvency legislation in South Africa, but also that South African insolvency law is not adequately answering the need to protect third parties in general in this respect. The shift away from creditor-friendly insolvency law already mentioned appears absent in the protection of the assets of solvent spouses when it comes to insurance policy benefits.

Section 21(2) of the *Insolvency Act* does provide some protection for the assets of the solvent spouse in that he may apply for the release of his assets from the trustee of the insolvent estate if he can prove release under the provision.<sup>47</sup> However, section 21(2) provides for release only after the vesting of the assets. It does not prevent the assets from vesting. Nonetheless, the court can prevent or cancel the vesting of the solvent spouse's property in two instances. Firstly, where the solvent spouse is carrying on business as a trader independently of the insolvent spouse and the court is satisfied that she is willing and able to make arrangements whereby the interest of the insolvent estate in the property will be safeguarded without such vesting.<sup>48</sup> Secondly, where it appears to the court that the solvent spouse is likely to suffer serious prejudice through the immediate vesting.<sup>49</sup> However, despite the court's intervention to provide

---

<sup>44</sup> Section 21(1) of the Act. Also see Bertelsmann *et al Mars: Law of Insolvency* 228; Smith, Van der Linde and Calitz *Hockly's Law of Insolvency* 97.

<sup>45</sup> Meskin *et al Insolvency Law* para 5.30.1.2. However, the vesting is temporary. See generally Smith, Van der Linde and Calitz *Hockly's Law of Insolvency* 97.

<sup>46</sup> See Mabe 2015 *THRHR* para 3.2.

<sup>47</sup> Section 21(2) of the Act defines five categories of property which the trustee is obliged to release to the solvent spouse. The solvent spouse bears the onus of proving her entitlement to the release of the property on one or more of these grounds. Meskin *et al Insolvency Law* para 5.30.2.

<sup>48</sup> See s 21(10) of the *Insolvency Act*.

<sup>49</sup> Section 21(10) of the *Insolvency Act*, Meskin *et al Insolvency Law* para 5.30.1.2.



interim release of the solvent spouse's assets, the solvent spouse still has to secure a release of his assets from the trustee.<sup>50</sup>

In this regard the solvent spouse may apply for a release under section 21(2)(c), which provides for a release of assets acquired by valid title by the solvent spouse during the marriage, against the creditors of the insolvent.<sup>51</sup> Further, were it not for the repeal of section 28 of the *Insolvency Act*, which provided for a release of property protected by other provisions, a solvent spouse could apply for a release in terms of section 21(2)(d) of the *Insolvency Act*, which refers to section 28.<sup>52</sup> It is submitted that the vesting of the assets of the solvent spouse may be prevented by the inclusion of a provision in insolvency legislation excluding the assets of the solvent spouse from the insolvent estate. Such an inclusion would be in line with the view expressed by Katz AJ<sup>53</sup> that although the interests of creditors in the insolvency process are paramount, regard should be given to other members of society, such as the solvent spouse, who are also affected by the insolvency process.

However, such exclusion of the assets of the solvent spouse would be inconsistent with section 21, which was enacted to prevent collusion between spouses married out of community of property and which was declared constitutional in *Harksen v Lane*.<sup>54</sup> Despite this, it is submitted that although in marriages out of community of property there are chances of collusion between spouses, where there is no evidence of such collusion section 21 appears to disadvantage the solvent spouse.<sup>55</sup>

From this discussion it is evident that the insolvent debtor's interests are preferred to those of creditors where life and other insurance benefits are concerned. This is shown by the fact that upon the sequestration of the estate of a person (where all the requirements of section 63 have been met), the proceeds of that person's insurance policy are excluded from his insolvent estate and would also not be available to pay the debts of his deceased estate where the policy benefit paid out on his death.<sup>56</sup> This happens irrespective of the amount of the proceeds of the policy and despite the application of the "creditor benefit" principle. This appears to be in line

---

<sup>50</sup> Meskin *et al Insolvency Law* para 5.30.1.2.

<sup>51</sup> Mabe 2015 *THRHR* para 3.1.

<sup>52</sup> Section 28 of the *Insolvency Act* was repealed by s 78 of the *Insurance Act 27 of 1943* (the old *Insurance Act*). See Evans *Critical Analysis of Problem Areas Pt IV*, Ch 9, para 931; Sharrock, Van der Linde and Smith *Hockly's Insolvency Law* 101; Mabe 2015 *THRHR* para 3.1.

<sup>53</sup> *SA Restructuring and Insolvency Practitioners Association* para 28.

<sup>54</sup> *Harksen v Lane* 1998 1 SA 300 (CC) held that s 21 does not infringe the provisions of the Bill of Rights. See Bertelsmann *et al Mars: Law of Insolvency* 230-234.

<sup>55</sup> Boraine and Evans *Law of Insolvency* para 4A6.

<sup>56</sup> Section 63(3)(a) of the LTIA.

with the international trend of moving away from a creditor-friendly approach to insolvency law to a more debtor-friendly approach.<sup>57</sup>

On the other hand, when it comes to the protection of the insurance policy benefits of third parties such as the solvent spouse, the South African insolvency law is shifting further away from the idea of protecting the assets of other stakeholders who are affected by insolvency proceedings. This is shown by the vesting of the assets of the solvent spouse upon the sequestration of the insolvent, and section 63's denial of protection to the solvent spouse's insurance proceeds.

Further, the protection of policy benefits against fraud is not relevant to the solvent spouse. Rather it appears to be aimed at advancing the interest of creditors of the insolvent estate.

Having established South Africa's insolvency law treatment of life and other insurance policies and the effect on third parties, the treatment of life and ill health insurance benefits in English insolvency law will be discussed.

### 3 The position in England and Wales

The bankruptcy procedure in England and Wales is regulated by the *Insolvency Act, 1986* (IA 1986). In terms of this legislation,<sup>58</sup> the bankrupt's estate vests in the trustee immediately upon his appointment.<sup>59</sup> The bankrupt's estate consists of all property<sup>60</sup> belonging to the bankrupt at the commencement of bankruptcy,<sup>61</sup> and any other property which is included in the bankrupt estate in terms of other provisions of the Act.<sup>62</sup> An example of "other provisions" which vest the property of the bankrupt in the trustee is section 307, which empowers the trustee of a bankrupt estate to claim property acquired by the bankrupt after the commencement of his bankruptcy but before his eventual discharge.<sup>63</sup>

---

<sup>57</sup> Mabe 2015 *THRHR* para 4.

<sup>58</sup> Section 306 of the IA 1986.

<sup>59</sup> Floyd, Brumby and Knight *Personal Insolvency* para 6-27; Fletcher *Law of Insolvency* para 8-002.

<sup>60</sup> Section 436 of the IA 1986 defines "property" to include money, goods, things in action, land, and every description of property wherever situated and also obligations and every description of interest, whether present or future or vested or contingent, arising out of, or incidental to, property. See also Fletcher *Law of Insolvency* paras 8-007 and 8-003.

<sup>61</sup> Bankruptcy of the debtor against whom a bankruptcy order has been made commences on the day on which the order is made, and continues until either the bankruptcy is discharged or the bankruptcy order is annulled. See ss 279-282 of the IA 1986.

<sup>62</sup> Section 283(1) of the IA 1986; Floyd, Brumby and Knight *Personal Insolvency* para 8-04; Fletcher *Law of Insolvency* paras 8-007 and 8-033.

<sup>63</sup> Section 307(1) of the IA 1986; Floyd, Brumby and Knight *Personal Insolvency* para 8-90; Fletcher *Law of Insolvency* para 8-033.

The IA 1986 does not have an equivalent of the South African section 21,<sup>64</sup> and so, unlike the position in South African insolvency law, the assets of the spouse of the bankrupt do not vest in the bankrupt estate upon his bankruptcy. This appears to be in line with the international approach of protecting the interests of all the parties affected by the insolvency process.

As in South Africa, there are exceptions to the vesting of the assets of the bankrupt in the trustee of the bankrupt estate. However, the IA 1986 does not as a general rule exclude the proceeds of life<sup>65</sup> and ill health insurance policies from the insolvent estate. Three situations arise in respect of life insurance benefits and bankruptcy in England and Wales. The first is where the bankrupt took out a policy of insurance upon his own life for his own benefit. The second is where the bankrupt is the life insured but someone other than the bankrupt pays the premiums.<sup>66</sup> The third occurs where the bankrupt took out a policy of insurance on his own life for the benefit of some other person.<sup>67</sup>

### **3.1 Insurance policy on the life of the insured for his benefit**

Where the bankrupt took out life insurance on his life for his benefit before the commencement of bankruptcy or even after the adjudication but failed to inform the trustee, the policy benefits are regarded as vesting assets and form part of his bankrupt estate.<sup>68</sup> The trustee of the bankrupt estate becomes the owner of the proceeds of the policy<sup>69</sup> and may use the monies to settle the bankrupt's debts.<sup>70</sup> This also applies to ill health insurance policies.<sup>71</sup>

As already mentioned, the situation is different in South Africa where the proceeds of life and disability insurance are excluded from the insolvent estate by virtue of section 63 of the LTIA<sup>72</sup> and are not used to pay the debts

---

<sup>64</sup> Section 21(1) of the *Insolvency Act* vests the assets of the solvent spouse in the trustee of the insolvent estate upon the sequestration of the insolvent.

<sup>65</sup> Evans and Boraine 2005 *De Jure* 287.

<sup>66</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 122a. Fletcher *Law of Insolvency* para 8-037.

<sup>67</sup> See generally Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6; Evans and Boraine 2005 *De Jure* 287.

<sup>68</sup> Fletcher *Law of Insolvency* para 8-037; *Tapster v Ward* (1909) 101 LT 503; Barrand 1910 *Journal of the Institute of Actuaries*; Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 168.

<sup>69</sup> Fletcher *Law of Insolvency* para 8-037. Also see Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 168.

<sup>70</sup> Evans and Boraine 2005 *De Jure* 287.

<sup>71</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 168.

<sup>72</sup> In *Pieterse v Shroobree* para 12 it was held that the proceeds of the policy do not reach the hands of the trustee.

of the insolvent, but are paid directly to the beneficiary<sup>73</sup> to the exclusion of the creditors of the insolvent estate.<sup>74</sup>

At first glance it appears that the treatment of life insurance policy benefits in England and Wales and South Africa differ and the insolvency process does not raise the same problems for third parties. However, as it will be shown, there are also exceptions to the vesting of life insurance policies in the estate of the bankrupt and these exceptions, as in South Africa, exclude certain third parties from protection.

### **3.2 Insurance policy on the life of the insured, premiums paid by some other person**

Where the premiums of the policy have been paid by someone other than the bankrupt whose life is insured,<sup>75</sup> a resulting trust will be created.<sup>76</sup> In such a case the person who has paid the premiums will be entitled to be repaid a percentage of his expenditure out of the proceeds of the policy if the trustee knew the arrangement.<sup>77</sup> However, if the person who paid the premiums intended it to be a gift or a loan, a resulting trust will not be created.<sup>78</sup> In such a case the official receiver is required to ascertain whether the payments were a gift or a loan before accepting that person's interest in the policy.<sup>79</sup>

### **3.3 Insurance policy on the life of the insured for the benefit of a third party**

Where the bankrupt took out life insurance on his life for the benefit of a third party, certain statutory exceptions to protect the proceeds of that life insurance from being used to pay the debts of the bankrupt apply.<sup>80</sup> One of these exceptions is the life insurance money of a deceased spouse that may be protected in favour of certain of his dependants in terms of the *Married Women's Property Act, 1882* (MWPA).<sup>81</sup> Section 11 of the Act provides:<sup>82</sup>

**11. Moneys payable under policy of assurance not to form part of estate of the insured.**

A married woman may effect a policy upon her own life or the life of her husband for her own benefit; and the same and all benefit thereof shall enure accordingly. A policy of assurance effected by any man on his own life, and

---

<sup>73</sup> *Pieterse v Shrosbree* para 12.

<sup>74</sup> See Mabe 2015 *THRHR* para 2.2.1.

<sup>75</sup> Fletcher *Law of Insolvency* para 8-037.

<sup>76</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 122a.

<sup>77</sup> Fletcher *Law of Insolvency* para 8-037.

<sup>78</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 122a.

<sup>79</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 122a.

<sup>80</sup> Evans and Boraine 2005 *De Jure* 287.

<sup>81</sup> Section 11 of the MWPA. Evans and Boraine 2005 *De Jure* 287; Clarke *Law of Insurance Contracts* para 5-4; Birds *Modern Insurance Law* para 19.3.1.

<sup>82</sup> Clarke *Law of Insurance Contracts* para 5-4A.

expressed to be for the benefit of his wife, or of his children, or of his wife and children, or any of them, or by any woman on her own life, and expressed to be for the benefit of her husband, or of her children, or of her husband and children, or any of them, shall create a trust in favour of the objects therein named, and the moneys payable under any such policy shall not, so long as any object of the trust remains unperformed, form part of the estate of the insured, or be subject to his or her debts: Provided, that if it shall be proved that the policy was effected and the premiums paid with intent to defraud the creditors of the insured, they shall be entitled to receive, out of the moneys payable under the policy, a sum equal to the premiums so paid.

Consequently, where an insurance policy is taken out for the benefit of a person other than the insured, a trust will be created for the benefit of that person.<sup>83</sup> The money payable under that policy will not form part of the insured's bankrupt estate.<sup>84</sup> Normally section 11 covers life policies payable on the death of the life insured,<sup>85</sup> but section 11 may also apply to policies that cover events other than death, such as accidental injury.<sup>86</sup> It follows then that although as a general rule ill health insurance policies vest in the trustee of the bankrupt estate, they may be excluded by section 11 if the accidental injury leads to ill health. This then places the treatment of ill health insurance in England and Wales on par with the position in South Africa, where section 63 of the LTIA excludes life and other insurance from the insolvent estate.

Although section 11 is limited to the life of the insured,<sup>87</sup> the individual whose life is insured cannot be the beneficiary of a section 11 trust.<sup>88</sup> This differs from section 63 of the LTIA, in terms of which only the insolvent can be the beneficiary of the life policy, although he might not be the life insured.<sup>89</sup>

Section 11 was created to protect the bankrupt's immediate family<sup>90</sup> and to control the destination of money paid out on the policy.<sup>91</sup> As a result, the beneficiaries of the policy are limited to dependants of the insured, and this is further limited to a spouse<sup>92</sup> or child<sup>93</sup> of the insured.<sup>94</sup> This is again different to South Africa's section 63 which appears to be aimed at

---

<sup>83</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 120.

<sup>84</sup> Birds *Modern Insurance Law* para 19.3.1.

<sup>85</sup> Birds *Modern Insurance Law* para 19.3.1.

<sup>86</sup> Clarke *Law of Insurance Contracts* para 5-4A1.

<sup>87</sup> Clarke *Law of Insurance Contracts* para 5-4A.

<sup>88</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 120.

<sup>89</sup> Section 63 of the LTIA allows the life insured to be the insolvent or his spouse.

<sup>90</sup> Evans and Borraine 2005 *De Jure* 287.

<sup>91</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 120.

<sup>92</sup> Section 11 of the LTIA also applies to insurances effected by civil partners. See Birds *Modern Insurance Law* para 19.3.1.

<sup>93</sup> "Children" includes children born out of wedlock and children adopted by the insured under an adoption order. See Clarke *Law of Insurance Contracts* para 5-4A5.

<sup>94</sup> Clarke *Law of Insurance Contracts* para 5-4A.

protecting the proceeds of life insurance only where the debtor is the beneficiary.

Since England and Wales do not have a section 21<sup>95</sup> equivalent, it appears that the spouse of the bankrupt in England and Wales is better protected than the solvent spouse in South Africa, where her assets vest in the trustee of the insolvent estate upon the sequestration of the insolvent. In addition, the insurance policy benefits of the English spouse of the bankrupt cannot fall into the bankrupt estate. Lastly, she does not carry the same burden of proof as regards the release of his assets from the trustee of the bankrupt estate.

Accordingly, where the insurance policy is for the benefit of a person other than the spouse or child of the deceased, section 11 does not apply and a trust will not be created in favour of that third person. As this “other third person” is not protected by the section 11 trust and does not fall under the exception to the general rule, it appears that his benefit will not be excluded from the bankrupt estate.<sup>96</sup>

If it is true that a third party other than a spouse or child does not fall under the exception to the general rule in England and Wales, the benefit will not be excluded from the bankrupt estate, which appears to be unfair to the third party. The injustice lies in the limitation of dependants to spouses and children. A dependant can also include a parent, a child who has not been officially adopted by the insured, or any family member who is financially dependent on the insured.<sup>97</sup> Section 11 does not consider these categories of beneficiaries. In this respect, it appears that section 11 does not protect the rights to property of third parties as opposed to the South African approach, which protects the assets of third parties from the insolvent estate.

As indicated, in South Africa the contract for the benefit of a third party<sup>98</sup> applies to our scenario above. In terms of this principle, the proceeds of the insurance policy are paid directly to the third party upon his acceptance of the benefit.<sup>99</sup> This happens whether the third party is a spouse, child, parent, or any other person who is financially dependent on the insured. As we have seen in the case of the solvent spouse, the proceeds of the insurance policy

---

<sup>95</sup> Section 21 of the *Insolvency Act*.

<sup>96</sup> Unless protected by some other legislation.

<sup>97</sup> The view that if a policy purports to benefit both persons who fall within the scope of s 11 of the LTIA and persons who are not, that a trust for the former will be created in terms of s 11, and an express trust without any resort to the Act for the latter will also be created, is supported. See Clarke *Law of Insurance Contracts* para 5-4A2.

<sup>98</sup> Evans and Borraine 2005 *De Jure* 270; Evans *Critical Analysis of Problem Areas* 281; *Pieterse v Shrosbree* para 8; *Warricker v Liberty Life* para 10.

<sup>99</sup> See *Oshry v Feldman* 2010 6 SA 19 (SCA) para 45; *Pieterse v Shrosbree* para 10; Bertelsmann *et al Mars: Law of Insolvency* 217.

vest in the trustee of the estate<sup>100</sup> and run the risk of falling permanently into the insolvent estate if the solvent spouse fails to prove release.<sup>101</sup> However, other third parties receive the proceeds of the insurance policy. As the contract for the benefit of a third party applies in South Africa, the creation of a trust to protect the proceeds of an insurance policy from falling into the insolvent estate would be unnecessary in respect of third parties other than the solvent spouse. A similar approach would have to be adopted in legislation in respect of the solvent spouse.

One should note that section 11 only applies to policies taken out by a married man or woman on his or her own life.<sup>102</sup> It finds no application where the insured is unmarried. Unless there is other legislation or law in England protecting insurance policy benefits taken by an unmarried bankrupt, the limitation of the protection of insurance benefits to married people only seems unfair, particularly to children born from unmarried parents. The inequality lies in the fact that even an unmarried bankrupt, as a breadwinner, may want to protect his insurance benefits from falling into his bankrupt estate and may have also taken life insurance for the benefit of his children. It would therefore be ideal to make provision for the needs of all children who are financially dependent on the bankrupt, even those born to unmarried parents.<sup>103</sup>

Section 11 of the MWPA also provides for circumstances where the policy was taken out and the premiums paid with the intent to defraud the creditors of the estate. This would be the case where the policy was taken out with the intent that the beneficiaries would receive monies that would otherwise go to creditors.<sup>104</sup> Where fraud is shown to exist in such a case, the creditors would be entitled to receive an amount from the monies payable under the policy equal to the premiums paid.<sup>105</sup> As section 11 is intended to make provision for the insured's bankrupt family despite his bankruptcy, it appears that a trust created under section 11 cannot be set aside as fraudulent under the IA 1986.<sup>106</sup>

However, if the trustee can establish that the trust was not created by the bankrupt in an attempt to deprive his creditors of the proceeds of the policy,

---

<sup>100</sup> Section 21(1) of the *Insolvency Act*.

<sup>101</sup> Section 21(2) of the *Insolvency Act*. See generally Smith, Van der Linde and Calitz *Hockly's Law of Insolvency* 97.

<sup>102</sup> Birds *Modern Insurance Law* para 19.3.1.

<sup>103</sup> This seems to be supported by the view that one of the purposes of s 11 is that there should be money for the family in spite of creditors. Clarke *Law of Insurance Contracts* para 5-4A3.

<sup>104</sup> Clarke *Law of Insurance Contracts* para 5-4A3.

<sup>105</sup> Clarke *Law of Insurance Contracts* para 5-4A.

<sup>106</sup> Sections 340 and 423 of the IA 1986; Clarke *Law of Insurance Contracts* para 5-4A3.



he will have no interest in the assurance policy.<sup>107</sup> This provision in section 11 is similar to section 63(4) of the LTIA. Although it would appear that the whole policy benefit would form part of the insolvent estate, section 63(4) does not explicitly indicate what would happen where fraud exists.<sup>108</sup>

#### 4 The position in the United States of America

Individual debtors in the United States of America can make use of the Chapter 7 liquidation proceedings or the Chapter 13 reorganisation proceedings. Under Chapter 7 the debtor surrenders his property to the trustee in exchange for a discharge from his debts.<sup>109</sup> The debtor who uses Chapter 13 retains his property and proposes a plan for the repayment of his debts from his future income with the court's approval.<sup>110</sup> Both proceedings provide for the automatic creation of a bankruptcy estate once a bankruptcy petition has been filed, with the bankruptcy estate becoming the owner of the debtor's property.<sup>111</sup> Although the Code deals with the scope of the bankruptcy estate and the property that falls into the estate, some limitations are imposed by the applicable state law such as state property law and some general federal law unless the *Bankruptcy Code* pre-empts or overrides such law.<sup>112</sup>

Section 541 of the Code<sup>113</sup> provides that subject to limited exceptions all the property that the debtor owned before petitioning for bankruptcy goes into the estate. Property includes amongst other things all legal or equitable interests of the debtor in property at the commencement of bankruptcy.<sup>114</sup> It also includes any interest in property that would have been the property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, provided that the debtor acquires or becomes entitled to acquire it within 180 days after the filing date.<sup>115</sup> Therefore, property that the debtor acquires after commencement may fall into the estate depending on when it was acquired<sup>116</sup> and the type of bankruptcy proceedings.

---

<sup>107</sup> Insolvency Service 2014 <https://bit.ly/36Y9Co5> ch 31.5, Pt 6, 121.

<sup>108</sup> Mabe 2015 *THRHR* para 2.2.2.

<sup>109</sup> Ferriell and Janger *Understanding Bankruptcy* 193.

<sup>110</sup> Ferriell and Janger *Understanding Bankruptcy* 193.

<sup>111</sup> Ferriell and Janger *Understanding Bankruptcy* 204.

<sup>112</sup> Elping, Brennan and Johnson 2012 *Norton Journal of Bankruptcy Law and Practice* 103; *In re Supreme Beef Processors, Inc* 468 F 3d 248 (5th Cir 2006) 255.

<sup>113</sup> Section 541(a)(1) of the *Bankruptcy Code*.

<sup>114</sup> Section 541(a)(1) of the Code. Elping, Brennan and Johnson 2012 *Norton Journal of Bankruptcy Law and Practice* 103.

<sup>115</sup> Section 541(a)(5) of the *Bankruptcy Code*.

<sup>116</sup> Section 541(a)(5) of the *Bankruptcy Code*.

The Code does not contain similar provisions with regard to the property of the solvent spouse, as does the South African *Insolvency Act*.<sup>117</sup> The property interests of the non-debtor spouse do not form part of the bankrupt estate and are therefore protected.<sup>118</sup> However, if the property is under the management and control of both spouses and one of them files for bankruptcy, the property forms part of the bankruptcy estate.<sup>119</sup> Nevertheless, where the property is exclusively controlled and managed by the non-debtor spouse or is utilised to pay the debts of that spouse only, it does not fall into the debtor's bankrupt estate.<sup>120</sup> Thus, the non-debtor spouse in the United States of America appears to be better protected in the event of the bankruptcy of his debtor spouse than the solvent spouse in South Africa, whose assets vest in the insolvent estate.

#### **4.1 Life insurance proceeds where the bankrupt debtor is the beneficiary**

When the bankrupt debtor is the beneficiary of an unmatured life insurance policy, where he is not the owner of the policy, he only has an inchoate expectation under that life policy.<sup>121</sup> Consequently, his rights do not fall into his bankrupt estate.<sup>122</sup> This is because the owner of an unmatured policy can still change the beneficiaries.<sup>123</sup> Therefore, the bankrupt debtor is not entitled to claim it yet. However, if the bankrupt is the beneficiary of a matured life insurance policy or death benefit and such a benefit is acquired within 180 days after the filing date and if that interest would have been the interest of the bankrupt before filing, it will fall into the bankrupt estate.<sup>124</sup> Thus, the money the bankrupt debtor receives as a benefit from a life insurance policy within 180 days of filing falls into the bankrupt estate.<sup>125</sup>

The critical date to the calculation of the 180 days is the date of the life insured's death as it is the date upon which the debtor acquires the right to receive the benefit.<sup>126</sup> The implication is that if the debtor acquires the property after 180 days from the date of filing, the property does not fall into the bankrupt estate.

---

<sup>117</sup> The Code does not have an equivalent of s 21 of the *Insolvency Act*.

<sup>118</sup> Ferriell and Janger *Understanding Bankruptcy* 196.

<sup>119</sup> Section 541(a)(2) of the Code.

<sup>120</sup> Ferriell and Janger *Understanding Bankruptcy* 198.

<sup>121</sup> *Wornick v Gaffney* 544 F 3d 486 (2<sup>nd</sup> Cir 2008) 492 (hereafter *Wornick v Gaffney*).

<sup>122</sup> *Wornick v Gaffney* 492.

<sup>123</sup> *In re Greenberg* 271 F 258 (2<sup>nd</sup> Cir 1921) 259 (hereafter *In re Greenberg*); Ferriell and Janger *Understanding Bankruptcy* 195.

<sup>124</sup> Section 541(a)(5)(C) of the *Bankruptcy Code*.

<sup>125</sup> Ferriell and Janger *Understanding Bankruptcy* 200.

<sup>126</sup> Ferriell and Janger *Understanding Bankruptcy* 201.

The Code does not specify the life insured as long as the beneficiary is the bankrupt debtor. For example, in *In re Woodson*<sup>127</sup> the court held that the life insurance proceeds that accrued to the debtor within 180 days of filing from the death of his wife fell into the bankrupt estate. The situation is different in South Africa, where the proceeds that are protected are from a life insurance policy where the debtor or his spouse is the life insured and the debtor is the owner of the policy. However, where the benefit accrues to the debtor after the 180 days and where the debtor has successfully exempted it, the situation is the same as in South Africa, at least in the case of Chapter 7 petitions, in that the benefit does not fall into the bankrupt estate and is not available to creditors.

In Chapter 13 cases the Code<sup>128</sup> expands the definition of the bankrupt estate to include all property of the kind specified in section 541 that the debtor acquires after the commencement of the case but before the case is closed, dismissed or converted under Chapters 7, 11 or 12.<sup>129</sup> Under Chapter 13 amounts of money that are acquired after filing are important to execute a reorganisation plan.<sup>130</sup> Therefore, in this instance the 180-day rule does not apply and thus it does not matter when the life insurance benefit was acquired after filing because all the property acquired after filing forms part of the bankrupt estate.<sup>131</sup>

#### **4.2 Life insurance policies where the debtor is the owner**

When the debtor is the owner of an unmaturing life policy, irrespective of whether the beneficiary is the bankrupt or a third party, the policy forms part of the bankrupt estate. The trustee who steps into the shoes of the bankrupt then acquires the power of appointment, in which case he has the right to change the beneficiaries because it is an inchoate expectation.<sup>132</sup> At this stage the beneficiary does not have a vested interest as the insured has an unfettered right to change the beneficiary at any time.<sup>133</sup> If the trustee elects to change the beneficiary from the third party back to the bankrupt debtor, the benefit will fall into the estate to benefit creditors unless that particular state exempts the benefit.<sup>134</sup> The effect of the exemption is that the benefit will be placed beyond the reach of the creditors.

---

<sup>127</sup> *In re Woodson* 839 F 2d 610 (9<sup>th</sup> Cir 1988), the debtor filed for bankruptcy a few days after the death of his wife and sought to exempt the insurance proceeds from his bankrupt estate.

<sup>128</sup> Section 1306(a)(1) of the *Bankruptcy Code*.

<sup>129</sup> Section 1306(a)(1) of the *Bankruptcy Code*.

<sup>130</sup> Ferriell and Janger *Understanding Bankruptcy* 225.

<sup>131</sup> See generally *Carroll v Logan* 735 F 3d 147 (4<sup>th</sup> Cir 2013) 148; *In Matter of Murdock* 547 BR 475 (Bankr SD G. 2015) 480.

<sup>132</sup> *Wornick v Gaffney* 490.

<sup>133</sup> *In re Greenberg* 261.

<sup>134</sup> Ferriell and Janger *Understanding Bankruptcy* 200.

This is the same as the South African *stipulatio alteri*, where third parties have only a "spes" that when the policy matures they can accept the benefit. However, before it matures they do not have legal rights because the trustee can always change the beneficiary since he steps into the shoes of the insolvent. Thus, a third party is not protected if the policy has not matured, because as in South Africa it is only a "spes" that in the future the third party will acquire a legal right. Consequently, since the right has not materialised, it is only an expectation.<sup>135</sup> The only difference is that in the United States of America the bankrupt debtor is allowed to exempt the beneficiary from the bankrupt estate in terms of section 522 of the Code.

Therefore, although an unmaturing policy forms part of a bankrupt estate, the debtor is allowed to exempt it from the estate in terms of section 522 of the Code.<sup>136</sup> Section 522 gives the bankrupt debtor the right to either use federal exemptions or state exemptions in this regard. However, section 522(b)(1) read with section 522(b)(2) may limit this election where a state has enacted legislation that prohibits the use of federal exemptions.<sup>137</sup> Whichever exemption is utilised by the debtor, the property will not fall into the bankrupt estate.

State law exemptions are largely similar, with a few states being notable for being creditor-friendly or debtor-friendly.<sup>138</sup> In such states the property that the debtor claims as exempt will not form part of the bankruptcy estate unless an interested party objects.<sup>139</sup> For instance, in the state of Mississippi all life insurance proceeds that accrue to the beneficiary are exempted by section 85-3-11 of the *Mississippi Code* of 1972.<sup>140</sup> Section 85-3-11 provides that life insurance proceeds including cash surrender and loan values up to \$50,000 are payable to the named beneficiaries free from the debts of the person whose life was insured even though the life insured paid the premiums.<sup>141</sup> The exemption does not apply to the portion of the benefit that exceeds \$50,000 as a result of premiums paid or other payments within 12 months of an issuance of a writ of seizure, attachment, garnishment or other process or the filing of bankruptcy proceedings.<sup>142</sup>

---

<sup>135</sup> Ferriell and Janger *Understanding Bankruptcy* 195.

<sup>136</sup> Section 522(d)(7) of the *Bankruptcy Code*, which relates to an unmaturing life insurance contract owned by the debtor, other than a credit life insurance contract. The federal exemptions allow a debtor to exempt up to \$12,625 (R181 619,97) of the cash value of a whole life insurance policy.

<sup>137</sup> Section 522(d)(7) of the *Bankruptcy Code*.

<sup>138</sup> Ferriell and Janger *Understanding Bankruptcy* 391.

<sup>139</sup> Section 522(l) of the *Bankruptcy Code*.

<sup>140</sup> Section 85-3-11 of the *Mississippi Code* of 1972, Annotated (the *Mississippi Code*).

<sup>141</sup> Section 85-3-11 of the *Mississippi Code*.

<sup>142</sup> Section 85-3-11 of the *Mississippi Code*.

The exemptions protect the proceeds from the deceased's debts but not from the beneficiary's bankrupt estate.<sup>143</sup> If the life insured dies whilst bankrupt, the proceeds of the life insurance policy will go straight to the beneficiary and only the amount that exceeds \$50,000 will be available to creditors. This is comparable to the South African situation where a third party is a beneficiary and has accepted the benefit. The proceeds of the life insurance will not form part of the bankrupt estate but will be paid to the beneficiary. The only difference is that under the *Mississippi Code* the beneficiary is entitled to claim the first \$50,000 of the proceeds although, before the amendment of section 63 of the LTIA, only R50 000 of the insurance benefit payable to the insolvent was excluded from the insolvent estate. In this respect, under both the *Mississippi Code* and the old section 63, the benefit was protected up to a certain amount and the surplus was available to the creditors. However, after the amendment of section 63 the whole benefit payable to the insolvent is protected, differentiating it from section 85-3-11 of the *Mississippi Code*.

Section 85-3-11(2)(b) of the *Mississippi Code* provides that any premiums paid with the intent to defraud creditors shall inure to the benefit of the creditors.<sup>144</sup> This provision is similar to section 63(4) of the South African LTIA, which provides for the loss of the protection of the proceeds if the policy is taken to defraud creditors.<sup>145</sup> The only difference is that under the LTIA the whole benefit accrues to the insolvent estate and under the *Mississippi Code* only the premiums paid with interests are payable to the creditors.

Generally in the United States of America when the debtor files a petition the right he has under a life insurance policy to surrender the policy for cash also vests in the estate. In *Wornick v Gaffney* the court held that section 3212 of the *New York Insurance Law*<sup>146</sup> exempted the cash surrender value of a policy where the life insured is the spouse of the beneficiary because the beneficiary owns no administrative interest.<sup>147</sup> Under South African law third parties will also not acquire rights under an unmaturing insurance policy because at that stage they only have an expectation, a "*spes*", to acquire the right once they accept the benefit.

## 5 Conclusion

The exclusion of the proceeds of life and disability insurance from the insolvent estate is intended to protect certain assets to benefit the insolvent

---

<sup>143</sup> *In re Lush* 544 BR 575 (Bankr ND Miss 2015) 586.

<sup>144</sup> Section 85-3-11(2)(b) of the *Mississippi Code*.

<sup>145</sup> Section 63(4) of the LTIA.

<sup>146</sup> Section 3212 of the *New York Insurance Law* (ch 28 of *McKinney's Consolidated Laws of New York Annotated*, 1984).

<sup>147</sup> *Wornick v Gaffney* 490, 492.

and certain third parties. Where the insolvent is concerned it appears to continue to do so in South Africa, in the United States of America and in England and Wales. However, where third parties are concerned the positions in all three countries differ.

As indicated, in South Africa the proceeds of life and disability insurance where the insolvent is the beneficiary, and his solvent spouse is the life insured, are excluded from the insolvent estate. The position is the same in England and Wales, where the proceeds of life and ill health insurance where the bankrupt is the beneficiary are also excluded from the bankrupt estate in terms of section 11 of the MWPA. In the United States of America the benefits are excluded only if they accrue to the insolvent after 180 days from the date of filing the petition in the case of Chapter 7. Where the debtor files a Chapter 13 petition the benefits fall into the insolvent estate. Further, the *Bankruptcy Code* does not specify if the debtor is the life insured, only that he is the beneficiary of a life insurance policy.

Where the beneficiary to the proceeds of life or disability insurance is a third party, in a South African insolvent estate section 63 of the LTIA does not apply, but a contract for the benefit of that third party is created. In terms of this contract, the proceeds of the life and disability insurance are paid directly to the third party without vesting in the trustee of the insolvent estate.

However, where the third party is a solvent spouse the contract for the benefit of a third party is of no help as the assets of the solvent spouse still vest in the trustee of the insolvent estate. As previously suggested, the vesting of the assets of the solvent spouse may be prevented by the inclusion in the insolvency legislation of a provision excluding these assets. Although this would mean that the courts would have to reconsider the *Harksen v Lane* judgment, it would nonetheless bring section 21 in line with the policy to protect the assets of third parties in the insolvent's possession.

As England and Wales, and the United States of America do not have a section 21 equivalent, they appear not to share the same problems as South Africa in this respect. As a result, the spouse of the bankrupt seems to be better protected by section 11 of the MWPA in England and Wales, which creates a trust to control the destination of the proceeds of a life policy. In the United States of America, the property of the solvent (non-debtor) spouse is expressly protected.

As indicated, however, section 11 only protects certain dependents, the spouse and children of the bankrupt. It appears that it does not cater for other third parties who might have been dependent on the bankrupt and whom the bankrupt might have intended to benefit from his insurance policy. If this is true and some other legislation does not protect these third parties' interests, they appear to be disadvantaged.

Furthermore, the distinction between married and unmarried persons in section 11 seems unfair to the latter group. A provision protecting the insurance benefits of unmarried people, especially where children are beneficiaries, should be considered in England and Wales.

Although South Africa and England and Wales both make some provision for the protection of the assets of third parties that are in the insolvent's possession during his sequestration, it is clear that the interests of third parties in the form of the solvent spouse (in South Africa), and dependants that are not a child or a spouse (in England and Wales) are not a priority. In both countries the priority is given to the interests of the insolvent debtor. Although this seems to be following the international trend of moving away from a creditor-friendly approach to insolvency to a more debtor-friendly approach, the interests of other parties that are indirectly involved in the sequestration of the debtor should also be taken into account and protected.

The American bankruptcy policy remains in the lead in the treatment of life insurance policy benefits under Chapter 7 bankruptcy proceedings and the balancing of the interests of all stakeholders affected by the proceedings. When the beneficiary is the bankrupt, the 180-days rule applies and the life insurance benefit forms part of the estate, unless if the benefit accrues after the 180 days, then it becomes part of the estate. However, if the owner of the policy is bankrupt and the nominated beneficiary is a third party, the benefit is paid to such a third-party beneficiary directly, irrespective of who is the third party.

It is hoped that as there is currently a proliferation of case law pointing to a shift towards an insolvency process that is more friendly to the needs of society as a whole, and not only the interest of creditors and debtors in South Africa, the need to protect the interest of the solvent spouse (as a member of society) where his insurance policy benefits are concerned will be answered.

## **Bibliography**

### **Literature**

Barrand 1910 *Journal of the Institute of Actuaries*

Barrand AR "Legal Notes on *Tapster v Ward*" 1910 *Journal of the Institute of Actuaries* 87-99

Bertelsmann *et al Mars: Law of Insolvency*

Bertelsman E *et al Mars: The Law of Insolvency in South Africa* 10<sup>th</sup> ed (Juta Cape Town 2019)

Birds *Modern Insurance Law*

Birds J *Modern Insurance Law* 9<sup>th</sup> ed (Sweet and Maxwell London 2013)



Boraine and Evans *Law of Insolvency*

Boraine A and Evans R *The Law of Insolvency and the Bill of Rights Compendium* (LexisNexis Butterworths Durban last updated October 2014)

Clarke *Law of Insurance Contracts*

Clarke MA *The Law of Insurance Contracts* 6<sup>th</sup> ed (Informa London 2009)

Cork Review Committee *Review Committee Report*

Cork Review Committee *Review Committee Report on Insolvency Law and Practice* (HMSO London 1982)

Elping, Brennan and Jonhson 2012 *Norton Journal of Bankruptcy Law and Practice*

Elping RL, Brennan KA and Jonhson B "Intersections of Bankruptcy Law and Insurance Coverage Litigation" 2012 *Norton Journal of Bankruptcy Law and Practice* 103-126

Evans *Critical Analysis of Problem Areas*

Evans RG *A Critical Analysis of Problem Areas in Respect of Assets of Insolvent Estates of Individuals* (LLD-thesis University of Pretoria 2008)

Evans 2011 *PELJ*

Evans RG "Legislative Exclusions or Exemptions of Property from the Insolvent Estate" 2011 *PELJ* 39-56

Evans and Boraine 2005 *De Jure*

Evans R and Boraine A "Considerations Regarding a Policy for the Treatment of Certain Beneficiaries of Life Insurance Policies in the Law of Insolvency" 2005 *De Jure* 266-294

Ferriell and Janger *Understanding Bankruptcy*

Ferriell J and Janger EJ *Understanding Bankruptcy* 4<sup>th</sup> ed (Carolina Academic Press Durham 2019)

Fletcher *Law of Insolvency*

Fletcher IF *The Law of Insolvency* 5<sup>th</sup> ed (Sweet and Maxwell London 2017)

Floyd, Brumby and Knight *Personal Insolvency*

Floyd R, Brumby F and Knight S *Personal Insolvency: A Practical Guide* 4<sup>th</sup> ed (Sweet and Maxwell London 2012)

Loubser 1997 *SA Merc LJ*

Loubser A "Ensuring Advantage to Everyone in a Modern South African Insolvency Law" 1997 *SA Merc LJ* 325-333

Mabe and Mbiriri 2022 *PELJ*

Mabe Z and Mbiriri E "The Payout of a Life Insurance Policy into an Unrehabilitated Insolvent's Estate: *Malcolm Wentzel v Discovery Life*

*Limited: In Re Botha v Wentzel* (1001/19) [2020] ZASCA 121 (2 October 2020)" 2022 *PELJ* 1-27

Mabe 2015 *THRHR*

Mabe Z "Life and Other Insurance Policy Benefits and the Property of an Insolvent Person" 2015 *THRHR* 237-247

Meskin *et al Insolvency Law*

Meskin PM *et al Insolvency Law and its Operation in Winding-Up* (LexisNexis Butterworths Durban last updated November 2022)

Reinecke, Van Niekerk and Nienaber *South African Insurance Law*

Reinecke MFB, Van Niekerk JP and Nienaber PM *South African Insurance Law* (LexisNexis Butterworths Durban 2013)

Roestoff and Boraine 2022 *THRHR*

Roestoff M and Boraine A "Is Genomineerde Begunstigde Ingevolge Lewensversekeringspolis Uitsluit van Beskerming teen Insolvensie?" 2022 *THRHR* 408-421

Sharrock, Van der Linde and Smith *Hockly's Insolvency Law*

Sharrock J, Van der Linde K and Smith A *Hockly's Insolvency Law* 9<sup>th</sup> ed (Juta Cape Town 2012)

Smith, Van der Linde and Calitz *Hockly's Law of Insolvency*

Smith A, Van der Linde K and Calitz J *Hockly's Law of Insolvency: Winding-Up and Business Rescue* 10<sup>th</sup> ed (Juta Cape Town 2022)

World Bank *Report on the Treatment of the Insolvency of Natural Persons*

World Bank Working Group on the Treatment of the Insolvency of Natural Persons *Report on the Treatment of the Insolvency of Natural Persons* (World Bank Washington DC 2013)

## **Case law**

### **South Africa**

*Ex parte Kroese* 2015 1 SA 405 (NWM)

*Harksen v Lane* 1998 1 SA 300 (CC)

*Wentzel v Discovery Life Limited: In Re Botha v Wentzel* 2021 6 SA 437 (SCA)

*Oshry v Feldman* 2010 6 SA 19 (SCA)

*Pieterse v Shroobree, Shroobree Love* 2005 1 SA 309 (SCA)

*Shroobree v Van Rooyen* 2004 1 SA 226 (SE)

*South African Restructuring and Insolvency Practitioners Association v Minister of Justice and Constitutional Development* 2015 2 SA 430 (WCC)

*Warricker v Liberty Life Association of Africa Ltd* 2004 3 SA 445 (SE)

*Wessels v De Jager* 2000 4 SA 924 (SCA)

### **United Kingdom**

*Tapster v Ward* (1909) 101 LT 503

### **United States of America**

*Carroll v Logan* 735 F 3d 147 (4<sup>th</sup> Cir 2013)

*In Matter of Murdock* 547 BR 475 (Bankr SD Ga 2015)

*In re Greenberg* 271 F 258 (2<sup>nd</sup> Cir 1921)

*In re Lush* 544 BR 575 (Bankr ND Miss 2015)

*In re Supreme Beef Processors, Inc* 468 F 3d 248 (5<sup>th</sup> Cir 2006)

*In re Woodson* 839 F 2d 610 (9<sup>th</sup> Cir 1988)

*Wornick v Gaffney* 544 F 3d 486 (2<sup>nd</sup> Cir 2008)

### **Legislation**

#### **South Africa**

*Financial Services Laws General Amendment Act* 45 of 2013

*Long Term Insurance Act* 52 of 1998

*Insolvency Act* 24 of 1936

*Insurance Act* 27 of 1943

*Insurance Act* 18 of 2017

#### **United Kingdom**

*Enterprise Act*, 2002

*Insolvency Act*, 1986

*Insolvency Act*, 2000

*Law Reform (Married Women and Tortfeasors) Act*, 1935

*Married Woman's Property Act*, 1882

*Statute Law (Repeals) Act*, 1969

**United States of America**

*Bankruptcy Code (Bankruptcy Reform Act of 1978)*

*Mississippi Code of 1972, Annotated*

*New York Insurance Law (ch 28 of the McKinney's Consolidated Laws of New York, 1984)*

**Internet sources**

Insolvency Service date unknown <https://bit.ly/3hOBcdG>

Insolvency Service date unknown *Guide to Bankruptcy*  
<https://bit.ly/3hOBcdG> accessed 14 June 2023

Insolvency Service 2014 <https://bit.ly/36Y9Co5>

Insolvency Service 2014 *Technical Manual* <https://bit.ly/36Y9Co5> accessed  
14 June 2023

**List of Abbreviations**

IA 1986

Insolvency Act, 1986

LTIA

Long Term Insurance Act 52 of 1998

MWPA

Married Women's Property Act, 1882

PELJ

Potchefstroom Electronic Law Journal

SA Merc LJ

South African Mercantile Law Journal

THRHR

Tydskrif vir Hedendaagse Romeins-  
Hollandse Reg