UNC SCHOOL OF LAW

NORTH CAROLINA LAW REVIEW

Volume 30 | Number 4 Article 16

6-1-1952

Insurance -- Suspension and Revival of Policy After Breach of Condition

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The point raised in some of the cases, including *Austin v. Drewe*, that the loss was due only to the negligence of the insured or his servants is of no weight whatever in denying recovery under the insurance policy. It is well settled that mere carelessness and negligence of the insured or his servants, not amounting to fraud, though the direct cause of the fire, are covered by the policy unless specifically excepted.[25] In fire risks it is one of the objects of insuring to secure indemnity against the consequences of negligence.[26]

The one possible objection against the viewpoint urged here is that fraudulent destruction of property in order to collect insurance might be made easier. But this danger exists in any kind of insurance and might be adequately guarded against by requiring convincing proof that the loss did not result from the intentional act of the insured.

It is submitted that the American courts should restrict the friendly fire doctrine to its original limitations as set forth in *Austin v. Drewe*. Recovery should be permitted where there is an actual burning[27] of the insured article, for in such case there is indeed, from a realistic point of view, a hostile fire.

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Insurance—Suspension and Revival of Policy After Breach of Condition

Plaintiff trucking corporation sought recovery in a federal district court in North Carolina from defendant insurance company for the loss of a quantity of cigarettes by theft from one of its trucks. Insured's driver parked the truck containing the cigarettes and went across the street to a cafe. He failed to turn on the alarm system on the truck which would sound a siren if the truck were moved.[1] The driver returned to

[25] Federal Ins. Co. v. Tamiami Trail Tours, 117 F. 2d 794 (5th Cir. 1941); Salmon v. Concordia Fire Ins. Co., 161 So. 340 (La. App. 1935); Harter v. Phoenix Ins. Co., 257 Mich. 163, 241 N. W. 196 (1932) (dissenting opinion); Weiner v. St. Paul F. & M. Ins. Co., 124 Misc. 153, 207 N. Y. Supp. 279 (1st Dep't 1924), *aff'd without opinion*, 214 App. Div. 784, 210 N. Y. Supp. 935 (1st Dep't 1925); 5 APPLEMAN, INSURANCE LAW AND PRACTICE §3114 (1941); 2 MAY ON INSURANCE §408 (3d ed. 1891).

[26] This was recognized by the Kansas court: "Negligence or inadvertence of an insured or of one of his employees of course ordinarily would not bar recovery. . . ." Youse v. Employers Fire Ins. Co., 238 P. 2d 472, 477 (Kan. 1951).

[27] By "burning" it is meant that injury or destructive change is produced by direct contact with the flame or by actual ignition. Depending on the physical characteristics of the insured article, it might or might not be consumed or reduced to ashes.

[1] "The trailer was equipped with the theft protection device, described in the policy and known as the Senior Babaco Alarm, consisting of two parts, the 'Sealed Load' alarm and the 'Parker alarm.'" ". . . the 'Parker' alarm is designed to prevent the unauthorized movement of the trailer. When the 'Parker' switch is 'on,' it is impossible to move the vehicle without sounding the siren alarm." Fidelity-Phenix Fire Ins. Co. of New York v. Pilot Freight Carriers, 193 F. 2d 812 at 814 (4th Cir. 1951).

the truck, and upon opening the door of the cab, was confronted by an armed man who forced him to get into the truck and drive it away. Ultimately the cigarettes were removed from the truck by the thieves. The policy on which this suit was brought provided that the alarm "on each trailer will be in the 'on' position when such vehicles are parked *unattended* . . . " (emphasis added). Further, the policy provided that the failure of the insured to comply with "any of the foregoing conditions precedent in any instance shall render [the] policy *null and void* as respects theft coverage for vehicles" (emphasis added).[2] The United States Court of Appeals for the Fourth Circuit, in applying the law of North Carolina, reversed the district court's judgment for plaintiff.[3] Recovery was denied on the grounds that there was an admitted breach of the condition; that the driver never came back into "attendance" so as to end the breach and thus revive the policy before the loss; and that there could have been no revival of the policy since the insured risk was increased during the breach of the condition.

The legal effect of a breach of a promissory warranty[4] or condition in a contract of insurance should ordinarily depend on the intent of the parties as expressed by the terms of the contract.[5] The policy may provide that a breach of a condition or warranty contained therein will merely suspend the operation of the policy during the breach.[6] On the other hand, the policy may provide that if there is a breach of a condition or warranty, the policy will become null and void.[7] Clearly if loss or damage occurs during the breach, there is no liability on the insurer under either type of provision.[8] But where there is a breach

[2] Fidelity-Phenix Fire Ins. Co. of New York v. Pilot Freight Carriers, 193 F. 2d 812 (4th Cir. 1951).

[3] Pilot Freight Carriers v. Fidelity-Phenix Fire Ins. Co., 98 F. Supp. 329 (M. D. N. C. 1951).

[4] ". . . most of the so-called warranties in insurance policies are not even promises in form, but are conditions. The use of the word 'warranty,' therefore, in insurance law is a misnomer. It means a condition inserted on the face of the policy or a statement of fact, on the exact truth or performance of which, unless excused, the duty of immediate performance of the insurer's promise depends. Warranties, as thus used to designate conditions in insurance policies, are divided into two classes, affirmative and promissory warranties. Affirmative warranties are statements of supposedly existing facts, on the truth of which the insurer's duty depends; promissory warranties are agreements that the insurer's duty shall be conditional on the future existence or happening of certain facts." 3 WILLISTON, CONTRACTS §673 (Rev. ed. 1936 and 1951 cum. supp.).

[5] 44 C. J. S. Insurance §290 (1945).

[6] National Reserve Ins. Co. v. Scudder, 71 F. 2d 884 (9th Cir. 1934); United States Fire Ins. Co., 118 N. J. Law 423, 193 Atl. 180 (1937); Hunt v. Dollar, National Union Fire Ins. Co., 224 App. Div. 136, 229 N. Y. Supp. 682 (4th Dep't 1928).

[7] See cases cited in notes 10 and 12 *infra.*

[8] Wallace v. Virginia Surety Co., 80 Ga. App. 50, 55 S. E. 2d 259 (1949); Traders' Ins. Co. v. Catlin, 163 Ill. 256, 45 N. E. 255 (1896); Schaefer v. Home Ins. Co., 194 S. W. 2d 718 (Kan. City Ct. of Appeals 1946); Procacci v. United States Fire Ins. Co., 188 N. J. Law 423, 193 Atl. 180 (1937); Hunt v. Dollar, 224 Wis. 48, 271 N. W. 405 (1937).

of a condition and this breach ceases before any loss occurs, the legal effect of such breach in the light of the contract provisions may give rise to a difficult problem.

Where the parties have provided for "suspension" during a breach of condition, the courts follow the expressed intention and allow recovery if the breach has terminated and in no way contributed to the loss.[9] However, where the policy provides that it is "void" if there is a breach of condition, the courts differ on the question of loss after the breach has terminated. Some construe the language literally, and even though the loss is in no way attributable to the terminated breach, these courts hold the policy completely void[10] unless the breach is waived by the insurer.[11] The reasoning behind this view is that the parties are free to contract as they wish, and any construction other than forfeiture would contravene the unambiguous terms of the policy. A larger number of courts take a more liberal view and hold that the policy is merely suspended during the breach and that it revives to full force and effect after cessation of the breach provided that at the time of loss there is no increase in the risk of loss arising from or because of the prior breach.[12] Statutes control the legal effect of a breach of condition or

[9] See cases cited in note 6 *supra*.

[10] Imperial Fire Ins. Co. v. Coos Co., 151 U. S. 452 (1894); Morgan v. Germania Fire Ins. Co., 104 Kan. 383, 179 Pac. 330 (1919); Dolliver v. Granite State Fire Ins. Co., 111 Me. 275, 89 Atl. 8 (1913); Kyte v. Commercial Union Assurance Co., 149 Mass. 116, 21 N. E. 361 (1889).

[11] The insurer may waive a breach of a condition in a policy of insurance by the insured so as to prevent a forfeiture under the strict "void" rule. "A waiver arises from acts, words, or conduct on the part of the insurer, done or spoken with knowledge of a breach of condition, which amount to a recognition of the policy as a valid, existing and continuing contract, or which are inconsistent with an intent to claim a forfeiture, or which are such as reasonably to imply a purpose not to insist on a forfeiture." 45 C. J. S. Insurance §704 (1946); Washington County Farmers' Mut. Fire Ins. Co. v. Reed, 218 Ark. 522, 237 S. W. 2d 888 (1951); Johnson v. Life Ins. Co. of Ga., 52 So. 2d 813 (Fla. 1951); Westchester Fire Ins. Co. of N. Y. v. Gray, 240 S. W. 2d 825 (Ky. 1951); Green v. Aetna Ins. Co., 196 N. C. 335, 145 S. E. 616 (1928); Horton v. Life Ins. Co. of Virginia, 122 N. C. 498, 29 S. E. 944 (1898).

[12] Henjes v. Aetna Ins. Co., 132 F. 2d 715 (2d Cir.), *certiorari denied*, 319 U. S. 760 (1943); Globe & Rutgers' Fire Ins. Co. v. Pruitt, 188 Ark. 92, 64 S. W. 2d 91 (1933); Steil v. Sun Ins. Office, 171 Cal. 795, 155 Pac. 72 (1916); Public Fire Ins. Co. v. Crumpton, 110 Fla. 151, 148 So. 537 (1933); Athens Mutual Ins. Co. v. Toney, 1 Ga. App. 492, 57 S. E. 1013 (1907); Traders' Ins. Co. v. Catlin, 163 Ill. 256, 45 N. E. 255 (1896); Aetna Ins. Co. v. Robinson, 213 Ind. 44, 10 N. E. 2d 601 (1937); Born v. Home Ins. Co., 110 Iowa 379, 81 N. W. 676 (1900); Germania Fire Ins. Co. v. Turley, 167 Ky. 57, 179 S. W. 1059 (1915); Home Ins. Co. v. Northington, 198 Miss. 650, 23 So. 2d 537 (1945); Schaefer v. Home Ins. Co., 194 S. W. 2d 718 (Kans. City Ct. of Appeals 1946); German Mutual Fire Ins. Co. v. Fox, 4 Neb. 833, 96 N. W. 652 (1903); Ohio Farmers' Ins. Co. v. Burget, 65 Ohio St. 119, 61 N. E. 712 (1901); McClure v. Mutual Fire Ins. Co., 242 Pa. 59, 88 Atl. 921 (1913); Graham v. Standard Fire Ins. Co., 119 S. C. 218, 112 S. E. 88 (1922); Mittet v. Home Ins. Co., 49 S. D. 319, 207 N. W. 49 (1926); Carolina Ins. Co. v. St. Charles, 20 Tenn. App. 342, 98 S. W. 2d 1088 (1937); Beecher v. Vermont Mutual Fire Ins. Co., 90 Vt. 347, 98 Atl. 917 (1916). Generally these cases apply the reasoning that forfeitures are not favored in the law. Some say that this rule accords with the real purpose of the provisions in the policy. See German Mutual Fire Ins. Co. v. Fox, 4 Neb. 833, 96 N. W. 652 (1903); Beecher v. Vermont Mutual Fire Ins. Co., 90 Vt. 347, 98 Atl. 917 (1916).

warranty in some states. For example, such statutes may provide that the breach of warranty or condition must contribute to the loss for the insurer to escape liability,[13] or that the insurer is liable unless such breach exists at the time of the loss and contributes to the loss,[14] or that any increase in the insured risk by use or change in the property will void the policy.[15]

The more liberal view as to the effect of a breach of a condition which "voids" the policy prevails in North Carolina.[16] In the instant case, there was an admitted breach of the condition requiring the use of the alarm when the truck was "unattended." In construing this word in the policy, the court defined "attendance" as involving "not merely physical presence but freedom to perform the duties of an attendant." The court then held that as a matter of law there was no revival of the policy because the driver did not come back into attendance before the loss (thereby not terminating the breach) as he was deprived of his freedom of action when he entered the cab of the truck by an armed bandit already in forcible possession of the truck. Since the driver had freedom to perform his duties *as an attendant* up to the time of his entrance into the cab, it would seem that the court, in effect, held that the "physical presence" required by its definition is that of being *in* the cab of the truck. Except where the policy defines "attendance,"[17] the few cases found construing this word or the word "presence" seem to require only that a driver be in such proximity to the truck as to be able to observe a theft of the contents.[18] In view

[13] TEX. STAT., REV. CIV. art. 4930 (1925).

[14] NEB. REV. STAT. §44-358 (1943). VA. CODE ANN. §38-8 (1950) provides that a breach of a condition in a policy of insurance concerning property in Virginia will not void the policy unless such breach exists at the time of loss or damage.

[15] GA. CODE ANN. §56-823 (1933) (The effect of this statute is to write a condition into the policy and provide for its consequences.)

[16] Barefoot v. Home Ins. Co., 204 N. C. 301, 168 S. E. 206 (1933); Landreth v. American Equitable Assurance Co., 199 N. C. 181, 154 S. E. 9 (1930); Crowell v. Maryland Motor Car Ins. Co., 169 N. C. 35, 85 S. E. 37 (1915); Cottingham v. Maryland Motor Car Ins. Co., 168 N. C. 259, 84 S. E. 274 (1915).

[17] Greenberg v. Rhode Island Ins. Co., 188 Misc. 23, 66 N. Y. S. 2d 457 (Sup. Ct. 1946).

[18] In Kinscherf Co. v. St. Paul Fire & Marine Ins. Co., 234 App. Div. 385 at 386, 254 N. Y. Supp. 382 at 383 (2d Dep't 1931), "attendance" was held to mean that if a driver of a vehicle is not actually "within or on the automobile, or so near thereto as to be able to observe a theft of the contents, he shall not be deemed to be in attendance at the time the loss occurs." A similar holding was made in Dreblatt v. Taylor, 188 Misc. 199, 67 N. Y. S. 2d 378 at 379 (Sup. Ct. 1947). Where a policy protected against theft "committed in the *presence* of such custodian . . . and of which [he] may be actually cognizant at the time . . ." (emphasis added), a theft was held to be in the presence of a custodian when he was inside a tavern within partial vision of his truck and saw the thieves drive it away. London v. Maryland Casualty Co., 210 Minn. 581, 299 N. W. 193 (1941). Under a similar provision, "presence" was held to be "physical proximity to and within the uninterrupted range of vision of the custodian." The court did not define "physical presence" but held that the theft of the truck involved was not

of the purpose of the alarm in the instant case to give a warning in the event of any *movement* of the truck, the court could reasonably have taken a similar view of the word "attendance" and defined it as "proximity by the driver sufficient to allow him to see and report any unauthorized movement of the truck," *i.e.*, such proximity by the driver as to be able to perform the same function as the alarm. The instant view which apparently requires either physical presence in the cab by the driver, or the alarm in the "on" position seems overly strict and not in line with the generally recognized principle that ambiguity in a contract of insurance is to be construed in favor of the insured.[19]

In addition, the court stated that even if it be assumed that the driver was in attendance before the crime was complete, there was not a revival of the policy because "such a revival should not and cannot take place unless *nothing* has happened in the meanwhile to increase the insurer's risk of loss."[20] The decisions from North Carolina[21] and other jurisdictions[22] which recognize the liberal rule indicate that not *any* increase in the insured risk which arises during the breach and which carries over after its termination to the time of loss will bar revival. Rather, these courts bar revival where there is an increased risk after the breach which extends to the time of loss and *which arose from and was caused by the breach itself*. Certainly there was, in the instant case, an increase in the risk which arose during the breach of the condition, but it did not arise *from* or *because* of the breach. The employment of the alarm would have in no way prevented the thief from climbing into the cab since the alarm would have sounded only if the truck had been rolled or moved.

The liberal "suspension and revival" rule seems most equitable. It

in the presence of the driver who had entered a building from which the truck was not visible and when he noticed the theft, the truck was being driven away and already 125 feet from him. Grimes v. Maryland Casualty Co., 300 Ill. App. 62, 20 N. E. 2d 982 (1939).

[19] Jolly v. Jefferson Standard Life Ins. Co., 199 N. C. 269, 154 S. E. 400 (1930); Crowell v. Maryland Motor Car Ins. Co., 169 N. C. 35, 85 S. E. 37 (1915); 44 C. J. S. Insurance §297 (1945).

[20] 193 F. 2d at 817 (emphasis added).

[21] Crowell v. Maryland Motor Car Ins. Co., 169 N. C. 35 at 38, 85 S. E. 37 at 39 (1915) The court, in holding that a policy had revived after the termination of a breach of condition, said, "The increase of risk *by the wrongful use*, if there was such, had entirely ceased and determined." (emphasis added)

[22] Henjes v. Aetna Ins. Co., 132 F. 2d 715 at 720 (2d Cir. 1943): "The insured may not *by breach of warranty* increase the risk and put that added burden upon the insurer." (emphasis added), Traders' Ins. Co. v. Catlin, 163 Ill. 256 at 258, 45 N. E. 255 at 257 (1896): "If a former increase of hazard has ceased to exist, and *that* increase in hazard at that former time in no way has affected the risk when the loss occurs, no reason exists why a forfeiture should result from a cause which occasions no damage." (emphasis added); Germania Fire Ins. Co. v. Turley, 167 Ky. 57 at 61, 179 S. W. 1059, at 1062 (1915): The court stated that a policy may suspend and revive after the breach terminates if "the increased hazard *caused by such prohibited use* in no way continues to affect the risk at the time of loss." (emphasis added)

fully protects the insurer since it fails to allow recovery if the terminated breach in any way affects the loss, and it recognizes the right of the insurer to declare a forfeiture at the time of the breach if he so desires.[23] A just and equitable rule may be entirely abrogated by unsympathetic or strict application, and the instant case seems to represent a rather strict application.

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Liens—Priority of Federal Tax Claims Over Inchoate Liens—Difference in Equity Receivership and Bankruptcy

A corporation was adjudged insolvent and a receiver appointed to liquidate the assets. On the question of priority of payment between federal tax claims under Section 3466 of the United States Revised Statutes[1] and the employees' liens for wages under G. S. 55-136,[2] the North Carolina Supreme Court held the federal claim was to be given priority.[3]

Section 3466 of the United States Revised Statutes, providing for priority of payment of debts due the United States, applies when the insolvent has been divested of ownership of his property.[4] The divest-

[23] Globe & Rutgers' Fire Ins. Co. v. Pruitt, 188 Ark. 92, 64 S. W. 2d 91 (1933); Aetna Ins. Co. v. Robinson, 213 Ind. 44, 10 N. E. 2d 601 (1937).

[1] 31 U. S. C. §191 (1946): "Whenever any person indebted to the United States is insolvent or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied; and the priority established shall extend as well to cases in which a debtor not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor, are attached by process of law, as to cases in which an act of bankruptcy is committed."

[2] N. C. GEN. STAT. §55-136 (1943): "In case of the insolvency of a corporation, partnership, or individual, all persons doing labor or service of whatever character in its regular employment have a lien upon the assets thereof for the amount of wages due to them for all labor, work, and services rendered within two months next preceding the date when proceedings in insolvency were actually instituted and begun, . . . which lien is prior to all other liens that can be acquired against such assets."

[3] Leggett v. Southeastern People's College, Inc., 234 N. C. 595, 68 S. E. 2d 263 (1951).

[4] Before the priority under Section 3466 attaches, the insolvency must be manifested in one of the modes specified under the section. In addition, "Under this act these rules have been clearly established: First, no lien is created; second, the priority established can never attach while the debtor continues the owner and in possession of the property, though he may be unable to pay all his debts; third, no evidence can be received of the insolvency of the debtor until he has been divested of his property in one of the modes stated; and fourth, whenever the debtor is thus divested of his property, the person who thus becomes invested with the title is thereby made a trustee for the United States. . . ." Beaston v. Farmers' Bank, 12 Pet. 102, 133 (U. S. 1838); Bramwell v. U. S. Fidelity & Guaranty Co., 269 U. S. 483 (1926); United States v. Oklahoma, 261 U. S. 253 (1923); Bishop v. Black, 233 N. C. 333, 64 S. E. 2d 167 (1951). The priority attaches at the date of the appointment of a receiver. Bramwell v. U. S. Fidelity & Guaranty Co., *supra*.