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Insurance -- 1954 Tennessee Survey

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INSURANCE—1954 TENNESSEE SURVEY

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I. LIABILITY INSURANCE

A. *Notice of Claims*

There were only two cases reported during the survey period on the subject of liability insurance. In the first of these, *Rural Education Ass'n, Inc. v. American Fire & Casualty Co.*,[1] the insured had notice of an accident on the day it occurred. Suit for injuries growing out of the accident was filed nearly seven months later, and not until the day after suit was filed did the insured notify the insurer of the accident. After judgment was obtained against it, the insured brought the present suit against its insurer. The insurance policy required that notice be given "as soon as practicable" following the accident. The district court held that a delay of seven months constituted a breach of this provision, and the Court of Appeals for the Sixth Circuit affirmed. In the absence of excuse for the delay or of waiver by the insurer, it is generally recognized that proper notice of claims is a condition precedent to insurance coverage.[2] No circumstances were shown in the present case to take it out of the general rule.

B. *Subrogation*

In the case of *Vaughn v. Gill*,[3] the liability insurance carrier of a tortfeasor sought, by subrogation, to recover contribution from an alleged joint tortfeasor. While the case is of interest principally in its discussion of the right of contribution,[4] the Supreme Court held that the original bill was defective in that it failed to state that it was brought by or at the instance of the insurer. The apparent party complainant was the named insured. In the body of the bill, however, was an averment that a right of subrogation in favor of the company existed and that the company "is subrogated" to the insured's rights. The Supreme Court said, "There is no assertion that the bill was filed at the direction of the Insurance Company, nor is there any allegation in the bill that any one authorized to act for the Insurance Company had exercised its right of subrogation under the policy."[5]

It is unfortunate that the court did not take this opportunity to clarify the procedural problem as to the proper method of bringing

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1. 207 F.2d 596 (6th Cir. 1953).
2. Phoenix Cotton Oil Co. v. Royal Indemnity Co., 140 Tenn. 438, 205 S.W 128 (1918); Foreman v. Union Indemnity Co., 12 Tenn. App. 89 (E.S. 1928).
3. 264 S.W.2d 805 (Tenn. 1953).
4. See the Survey article on Torts, *infra* p. 951.
5. 264 S.W.2d at 807.

subrogation suits in this state. Unlike the statutes in most of the states, the Tennessee "real party in interest" statute[6] does not clearly state how a suit brought by one person for the benefit of another should be captioned.[7] Many years ago the Supreme Court held that a subrogation suit could be maintained by the insurer in the name of the insured, and apparently it did not require that there be any averment as to the beneficial party in interest.[8] There would seem to be little doubt, however, that an insurer could bring such a suit in its own name also, and likewise that the insurer could in any subrogation suit be required to give bond for costs, even if it sued in the name of its insured.[9]

The Supreme Court in the present case did not cite its earlier decision; and its treatment of the matter was brief. The court apparently disapproved of the practice of bringing a subrogation suit in the name of the insured only, at least without a specific averment in the pleadings as to the nature of the action. No authority of any sort was cited, however, and the matter must still be regarded as being in doubt. It is to be hoped that the court will clarify the point in the

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6. TENN. CODE ANN. § 8619 (Williams 1934).

7. In cases involving assignments, it is generally considered that the assignee may sue (1) in his own name, (2) in the name of the assignor, or (3) in the name of the assignor for the use of the assignee. See CARUTHERS, HISTORY OF A LAWSUIT 49-50 (7th ed., Gilreath, 1951); HIGGINS & CROWNOVER, TENNESSEE PROCEDURE IN LAW CASES §§ 334-36 (1936).

8. Anderson v. Miller, 96 Tenn. 35, 33 S.W. 615 (1896); Lancaster Mills v. Merchants' Cotton-Press & Storage Co., 89 Tenn. 1, 58, 14 S.W. 317 (1890). See also City of Nashville v. Mason, 7 Tenn. Civ. App. 444 (1917).

9. In most types of subrogation suits (partial losses being the principal exception), the insurer would be the real party in interest and would constitute "the real plaintiff of record" under TENN. CODE ANN. § 8619 (Williams 1934). As such the insurer would be liable for costs under TENN. CODE ANN. § 8620 (Williams 1934).

A problem of considerable importance in jury cases is whether the defendant may show, either in qualifying the jury or by evidence, that the real plaintiff is a subrogation carrier. Some of the circuit courts do not permit this practice. The appellate courts do not appear to have considered the point in Tennessee. *Anderson v. Miller*, 96 Tenn. 35, 33 S.W. 615 (1896) is not authority forbidding the practice; the court in that case was dealing with the substantive right of subrogation, not with matters of practice. It struck as insufficient a plea that the plaintiff, who was the insured, had been compensated by insurance; no question was raised as to who was the real party in interest. In *Harriman & N.R.R. v. McCartty*, 15 Tenn. App. 109, 113 (E.S. 1932), the Court of Appeals held that it was improper to ask a plaintiff how much fire insurance he carried. The reasons stated, however, were that such testimony did not bear on the value of the property destroyed, and that payment to the plaintiff by an insurer did not bar a suit by him on behalf of the insurer. The opinion does not reveal whether in fact the plaintiff was so suing, and the matter of identifying the real party in interest does not seem to have been raised. In view of the wording of TENN. CODE ANN. § 8619 (Williams 1934), it would seem proper to permit a defendant to show to a jury that the suit is brought by an insurer, for the purpose of ascertaining whether any jurors had an interest in "the real plaintiff of record." In many of the other states having "real party in interest" statutes, subrogation actions are required to be brought directly in the name of the insurer, so that the problem here stated does not arise. Notes, 96 A.L.R. 864, 875-79 (1935), 157 A.L.R. 1242, 1247-51 (1945).

future, or that the legislature will make the "real party in interest" statute more explicit.

II. Fire, Theft and Casualty Insurance

A. *Fire Insurance*

In the case of *Frederick v. New England Fire Ins. Co.*,[10] the Court of Appeals reviewed a jury verdict in favor of the insured on a fire insurance policy. Proof of loss had been filed with the company following the fire. Thereafter the company had the insured examined under oath as to the circumstances surrounding the loss. When the company later denied liability, the insured sued, and the company defended on the ground that the insured either burned the property herself or had it burned. Conflicting testimony was introduced at the trial as to the circumstances under which the fire occurred. The trial court set aside one jury verdict for the insured, but approved a second such verdict. The Court of Appeals held that there was ample evidence to show that the insured did not burn the property and that she was not present when the fire occurred. It accordingly affirmed the verdict.

In this case, the Court of Appeals affirmed an award by the jury of a statutory penalty.[11] The property which burned was subject to a mortgage, and the fire policy contained a standard mortgage clause. Interest on the mortgage continued to accrue after the fire, and the insured was accordingly faced with an increasing interest liability because of the company's refusal to pay on the policy. She had been forced to incur legal expenses and other costs also because of this refusal, and the Court of Appeals held that under these circumstances, the penalty could properly be awarded by the jury.[12]

An interesting case dealing with waiver and estoppel was decided by the United States District Court for the Eastern District of Tennessee.[13] In this case a policy of fire insurance on vehicles and equipment was issued by the company's agent five days before the application for the policy was filled out. The agent was not a licensed fire insurance broker. After delivering the policy, he interviewed the insured and obtained information for the application from him, making pencil notes thereon. The insured signed the form, and the agent later filled in the blanks in type, leaving his pencilled notes on the face of the application. Many of the typed answers were supported

10. 259 S.W.2d 879 (Tenn. App. M.S. 1953).
11. Tenn. Code Ann. § 6434 (Williams 1934).
12. The penalty is allowed only if the court or jury finds that the insurer's failure to pay was in bad faith, and, in addition, that the insured has sustained additional loss or expense by the delay. The amount of the penalty is measured by such additional expenses and damages, up to a maximum of 25% of the policy proceeds.
13. Trantham v. Canal Ins. Co., 117 F. Supp. 241 (E.D. Tenn. 1953).

by no pencil notes, and some of the pencilled entries were unintelligible even to the agent, who testified on the trial.

Eight months after the application was received by the company, the insured sustained a fire loss. The company for the first time then asserted that the application contained misrepresentations which vitiated the policy. The company insisted that it relied on the application, not in issuing the policy, but in refraining from cancelling the same, alleging that it would have cancelled the policy had the application revealed the truth about certain prior losses of the insured. There was testimony in the record, however, that the soliciting agent knew the true facts concerning such losses when he filled out the application.

The district court very properly held that the company was estopped from asserting this defense, and that it had, by leaving the crudely-drawn application on file without inquiry for eight months, waived any right to question its contents. The condition of the application was sufficient to put the insurer on inquiry, and it was chargeable with knowledge of facts which such inquiry would have revealed, as well as with any knowledge which its agent may have had concerning the true facts.[14]

B. *Theft Insurance*

One of the most striking decisions on insurance during the survey period was that of the Supreme Court in *American Indemnity Co. v. Southern Missionary College.*[15]

In December 1950, the insurer issued to the college, a religious non-profit institution, a policy indemnifying it against "direct" losses from robbery or safe burglary occurring on its premises. The college conducted several mercantile enterprises for the benefit of its students and faculty, including a college bookstore. In July 1951, a subsidiary corporation for profit was organized to operate these mercantile enterprises. All of its stock was taken by the college, which in turn delivered to the subsidiary all of the assets of the bookstore and the other commercial ventures. The officers of the two corporations were identical. No change was made in the theft policy mentioned above.

In July 1952, the bookstore suffered a large burglary loss. The

14. See Hayes & Sons v. Stuyvesant Ins. Co., 194 Tenn. 35, 250 S.W.2d 7 (1952), discussed in the 1953 *Survey,* 6 VAND. L. REV. 1073-74 (1953) (knowledge of automobile agency as to actual use of vehicle imputed to insurer where agency solicited application). Had the agent been a licensed fire insurance broker in the principal case, the exception in TENN. CODE ANN. § 6087 (Williams 1934) would have been applicable, and the broker's knowledge would not have been imputed to the insurer; this section makes the broker the agent of the applicant for insurance. All other soliciting agents are made the agents of the insurance company in all matters pertaining to the application and the policy.

15. 195 Tenn. 513, 260 S.W.2d 269 (1953).

college insisted that the theft policy was applicable to the loss, and in its original bill filed in the case there was an averment that the college had sustained a burglary loss on its premises. The insurer demurred on the grounds that the bookstore was owned by the subsidiary, an entirely different entity from the college, and that the policy did not cover this subsidiary and was not issued to it. The chancellor overruled this demurrer but permitted an appeal from his ruling.

In a split decision, four members of the Supreme Court sustained the chancellor's ruling and held the demurrer insufficient. The majority opinion stated that the two corporations were "practically indistinguishable" except in name,[16] and that the parent stockholder had an insurable interest in the property of its subsidiary which was stolen. The court "pierced the corporate veil" and held the insurer liable. The dissenting opinion insisted that no property owned by the insured college had been taken, and that while the college did have an insurable interest in the stolen property, it had not insured that interest. The loss was that of the owner of the property, which was the subsidiary, and there was no "direct" loss to the insured.

Insofar as the demurrer was concerned, the result reached may have been proper, since the original bill alleged a direct loss to the insured. This allegation was admitted by the demurrer for the purpose of testing the sufficiency of the pleadings, and for that reason the demurrer may not have been well taken.[17] The demurrer also appears to have alleged new facts and to have been defective as a "speaking" demurrer.[18]

The majority opinion, however, was not based on the pleadings but on the merits. Its rationale has received critical comment[19] for the court apparently failed to differentiate between two entirely different problems. The question of whether the college had an insurable interest in the subsidiary's property was not raised by the insurance company. The insurer admitted that the college did have such an interest, and the point is well settled that a parent corporation, being a stockholder, does have an insurable interest in the property of a subsidiary.[20] The parent has no title or ownership in such property, however. The question of whether the college owned the stolen property and sustained a "direct" loss by its theft presented an entirely different problem from that of insurable interest, and the Court left unanswered the insurer's contention that its policy was simply not

16. 195 Tenn. at 519, 260 S.W.2d at 272.
17. GIBSON, SUITS IN CHANCERY §§ 301-04 (4th ed., Higgins & Crownover, 1937).
18. GIBSON, SUITS IN CHANCERY § 307 (4th Ed., Higgins & Crownover, 1937).
19. 22 TENN. L. REV. 234 (1954).
20. Donaldson v. Sun Mut. Insurance Co., 95 Tenn. 280, 32 S.W. 251 (1895).

issued to the subsidiary but to the parent and did not cover this loss. The real controversy in the case would appear to have been, not one of insurable interest, but of the scope of coverage of the policy.

In another case dealing with theft coverage,[21] an insurer sought to avoid liability on a fidelity policy on the ground that the employer to whom the policy was issued had knowledge of prior defalcations by the employee. It is clear that the employer would have had a duty to the insurer to reveal this information if he possessed it.[22] The case, therefore, simply presented a factual issue as to whether the employer did have such knowledge. From the testimony, the district court had found in favor of the employer, and the Court of Appeals held that there was substantial evidence to support this ruling.

C. *Casualty Insurance*

In the interesting case of *Gillespie v. Federal Compress & Warehouse Co.*,[23] minority stockholders of a large cotton warehousing company launched a general attack on the company's insurance program. One major point of attack was that the company carried insurance on goods in transit, thereby assuming a risk which it was not obligated to incur. The stockholders also alleged that the company was carrying flood insurance with a company whose assets were insufficient to cover the risk.

The Court of Appeals found no merit in any of the various contentions of the stockholders. The warehousing company as bailee clearly had an insurable interest in the property and could insure its full value on behalf of the owners.[24] It was also held to have an interest in the goods in transit, particularly in view of the fact that losses often occurred under circumstances making it impossible to determine whether they occurred in transit or in the warehouse, and the company was entitled to protect itself on such claims. By statute, it was authorized to carry insurance,[25] so that its program was not *ultra vires,* as claimed by the stockholders.

Although the primary insurer was a small company, the court pointed out that it had reinsured the flood risk, which was substantial, with foreign insurance companies. In the reinsuring agreements, these companies agreed to submit to jurisdiction of the Tennessee courts, and the reinsurance was made available directly to the company. Without such provisions, of course, the insurers would have been

21. Pacific Employers Ins. Co. v. Banks-Olshine Co., 207 F.2d 595 (6th Cir. 1953).
22. Herbert v. Lee, 118 Tenn. 133, 101 S.W. 175, 121 Am. St. Rep. 989 (1906).
23. 265 S.W.2d 21 (Tenn. App. W.S. 1953).
24. Lancaster Mills v. Merchants' Cotton-Press & Storage Co., 89 Tenn. 1, 45, 14 S.W. 317 (1890).
25. TENN. CODE ANN. § 3831 (Williams 1934).

liable only to the primary insurer.[26] Under all of the circumstances, the court rejected the criticism of the complainants.

III. Disability and Health

Of considerable interest is the case of *King v. Mutual Life Ins. Co. of New York*[27] decided by the Northern Division of the United States District Court for the Eastern District. The action grew out of refusal by the insurer to pay monthly disability benefits claimed to be due under a policy providing for same in the event of total permanent disability. The defendant moved to strike three counts of the complaint. The first count sued for accrued monthly benefits together with interest, the Tennessee statutory penalty, plus a refund of premiums paid since commencement of disability. No attack was made upon this count. The second count asked for a decree of specific performance requiring the defendant to pay future monthly benefits as they became due and enjoining defendant from requiring plaintiff to attend physical examinations outside his home county and from requiring more than one annual examination. The third count sought to recover the present value of all future benefits including a death benefit, the recovery to be based upon the life expectancy of the insured. Apparently this count alleged a breach of the whole policy and a repudiation by defendant. However, it does not appear that it was alleged that the company had gone further than to deny that the defendant was disabled as claimed. The fourth count sought to rescind the entire contract and recover all premiums paid since the issuance of the policy, together with interest. The defendant moved to strike the second, third and fourth counts or in the alternative for summary judgments thereon. The court granted the motion to strike. It was recognized that under the Code of Tennessee, the insurance policy was to be treated as a Tennessee contract and governed by Tennessee law,[28] and the *Erie Railroad*[29] doctrine was noted. The motion as to the second count was granted upon the grounds that to permit the relief sought therein would require the court to remake the contract entered into between the parties. In sustaining the motion as to counts three and four, the court gave a common reason and also an additional reason as to each of them. The common reason assigned was that the Tennessee penalty statute[30] impliedly furnishes the exclusive remedy in such cases and by inference excludes allowance of damages for anticipatory breach sought in count three, and also the relief upon a theory of rescission as sought in count four. More significantly, the court points out that no Tennessee case was fonnd

26. Ruohs v. Traders' Fire Ins. Co., 111 Tenn. 405, 78 S.W. 85 (1903).
27. 114 F. Supp. 700 (E.D. Tenn. 1953).
28. Tenn. Code Ann. § 6086 (Williams 1934).
29. Erie R.R. v. Tompkins, 304 U.S. 64, 58 Sup. Ct. 817, 82 L. Ed. 1188 (1938).
30. Tenn. Code Ann. § 6434 (Williams, 1934), note 12 *supra.*

which treated a contract of this sort as an entire contract; but rather the Tennessee Supreme Court[31] has indicated that the causes of action for failure to make periodic payments are severable. Accordingly, the doctrine of anticipatory breach was held not to apply. In this reasoning, the court is clearly supported by the overwhelming weight of authority.[32]

The additional reason assigned for granting the motion as to count four was simply that there was no basis for inferring that there was any fraud in the inception of the contract and that the allegations failed to make out a case for rescission.

It accordingly appears that the court was correct in the conclusions reached and that the separate reasons assigned in support of his action as to counts three and four are sound. However, there would seem to be some question as to the soundness of the common reason. The Tennessee statute, permitting the imposition of a penalty where the refusal to pay is in bad faith, is simply a penal statute; on principle good faith or bad faith should have nothing to do with the legal questions as to whether or not such a contract is entire or severable, or whether or not facts justifying a rescission are made out.

Reserve Life Insurance Co. v. Boss[33] simply follows the general rule that where a loss is within the general coverage provisions of a policy of insurance the burden of proof is upon the insurer who seeks to avoid liability under an exception contained therein. On November 6, 1950, the insurer had issued a health policy covering plaintiff, his wife and daughter. The plaintiff's wife underwent an operation on June 9, 1951, and this suit was for medical expenses in connection therewith. Among the expenses which the insurer agreed to pay were those of any surgical operation "resulting from sickness . . . if the operation is performed after this policy has been in effect for six months or more from the date hereof." The insurer sought to deny liability under a provision of the policy exempting it from liability

31. Atkinson v. Railroad Employees' Mutual Relief Society, 160 Tenn. 158, 22 S.W.2d 631 (1929).

32. APPLEMAN, INSURANCE LAW AND PRACTICE § 11255 (1947); Notes, 81 A.L.R. 379 (1932), 99 A.L.R. 1171 (1935). It is interesting that among the cases indicating a contrary view is the case of *Federal Life Insurance Co. v. Rascoe*, 12 F.2d 693 (6th Cir.) *cert. denied*, 273 U.S. 722, (1926), which case was initially tried in the District Court for the Middle District of Tennessee. This case, over a convincing dissent, held that such a contract was a single contract and affirmed the overruling of a demurrer to an amended declaration that sought the present value of future disability benefits based upon life expectancy of the insured. The opinion was severely limited, if not overruled, by subsequent decisions of the Supreme Court in *Mobley v. New York Life Insurance Co.*, 295 U.S. 632, 55 Sup. Ct. 867, 79 L. Ed. 1166 (1935), and in *New York Life Insurance Co. v. Viglas*, 297 U.S. 672, 56 Sup. Ct. 615, 80 L. Ed. 971 (1935). Moreover, most of the cases in apparent disagreement with the above have found special facts amounting to an actual repudiation as distinguished from a simple denial that the insured is disabled within the meaning of the policy.

33. 264 S.W.2d 587 (Tenn. App. M.S. 1953).

where the disease occasioning the expenses originated before the policy had been in effect for 15 days. The case had been tried below on an appeal from the court of general sessions, without a jury and the circuit court had affirmed a judgment for the plaintiff. The Court of Appeals held that the defendant had failed to carry the burden of proof imposed upon it and accordingly affirmed.

In *Gibbons v. Mutual Benefit Health and Accident Association*,[34] the significant question was one of tender. The company had issued a sickness and accident policy which provided for payments of $100 per month if the insured became totally disabled. A few months after issuance, the insured filed proof of disability. The company denied liability on the ground of fraud in procurement of the policy and tendered the premium received by it. The insured further alleged that subsequently an agent of the company stated to him that there was absolutely no liability on the policy but offered him $500 in full settlement of all claims against the company. The insured accepted this money and executed a release. This bill was filed in the chancery court alleging that the agent's statements of no liability were false and fraudulent and that the settlement offer was accepted because the insured was uneducated and sick. The relief sought was that the settlement be declared void and the insurer be required to pay according to the provisions of the policy. The bill also alleged that the company under the policy owed the complainant more than the $500 previously paid to him and asked that said sum be credited against the judgment to be rendered. The company filed a demurrer to the bill upon the grounds that a repayment or tender of the $500 was a prerequisite to the maintenance of the suit. The chancellor sustained the demurrer, and the Supreme Court affirmed. The allegation in the bill that the company was indebted to complainant in excess of $500 failed to meet the requirement of tender in that such allegation only stated a conclusion of the pleader which was not admitted by a demurrer. While previous Tennessee cases,[35] requiring that one who seeks to avoid an accord or satisfaction agreement on the ground that it was attained by fraud must tender back the money received under the executed agreement, have been based upon a claim *ex delicto*, the court concluded that there is no reason in principle why a different rule should be applied where the claim is *ex contractu*.

In *Berryhill v. Mutual Benefit Health and Accident Association*,[36] (two cases) there was presented the question as to the duty imposed upon an insurance applicant to read the application which had been incorrectly completed by the insurance agent. Two suits had been

34. 195 Tenn. 339, 259 S.W.2d 653 (1953).
35. See Glover v. Louisville & N.R.R., 163 Tenn. 85, 40 S.W.2d 1031 (1931).
36. 262 S.W.2d 878 (Tenn. App. M.S. 1953).

filed, one upon a sickness and accident policy and the other upon a hospital and medical benefit policy. The plaintiff had previously had some physical troubles, which had cleared up and it was his position that he advised the agent thereof but the agent had not so disclosed in filling out the application, but, on the contrary, had made incorrect answers to some of the questions. It can be assumed, although it does not directly appear, that the agent denied that he was furnished information contrary to that appearing in the application. The trial court had declined to direct a verdict and the jury found for the plaintiff. The Court of Appeals approved the action of the trial judge in not directing a verdict upon the grounds that there was ample evidence to support the jury's finding that the applicant had informed the agent of his past physical troubles and he had written wrong answers in the application without the knowledge of the insured. The court further found that there was no fraud or collusion between the agent and the insured. The opinion makes no mention of the signing of the application by the insured, but it probably can be assumed that had there been a departure from custom in this regard, it would have been mentioned. In its apparent holding that there is no absolute duty upon the applicant to ascertain and correct erroneous statements in an application filled in by the agent, the decision is supported by earlier Tennessee cases among them being *Industrial Life & Health Ins. Co. v. Trinkle.*[37] Yet among the cases cited by the court is *Beasley v. Metropolitan Life Insurance Co.*[38] which is difficult to reconcile with the present case or with the holding in the *Trinkle* case. In the *Beasley* case, the Supreme Court held that a verdict for the defendant should have been directed at the conclusion of the plaintiff's proof which was to the effect that the answers in the application completed by the agent were false but that the applicant had given the agent correct information and the applicant did not read the application after it was completed, although he then signed it. The *Beasley* case mentioned the *Trinkle* case, but did not discuss or distinguish it; and it appears that the principal case is more in line with the previous Tennessee authorities than is the *Beasley* case.

37. 185 Tenn. 434, 206 S.W.2d 414 (1947).
38. 190 Tenn. 227, 229 S.W.2d 146 (1950).