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TOPIC: Agent Did Not Clearly Exceed Scope of Authority in Selling STOLI Policy

CITATION: *Weyland v. Union Central Life Insurance Company*, 2016 WL 750433, No. G051071 (Ct. App. 4th Dist Div. 3 CA, Feb. 26, 2016).

SUMMARY: In this case against the insurer, its agent sold an insured STOLI policy with an aggregate face amount of $10 million. The agent allegedly guaranteed that the insured would "double his money" in two years. But allegedly, he did not advise the insured of any economic factors that could affect the value of his policies on the secondary market or of the risk that he may not be able to sell his policies.

As a result of insureds living longer than expected, life settlement companies changed their life expectancy factors, which, coupled with the economic downturn in 2008, the insured could not sell his policies and they subsequently lapsed.

The insurer, Union Central, filed a motion for summary judgment stating that the agent exceeded the "scope of his authority" and thus Union Central could not be held vicariously liable. The trial court granted the motion and dismissed the case, but the appeals court held that most claims should go to trial.

RELEVANCE: The key legal question was whether or not the insurer was responsible for the negligence of its agent. In order for the plaintiff to be successful, the court had to find that the agent was performing with*in* the scope of his authority.

The court emphasized that the insured has to *know* that the agent was acting outside of the scope of authority for the insurer to prevail. It stated:

> The evidence also fails to show [the insured] had notice of the limitations [the insurer] placed on [the agent's] authority to sell its life insurance policies. Nothing in the applications …completed or any of the other information he received from [the agent] or [the insurer] informed him [the insurer] prohibited [the agent] from selling any ...life insurance policy to an insured who intended to resell the policy on the secondary market.

The court found that summary judgment should not have been granted.

In light of the decision in this case, it would appear to be a best practice for insurers wishing to avoid vicarious liability for STOLI sales to ensure that their applications include a clear and affirmative statement that if an agent suggests or implies that the policy be sold in the secondary market, that this representation is beyond the agent's scope of authority. This message should be included in marketing materials and also in any phone interviews.

FACTS: An agent met with a proposed insured and outlined a proposal that the insured could double his money in two years. The idea was to purchase $10 million in coverage and then sell the policies to a life settlement company after two premiums were paid. In his marketing pitches, the agent represented that the insured could sell the policy in two years for almost $900,000, but that the policy premiums during that period would only be about $479,000.

After two years had elapsed, two major things had changed in the resale market. First, life settlement companies realized that their life expectancy tables were understating life expectancy. This meant that the settlement companies were getting much less profit, since the expected death proceeds were being paid much later than anticipated. Second was the recession of 2008, which dried up sources of capital that the life settlement companies used to purchase the life policies.

As a result, when the insured tried to sell the policies, there were no buyers. Ultimately the policies lapsed. The insured sued the agent, the insurer, and the life settlement company that the agent represented would buy his policies. The claim in

the suit was for $1.8 million, which represented the premiums paid, the loss of profit on the sale that never occurred, and punitive damages.

At trial, the insurer filed a motion for summary judgment, which was successful. On appeal, the key issue was whether the insurer could be liable for the negligent acts of its agent. When an insurer is held liable for the actions of its agent, the legal concept is called "vicarious liability." In order to prove vicarious liability for the negligence of the principal (the insurer) the plaintiff has to prove negligence first against the agent. The plaintiff asserted that the agent was negligent because he would not have bought the life insurance policies if the agent had disclosed the revisions to the life expectancy tables and the impact they had on the policies' value, or if the agent had disclosed the possibility other economic factors, such as a recession, could reduce the policies' value or prevent the insured from selling them.

A principal will be liable for an agent's negligent actions or omissions that occur during the course and within the scope of the agent's employment. This means that two separate elements have to be proven:

1. First, the agent must be performing duties for the principal at the time of the negligence.

2. Second, the negligent activity must have been within "the scope of authority" granted by the principal to the agent by contract or as a matter of law.

The insurer acknowledged it appointed the agent, however, it nonetheless contended that it could not be vicariously liable for his conduct as a matter of law because the agent exceeded the scope of his authority. The basis for the insurer's contention was that it prohibited its agents from selling life insurance policies to insureds who intend to resell the policies on the secondary market, and therefore the agent acted outside the scope of his authority when he sold policies for resale and failed to disclose the associated risks to the insured. The insurer pointed to a signed "Statement of Intent" which both the agent and the insured signed stating that they did not intend to resell the policies. The agent and the insured both knew that the opposite was true.

The court noted that under California law, vicarious liability in the insurance context occurs under a "general rule" which states "... in the absence of notice, actual or constructive, to the insured of any limitations upon such agent's authority, a general agent may bind the company by any acts, agreements or representations that are

within the ordinary scope and limits of the insurance business entrusted to him, although they are in violation of private instructions or restrictions upon his authority."

The appeals court held that the insured did not have actual or constructive notice that the proposed future sale of the policy in the secondary market was beyond the scope of the agent's authority. The insurer had clearly demonstrated that a secondary sale was prohibited, but had not proven that it was beyond the agent's scope of authority. The appeals court said an agent's authority ".. included not only selling the policies, but also describing the policies and making representations to potential purchasers about the policies' coverage, costs, and other characteristics. Whether an insured could sell a policy on the secondary market is a characteristic of the policy an insurer reasonably could expect an agent to discuss with a potential purchaser—especially a high net worth purchaser…"

Thus, the court concluded that the insurer had to prove that the insured knew that the agent was acting beyond the scope of the agent's authority. The court analyzed this issue as follows:

> Nothing in the applications … completed or any of the other information he received .. informed [the insured] that [the agent] was prohibited from selling any … life insurance policy to an insured who intended to resell the policy on the secondary market. The Statement of Intent … completed to obtain the policies asked whether he had the present intent to sell the policies and if he had spoken to anyone who offered to buy his policies. Although these questions raised the issue of resale, they did not inform that [the insurer] prohibited its agents from selling policies for resale purposes or, more importantly, that [the agent] would be acting outside the scope of his authority if he sold policies … for resale purposes. We therefore conclude the trial court erred in granting …summary adjudication on … breach of fiduciary duty, fraud, and negligent misrepresentation claims …as a matter of law.

The bottom line is that it is incumbent on insurers to clearly and affirmatively state that a secondary sale of a policy is beyond an agent's scope of authority if they want to avoid vicarious liability for the agent's negligence.

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