

NONPRECEDENTIAL DISPOSITION

To be cited only in accordance with FED. R. APP. P. 32.1

United States Court of Appeals**For the Seventh Circuit****Chicago, Illinois 60604**

Argued November 18, 2022

Decided January 25, 2023

BeforeMICHAEL B. BRENNAN, *Circuit Judge*THOMAS L. KIRSCH II, *Circuit Judge*JOHN Z. LEE, *Circuit Judge*

No. 22-1685

IN RE: DAVID R. FACCONO,
*Debtor-Appellant.*Appeal from the United States
Bankruptcy Court for the Northern
District of Illinois, Western Division.

No. 20-81450

Thomas M. Lynch,
*Bankruptcy Judge.***ORDER**

Debtor David Faccone filed for bankruptcy under Chapter 7 of the Bankruptcy Code and sought to exempt from his estate, under Illinois law, an annuity that he had purchased for himself and designated his wife to inherit upon his death. The bankruptcy court denied the exemption. We affirm.

Background

Faccone purchased a product from a financial-services company. The contract referred to the product as an “annuity” policy. (The bankruptcy court questioned whether the policy is in fact an “annuity,” but we will refer to it as one for simplicity’s sake.) Under this contract, Faccone deposited a lump sum into the annuity, which the company then invested in mutual funds. The contract lists Faccone both as the “owner” (the person whose funds are being invested) and the “annuitant” (the recipient of payments). After a certain number of years, the annuity will “mature,” and Faccone will receive guaranteed payments for a fixed number of years or for life. Faccone has the option to withdraw money from the annuity before it matures, but he would have to pay a penalty for doing so. The amount of this early withdrawal penalty decreases over time. Notably, any payments from the account—before or after maturation—go only to Faccone, as both the owner and annuitant. Faccone listed his wife as the “beneficiary” of the annuity. If Faccone dies before the annuity is depleted, his wife will receive the balance. But Faccone has the unrestricted right to change the beneficiary at any time.

Faccone filed for Chapter 7 bankruptcy in 2020. After two amendments to his schedules, Faccone listed the annuity—which then had a value of over \$250,000—as exempt from the bankruptcy estate under 735 ILL. COMP. STAT. 5/12-1001(f), which applies to certain types of “annuity contracts.” The bankruptcy trustee and Doris Geraci, a creditor, objected. (For simplicity, we refer to both objectors as “the trustee.”)

The bankruptcy court sustained the objections and concluded that the annuity was not exempt under § 12-1001(f). The court explained that the statute exempted only “agreements that are . . . essentially insurance contracts.” *In re Faccone*, 636 B.R. 777, 784 (Bankr. N.D. Ill. 2022). The policy here, the court continued, was more like a retirement investment account—and thus was not even an annuity, let alone an insurance policy. *Id.* at 786–87. Alternatively, the court reasoned that the annuity failed to meet another of the statute’s necessary conditions: it was not “payable to” Faccone’s wife. True, when Faccone died, the account would pass to his wife. He could, however, withdraw the principal at any time, and he is expected to be the payee, pre- or post-maturation. Thus, the court reasoned, the fact that the annuity may be “payable to” his wife at a future time was “incidental” and insufficient to exempt the account from the bankruptcy estate. *Id.* at 787.

Faccone appealed to the district court. Ultimately, the district court remanded the case to the bankruptcy court, and the bankruptcy court certified a direct appeal to

us pursuant to 28 U.S.C. § 158(d)(2)(A) and Federal Rule of Bankruptcy Procedure 8006. We accepted the direct appeal.

Analysis

This case requires us to interpret an Illinois statute. Illinois debtors, such as Faccone, can claim only the bankruptcy exemptions that Illinois law allows. *In re Hernandez*, 918 F.3d 563, 566–67 (7th Cir. 2019) (citing 11 U.S.C. § 522(b) and 735 ILL. COMP. STAT. 5/12-1201). Faccone contends 735 ILL. COMP. STAT. 5/12-1001(f) exempts his annuity. That subsection applies to

[a]ll proceeds payable because of the death of the insured and the aggregate net cash value of any or all life insurance and endowment policies and annuity contracts payable to a wife or husband of the insured, or to a child, parent, or other person dependent upon the insured, or to a revocable or irrevocable trust which names the wife or husband of the insured or which names a child, parent, or other person dependent upon the insured as the primary beneficiary of the trust, whether the power to change the beneficiary is reserved to the insured or not and whether the insured or the insured's estate is a contingent beneficiary or not.

When sitting in bankruptcy and interpreting an Illinois statute, we apply Illinois rules of statutory construction. *See Hernandez*, 918 F.3d at 566; *see also Jafari v. Wynn Las Vegas, LLC (In re Jafari)*, 569 F.3d 644, 648 (7th Cir. 2009) (“[S]tate law governs the validity of most property rights, and . . . bankruptcy courts must apply the relevant state law.”). Because the Supreme Court of Illinois does not have a relevant ruling interpreting the exemption Faccone seeks, we look to related precedent from Illinois courts to determine how the state's highest court would decide this issue. *Cage v. Harper*, 42 F.4th 734, 739–40 (7th Cir. 2022). We review the bankruptcy court's decision *de novo*. *See Hernandez*, 918 F.3d at 566.

Faccone argues that he is entitled to the exemption under § 12-1001(f) because any proceeds of the annuity are “payable to” his wife, the beneficiary of the annuity, upon his death. We disagree for two reasons.

First, we agree with the bankruptcy court that Faccone's annuity is not the sort of financial product contemplated by the exemption. Read as a whole, § 12-1001(f) exempts certain insurance policies and other similar agreements that provide monetary benefits to dependents of the insured policyholder. This reading is consistent with the

view of other Illinois bankruptcy courts that have held that a financial instrument does not fall within the exemption when it provides a death benefit that is “merely incidental” to the primary purpose of the instrument. *See, e.g., In re Lesak*, No. 11 B 34825, 2012 WL 1029313, at *3 (Bankr. N.D. Ill. Mar. 26, 2012) (holding annuity created as part of structured litigation settlement was not subject to the § 12-1001(f) exemption, even though it provided a death benefit to the wife of the annuitant, because the “fundamental purpose of the annuity” was compensation for underlying litigation); *In re Bowen*, 458 B.R. 918, 922 (Bankr. C.D. Ill. 2011) (holding the exemption did not apply to disability insurance policies that had an “incidental” life-insurance component).

Faccone’s annuity is such an instrument. Faccone controls the annuity, has the sole right to payments from the annuity during his lifetime, and is entitled to withdraw his investment, in whole or in part. While Faccone’s wife is presently entitled to anything that remains of the annuity after Faccone dies, he can change the beneficiary or withdraw the funds at any time. We thus agree with the bankruptcy court that Faccone’s wife’s mere potential right to some portion of the annuity, at some indeterminant point in the future, does not render the annuity’s proceeds presently “payable to” her. Therefore, the life-insurance feature of the annuity is “incidental” to its primary function of providing Faccone with a recurring payment.

Second, we conclude that Faccone’s reading runs counter to the purpose of Illinois’s bankruptcy exemptions: to provide for the basic needs of debtors and their dependents during periods of financial difficulty. *Thomas v. Ill. Dep’t of Healthcare & Fam. Servs.*, 48 N.E.3d 721, 731 (Ill. App. Ct. 2016) (quoting *In re Marriage of Logston*, 469 N.E.2d 167, 172–73 (Ill. 1984)); *In re Belcher*, 551 F.3d 688, 690 (7th Cir. 2008). Although the money is slated to go to Faccone’s wife when he dies, nothing stops Faccone from withdrawing the annuity’s entire value after the bankruptcy estate closes. (Although the annuity has early withdrawal fees, Faccone can still access the money, and the fees eventually reduce to \$0.) Thus, as the trustee points out, Faccone’s reading would allow a debtor to exempt money beyond financial necessity—even hundreds of thousands of dollars, as in Faccone’s annuity—by naming a spouse to inherit an annuity that has no or minimal early withdrawal penalties. Even good-faith investments in an annuity like Faccone’s would result in windfalls under his proposed reading of the exemption. In a related scenario, the Supreme Court said that allowing a debtor to exempt an inherited IRA would run counter to bankruptcy policy because the holder could access the funds at any time. *Clark v. Rameker*, 573 U.S. 122, 128–30 (2014). Allowing debtors to exempt financial products that they can then immediately cash out would turn their “fresh start into a free pass.” *Id.* at 130 (cleaned up).

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For these reasons, the judgment of the bankruptcy court is affirmed.