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**TOPIC: Case Alleging Negligence Against Insurer That Allowed Change of Beneficiary to Person with No Insurable Interest Is Allowed to Continue**

**CITES:** [Ex Parte Liberty National Life Insurance Company](#), No. 1140612, 2016 WL 1171505 (S.Ct.AL March 25, 2016); [Life Insurance Co. v. Weldon](#), 267 Ala. 171, 100 So.2d 696 (1957); [Ala.Code 1975, § 27-14-3](#).

**SUMMARY:** This is an insurable interest case of first impression that went all the way to the Alabama Supreme Court. This case presented the following question:

Can a policy issued validly and in good faith be modified to substitute a beneficiary, regardless of whether or not that beneficiary has an insurable interest in the life of the insured (assuming neither state law or the policy itself provide otherwise)?

Here, a negligence suit was brought by the personal representative of a decedent’s estate against an insurer. The plaintiff charged that the insurer was negligent in failing to determine that, at the time stepmother requested that she personally be named beneficiary, she had no insurable interest in the life of the decedent. The complaint further alleged that stepmother had been unjustly enriched in amount equal to the insurance proceeds that had been paid to her at the insured’s death.

The lowest court to hear this case dismissed the claim. Then, an Alabama state appeals court reinstated that case. We wrote about that decision in *WRNewswire* 14.12.29.

Now, the Supreme Court of Alabama has held that the insurable-interest for life insurance must exist *only* at the time the contract is made (i.e., “becomes effective”). It need *not* exist at the time the insured dies. But as to the dismissal of the case, the court said, “The Court does not consider whether the plaintiff will ultimately prevail, but only whether she may possibly prevail.” So it allowed the case – and the allegation of negligence by the insurer in allowing the substitution of beneficiary - to continue.

**RELEVANCE:** This case reminds insurers, agents, and brokers to take great care with respect to insurable interest. Regardless of how this case is ultimately resolved, it contains reminders and lessons about insurable interest, how it works, its great importance, and a warning that everyone involved with life insurance must assure the appropriate parties possess insurable interest – at least at the contract’s inception.

An insurable interest is one based on the presence of a reasonable expectation of pecuniary advantage through the continued life, health, or bodily safety of another person and consequent loss by reason of his or her death or disability, or a substantial interest engendered by love and affection in the case of individuals closely related by blood or by law. Insurable interest is a principle designed to discourage speculation in human life. It does so by making wager contracts on human lives void. This public-policy principle prohibits a person from directly or indirectly insuring the life of a person in whom he or she has no insurable interest.

This case highlights my theory that there are really two insurable interest tests that must be met with respect to life insurance: First, there is the insurable interest required by insurers to meet their financial, health, and moral underwriting standards. Second, there is the insurable interest imposed and required under state law. The two tests may be similar but might also differ significantly. But *both* the insurer’s threshold tests *and* state law requirements must be met to have a valid, enforceable insurance policy.

Here are some basic tenants of insurable interest:

- Assuming a lack of fraud or deception, a person has an unlimited insurable interest in his or her own life. (The “unlimited insurable interest” concept presupposes that the policy was obtained in *good faith* and *not* for the

purpose of speculating upon the hazard of a life in which the insured has no interest; i.e, that it was not part of a pre-arranged plan to have the policy owned by a stranger).

- Courts will not permit mere strangers to speculate upon the life of one whose continued life would bring them no expectation of possible benefit or advantage.
- Third party policy owners must have an insurable interest on the life of the insured – but *only* at the time the life insurance contract becomes effective.
- Generally, the beneficiary of life insurance need not have an insurable interest in the life of the insured at the date of the insured's death. In the first article on the appeals court decision in this case, we noted how hard it would be for insurers to monitor and police this if it were otherwise.
- If a life insurance contract is held to be void because of a lack of insurable interest, the insurer has no liability under the contract but in most cases will be required to repay all premium payments (typically – but not always – without interest) to the party who paid the premiums. In some states, if there is a failure of insurable interest, the policy is valid, but will be payable to the insured's estate.

The Alabama Supreme Court decision is very interesting because it does not fully answer key questions:

- If Alabama law only requires insurable interest at policy inception, how could the carrier could still have been negligent in honoring the beneficiary change?
- What kind of duty do insurance companies have to police policy changes?

**FACTS:** Benjamin Miller (Senior) purchased a policy on the life of his son, Benjamin Jr. (Junior), in whom he presumably had an insurable interest under state law. At some point, Senior changed the beneficiary of the policy to himself. Senior died. At that point, Junior was still alive and Senior's estate owned the policy. About six months later, Junior, the insured, died.

While the insured was still alive but shortly after Senior's death, Senior's widow, Leanne Miller, was named administrator of Senior's estate. As such, she requested

that Liberty National change the beneficiary and make her—personally—the beneficiary of the proceeds of the policy on Junior’s life. Liberty National made the requested change and when Junior died, it paid the proceeds to Leanne.

Misty Barton, personal representative of Junior’s estate, sued both Liberty National and Leanne Miller, the beneficiary. The estate asserted that, because Leanne had no insurable interest in the continued life of Junior, her stepson, Leanne’s naming herself as beneficiary of the policy was ineffective and void. The estate also asserted Liberty National had been negligent in failing to determine, at the time Leanne requested that she be named beneficiary, that Leanne had no insurable interest in the life of Junior; that, as a proximate consequence of the negligence and wrongful conduct of Liberty National, Junior’s estate had been deprived of those benefits; and that Leanne’s actions had resulted in her being unjustly enriched in an amount equal to the insurance proceeds that had been paid to her by Liberty National.

The insurer countered that a validly issued policy can (unless the policy provides otherwise) be subsequently modified to name another person as beneficiary, irrespective of whether that other person has an insurable interest in the life of the insured.

The trial court granted Liberty National’s motion to dismiss.

However, the appeals court agreed to hear arguments by the insured son’s estate that Liberty National’s allowance of Leanne’s change to the beneficiary of the policy created a *wager policy*, which is void under Alabama law, thereby depriving Benjamin Jr.’s estate of the insurance proceeds to which it was entitled.

Here, the insurer, Liberty National, argued that the legislature “did not intend to require an insurable interest to exist beyond a life insurance policy’s initial issuance” and that “[a] policy of life insurance, taken out by the insured himself or by a person having an insurable interest in the life of the insured, in good faith may, unless the policy provides otherwise, be assigned to anyone as any other chose in action without regard to whether the assignee has an insurable interest in the life insured or not.”

However, the appeals court held that there is a distinction between an assignment and a change of beneficiary. “The matter of change of beneficiary and assignment of policies are two separate and distinct things. An assignment is the transfer by one of his right or interest in property to another. The power to change the beneficiary is the power to appoint.” It decided that Alabama state law merely allows a person who

has taken out an insurance policy on the life of another while he or she had an insurable interest in the insured, to still receive benefits from that policy if, at the time the loss occurs, he or she no longer has an insurable interest in the insured. But the appeals court went on to say the law does not allow for the change of a beneficiary on the policy of another when the proposed new beneficiary does not possess an insurable interest in the insured. Since Leanne did not have an insurable interest in Junior either when the policy was issued or at any later date, the appeals court held that her change of beneficiary to herself was not effective.

In essence, the appeals court stated that an insurer has a duty to use reasonable care to ascertain whether the intended *beneficiary* of the policy had an insurable interest in the life of the person to be insured - even though the original policy owner, the insured's father, presumably possessed insurable interest at the time he purchased the policy on his son's life. So the appeals court reinstated the estate's negligence claim against the insurer and remanded it for further proceedings.

The Alabama Supreme Court reversed the appeals court's judgment requiring an insurable interest to exist beyond the moment the policy becomes effective. But it concluded that the estate potentially could maintain a cause of action against Liberty National alleging negligence on its part in allowing Leanne, either as personal representative of Benjamin Sr.'s estate or individually, to substitute herself as beneficiary on the policy insuring Benjamin Jr.'s life. So the case will continue.

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