Unknown policies play havoc on distribution of proceeds

The Day case from Nova Scotia (Day v. Day, 2009 NSSC 98 (CanLII) provides an interesting set of facts and events to ponder. It highlights the importance of informing family members of existing policies and beneficiary designations.

Frank Day died in January 2001 with no will or estate plan. His son, Troy, became his court appointed administrator. Mr. Day was divorced. In addition to his son Troy, he had two younger children, Courtney and Joshua. Courtney and Joshua were both minors and they were half siblings to Troy. A court order from 1998 obligated Mr. Day to maintain life insurance for the maintenance of the two minor children and he was also granted custody of them.

At the time of his divorce, Mr. Day had two life insurance policies and his sister, Marilyn Conrad, was named as beneficiary under both policies. Undoubtedly, he had named her as beneficiary because of his close relationship with her. She also assisted him with his financial affairs.

Shortly after Mr. Day's death, his ex-wife, Laverne Day, found a policy with Primerica for $50,000 plus a maximum of another $10,000 for inflation. Letters were exchanged between lawyers for Ms. Day and Ms. Conrad regarding the intention of these proceeds. At trial, Ms. Conrad indicated that, although she was not specifically aware of the policy, she knew that her brother Frank would have wanted the proceeds for his younger children. However, she also thought that both she and Troy could also benefit from the proceeds.

Another policy was found long after the Primerica policy. The group accidental death policy with CUMIS Life Insurance Company for $200,000 came as a surprise to Ms. Conrad, who found it in Mr. Day's home. Ms. Conrad now felt justified in benefiting herself and Troy. She indicated at trial that she discussed a proposal in relation to the distribution of proceeds with Ms. Day before actually making a distribution.

This proposal included a distribution to all three children and a payment to Ms. Conrad. The lion's share of the proceeds were to be paid for the minor children's maintenance,

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with a lump sum payment at age 25 to Courtney and Joshua. She obtained a written consent from Ms. Day regarding the distribution and, accordingly, distributed $30,000 to herself and $30,000 to Troy. In her mind, obtaining the consent was pivotal before making any distribution of proceeds.

At trial, the court first reviewed the provisions of the court order and determined that it had created an actual trust of the insurance proceeds. The trust was created by Mr. Day in favour of Courtney and Joshua and administered by a designated trustee for the maintenance of the children. The amount of the proceeds was not relevant given that the provisions of the court order did not specify an exact face amount.

The next issue determined whether Laverne Day was their guardian and, if so, whether she could consent, on behalf of the children, to a breach of the trust for the children. The court concluded Laverne provided consent, but she had no authority to bind Courtney and Joshua Day to that consent.

Ms. Conrad's lawyer argued that the court should give his client discretion in relation to the distribution of the proceeds. He relied on the Nova Scotia Trustee Act which provides that the court had the discretion to excuse any breach of trust arising from acting honestly and reasonably.

In reviewing the facts, the court determined that Ms. Conrad acted honestly when she made payments to herself and Troy. Although it was an error in judgment, the court indicated the breach was reasonable. The court concluded that Ms. Conrad, having known her brother well, knew that he would have wanted to benefit his first child as well as the younger two.

The court went on to say that it would be unfair to have Troy's proceeds paid back and, realistically, the proceeds could not now be recovered because Troy had used them. Troy had also provided a signed release to Ms. Conrad that indicated that he would make no further claim against the estate, even though a disproportionate share of the proceeds had gone to the younger children. This was considered a positive outcome.

The court, however, did not agree to the distribution of funds to Ms. Conrad personally. The same arguments could not apply to her situation.

There is a good lesson to be learned from the Day case. No one seemed to know what policies actually existed or who had been named beneficiary. This was evident when Ms. Conrad discovered the second policy. The amount of the policies was also unknown and it was not clear whether both policies were to satisfy the court order obligation.

Clients need to properly document what policies exist and if there is a court order, they need to determine whether the policies in effect are subject to the court order. Communicating to family members as to the designations made on the policies is also very important. If Mr. Day had taken these steps, along with making an estate plan that contemplated his court order obligations, then perhaps the cost of litigation could have been avoided.

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