

Legally speaking: Botched beneficiary designations

Harold Geller



(October 2008) Frequently when I review an insurance agent's or investment advisor's files I am surprised to see that a simple estate **planning** step has gone awry. In an RRSP or RIF there should always be a beneficiary designation. In life insurance especially, failing to have a designated beneficiary simply makes no sense.

Given the role both these investment vehicles play, leaving beneficiary designations incomplete is an invitation to a lawsuit. An advisor and his dealer or insurer also court an invitation to litigation when the paperwork shows contradictory intentions related to the beneficiary designation.

Let's start first with the RRSP and RIF scenario. Including a revocable beneficiary designation would seem to be an obvious step for almost all RRSPs and RIFs. Simply put, a beneficiary designation permits the payment of invested funds to beneficiaries outside of an estate. In the normal course, this direct mode of payment can be preferable for three reasons:

1. Estate-related fees will not be levied.
2. The investments can be promptly and easily transferred; and
3. The beneficiary can be distinct from those named in the will or by applicable law.

While not all beneficiary designations should be irrevocable — even the seemingly soundest marriage or partnership is susceptible to dissolution and an irrevocable beneficiary designation may be regretted following a separation — there is a creditor-proofing benefit if the beneficiary designation is irrevocable. Care should be taken to explain that an "irrevocable" beneficiary designation cannot be changed without the consent of the beneficiary.

Furthermore, a regular review of the beneficiary designation with your client is a part of standard customer service; it's a basic part of financial planning and a great way to show your professionalism.

When transferring a client's RSP or RIF account between dealers, an advisor should take care to obtain specific instructions from the client with respect to beneficiary designations. Failure to obtain instructions and to record an explanation of the importance of the beneficiary designation can result in an advisor being liable to the disappointed beneficiary. This is demonstrated in the 2001 and 2002 British Columbia Supreme Court and Court of Appeal cases, *Desharnais v. Toronto-Dominion Bank*.

Care should also be taken to avoid filling in a mutual fund or insurance investment beneficiary box when no beneficiary designation is legally possible.

The "orphan" beneficiary designation is an example of the type of error that occurs. In the 2003 Saskatchewan Queen's Bench case, *Mayer v. Nordstrom*, the father, Mr. Mayer, wished to leave money to his son, Garry.

At first, the father purchased an annuity with the son listed as his beneficiary. When the annuity matured, his advisor recommended that the assets be invested

in a mutual fund. Although the beneficiary designation was completed, the mutual fund was in an open account, making that designation void. The advisor was liable for the son's loss when the money was paid into the estate and divided amongst the estate beneficiaries.

The advisor claimed to have warned the father about this problem but the advisor could not explain away the fact that the son's name appeared in the beneficiary designation box on the RSP application. The responsibility, in this case, was on the advisor to demonstrate through objective evidence (notes or records) that he gave warning about the problem. Few advisors make such notes or records.

More Legally Speaking...

- [Botched beneficiary designations](#)
- [The OSC states the obvious](#)
- [Volatility, prepared clients and opportunity](#)
- [The KYC process](#)
- [Professional networks, service and liability](#)
- [Bank insurance, consumer rights](#)
- [E&O claims - time to circle the wagons](#)
- [TPAs: helpful product or potential nightmare?](#)
- [Goodwill undone](#)
- [When changing dealers](#)

This reasoning would also apply to an annuity with no guarantee period. Completing a beneficiary designation in such an insurance policy would be confusing to a policyholder and this would, ultimately, be resolved in the intended beneficiaries' favour unless a specific warning to the client was documented. One would think that such an error could not occur during the underwriting process, but it happens.

With life insurance contracts, failing to clearly designate beneficiaries is nearly inexcusable. A life insurance contract, by its very nature, foresees the possibility of death. Failing to implement plans for the possibility of death, by failing to designate a beneficiary, undermines a fundamental part of the planning process and purpose of the product.

Incomplete beneficiary designations that result in payment of funds to the estate result in an avoidable tax on the proceeds. So too, failing to confirm that the existing beneficiary designation should remain in place, that the intentions of the policyholder have not changed, is a failure of the agent's "continuing service" obligation and a lost opportunity for potential further sales.

An estate can sue an advisor for negligent beneficiary designations. In my view, beneficiaries who were supposed to receive the bequest can also sue under the negligence law as "disappointed beneficiaries." The liability — to a disappointed beneficiary and to the deceased's estate in certain circumstances, comes from the advisor's failure to carry out the client's intentions and instructions.

An advisor who fails to address the designation issue properly when it is possible, takes great risks with his or her reputation, liability, and the client-advisor relationship.

Harold Geller is an expert on legal issues affecting financial intermediaries. Harold

assists and represents dealers, MGAs, branch managers, compliance officers and advisors dealing with their compliance, regulatory and negligence issues. Harold also helps financial intermediaries with internal business and their clients' legal issues. Harold is a well-known industry commentator, a CE provider and administrator with foradvisorsonly.com. Harold's law firm, Doucet McBride LLP, also provides advice on tax issues, Succession Planning, Retirement Planning, Estate Planning and buying and selling books of business. Harold can be reached at hgeller@doucetmcbride.com.

(10/23/08)