AALU Newswire
Leadership for Advanced Life Underwriting®
An AALU Washington Report

Friday, 13 November 2015 WRN# 15.11.10

The *WRNewswire* is created exclusively for AALU Members by insurance experts led by Steve Leimberg, Lawrence Brody and Linas Sudzius. ***WRNewswire*** **#15.11.10 was written by Linas Sudzius of Advanced Underwriting Consultants.**

The AALU *WRNewswire* and *WRMarketplace* are published by the Association for Advanced Life Underwriting® as part of the Essential Wisdom Series, the trusted source of actionable technical and marketplace knowledge for AALU members—the nation's most advanced life insurance professionals.

TOPIC: Confusion Over Policy Replacement Leads to Litigation

CITATION: *Beasley v. Sutton*, No. 2014-CA-00453-COA (Ct. App. MS Oct 27, 2015).

SUMMARY: Dr. Trey Sutton was the minority shareholder with Dr. Christopher Spraberry, the majority owner of a dental practice. The parties entered into a buy-sell agreement with respect to the practice in 2006, and Sutton later owned, and was beneficiary of, $2 million of coverage on Spraberry's life to fund Sutton's obligation under the buy-sell agreement.

In late 2008, the parties worked together to increase the amount of buy-sell coverage, allegedly agreeing to $3 million of new funding to replace the old policy.

The existing $2 million of buy-sell life insurance Sutton owned on Spraberry was never canceled. Just after the new policy purchase, $1.7

million of personal coverage on Spraberry's life was allowed to lapse. After Spraberry's subsequent death, Sutton collected $5 million of death proceeds, $2,000,000 from the original policy and $3,000,000 from the new policy. Spraberry's heir, his surviving sister Audrey Beasley, brought suit to collect $700,000 of death proceeds under a policy that she alleged lapsed by mistake during the replacement process.

The trial court granted summary judgment to Sutton, and Audrey appealed. The appeals court reversed in part, ordering the case to trial on the facts.

RELEVANCE: Clients often have multiple life insurance policies intended for more than one purpose. This kind of situation can occur where a client owns a closely held business and seeks to fund a death-time buyout, but also has family needs that are protected with personal coverage.

When multiple policies exist—and where the ownership of different coverages on the same life is in separate hands—any replacement of one or more of the contracts can get complicated.

Here, the insured apparently intended to replace buy-sell coverage, but ended up lapsing personal coverage by mistake instead. The minority owner of the business, who had the power to cancel the old buy-sell funding coverage, did not do so, and the insured's family felt he was unjustly enriched when he collected $5 million of death benefit rather than $3,000,000.

Professional agents who are working with clients to replace coverage should follow a checklist approach to make sure all relevant policies are properly identified, and any paperwork that needs to be signed by parties other than the insured should be properly obtained. This is especially true when the replacing agent is different from the writing agent.

In this case, the lack of clarity with regard to all the parties' intentions during the replacement stage and lack of communications led to uncertainty and expensive litigation after the insured's death.

FACTS: Christopher Spraberry was a dentist and the majority shareholder of Spraberry Dental Clinic in Gulfport, Mississippi.

In 2006, Trey Sutton entered into dental practice at the clinic with Spraberry immediately upon Trey receiving his license. Sutton had a twenty-five percent ownership interest in the clinic, while Spraberry owned the rest.

In 2008, an agent assisted Spraberry in obtaining several life insurance policies from The Guardian Life Insurance Company. In February 2008, the agent also helped Spraberry convert an existing $700,000 Guardian term policy to a whole-life policy with Spraberry's sister Audrey as the primary beneficiary.

On April 15, 2008, Guardian issued two other separate policies: a term-life policy in the amount of $2 million, with Sutton as the sole owner and beneficiary; and a whole-life policy in the amount of $1 million, owned by Spraberry, with Spraberry's wife and child as the beneficiaries.

The premium for the $2 million policy was paid for by the clinic, and this policy was intended to fund a buy-sell agreement executed between Spraberry and Sutton to preserve the dental practice in the event of Spraberry's untimely passing.

In November 2008, Spraberry discussed with another insurance agent the purchase of some other life insurance. They decided that $3 million of coverage would be sufficient for the purchase of the clinic in the event either dentist untimely passed away. The agent's understanding was that a

new $3 million policy on his life would replace any other policies used to fund the buy-sell agreement.

After the discussion, a $3 million whole-life insurance policy on Spraberry's life issued by Phoenix Life Insurance Company (Phoenix) was obtained. Phoenix sent a replacement notice to Guardian, listing the policy numbers for the $1 million policy (owned by Spraberry) and $2 million policy (owned by Sutton), and stating it had received an application for new insurance, which indicated an intention to replace these existing Guardian policies.

Spraberry subsequently instructed his sister Audrey to cancel the $1 million and $2 million Guardian policies because the $3 million Phoenix policy was replacing them. Beasley listed two policy numbers in a cancellation letter, but instead of the number for the $2 million policy, she mistakenly listed the number for the $700,000 policy. Beasley faxed the cancellation letter to the Guardian agent on Spraberry's behalf, but Guardian never received the request to cancel the two policies. Two weeks after receipt of the letter, the Guardian agent realized the policy numbers did not match the coverage amounts.

A Guardian representative subsequently noted Spraberry did not have the legal authority to cancel the $2 million policy, since Sutton was its sole owner.

In December 2008, Spraberry executed two stop-payment orders to terminate automatic drafts for the premiums on the two Guardian policies in the letter: the $1 million and $700,000 policies.

The Guardian agent tried to call Spraberry beginning in December 2008 about the possible mix-up in policy numbers, leaving numerous voice-mail messages in order to talk about the December 8 notice of cancellation. Guardian also sent several lapse notices to Spraberry, requesting he reinstate the policies.

The termination date of the $700,000 policy for nonpayment of premiums was December 20, 2008. Both the $700,000 and $1 million policies lapsed for failure to pay the premiums.

Spraberry died in an accident at his home on May 16, 2009. Beasley claimed she confronted Sutton and told him that Spraberry intended to cancel the $2 million policy in favor of the $3 million policy, and not the $700,000 that named her as a beneficiary. Beasley testified that Sutton promised to "make it right." Beasley stated that after Spraberry died, when it came to light that the $700,000 policy no longer existed, Dr. Sutton promised that Beasley was going to get the money.

On December 10, 2009, Sutton paid Beasley $100,000. Sutton claimed this payment was a gift to Beasley; Beasley claimed it was partial payment for the $700,000 policy.

On December 20, 2010, Beasley claimed that she discussed the life insurance situation with Sutton and his payment of the remaining $600,000, and he further discussed his concern about the best way to pay her and avoid tax consequences. Beasley and her husband soon purchased a home, allegedly in reliance on Sutton's promise to pay the remaining $600,000.

In October 2011, Beasley filed a complaint against Sutton and others in state court seeking to recover the amount of $700,000. She raised three causes of action relating to Sutton: unjust enrichment, promissory estoppel, and equitable estoppel. Following completion of discovery, Sutton filed a motion for summary judgment. The trial court granted summary judgment to Sutton on all of Beasley's claims. Beasley appealed.

The appellate court ruled that a jury could find that Sutton had promised to give Beasley $700,000 of the $3 million death benefit he received, and

that Beasley had relied on that promise to her detriment. If proven, those facts would create a valid claim under Mississippi law. The appeals court sent back the case to proceed at the trial court.

DISCLAIMER

This information is intended solely for information and education and is not intended for use as legal or tax advice. Reference herein to any specific tax or other planning strategy, process, product or service does not constitute promotion, endorsement or recommendation by AALU. Persons should consult with their own legal or tax advisors for specific legal or tax advice.