Fordham Law Review

Volume 9 | Issue 3 Article 6

1940

# Legal Effects of Delay in Acceptance of Insurance Applications

## LEGAL EFFECTS OF DELAY IN ACCEPTANCE OF INSURANCE APPLICATIONS

The question presents itself whether an insurance company is liable in an action for neglect or unreasonable delay in acting upon an application for insurance where, but for such delay, the application would have been approved and the insurance issued in time to have protected the applicant against a loss which occurred during the period of such unreasonable delay.

There is a definite divergence of legal opinion as to the solution of this problem which, despite numerous decisions over a period of time from the highest courts of many jurisdictions, remains today without any definite solution. In the most recent reports three courts before which the problem was squarely presented arrived at their results on widely different legal reasoning. This was true notwithstanding that in two instances the court held against the insurer.[1]

The doctrine that an insurance company is under an affirmative legal duty to act promptly on an application of insurance where there is nothing further for the applicant to do and to notify the applicant of acceptance or rejection is not of recent origin. It was first expressly laid down by the Supreme Court of Hawaii in 1897.[2] But it was not until 1912, in *Boyer v. State Farmers Mutual Hail Ins. Ass'n*[3] followed a year later by *Duffie v. Banker's Life Ass'n*[4]

1. Zayc v. John Hancock Mutual Life Ins. Co., 338 Pa. 426, 13 A. (2d) 34 (1940), holding that the insurance company is not liable in negligence; Behken v. Equitable Life Assurance Soc., 293 N. W. 200 (Sup. Ct. N. D. 1940), holding the insurance company is liable in negligence; American Life Ins. Co. v. Hutcheson, 109 F. (2d) 424 (C. C. A. 6th, 1940), holding the insurer liable on theory of contract.

2. Carter v. Manhattan Life Ins. Co., 11 Hawaii 69 (1897). This, a leading case, relied upon dicta in the following cases: Stewart v. Helvetia Swiss Fire Ins. Co., 102 Cal. 218, 36 Pac. 410 (1894); Trask v. German Ins. Co., 53 Mo. App. 625 (1893); Walker v. Farmer's Ins. Co., 51 Iowa 679, 2 N. W. 583 (1873); Perkins v. Washington Ins. Co., 4 Cow. 645 (N. Y. 1825).

3. Boyer v. State Farmer's Mutual Hail Ins. Co., 86 Kan. 442, 121 Pac. 329 (1912). In this case the plaintiff on July 7th, 1909, made an application to defendant's agent for hail insurance on a growing crop and gave a note for the premium. The agent did not send the application or the note to the company until July 10th, and they were not received by the company until July 12th. On July 11th, a violent hailstorm totally destroyed the crop. Had the agent promptly sent the application to the company it would have been received and a policy would have been issued before the loss.

4. Duffie v. Banker's Life Ass'n of Des Moines, 160 Iowa 19, 139 N. W. 1087 (1913). Joseph M. Duffie, on June 8th, 1911, made an application for life insurance to the defendant's agent who failed to send the application to the defendant's home office after Duffie had undergone a physical examination by defendant's physician. Duffie died on July 9th, 1911, and his widow named as beneficiary in the application brought action to recover damages on the theory of negligence. Upon her appointment as administratrix she filed a petition of intervention wherein she prayed for damages to the estate. A verdict was directed for the defendant, but on appeal it was held that whether there was negligence on the part of the defendant in failing to act upon the application was a question for the jury to determine. It further held that as the injury, if any, was to the decedent, Mrs. Duffie, suing as administratrix and not as the proposed beneficiary, could maintain an action for damages.

that the doctrine gained its real impetus in the United States. Thereafter, until the beginning of this decade, a definite trend in the law attached liability to the insurance company. But since 1930, a number of cases indicate that the legal tide may be turning against the liability of the insurance company because of mere inaction.[6] This recent development in favor of insurance companies may be a result of a reconsideration of the rights and duties of the parties and a studied analysis of the underlying legal factors involved, as well as the social and economic forces. It is therefore timely to consider the variant theories which are used to create or deny liability. The jurisdictions which have allowed liability against the insurance companies have based their decisions on widely differing legal theories. Whether this demonstrates a weakness in the reasoning of these holdings it is difficult to say in some instances, but such disparity of logic is definitely apparent in others. The theories advanced for holding the company liable can be placed into these general groups, *ex contractu, quasi ex contractu* and *ex delicto.*

*Liability ex contractu*—Considering the liability of the insurance company as one which arises out of contract, it has been held that continued silence by an insurance company after submission of the application ripens into a binding contract. The application is regarded as an offer to the insurance company in the business of soliciting such offers and which is impliedly stating that a failure to reject such an offer within a reasonable time may be construed as an acceptance which binds the company in accordance with the contract terms.[7] This argument is unsound and in violation of basic principles of contract law.[8]

5. The historical parents of the doctrine, the Boyer case, note 3, *supra,* and the Duffie case, note 4, *supra,* had their influence felt in many jurisdictions. Among those allowing recovery are included Alabama, California, Colorado, Idaho, Iowa, Kansas, Kentucky, Louisiana, Michigan, Nebraska, North Carolina, North Dakota, Oklahoma, Washington, Wisconsin, 15 A. L. R. 1026 (1918); Zayc v. John Hancock Mut. Life Ins. Co., 338 Pa. 426, 13 A. (2d) 34 (1940) n. 1; see also Reck v. Prudential Life Ins. Co., 116 N. J. L. 444, 184 Atl. 777 (1936), holding that under the terms of the application, approval could be assumed unless notification of rejection was made within a reasonable time.

6. Liability has been negatived in the following jurisdictions: Arkansas, Connecticut, Illinois, Indiana, Mississippi, Minnesota, Pennsylvania, Texas, and West Virginia. Zayc v. John Hancock Mutual Life Ins. Co., 338 Pa. 426, 13 A. (2d) 34 (1940) n. 2.

Several jurisdictions have refused to take a definite or final position for one reason or another. They include: Ohio [Veser v. Guardian Life Ins. Co., 44 Ohio App. 29, 185 N. E. 565 (1932)]; Montana [Weaver v. West Coast Life Ins. Co., 99 Mont. 296, 42 P. (2d) 729 (1935) (on the ground that no damage was shown)]; Missouri [Forck v. Prudential Ins. Co. of America, 66 S. W. (2d) 983 (Mo. App. 1933) (court tends toward liability); Mathews v. N. Y. Life Ins. Co., 128 S. W. (2d) 327 (Mo. App. 1939) (tends toward liability on the basis of estoppel)]; Wyoming [Dunne v. Western Nat. Life Ins. Co., 35 Wyo. 59, 246 Pac. 246 (1926) (where there is a failure to pay a premium no liability attaches)].

7. Preferred Acc. Ins. Co. v. Stone, 61 Kan. 48, 58 Pac. 986 (1899); Robinson v. U. S. Ben. Soc., 132 Mich. 695, 94 N. W. 211 (1903); and very recently reaffirmed in Amer. Life Ins. Co. of Ala. v. Hutcheson, 109 F. (2d) 424 (C. C. A. 6th, 1940).

8. RESTATEMENT, CONTRACTS (1932) § 72; 1 WILLISTON, CONTRACTS, 891 ff. (1936);

If the company is dilatory in indicating its decision on the application, a clear remedy is open to the applicant: he may insist upon prompt action, or withdraw his offer and reclaim the down payment. But the applicant cannot rely on the supineness of the company, coupled with a failure to act on his own part, and erect a binding contract out of the dual failure to act.[9]

It has been held that there is nothing about an insurance application which ought to take it out of ordinary, established rules of contract. In *Swentusky v. Prudential Life Ins. Co.*,[10] the court argued, despite a recognition that the failure to act upon the policy may result in a loss to the applicant and to potential beneficiaries, that these hardships incident to delay are not peculiar to the insurance calling. An offer to purchase needed goods, in anticipation of a rise in prices, may result in loss by the failure of the offeree to act upon it within a reasonable time. Yet no liability would attach in such a situation as a result of silence on the part of the offeree.

Of course it is well established that there may be a duty to speak under special circumstances[11] but this special rule does not seem to have any application to the problem herein considered. Indeed, the special circumstances necessary to create a duty to speak are generally negatived in the application by express conditions set down therein. Such application usually contains the express reservation that the company shall not be bound until the application is approved, the policy issued, and the first premium paid. The attaching of liability to the insurer on the theory of acceptance by silence may be explained, in part, by the fact that the court is forced into the position of either holding the company liable on that theory or not at all since the action was instituted against the company on the theory of contract.

Another ingenious method of erecting a contractual liability against the insurance company runs through the cases. It has been held that the retention of payments made in advance beyond a reasonable time constitutes an acceptance.[12] There can be no question that, unless otherwise expressly agreed, the payment made upon the submission of the application for a policy is to be returned if there is no acceptance. But is the failure to return a premium an indication of an acceptance? The argument is offered that the company in

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Corbin, *Offer and Acceptance and Some of the Resulting Legal Relations* (1917) 26 YALE L. J. 1691.

9. Gold Life Ins. Co. v. Mayes, 61 Ala. 163 (1878). *See also* Savage v. Prudential Life Ins. Co., 154 Miss. 89, 121 So. 487 (1929); Munger v. Equitable Life Assur. Soc. of U. S., 2 F. Supp. 914 (D. C. Mo. 1933).

10. Swentusky v. Prudential Ins. Co. of America, 116 Conn. 526, 165 A. 686 (1931).

11. Corbin, *supra* note 8.

12. Preferred Acc. Ins. Co. v. Stone, 61 Kan. 48, 58 Pac. 986 (1899); Robinson v. U. S Ben. Soc., 132 Mich. 695, 94 N. W. 211 (1903); Great Southern Life Ins. Co. v. Dolan, 239 S. W. 236 (Tex. Civ. App. 1922); In Cloyd v. Republic Mutual Fire Ins. Co., 137 Kan. 869, 22 P. (2d) 431 (1933) and Stearns v. Merchant's Life & Cas. Co., 38 N. D. 524, 165 N. W. 568 (1918) acceptance was found in express agreement that payment would be refunded if no policy was issued. See also RESTATEMENT, CONTRACTS § 72 (2).

fact has not "retained" the money as an act of acceptance of the offer but has merely failed to return it and that the applicant might have it back on demand at any time.[13] An attempt to spell out a mutual intent to enter into a contract under such circumstances woud be a distortion of the legal effects of the retention of a premium or the tardiness of the company in returning it to the applicant.

Sometimes elements of estoppel have been resorted to in seeking to establish a basis for liability against the insurer.[14] Professor Vance[15] has stated that in order to establish an estoppel the one making such claim must prove: (a) that a false representation was made as to some fact material to the contract, (b) that such representation was made with the expectation that it would be acted upon, (c) that claimant in good faith did rely upon it, and (d) that in so relying he acted to his prejudice. It can be seen that the elements of estoppel are lacking in the ordinary case where an action is brought against the insurer for his failure to act upon the application within a reasonable time. The insurer certainly cannot be held to have made a false representation of fact. The fact that an applicant may have been "lulled into a sense of security" from the mere fact that he filled out an application cannot work an estoppel against the insurer.[16]

An implied in fact agreement is another legal formula which some jurisdictions have used as a means of attaching liability to the insurer.[17] However, a contract implied in fact, no less than an express contract, has its inception in the intent of the parties. It necessitates a mutual meeting of the minds of the parties coupled with an intent to promise and to be bound.[18] While there can be no quarrel with a feeling that the insurance company ought to act upon the application promptly and forward word of acceptance or rejection to the applicant, any attempt to work out an implied in fact contract is weak. No such agreement is expressly made and no unexpressed intent to make such agreement in fact could be or should be implied. Indeed it has been suggested that, if the courts should decide that there is an implied contract, within a

13. (1935) 3 U. OF CHI. L. REV. 39, 47.

14. Preferred Acc. Ins. Co. v. Stone, 61 Kan. 48, 58 Pac. 986 (1899); Robinson v. U. S. Ben. Soc., 132 Mich. 695, 94 N. W. 211 (1903); Great Southern Ins. Co. v. Dolan, 239 S. W. 236 (Tex. Civ. App. 1922); Mathews v. N. Y. Life Ins. Co., 128 S. W. (2d) 327 (Mo. App. 1939). *Cf.* Gonsoulin v. Equitable Life Assur. Soc. of U. S., 152 La. 865, 94 So. 424 (1922).

15. VANCE, INSURANCE (2d ed. 1930) § 138, p. 514 ff.

16. More v. N. Y. Bowery Fire Ins. Co., 130 N. Y. 537, 29 N. E. 757 (1892); Winchell v. Iowa State Ins. Co., 130 Iowa 189, 72 N. W. 503; Conn. Mutual Life Ins. Co. v. Rudolph, 45 Tex. 454; Reed v. Prudential Ins. Co., 229 Mo. App. 90, 73 S. W. (2d) 1027 (1934). *See also* note 19.

17. Fox v. Volunteer State Life Ins. Co., 185 N. C. 121, 116 S. E. 266 (1923); De Ford v. N. Y. Life Ins. Co., 75 Colo. 146, 224 Pac. 1049 (1924); Columbian Nat. Life Ins. Co. v. Lemmons, 96 Okla. 228, 222 Pac. 255 (1923); Kukuska v. Home Mutual Hail-Tornado Ins. Co., 204 Wis. 166, 235 N. W. 403 (1931).

18. 1 WILLISTON, CONTRACTS (1936) § 83.

short time all insurance companies would incorporate in their application blanks stipulations expressly negativing such agreement.[19]

*Liability quasi ex contractu*—At least one court seeks to hold the insurance company upon a theory of quasi contract.[20] If unjust enrichment of the insurance company could be shown this argument may be tenable. Some theory of quasi contract must be invoked which will create liability for the face value of the policy. But the fact that a conditional deposit was paid does not spell out a case of unjust enrichment, at least in excess of amount of premium paid and unjustly retained. The plaintiff is always entitled to demand his money back, no other special circumstances appearing. From the foregoing, it can be seen that the courts have encountered considerable difficulty in attempting to hold the insurer liable on any theory of contract whether express, implied in fact or implied in law.

*Liability ex delicto*—The *Duffie* case[21] formulated a tort liability against the insurance carriers based on the duty of reasonable care. This theory was seized upon by several courts but again weaknesses in its formulation may be noted. While it is not difficult to prove dilatory methods of the insurance company in acting upon the policy, courts are unable satisfactorily to create a legal duty arising out of such delay. The *Duffie* case first suggested that an insurance company doing business under a franchise has assumed a duty toward the public, and several jurisdictions have followed this line of reasoning.[22] But does the franchise *per se* establish any such duty? If so it applies to other corporations as well, operating under a franchise. It must be something more than the *franchise* that creates the special duty to act and to act promptly. The franchise to engage in the insurance calling should impose no more duty to act without delay upon an application for insurance than would be required of a bank receiving an application for a loan.[23]

A closely related argument is that such companies are under a duty to act promptly since the insurance business is one that is greatly affected with the public interest.[24] It is undisputed that the public interest is great in such cases.

19. (1927) 75 U. PA. L. REV. 204, 224.

20. Kukuska v. Home Mutual Hail-Tornado Ins., 204 Wis. 166, 235 N. W. 403 (1931).

21. Duffie v. Banker's Life Ass'n, 160 Iowa 19, 139 N. W. 1087 (1913).

22. De Ford v. N. Y. Life Ins. Co., 75 Colo. 146, 224 Pac. 1049 (1924). Wilken v. Capital Fire Ins. Co., 99 Neb. 828, 157 N. W. 1021 (1916); Columbian Nat'l Life Ins. Co. v. Lemmons, 96 Okla. 228, 222 Pac. 255 (1923).

23. (1935) 3 U. OF CHI. L. REV. 39, 51. Swentusky v. Prudential Life Ins. Co. of America, 116 Conn. 526, 165 Atl. 686 (1933); Miller v. Illinois Life Ins. Co., 255 Ill. App. 586 (1930); Amer. Life Ins. Co. v. Nabors, 124 Tex. 221, 76 S. W. (2d) 497 (Tex. Comm. App. 1934).

24. Wallace v. Metropolitan Life Ins. Co., 212 Wis. 346, 248 N. W. 435 (1933), De Ford v. N. Y. Life Ins. Co., 75 Colo. 146, 224 Pac. 1049 (1924); Wilken v. Capital Fire Ins. Co., 99 Neb. 828, 157 N. W. 1021 (1916); Fox v. Volunteer State Life Ins. Co., 185 N. C. 121, 116 S. E. 266 (1923); Security Ins. Co. v. Cameron, 85 Okla. 171, 205 Pac. 151 (1922); Columbian Life Ins. Co. v. Lemmons, 96 Okla. 228, 222 Pac. 255 (1924); Dyer v. Missouri State Life Ins. Co., 132 Wash. 378, 232 Pac. 346 (1925).

But no more so than in others.[25] True, the duty of the insurance company to act may be the subject of legislation and is seemingly within the police powers of the State.[26] But this provides no basis for the exercise of the legislative function by the court and such judicial legislation has evoked criticism.[27]

The same idea of imposed responsibility, due to the nature of the insurance business, is found in the leading *Boyer* case.[28] Herein it is stated arbitrarily that there is a duty on the insurance agent to forward the application to the company. The court reasoned that there is sufficient damage to be apprehended from delay in passing on the application and that a reasonably prudent businessman would have acted with diligence. The court without setting forth any reasons, argues that if the agent alone be considered it is clear enough that he would be liable if his negligent retention of the application prevented its timely acceptance. Since the agent is merely the arm of the defendant,—so runs the argument—the obligation to accept or reject is ultimately the obligation of the defendant. Thus, it concluded that the duty of the defendant to secure prompt transmission of the application from the solicitor's field to the central office is quite apparent. It is to be regretted that the court treated the problem with such brevity and without explaining the reasons that prompted him to reach the result.[29]

*Zayc v. John Hancock Mutual Life Insurance Co.*[30] and *Behken v. Equitable Life Assurance Society*[31] raise the problem of the proper party to bring the action. This is limited only to cases involving life insurance, for if any duty in other insurance relations is owing, it is to the applicant. The aforementioned cases prefer to give the beneficiary the right to bring the action. But the majority of jurisdictions[32] have held that the decedent's estate is the proper

25. It has been held that there is no apparent reason why an insurance contract should be regarded as of any more interest to the public than a contract of employment. It is of as much importance to the public that a person and his dependents have support during his lifetime, by wages or salary as that his beneficiaries have a competency, through insurance after his death. It has never been held that delay in passing upon an application for employment affected the public interest to the extent that it made employers liable for all damages arising from such delay. Thornton v. Nat. Council Junior Order United American Mechanics, 110 W. Va. 412, 158 S. E. 507 (1931). See also Swentusky v. Prudential Life Ins. Co., 116 Conn. 526, 165 Atl. 686 (1933); Amer. Life Ins. Co. v. Nabors, 124 Tex. 221, 76 S. W. (2d) 497 (1934); Schliep v. Commercial Cas. Ins. Co., 191 Minn. 479, 254 N. W. 618 (1934).

26. Nat. Union Fire Ins. Co. v. Wanberg, 260 U. S. 71 (1922); German Alliance Ins. Co. v. Kansas, 233 U. S. 389 (1914).

27. Munger v. Equitable Life Assur. Soc., 2 F. Supp. 914 (W. D. Mo. 1933).

28. Boyer v. State Farmer's Mutual Hail Ins. Co., 86 Kan. 442, 121 Pac. 329 (1912).

29. (1927) 75 U. OF PA. L. REV. 207, 224.

30. 338 Pa. 426, 13 A. (2d) 34 (1940).

31. 293 N. W. 200 (Sup. Ct. N. D. 1940).

32. Royal Neighbors of America v. Forlenberry, 214 Ala. 787, 107 So. 846 (1926); Veser v. Guardian Life Ins. Co., 144 Ohio App. 293, 185 N. E. 565 (1931); Stray v. Western States Life Ins. Co., 163 Wash. 329, 300 Pac. 1046 (1931); Forck v. Prudential

party to bring the action since no relationship exists between the insurer and the beneficiary. It would seem that the decedent's estate could claim as damages only the amount of the premium that has been paid.[33] It is submitted that the beneficiary named in the application is the proper party to bring the action, for then the amount of the policy is the measure of damages, and the unjust result which follows an action by the decedent's estate is done away with.[34]

Despite the technical difficulties of formulating legal theories which render the insurance company liable, it is submitted that the rules holding the insurance companies liable for their delay are economically desirable. Courts are aware that insurance plays an extensive part in our complex civilization and that the business is quasi-public in character. The tendency is to shift, wherever possible, the burden of loss due to accident or catastrophe from the individual to the community, or a group within the community. In some instances this policy has been carried into effect by legislation, as in Workmen's Compensation Laws, but the courts have also been ready to further it in their treatment of the rules of common law.[35]

The soundest solution would appear to be the enactment of proper legislation stating precisely duties of insurance companies in the matter of insurance applications. If the insurer is to be held liable, the statute should specifically state at what point and under what circumstances such liability is to arise. North Dakota has adopted a statute[36] which was definitely upheld as constitutional in the United States Supreme Court.[37] The suggested statute should grant the right of action to the named beneficiary, if one appears, since this would be in accordance with the decedent's express wishes and would prevent creditors of the decedent from satisfying their claims out of this fund, thereby following the rule in all cases where the policy is actually issued.

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Ins. Co., 66 S. W. (2d) 983 (Mo. App. 1933). *See also* Duffie v. Banker's Life Ass'n, 160 Iowa 19, 139 N. W. 1087 (1913); De Ford v. N. Y. Life Ins. Co., 75 Colo. 146, 224 Pac. 249 (1924); Miller v. Illinois Life Ins. Co., 255 Ill. App. 586 (1930).

33. Thornton v. Nat. Council Junior Order United Amer. Mechanics, 110 W. Va. 412, 158 S. E. 507 (1931).

34. (1927) 75 U. OF PA. L. REV. 207, 225.

35. *Ibid.*

36. N. D. COMP. LAWS ANN. (1913) § 4902.

37. Nat. Union Fire Ins. Co. v. Wanberg, 260 U. S. 71 (1932). *See also* German Alliance Ins. Co. v. Kansas, 233 U. S. 389 (1914), settles right of a state legislature to regulate conduct by insurance corporation as a business affected with public interest.