Lack of Buy-Sell Agreement Allows Surviving Business Owner to Keep Death Benefit For Himself:

Selzer v. Dunn, No. 12-12-00150-CV (Texas Court of Appeals 2014)

Summary

The Court of Appeals in the 12th District of Texas found that a surviving business owner was not required to use life insurance proceeds to purchase his deceased co-owner's shares because there was no written buy-sell agreement.

Related Information

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Facts

Michael Varner and Robby Dunn were co-owners of Cleanline Products, Inc., each owning fifty percent of the company's shares. Prior to 2008 they discussed the creation of a buy-sell agreement to prepare for the death of either owner. Their attorney provided several drafts as examples of possible cross-purchase agreements, *but no agreement was ever signed*.

In 2008, Lincoln Financial Life Insurance Company issued two life insurance policies:

- Varner was the owner and beneficiary of a $2 million policy on Dunn's life, and
- Dunn was the owner and beneficiary of a $2 million policy on Varner's life.

Cleanline paid the premiums for both policies.

Varner died in 2010. Tracey Selzer, Varner's ex-wife and administrator of his estate, claimed that Varner's estate was entitled to the death benefits from the policy owned by Dunn on the basis that a buy-sell agreement existed. Selzer argued that Dunn's refusal to use the proceeds to purchase all the Cleanline shares from Varner's estate constituted a breach of contract and a breach of fiduciary duty. As for Dunn, he asked the court to honor the fact that he (Dunn) was named sole beneficiary of the policy insuring Varner and was thus entitled to all of its death benefit.

The trial court agreed with Dunn and dismissed Selzer's claims. Selzer appealed. The Twelfth Court of Appeals of Texas reviewed the case.

Court's analysis

The court of appeals agreed with the trial court, holding that Dunn was the beneficiary and entitled to 100% of the death benefit proceeds. The cross purchase agreement – namely the

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alleged oral contract referred to in Selzer's breach of contract claim – never existed between the two shareholders.

The court found that there was no "meeting of the minds" (a critical element of any contract) between Varner and Dunn when it came to the important details of the buy-sell agreement, including how the death benefits should be used to purchase stock. Several witnesses testified that Varner (now dead) had a general idea that Dunn owned a policy on Varner's life so that Dunn could buy stock from Varner when Varner died. But there was no evidence that the two parties ever agreed upon significant details of the buyout, specifically the stock's purchase price and how much of the stock was to be bought from the estate. The court ruled that the unsigned drafts of cross-purchase agreements were not enough to show a "meeting of the minds" as to the purchase price and quantity of stock to be purchased. Because there was no agreement regarding these material provisions, the court ruled that there was no contract for Dunn to breach.

The court quickly dismissed the breach of fiduciary duty claim, stating that because this was a matter involving a purely economic loss it should be resolved under contract law rather than tort law.[1]

Our comments

1. Have a written buy-sell agreement. Attorneys are not trying to scare you into legal fees when they recommend a written agreement! The written agreement provides a legal enforcement tool for the deceased's estate if a co-owner of a closely held business attempts (whether through ignorance or deceit) to keep for himself the death benefit dollars that are meant for buying the deceased's shares, or to otherwise get out of or change the terms of any agreement.

2. Some courts may find a valid agreement without a written document, but why risk it? The court in this case *would* have found a valid agreement *if* the estate could have proven that there was a meeting of the minds concerning the stock price and the amount of stock to buy, but they were not able to do so even with unsigned drafts of the agreement. Proving that an agreement exists without a written document is an uphill battle, and the risks of going without one far outweigh any benefits, if there are any.

3. The deceased's estate can be left holding stock that's worth less. If there is no agreement that requires the still-living business owner to buy any shares, the estate can easily be stuck with shares in a business that has lost significant value because it just lost a key employee. This low value might be depressed even further if the deceased's estate has to carry out a fire sale of the stock to quickly generate cash for paying estate taxes or other post-mortem expenses.

4. Lack of an agreement can hurt the still-living business owner, too. What if the still-living business owner *wanted* to buy the shares from the estate, but the estate refused because there

[1] A "tort" is a civil wrong (as opposed to a crime) that is not based on contract. Examples of torts include negligently breaching a fiduciary duty, recklessly driving through a stop sign, or intentionally defaming someone, and hundreds of other acts.

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was no written agreement? The still-living owner might very well have planned to acquire 100% ownership and control of the company, but he could be forced to share the company with whoever receives the business interest from the deceased's estate (e.g., the deceased business owner's spouse and children) if they don't want to sell their interest.

Conclusion

This case shows that one of the most important aspects of good planning is to actually execute the plan, which includes signing documents. Conscientious planners see to it that "T"s are crossed and "I"s are dotted. If not, the consequences can be bad all around.

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