Redefining the ‘Doctrine of Insurable Interest’ for Life Insurance – The New Dimensions!

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Redefining the ‘Doctrine of Insurable Interest’ for Life Insurance - The New Dimensions!

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An ‘insurable interest’ is a term referring to the relationship between a policy’s insured person or property and the potential beneficiary. The beneficiary must have an insurable interest in the insured person or property to receive payment of the policy if the insured died while the policy was in force. Lawrence, J, defined ‘insurable interest’ in the case of Lucena v. Craufurd1 as “A man is interested in a thing to whom advantage may arise or prejudice happen from the circumstances which may attend it; interest does not necessarily imply a right to the whole or a part of the thing, but having some relation to or concern in the subject of the insurance, which relation or concern by the happening of the perils insured against may be so affected as to produce a damage, detriment or prejudice to the person insuring; and where the man is so circumstanced with respect to matters exposed to certain risks or dangers, he may be said to be interested in the safety of a thing. To be interested in the preservation of a thing, is to be so circumstanced with respect to it as to have benefit from its existence, prejudice from its destruction.”

Insurable interest is necessary to the validity of an insurance contract, whatever be the subject matter of the policy, whether upon property or life. If there is no insurable interest the contract is void, and unenforceable. In particular, where an insurable interest does not exist at the time the contract for insurance was made, the insurance contract is void from its inception. However, the cessation of an insurable interest does not affect the validity of the insurance contract where an insurable interest existed at the time the policy was issued.

In all life insurance cases there must be 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 assured2.

While the lack of an insurable interest will ordinarily render an insurance policy void and unenforceable on public policy grounds, where there are several insured under a policy, and all do not have the requisite insurable interest, the policy is invalid only as to those lacking an insurable interest.

THE DEVELOPMENT

The concept of ‘insurable interest’ first surfaced in the lex mercatoria of the Middle Ages3. At that stage insurance was understood to be of a pure indemnity nature covering the insured only for patrimonial loss or damage caused by the peril insured against. The earliest reference to insurable interest simply emphasised this characteristic of insurance. Since the insurer’s contractual undertaking was to indemnify the insured for patrimonial loss, the later had to prove that he had a financial interest upon the happening of the insured event because there could be no loss without an interest4. In this very respect insurance was considered to differ from a wager because wagers did not contain indemnity clause.

Prior to the end of the eighteenth century, English courts permitted and enforced various gaming or wagering contracts made by persons who had absolutely no insurable interest in the life of another person.

In life insurance, wagering or gaming practices developed in the eighteenth century. Popular accounts of the period describe the practice of purchasing insurance on the lives of those being tried for capital crimes. These policies constituted naked wagers on whether the accused would ultimately be convicted and executed for the alleged offence. A related practice was the purchase of insurance on the lives of famous, elderly persons; the premium would be a function of what was known about the person’s health, including any recent illnesses. Insuring a life in which one has no interest creates a temptation to bring the insured’s life to an early end, but the greater concern in eighteenth-century England was the practice of wagering.

Consequently, in order to put an end to life insurance contracts that had no insurable interest in the life of the insured and which had become a cover for a multitude of wagering and

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4. Ibid
gaming contracts the British Parliament in 1774 passed a statute holding that any life insurance contract without an insurable interest in the life of the insured would henceforth be null and void. Unfortunately, Parliament left to the courts the daunting task of how to interpret and enforce this archaic, poorly drafted, and ambiguous statute.

During the nineteenth century and early twentieth century, most American courts likewise recognized the insurable interest requirement for life insurance policies, purportedly based upon early English common law precedent. For example, in Commonwealth Mutual Life Insurance Co v. Schaefer, Bradley, J. declared:

"It is generally agreed that mere wager policies that is, policies in which the insured party has no interest whatever in the matter insured, but only an interest in its loss or destruction are void, as against public policy. This was the law of England prior to the Revolution of 1688. But after that period, a course of decisions grew up sustaining wager policies. The legislature finally interposed, and prohibited such insurance first, with regard to marine risks, by the statute of 19 Geo. II, c. 37, and next, with regard to lives, by the statute of 14 Geo. II, c. 48. In this country, statutes to the same effect have been passed in some of the States; but where they have not been, in most cases either the English statutes have been considered as operative, or the older common law has been followed."

In the United States, the insurable interest doctrine for life insurance was first adopted by a majority of State courts, and was subsequently adopted by a majority of the State legislatures, where insurable interest statutes for life insurance were enacted within comprehensive state insurance codes.

A GLOBAL COMPARISON

(a) English Law: The insurable interest found its place for the first time in the Life Assurance Act, 1774 wherein sections 1 and 3 talked about the insurable interest and it is still in force. Earlier there was no distinction between life assurance contracts and indemnity insurance, but this myth was broken by the landmark judgment in Dalby v. Indian and London Life Assurance Co wherein it was pointed that an interest is required to exist at the time of the conclusion of the contract and a future speculative interest would therefore not do. Once again in a recent case of Feasey v. Sun Life Insurance Corp. of Canada the court confirmed that the interest necessary for life assurance must sound in money. At the same time it acknowledged the differences between indemnity and non-indemnity insurance. The English law has not made much progress in terms of developing this doctrine and there is a need of reform in this regard.

(b) American Law: Though the law prevailing in America was adopted from the English law, unlike the English law the American law of ‘insurable interest’ recognises close relationship of affinity, love and affection, with the life to be insured. The American courts have also recognized insurable interest which is based upon ‘expectation of benefit’ such as that enjoyed by a person who is de facto maintained by another without there being any legal duty on him to do so. A few states have also approved the consent by the life insured to be sufficient proof of ‘insurable interest’.

(c) Australian Law: Australian law has drifted from the English law and is governed by the Insurance Contracts Act of 1984. As per the Act a person has an ‘insurable interest’ only in his/her life and in the life of his/her spouse. It further provides that a parent and a guardian has an insurable interest in the life of a child who has not yet attained the age of 18 years and a general provision relating to body corporate wherein an insurable interest is there in life of an employee or an officer.

(d) German Law: The Insurance law in Germany stands at a totally different footing as ‘insurable interest’ is not a pre requisite for an insurance contract of life assurance but in case the life of a third person is insured, there must be a prior written consent by the life insured if the sum insured exceeds the ordinary burial cost.

THE INDIAN SCENARIO

Insurance in India is almost 185 years old and came with the British invasion. Since then a lot of ink has been spilt on making regulatory mechanisms and legislations to control the business of Life Insurance in India but none of the acts describes ‘insurable interest’. The doctrine of ‘insurable interest’ has become sine qua non for the life insurance business and traces its roots to the English laws. Since then till date the doctrine

5. Life Assurance Act, 1774
6. The act stated: Whereas it hath been found by Experience, that the making of Insurances on Lives, or other Events, wherein the assured shall have no Interest, hath introduced a mischievous Kind of Gaming: For Remedy whereof, be it enacted
7. 94 U.S. 457 (1876)
8. Ibid at p. 460
10. N. Y. Ins. Law § 3205 (McKinney 2000); Pa. Stat. Ann. tit. 40, § 512 (West 1999) ("N person shall cease to be insured the life of another, unless the beneficiary named ... has an insurable interest in the life of the insured.")
11. (1854) 15 CB 364 (Ex.Ch.)
14. Ibid.
15. Par 159(2) VVG of German Insurance Contract Act of 1908.
has been followed without much change, though the society has moved a lot ahead.

THE NEW DIMENSIONS

The following need consideration and deliberation in tracing the new dimensions for the doctrine of ‘insurable interest’.

A family love and affection insurable interest in the life of another, based upon a close family relationship, may be created either by consanguinity or affinity. It is predicated on the assumption that such love and affection normally exists between close family members, and that this familial love and affection will normally provide adequate social and legal safeguards against premeditated homicide by another family member to procure substantial life insurance proceeds from an untimely or premature death. But at the same time this old principle might not be true in the light of the changing moralities in the youths today. The increasing number of divorced couples, many entering second or third marriage after the separation with the previous one once again puts a question mark on this principle to be accepted.

Under the modern majority view, each spouse in a life insurance contract is considered to have a love and affection insurable interest in the life of the other spouse.

But there is a difference of opinion on the fact that whether such an insurance policy can be taken on the life of the other spouse without his or her consent. This can be seen and understood from the case of Ramey v. Carolina Life Insurance Co., wherein a wife procured a life insurance policy on the life of her husband without his knowledge and consent, and then she poisoned him with arsenic. The husband suffered serious injuries and subsequently sued the life insurance company, alleging that the insurer knew of his lack of knowledge and consent at the time his wife procured the life insurance policy. The South Carolina Supreme Court affirmed a judgment in favor of the plaintiff husband based upon the following: “It is a general rule that a policy of life insurance taken out without the knowledge or consent of the insured person is against public policy and unenforceable. A wife, for example, cannot be permitted to obtain insurance on the life of her husband without his knowledge and consent; such a practice, it has been deemed, might be a fruitful source of crime.”

The Indian legislations are still silent in this regard and no case has come up before the Supreme Court on this point.

Another very interesting question which arises out of this principle is that if a love and affection insurable interest generally exists between the spouses based upon their marriage, what happens in the event of divorce? As per the followed procedure the insurable interest is only looked into at the time of taking the policy and not at the time of claiming. But in the event of divorce the insurable interest also comes to an end, but this is not taken into consideration because of the long prevailing practice which would again render such insurance contracts as wagers.

The insurable interest doctrine is also silent in cases of non-traditional families or de facto families. Although the Indian Contract Act, 1872 recognizes the existence of de facto families and makes the de facto husband liable for the acts of the de facto wife but when the same is not recognized by insurance contract. This too needs reconsideration. The courts and the law makers need to examine this point closely and should not differentiate between a legal marriage and a couple living together without the stamp of the law when the issue involves unmarried cohabitants who have entered into a civil union or a domestic partnership which is well recognized by the laws prevailing in United States. Even though such relations might be able to show love and affection and economic interest but still are not recognized by insurance contracts.

Finally does a fiancé have an insurable interest in her fiancé, and vice versa? Although some courts in America have recognized a love and affection insurable interest of a fiancé in the life of her fiancé, a fiancé is not usually considered to be economically dependent on the insured if a life insurance policy expressly requires such economic dependency for its beneficiaries. In an early landmark case of Chisolm v. National Capitol Life Insurance Co., Miss Chisolm, who was engaged to Mr. dark, became concerned about the possibility of her fiancé’s untimely death, and obtained an insurance policy on his life, paying all the premiums herself. Subsequently, Mr. Clark died before their marriage was ever solemnized. The Supreme Court of Missouri held that Miss Chisolm could recover the life insurance proceeds, and this would not constitute a wagering contract because a valid contract of marriage was subsisting between them. Had the fiancé lived and violated the marriage contract, she would have had a breach of promise to marry action for damages. Had he lived then as his wife, she would have been entitled to support. Had the defendant, life insurance company been as willing to observe and fulfill its obligations as it was to receive premiums, then this case would have never occupied the time of the courts.

CONCLUSION

It is observed that the law of life insurance on insurable interest in India is in a state of chaos. Though the roots of the doctrine of ‘insurable interest’ lies in the English law but at the same time the various developments taking place in other parts of the world also have to be looked into and the changing social conditions need to be taken into account to redefine the doctrine of ‘insurable interest’. Insurable interest forms the life line of all life insurance contracts and therefore it is very essential to regulate and define this doctrine in light of the above highlighted issues. It is also necessary to make provisions for the same. Finally, based upon the crucial underlying importance of the insurable interest requirement, it is strongly supported that the doctrine of ‘insurable interest’ should be redefined to incorporate the social changes and accordingly the legislative and regulatory texts should be developed to regulate its use by the insurance sector.

16. 135 S.E.2d 362.
17. 52 M o. 213 (1873).