PUBLIC POLICY AND INSURABLE INTEREST IN LIFE INSURANCE*

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There are two well-established rules of insurance law in relation to the topic to be discussed. One, that an applicant-beneficiary must possess an insurable interest in the life of the person to be insured. Two, that the issuance of a life insurance policy to an applicant-beneficiary having no insurance interest is contrary to public policy and therefore void.

Historically, there is some uncertainty as to whether or not the English common law required that a beneficiary of a life insurance contract must have an insurable interest in the life of the insured.[1] The uncertainty, however, ends with the passing of the statute of 14 George III, c. 48(1774), which provided that no insurance shall be issued without the beneficiary having an insurable interest; and, if issued, shall be null and void.[2]

Whether this statute was declaratory of the common law or not, the courts of the American states have generally held that wager policies are against public policy and void.[3]

An insurable interest, generally, is that interest (required by law) created by the relation between the insured and the contingent event insured against which would cause a loss to the insured should the event actually occur.[4] It is also such an interest which precludes any wagering intent on the part of the person who will benefit by the event occurring.[5]

In property insurance, this requirement is intended to indemnify the insured against loss,[6] whereas in life insurance it is not intended for indemnification.[7] Generally, in property insurance, it need not exist when the policy is issued, but must exist at the time the event insured against occurs,[8] whereas in life insurance, gen-

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[1]III *The American and English Encyclopaedia of Law* 930-931 (2d ed. 1897).

[2]Patterson and Young, *The Law of Insurance* 226-227 (4th ed. 1961).

[3]Vance, *Insurance* 184 (3d ed. 1951).

[4]Patterson, *Essentials of Insurance Law,* 109 (2d ed. 1957).

[5]Vance, *Insurance* 157 (3d ed. 1951).

[6]Riegel and Miller, *Insurance Principles and Practices* 109 (3d ed. 1947).

[7]*Ibid.*

[8]Patterson, *Essentials of Insurance Law* 153 (2d ed. 1957).

erally, it must exist when the policy is issued but need not exist at the time the event insured against occurs.[9]

In *Warnock v. Davis* the United States Supreme Court has said,

> "It is not easy to define with precision what will in all cases constitute an insurable interest, so as to take the contract out of the class of wager policies. . . . But in all cases there must be a reasonable ground, founded upon the relations of the parties to each other, either pecuniary or of blood or affinity, to expect some benefit or advantage from the continuance of the life of the assured. Otherwise the contract is a mere wager, by which the party taking the policy is directly interested in the early death of the assured. Such policies have a tendency to create a desire for the event. They are, therefore, independently of any statute on the subject, condemned, as being against public policy.[10]"

General rule requires that an applicant-beneficiary have an insurable interest in the insured at the time of the purchase of the life insurance policy. This rule does not prevent the applicant-beneficiary from buying a policy.[11] It merely makes the policy void and unenforceable,[12] if it is subsequently found that he did not have an insurable interest at the inception of the policy.

The recent *Liberty National Life Insurance Co. v. Weldon* case[13] has renewed interest in the question of public policy in relation to insurable interest in life insurance. Gaston Weldon sued the Liberty National Life Insurance Co. *et al.* to recover damages of $100,000.00 for the wrongful death of his minor child. The Supreme Court of Alabama affirmed a $75,000.00 judgment of the lower court.

Weldon's daughter, Shirley Dianne, approximately two and one-half years of age, died on May 1, 1952. There were three life insurance policies, issued by three different companies, on her life, totalling $6,500.00 of insurance. The policies were issued on December 1, 1951, April 23, 1952, and in the latter part of March, 1952.[14]

Mrs. Earle Dennison, Shirley's aunt-in-law (the widow of a brother of Shirley's mother), was the applicant purchasing the insurance in each case. She was also designated as beneficiary in each policy. She paid the premiums for each policy, and Shirley's parents did not know of the existence of, nor did they consent to, any one of these policies. The aunt-in-law did not provide for the child in any way whatever, and the child did not live with her. Shirley died from arsenic poisoning. Her aunt-in-law was tried, convicted, and executed for her murder.

All the applications listed Mrs. Dennison as aunt, rather than aunt-in-law. None of the three companies made any reasonable effort to ascertain whether the aunt-in-law had an insurable interest in Shirley's life. In Alabama the aunt re-

[9]*Ibid.,* 188.

[10]104 U.S. 775, 779 (1881).

[11]Mowbray and Blanchard, *Insurance, Its Theory and Practice in the U.S.* 56 (4th ed. 1955).

[12]*Ibid.*

[13]100 So. 2d 696 (Ala. 1957).

[14]Liability on these policies was not an issue. All parties to the action conceded they were void, and the case was tried as an ordinary negligence case.

lationship, by itself, does not constitute an insurable interest.[15] Also, the in-law relationship alone is not considered to create an insurable interest.[16]

"After the death of Shirley Dianne the family became extremely suspicious concerning the deaths of two other children. Their remains were exhumed and examination revealed that they also contained arsenic. Mrs. Dennison had insured them and had collected."[17]

Both counsel for the plaintiff and counsel for the defendants, in the Weldon case, agreed that since the aunt-in-law had no insurable interest in Shirley's life the policies purchased by Mrs. Dennison were illegal and void as repugnant to public policy. The question, however, is again raised—does the concept of public policy automatically void a life insurance contract when the applicant-beneficiary has no insurable interest?

Public policy is variable. All societies, at any one time, do not agree upon a similar concept of what public policy should be. The same society, at different times, may slightly alter or radically change its concept of what its public policy should be. As the mores of a society change, so does its public policy.

In the matter of insurable interest in the United States there is a consistency of view that life insurance sold to an applicant-beneficiary without insurable interest is against public policy. The courts, however, in applying this concept of public policy to the collateral issues arising from the insurable interest rule, have created uncertainty, so much so that the question is raised whether the insurable interest rule is for the protection of the public (a true public policy) or whether it is merely a defense for the insurer. It is difficult to determine whether the courts are primarily concerned with the safety of those insured or with the protection of the insurance companies.

Case law, as it has developed in the United States, is inconsistent with the concept of public policy which is applied. The law which was intended to protect the public[18] has been protecting the companies. If lack of insurable interest in an applicant-beneficiary is a true public policy issue, it seems inconsistent that the defense must be specially pleaded. "It is generally held that, to be available, the defense of lack of insurable interest must be specially pleaded."[19]

If the company does not raise the issue, by specially pleading it, the aspect of public policy is lost sight of. If the company chooses to pay the proceeds of the policy to the applicant-beneficiary, the consideration of public policy is again dispersed. If the company chooses to place the policy proceeds into court by interpleader, public policy again disappears. If public policy is truly the basic consideration, why is control given to the insurance company to elect which course it will take, among which are courses which eliminate the public policy consideration?

The issuance of life insurance policies to an applicant-beneficiary with a dis-

[15]Commonwealth Life Ins. Co. v. George, 248 Ala. 649, 28 So. 2d 910 (1947).

[16]National Life and Accident Ins. Co. v. Middlebrook, 27 Ala. App. 247, 170 So. 84 (1936).

[17]From an address (p. 5) delivered before the Legal Section of The American Life Convention, October 1958, by John W. Gillon (Spain, Gillon, and Young) of counsel for the Liberty National Life Ins. Co.

[18]McCahan, *The Beneficiary in Life Ins.* 32 (1948).

[19]Keeton v. National Union, 178 Mo. App. 301, 165 S.W. 1107 (1914).

regard of the insurable interest rule cannot be justified. It is public policy to discourage inducement to murder. To say mere that the contract is void ad initio does not accomplish this. In fact, it may even tend to encourage murder. A truly sound public policy will discourage any such temptation by prohibiting the making of the contract in the first instance. In the words of Justice Lawson of the Alabama Supreme Court, "There is no justification for the creation of such a risk to the insured and there is no social gain in the writing of a void policy of insurance."[20]

It seems the courts retain a strong public policy consideration only in direct relation to the issue of voiding the policy. Yet despite this strong public policy concern, the courts very early decided that insurable interest does not have to continue to exist once it has been present at the inception of the policy.[21]

The presence of insurable interest in the applicant-beneficiary by itself is insufficient to satisfy public policy considerations. The consent of the person whose life is being insured is also required. It probably is true that consent is even more important than insurable interest, although consent alone will not eliminate wagering. Waiver, estoppel, laches, or the incontestible clause are all ineffective since the contract is void ab initio as against public policy despite the fact that a company knowingly issues such a policy and continues to accept premiums.

The public policy concept is born of the desire to protect the life of the insured and to avoid wagering (on lives). This concept, then, must apply only in relation to the applicant-beneficiary, for it is he who would gain by the death of the insured. If he does not have an insurable interest in the life insured, public policy should defeat his gaining on the wager (assuming insured's death to be natural); instead, it voids the policy. It would, therefore, follow that if the insured's death is caused by illness, the policy should not be voided because the applicant-beneficiary had no insurable interest at the time of the purchase of the policy. As long as the applicant-beneficiary was not a cause of the death, as long as he does not gain by the death, the policy payment should revert to the estate of the insured. To void the policy is to protect the insurance company against its own negligence in selling a policy to one who had no insurable interest. If the applicant-beneficiary without insurable interest dies prior to the insured and the insured continues to pay the premiums and designates himself (or anybody having an insurable interest) as beneficiary, it seems only equitable that the policy should not be technically void because an insurable interest did not exist at the inception of the policy. This can be accomplished by inserting a provision in the original contract, and would better serve public policy than the voiding of such a contract.

Furthermore, the applicant-beneficiary's failure to comply with the insurable

[20]Liberty National Life Ins. Co. v. Weldon, 100 So. 2d 696, 708 (Ala. 1957).

[21]May, *The Law of Insurance* 166 (1891) says, "In general, it is essential that the insured be possessed of an interest, both at the time when the insurance is effected and at the time of the loss. . . . This doctrine was early applied to life as well as to marine and fire policies (Godsall v. Boldero, M.T. 1809, K.B. 9 East, 72), but has undergone some modifications in life insurance." As the relaxation of the principle of indemnity occurred in the field of life insurance the necessity for insurable interest being present at the time of death of the insured began to disappear. The U.S. Supreme Court has said that the contract of life insurance is not one of indemnity and that insurable interest is required only at its inception (Phoenix Mutual Life Ins. Co. of Hartford v. Bailey, 13 Wall (U.S.) 616 (1871).

interest rule should not release the insurer from his contract. Where the insured dies from any cause other than murder, the voiding of the contract is a mere excuse not to perform an otherwise enforceable contract. The contract has failed only in relation to the original applicant-beneficiary (as if he had died). The insured's estate should automatically become the beneficiary by terms which should be in the original contract. It is basically inequitable to permit an accessory (with superior knowledge and possible negligence) to an illegal contract to keep the advantages and to escape the risks. In some jurisdictions the insurance company is permitted to retain the unearned premiums. This may encourage companies to write such policies though publicly disclaiming such an interest. It may encourage their negligence in selling to applicant-beneficiaries without insurable interest.

In view of all this it appears only just that public policy considerations should preclude recovery only on the part of the wrongdoer (the applicant-beneficiary) and his successors. Public policy did not intend to relieve the insurance company from its contractual obligations nor should it eliminate the rights of all others. Public policy should permit reversion of the insurance proceeds to the insured's estate, or escheat to the state when no heirs are available.

The public policy of conserving human life is more important than the factor of requiring the insurance companies to check for the existence of insurable interest at the time of the purchase of the policy rather than at the time of death. This is no more difficult at the time of the application than at the time of death. Checking at death-time, however, becomes a possible means of avoiding payment. Checking at the time of application is taking cognizance of a public policy consideration which accomplishes what the law originally intended and still does intend.

It is generally admitted that a life insurance contract sold to an applicant-beneficiary without insurable interest is an illegal contract because it is contrary to public policy. Consequently, there can be no doubt that the life insurance policy issued to the applicant-beneficiary with no insurable interest is an illegal contract wherever insurable interest is required by statute or judicial determination. Since the law usually leaves the parties to such a contract where it finds them, the insurance company may refuse to pay such applicant-beneficiary.

An insurance policy issued on the life of a person makes him the subject matter of a contract. As the subject matter of a contract which may engender risk to his well-being he should have some rights in the contract as originally made. An individual's right to be let alone is impaired by making him the subject matter of a contract, particularly since the insured is given no protection or advantage for being the subject of the contract. In fact, though it is the insured who may suffer some detriment, it is the insurer who is permitted to gain by the illegality of the contract. In this regard courts in the United States hold that fraud by one party to the contract or mutual mistake common to both may lead to the reformation of a life insurance contract.[22]

Knowledge of the applicant-beneficiary's lack of insurable interest may conceivably constitute a fraud on the insurer's part. This fraud should be sufficient to uphold a reformation of the contract. The contract is against public policy only

[22]Yablon v. Metropolitan Life Ins. Co., 200 Ga. 693, 38 S.E. 2d 534 (1946); American National Ins. Co. v. McPhetridge, 28 Tenn. App. 145, 187 S.W. 2d 640 (1945).

in relation to the applicant-beneficiary without insurable interest. Therefore, the contract should be void only as to this applicant-beneficiary. The contract is then left without a beneficiary and should revert to the insured's estate.

It seems reasonable to construe the insurer's duty to investigate whether insurable interest exists as an implied condition precedent of the contract. When the insurer knows the applicant-beneficiary has no insurable interest, he should be under a duty to refuse to issue the policy.

The insurer's acceptance of periodic premiums, coupled with the promise to perform inherent in accepting these premiums, should be considered as re-activating the contract at each payment. The applicant-beneficiary without insurable interest at inception may develop an insurable interest (for instance, by becoming a creditor of the insured) which is then present when the next premium payment is made. Yet this contract is still void under present law.

The courts continue to hold that the contract is illegal, therefore void ab initio. There seems to be but slight concern for the equities involved, slight concern for the misuse of the "in pari delicto" concept, little or no concern for justice, little or no concern for the spirit of the law, little or no concern for unjust enrichment, and little or no concern for superior knowledge on the insurer's part.

Both murder and wagering are encompassed within the concept of public policy; both are involved in the insurable interest rule.

In *Grigsby v. Russell* the court said,

> "The very meaning of an insurable interest is an interest in having the life continued and so one that is opposed to crime and what perhaps is more important, the existence of such an interest, makes a roughly selected class of persons who by their general relations with a person whose life is insured are less likely than criminals at large to attempt to compass his death.[23]"

These words emphasize the need for an insurable interest in order to minimize or eliminate the potential murder involved in the sale of a life insurance policy to one who has no concern about the life insured. Much has been written in opinions, texts, and articles about the need for insurable interest to minimize murder or to eliminate wagering.

The "text authorities have expressed the view that the prevention of wagering is the main reason for the rule, and that it is designed only secondarily to lessen the temptation to commit murder."[24] Patterson says, "The law does not rigorously forbid the creation of situations in which one person may gain by the death of another."[25] It is true that a remainderman can gain by the early death of a life tenant yet the law does not eliminate the use of a life estate. It is likewise true that an expectant heir can gain by the early death of his testator, yet the law does not eliminate the use of wills. It does not necessarily follow that the desire to minimize possible murders is the lesser one compared to the general desire to eliminate wagering. It should be emphasized that even though the wagering concept may be considered by some as the more important reason for the insurable interest rule, the

[23]32 Sup. Ct. 58 (1911).

[24]1 Couch, *Cyclopedia of Insurance Law* 778 (1929).

[25]Patterson, *Essentials of Insurance Law* 158 (2d ed. 1957).

subject matter of the wager is human lives and to wager on lives must encompass the possible murder motive. The risk of inducement to the crime of murder is a part of the broader doctrine of invalidity as a wager.[26] The two are inseparable. There is a moral hazard present in the sale of a life insurance policy in each instance where the applicant-beneficiary has no insurable interest. If the inducement to murder was not a factor, wagering on lives would possibly be no less contrary to public policy than parimutuel betting. It is just this murder factor which makes wagers on lives the moral risk it is and emphasises the public policy involved.

Many writers have further argued that since the punishment for murder is so severe and since the beneficiary cannot gain by his deliberate crime, this alone is sufficient to deter one from committing murder in order to collect the life insurance proceeds. This is not essentially true. Human nature being what it is, there are always some foolish, desperate or risk-loving individuals who will chance murder, expecting not to be caught. In life insurance contracts with a double indemnity clause for accidental death the big inducement in making the crime appear as an accident is not only escaping punishing for the crime but receiving the increased proceeds as well.

It may also well be argued that "a potential criminal who is not deterred from murdering by these well-known rules of law, is not likely to stop in the face of the doctrine of insurable interest whose details are by no means clearly established."[27] The insurable interest rule will not eliminate murder but there likewise can be no doubt that it may assist in minimizing the inducement to commit murder. Unless educated to insurance terminology, the average person has little concept of the meaning of insurable interest. Too many people have never even heard of the term. Certainly nobody can be deterred by something he knows nothing about.

This may be all the more reason for placing the responsibility of enforcing the insurable interest rule on the party to the contract who does know about it—the insurance company. These companies claim, moreover, that they are not interested in selling to one without insurable interest.

It is well-settled law that a murderer cannot benefit from his own wrong[28] even when he has an insurable interest in the life of the deceased. A potential murderer would be deterred from committing the crime if he knew he could not collect because he had no insurable interest, even though he were acquitted of the crime. There are different results possible if it is remembered that for a criminal conviction (or acquittal) murder must be found "beyond a reasonable doubt," whereas in a civil case murder may be proven by a preponderance or slightly greater weight of the evidence. Therefore, one who is convicted of killing the insured may have the matter passed on again in a civil suit to obtain the insurance proceeds,[29] particularly since the criminal evidence or judgment would not be admissible in the civil proceedings.[30]

Where the insured is unlawfully and intentionally killed by a beneficiary

[26]Magee, *Life Insurance* 326 (3d ed. 1958).
[27]6 B.U.L. Rev. 114 (1926).
[28]Schmidt v. Northern Life Association, 112 Iowa 41, 83 N.W. 800 (1900).
[29]Gholson v. Smith, 210 Miss. 28, 48 So. 2d 603 (1950).
[30]Goodwin v. Continental Casualty Co., 175 Okla. 469, 53 Pac. 2d 241 (1935).

who is subsequently acquitted in a criminal action, the beneficiary generally cannot collect the insurance.[31] Where the beneficiary must first be convicted of the homicide, an acquittal would permit him to collect the insurance.[32] Or, where a record of the conviction of the beneficiary for murdering the insured is held to be prima facie evidence of his guilt, he cannot collect.[33] On the other hand, a manslaughter conviction may mean there was no intentional injury and the beneficiary can recover[34] and, in other jurisdictions, he still cannot recover because of public policy.[35] If, however, the murderous beneficiary cannot collect the proceeds, who does collect them?

Where the murderous beneficiary had an insurable interest (and the contract, therefore, is not void ab initio), and no intent to murder existed at the time of the purchase of the policy, or the policy had no clause specifically voiding it under these circumstances, the insurance company must still pay the policy proceeds to the estate of the deceased. This is done under a constructive trust theory (the beneficiary holding the proceeds in trust for the insured's estate) or under the concept that the beneficiary having disqualified himself the company will pay out the proceeds just as if no beneficiary existed at all. Where the murderous applicant-beneficiary has no insurable interest, however, the contract being void ab initio, the insurance company makes payment to nobody.

The courts generally hold that the murderous beneficiary (with an insurable interest) forfeits only his rights and the rights of those claiming through him but that the insurer is not relieved from liability.[36] Since one of the important reasons for the insurable interest rule is to prevent murder, declaring such a contract void ab initio does not prevent the making of the contract nor have the deterrent effect relative to the crime. State statutes should require that the presence of insurable interest be checked by the insurance companies prior to the issuance of the policy, adding a penalty for the making of the contract.

Especially in relation to policies upon the lives of children must greater care be taken to see that insurance is sold only to one having the strongest desire to see that child's life continue. As one court has said,[37] "The insurance of children who are helpless and under the control and authority of others, is susceptible of such possibilities of evil that it should not be encouraged."

Present law permits the insurer to be relieved of liability under the following circumstances: First, when the beneficiary procures the policy with the intention to murder the insured.[38] Every sale of a life insurance policy carries an implied condition that the beneficiary will not murder the insured, or, as Patterson says, "every life insurance contract in which the insured and the beneficiary are not the same person creates a temptation to the beneficiary to murder the insured in the sense

[31]New York Life Ins. Co. v. Murdaugh, 94 F. 2d 104 (S.C. 1938).
[32]Noller v. Aetna Life Ins. Co., 142 Kan. 35, 46 Pac. 2d (1935).
[33]Sovereign Camp, W.O.W. v. Gunn, 227 Ala. 400, 158 So. 192 (1934).
[34]Minasian v. Aetna Life Ins. Co., 295 Mass. 1, 3 N.E. 2d 17 (1936).
[35]**Mackowiak v. Polish Union of America, 258 N.Y.S. 134, 236 App. Div. 44 (1932).**
[36]Schmidt v. Northern Life Ass'n., 112 Iowa 41, 83 N.W. 800 (1900).
[37]Prudential Ins. Co. v. Jenkins, 15 Ind. App. 297, 43 N.E. 1056 (1896).
[38]New York Mutual Life Ins. Co. v. Armstrong, 117 U.S. 591, 6 S. Ct. 877 (1886).

that the opportunity for gain exists if only the crime can be concealed."[39] Second, when a clause is inserted in the contract providing that murder of the insured by the beneficiary voids the entire contract.[40] Third, when the murderous beneficiary is the sole heir of the insured.[41] This latter is, of course, open to discussion. Where the first two conditions listed above are not present there is always the possibility of escheat to the state of the face value of the policy.

Justice Holmes recognized that even where an insurable interest was present, the risk of murder was not excluded. He said, though, that the danger is greatly increased "if the whole world of the unscrupulous are free to bet on what life they choose,"[42] adding that "the law has no universal cynic fear of the temptation opened by a pecuniary benefit accruing upon a death. It shows no prejudice against remainders after life estates, even by the rule in *Shelley's* case."[43]

There are cases on record[44] in which one person without insurable interest has purchased insurance on the life of another for the purpose of murdering him to recover the proceeds of the policy. This is proof that the evil sought to be avoided by the insurable interest rule is real.

The mortality tables upon which premium rates are based include deaths of all types. Certainly deaths by murder were not excluded in devising these mortality tables. All the premium payments received by the companies cover payments in case of deaths by murder. The companies are, it may be said, unjustly enriched with each payment, however small, if they are not obligated to pay the policy proceeds to the insured's estate or the state. Certainly, public policy did not intend this result.

Both the wagering concept and the murder concept have been subject to dispute and "at one time or another have been assailed as unsound reasons for the requirement of insurable interest."[45] Neither one is probably more important than the other. The point is one cannot be emphasized to the detriment of the other. Certainly neither one can be completely ignored.

Let it become common knowledge that policies are sold to applicant-beneficiaries having no insurable interest and without the consent of the insured (or his parents), and many people will begin to question the advisability of it all. This would be especially true during periods of social and economic stress. It is small consolation to the murdered (and his family) that the murderer cannot collect on the policy, or is executed if he is caught.

It has been shown that the public policy concept is basic to the determination that the contract is illegal and, as such, void ab initio, and the concept of murder v. wagering has been compared as underlying the public policy idea.

[39] 18 Colum. L. Rev. 381, 389 (1918).

[40] Markland v. Modern Woodmen of America, Mo. App. 1919, 210 S.W. 921 (1919).

[41] McDonald v. Mutual Life Ins. Co., 178 Iowa 863, 160 N.W. 289 (1916).

[42] Grigsby v. Russell, 222 U.S. 149, 155 (1911).

[43] *Ibid.*

[44] New York Mutual Life Ins. Co., v. Armstrong 117 U.S. 591, 6 Sup. Ct. 877 (1886); Goldstein v. New York Life Ins. Co., 225 App. Div. 642, 234 N.Y.S. 250 (1928); Henderson v. Life Ins. Co. of Va., 176 S.C. 100, S. E. 680 (1935).

[45] Cooke, *Life Insurance* Sec. 58 (1891).