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It seems reasonably clear that, if I direct my broker to purchase 100 shares of xyz stock in the name of my son and I pay the purchase price, I have transferred 100 shares of xyz stock, not the dollars paid.⁶²

If a decedent seeks out the insurer, negotiates all the terms of the policy, requests the insurer to create all the policy rights in another, and pays the first premium which actually brings the contractual rights, as evidenced by the policy issued, into existence, to say that this is not a "transfer" by the decedent is to put form over substance. If the decedent continues to pay the premiums, he remains the motivating force of the transaction, at least with respect to the amount of proceeds attributable to the premium payments within three years of his death. The premium was paid to the insurer to purchase an asset—the asset being the insurer's promise to pay the policy proceeds on the death of the insured. Inherent in life insurance is the fact that the value of the company's promise to pay is always increasing in value as death draws nearer. The decedent's payment to the insurer is prompted by the knowledge that this manner of payment will assure him of getting something more for his money, *i.e.*, a benefit to the donee greater than the dollars paid for the premium payment, in the form of insurance proceeds in excess of the money paid.

On balance, the pro rata valuation (the Revenue Ruling's procedure for valuation) seems to be the method which best carries out the prior policies and decisions regarding the taxation of gifts in contemplation of death. It takes cognizance of the donor's intent in paying the premiums and does not violate the congressional intent that underlays the amendments to section 2042.⁶³

MICHAEL DONWELL GUNTER

Insurance—Life Insurance Applications: Opinion Answers or Material Misrepresentations

With its recent decision in *Prudential Insurance Co. of America v. Barden*,¹ the Court of Appeals for the Fourth Circuit may have demonstrated that the converse of the time-worn judicial apology, "hard cases make bad law," is not necessarily true. Beneath *Barden's* deceptively

⁶² Stephens, *The Clifford Shadow over the Federal Estate Tax*, 4 GA. L. REV. 233, 248 (1970).

⁶³ See Note, 82 HARV. L. REV., *supra* note 40, at 1771.

¹ 424 F.2d 1006 (4th Cir. 1970).

simple exterior, one finds a questionable application of an established insurance law doctrine that is worthy of close scrutiny.

On September 29, 1966, Frank Barden, forty-eight years old and an accountant by profession, applied for two policies on his life, each in the amount of ten thousand dollars. His written application under a group plan for the American Institute of Certified Public Accountants avowed the completeness and truth of its contents, among which were the following questions and Barden's corresponding answers:

10. Has the Person Proposed for Insurance ever been treated for or had any indication of: Yes No

. . .

(d) Stomach or Intestinal Trouble? (X) ()

11. Has the Person Proposed for Insurance within the past 5 years:

(a) Had or been advised to have a surgical operation? Yes No
(X) ()

(b) Been a patient in or advised to enter a hospital or sanitorium? (X) ()

(c) Consulted, been attended or examined by a doctor or other practitioner? (X) ()

12. Has the Person Proposed for Insurance any physical deformities, impairments or ill health not recorded in answer to Question 10 or 11?

Yes No
() (X)

13. What are the complete details of all "Yes" answers to Questions 10, 11 and 12?

Question No.	Condition, Details and Number of Attacks (if operated, so state)	Duration of Disability	Complete Recovery	
			Month	Year
10(d)	Appendicitis Operation	5 days	May	1964

Names and Addresses of Physicians and Hospitals

Dr. O.E. Bell
Memorial Hospital
Rocky Mount, N.C.²

² *Id.* at 1007.

With the exception of the disclosed appendectomy, Barden omitted all mention of his lengthy medical history which included diagnoses of a ruptured blood vessel in the stomach or esophagus, cirrhosis of the liver, and acute alcoholism.³ The policies were issued on October 1 and remained in force until the insured's death from acute pancreatitis three months later.

In the insurer's subsequent suit to rescind the policies because of alleged material misrepresentations, the trial court granted its motion for summary judgment and concluded that "in fact and in law the answers to questions 12 and 13 . . . were clearly false, with no waiver or estoppel on the part of . . . [the company]; that said answers were material as a matter of law. . . ."⁴ On appeal, with the evidential facts not in dispute, the Court of Appeals for the Fourth Circuit reversed, finding that the insurance company had failed to prove a misrepresentation and in any event, the company by issuing the life insurance policy waived any claim it had of material misrepresentation.⁵

Section 58-30 of the North Carolina General Statutes provides:

All statements or descriptions in any application for a policy of insurance, or in the policy itself, shall be deemed representations and not warranties, and a representation, unless material or fraudulent, will not prevent a recovery on the policy.⁶

The purpose of this statute is to prevent the insurer from avoiding payment of honest losses upon technicalities and strict construction of the insurance contract.⁷ Its use of the disjunctive, "or," is singularly im-

³ Within one year after the disclosed appendicitis operation, Barden was readmitted to the same hospital on complaint of nausea and vomiting of blood. Following two injections of whole blood and glucose, he remained there for over a week pending a final diagnosis of a ruptured blood vessel in the stomach or esophagus. Gall bladder difficulty had been suspected, but tests for the disorder proved negative. On January 17, 1966, he consulted a different physician (Dr. Weeks) from the one who had attended him in the past (Dr. Bell) in order to receive a general check-up because of excessive fatigue. Dr. Weeks' examination resulted in a diagnosis of acute alcoholism with directions to remain on a special diet and abstain completely from alcoholic indulgence. Three months later (and only five months prior to his application for insurance), Barden was admitted to Rocky Mount Sanitarium Hospital due to abdominal pain, nausea and frequent regurgitation of food. After a six day convalescence, he was released—this time with a diagnosis of cirrhosis of the liver. From this date until the time of his death he continued periodically to consult Dr. Weeks, who, though noting some improvement in Barden's condition, kept his original directions in force. *Id.* at 1008-12.

⁴ *Id.* at 1007.

⁵ *Id.* at 1006.

⁶ N.C. GEN. STAT. § 58-30 (1965).

⁷ *Garvey v. Old Colony Ins. Co.*, 153 F. Supp. 755, 757 (E.D.N.C. 1957); *Cot-*

portant to the insurer, for it obviates the necessity of proving knowledge or intent in a suit to rescind the policy because of a misrepresentation of a material fact.⁸ In North Carolina the issue of materiality is resolved by the application of what has been termed the "individual insurer" rule:⁹ If the knowledge or ignorance of the disputed fact would naturally influence the judgment of the insurer in accepting the risk or in fixing the rate of the premium, then that fact is deemed to be material.¹⁰ Ordinarily, the resolution of this question is for the jury,¹¹ but like many general rules, this, too, is subject to exception. In an application for a policy of life insurance, it is established law in North Carolina that written questions relating to health, and written answers thereto, are considered material as a matter of law.¹² In such cases, the only relevant inquiries for the jury are whether the insured made the statement and if so, whether it was false.¹³

In ruling upon the effect of the insured's answer to question 12, the court neatly avoided the issue of materiality by treating the inquiry as if it called only for an opinion. Basing its decision upon the physician's optimistic reports of the preceding May and August,¹⁴ the court concluded that these reports

tingham v. Maryland Motor Car Ins. Co., 168 N.C. 259, 261, 84 S.E. 274, 275 (1915).

⁸ See Walker v. Philadelphia Life Ins. Co., 127 F. Supp. 26, 29 (E.D.N.C. 1954); Tolbert v. Mutual Benefit Life Ins. Co., 236 N.C. 416, 418, 72 S.E.2d 915, 917 (1952); Inman v. The Sovereign Camp of the Woodmen of the World, 211 N.C. 179, 181, 189 S.E. 496, 497 (1937).

⁹ Note, *Insurance: Concealment and Misrepresentation as Grounds to Avoid Policy*, 5 U.C.L.A.L. Rev. 332, 334 & n.15 (1958).

¹⁰ E.g., Garvey v. Old Colony Ins. Co., 153 F. Supp. 755, 757 (E.D.N.C. 1957); Tolbert v. Mutual Benefit Life Ins. Co., 236 N.C. 416, 418-19, 72 S.E.2d 915, 917 (1952); Wells v. Jefferson Standard Life Ins. Co., 211 N.C. 427, 429, 190 S.E. 744, 745 (1937); Gardner v. North State Mut. Life Ins. Co., 163 N.C. 367, 374, 79 S.E. 806, 809 (1913).

¹¹ E.g., Senandoah Life Ins. Co. v. Hawes, 256 F. Supp. 366, 367 (E.D.N.C. 1966); Carroll v. Carolina Cas. Ins. Co., 227 N.C. 456, 458, 42 S.E.2d 607, 608 (1947); Howell v. American Nat'l Ins. Co., 189 N.C. 212, 217, 126 S.E. 603, 605-06 (1925).

¹² E.g., Shenandoah Life Ins. Co. v. Hawes, 256 F. Supp. 366, 367 (E.D.N.C. 1966); Sims v. Charlotte Liberty Mut. Ins. Co., 257 N.C. 32, 40, 125 S.E.2d 326, 332 (1962); Rhinehardt v. North Carolina Mut. Life Ins. Co., 254 N.C. 671, 673, 119 S.E.2d 614, 616 (1961).

¹³ Sims v. Charlotte Liberty Mut. Ins. Co., 257 N.C. 32, 40, 125 S.E.2d 326, 332 (1962); Rhinehardt v. North Carolina Mut. Life Ins. Co., 254 N.C. 671, 673, 119 S.E.2d 614, 616 (1961).

¹⁴ 424 F.2d at 1007.

were certainly sufficient to justify a lay patient to believe that a few weeks later, without an intervening sickness, he could say in good faith that he was not then suffering from "any physical deformities, impairments or ill health not recorded" in the catechism of 10 and 11.¹⁵

Although such an approach might be justified in light of *Jeffress v. New York Life Insurance Co.*,¹⁶ it would appear that the court overstepped its function in passing upon the insured's good faith. When weighed against the evidence of the insured's medical history and his knowledge of the past diagnoses,¹⁷ his good faith in responding to question 12 would not appear to be so overwhelming as to justify the appellate court's summary decision in the insured's favor.

In addition, the court's analysis of question number 12 would seem to permit recovery based upon the insured's bona fide belief of his *apparent* state of health. Besides being out of harmony with a number of other courts,¹⁸ such an effect would seem to contradict *Hines v. New England Casualty Co.*,¹⁹ upon which *Jeffress* relies.²⁰ In *Hines* the applicant for insurance had stated that he was in "sound condition, mentally and physically,"²¹ despite his knowledge of an existing hernia. In the insurer's subsequent suit to rescind the policy, the court held for the defendant, but added:

Few people are absolutely exempt from some variation from a perfect condition, and, unless such variation is specifically asked about in the application and denied, it is not a matter vitiating the policy, unless the

¹⁵ *Id.* at 1008.

¹⁶ 74 F.2d 874 (4th Cir. 1935). "[W]here an inquiry as to physical condition or previous illness calls for what is in effect an opinion by the applicant, an answer made in good faith will not avoid the policy." *Id.* at 876.

¹⁷ 424 F.2d at 1007.

¹⁸ *E.g.*, *Perkins v. John Hancock Mut. Life Ins. Co.*, 100 N.H. 383, 128 A.2d 207 (1956); *National Life & Accident Ins. Co. v. Whitlock*, 198 Okla. 561, 180 P.2d 647 (1947); *Grover v. John Hancock Mut. Life Ins. Co.*, 119 Vt. 246, 125 A.2d 571 (1956).

The rationale of the actual good health doctrine is that the parties, being free to contract as they pleased, have in unmistakable terms made the fact of good health a condition precedent to insurance coverage and that it is not within the province of the court, whatever its sympathies, to remake the insurance contract, either by deleting the good health clause or by reading into it language which is not there.

Wick, *The Good Health Clause—What it Says and What Some Courts Say it Says*, 23 *INS. COUNSEL J.* 311, 313 (1956) [hereinafter cited as Wick].

¹⁹ 172 N.C. 225, 90 S.E. 131 (1916).

²⁰ 74 F.2d at 876.

²¹ 172 N.C. at 226, 90 S.E. at 132.

variation was serious enough to affect his "soundness" so that any one would say *who knew the facts*, "He is not a sound man."²²

Thus, what began in *Hines* as a third party's opinion of *actual* health founded upon *scienter* has, in *Jeffress*, evolved to the point of permitting the applicant's statement of *apparent* state of health founded upon good faith *belief*.²³ Although the approach taken in *Jeffress* (and thereby, *Barden*) seems more in keeping with the policy behind section 58-30 of the North Carolina General Statutes,²⁴ the decision in *Hines* serves as a reminder of the jury's role as the trier of fact. In *Hines*, the jury was confined to determining whether the insured was or was not a sound man. With the subsequent liberalization of the rule in *Jeffress*, the jury should at least have been given the opportunity in *Barden* to decide whether the insured had a bona fide belief that he was in good health, and if so, whether such belief was reasonable.²⁵

In passing upon the insurer's assertion of incompleteness in question 13, the court branded the inquiry as an "omnibus inquisition for details."²⁶ Such a label is misleading in light of the fact that treatment for slight or temporary indispositions may be regarded as immaterial where the applicant fully discloses medical treatment for a serious ailment administered at or about the same time.²⁷ Standing alone, therefore, question 13 requires that the applicant for insurance disclose only those facts and circumstances which, from a pragmatic standpoint, would be likely to affect the insurer's judgment in accepting the risk or in fixing the rate of the premium. Yet, in deciding that question thirteen was suitably answered in the context of question 10, the court only concerned itself with the insured's liver ailment. Nowhere did the court mention the diagnosis of

²² *Id.* (emphasis added).

²³ *But cf.* *Huffman v. State Capital Life Ins. Co.*, 8 N.C. App. 186, 174 S.E.2d 17 (1970). Decided one month after *Barden*, this case seems to imply a continued adherence to the actual good health doctrine. In support of this doctrine, it has been argued that the average layman both knows and understands the distinction between the term "good health" as used in daily conversation and "good health" as used in formal insurance contracts. The latter is understood to be a condition precedent to the enforceability of the contract and thereby could only mean actual good health. *Wick* at 317.

²⁴ N.C. GEN. STAT. § 58-30 (1965). See p. 562 *supra*.

²⁵ *Cf.* *Franklin Life Ins. Co. v. William J. Champion & Co.*, 350 F.2d 115, 126 (6th Cir. 1965); *Union Life Ins. Co. v. Davis*, — Ark. —, 449 S.W.2d 192, 195 (1970).

²⁶ 424 F.2d at 1008.

²⁷ *E.g.*, *Jeffress v. New York Life Ins. Co.*, 74 F.2d 874, 877 (4th Cir. 1935); *Anthony v. Teachers' Protective Union*, 206 N.C. 7, 11, 173 S.E. 6, 8 (1934).

a ruptured blood vessel in the stomach or esophagus or the insured's history of vomiting blood.²⁸ Certainly the former condition constitutes "stomach or intestinal trouble," and the facts of *Thomas-Yelverton Co. v. State Capitol Life Insurance Co.*²⁹ so closely parallel the latter symptom as to raise grave questions as to the court's propriety in omitting it from their analysis.

Similarly, the court explains away any culpability of the insured in failing to enumerate the circumstances surrounding the affirmative answers to question 11 by ruling that the insurer already had the equivalent of the information it sought.³⁰ Quoting from *Gouldin v. Inter-Ocean Insurance Co.*,³¹ the court pointed out:

Knowledge of facts which the insurer has or should have had constitutes notice of whatever an inquiry would have disclosed and is binding on the insurer. The rule applies to insurance companies that whatever puts a person on inquiry amounts in law to "notice" of such facts as an inquiry pursued with ordinary diligence and understanding would have disclosed.³²

Although this argument is entitled to some weight in light of the insured's limited response to question 13, which in turn left his affirmative replies to question 11 unanswered, the court destroys much of its force by an earlier observation. In ruling that the insured had answered question 11 as fully as its broad phraseology would permit, the court admitted:

Each of these rejoinders could well have been referable to the appendectomy. Likewise they could have related to the medical attention he received for liver troubles or to any of the possible maladies not appearing in question 10. No deception or half-truth is proved here.³³

Although no deception or half-truth was proved in question 11, this same statement highlights the fallacy of the argument that the insurer was in possession of facts sufficient to put it on notice in question 13. It is true that insurance contracts are to be construed liberally in favor of the

²⁸ 424 F.2d at 1007.

²⁹ 238 N.C. 278, 77 S.E.2d 692 (1953). Here, the insured's negative response to a question pertaining to the existence of any diseases of the stomach was held to afford sufficient grounds for rescission on the insurer's showing that the insured had experienced the vomiting of blood in connection with a peptic ulcer.

³⁰ 424 F.2d at 1009.

³¹ 248 N.C. 161, 102 S.E.2d 846 (1958).

³² 424 F.2d at 1010.

³³ *Id.* at 1009.

insured.³⁴ But though the sword may cut sharper on the side of the insured, this does not necessarily imply that it cannot be double-edged at all. Just as the responses to question 11 might have alluded to either the insured's appendectomy or liver ailment, so too might the limited response to question 13 have indicated that the affirmative answers in question 11 were similarly limited to question 10(d). Inasmuch as the opinion of the individual insurer is favored over that of similar or reasonably prudent insurers upon the issue of materiality,³⁵ it would seem reasonable to afford the specific insurer an opportunity to show its interpretation of a disputed answer when the representation is deemed material as a matter of law.

Even assuming that the insurer did have a duty of inquiry, it could only be held to those facts which an investigation pursued with ordinary diligence would have disclosed.³⁶ Had it undertaken such an inquiry, it is highly doubtful that it would have obtained the vital information with which it was ultimately charged. The only details disclosed in question 13 concerned the insurer's hospitalization at Memorial Hospital under the care of Dr. Bell. Although an investigation of the hospital records would have revealed the insured's subsequent admittance for the vomiting of blood, it would have shown that he left the hospital apparently well and with no indications of his extensive liver ailment.³⁷ Nor is there any suggestion either that Dr. Bell was aware of the insured's later treatment by Dr. Weeks or that Memorial Hospital had any record of the insured's confinement at the other sanitarium.³⁸

In its concluding remarks the court holds that even if the insured had concealed material facts, the insurer waived the defect and elected to treat them as immaterial.³⁹ It is clear that an insurer may waive provisions that are inserted in an insurance contract for its benefit.⁴⁰ By acting on an answer that is unresponsive or manifestly incomplete, an insurer precludes later objection on its part.⁴¹ "But . . . the mere fact that the insurer has

³⁴ *E.g.*, National Bank v. Fidelity & Cas. Co., 125 F.2d 920, 923 (4th Cir. 1942); Suits v. Old Equity Life Ins. Co., 249 N.C. 383, 386, 106 S.E.2d 579, 582 (1959); Mills v. Metropolitan Life Ins. Co., 210 N.C. 439, 441, 187 S.E. 581, 582 (1936).

³⁵ Note, 5 U.C.L.A.L. REV., *supra* note 9, at 334 & n.15.

³⁶ Note, *Insurance—Insurer's Duty—Investigation for Suspected Fraud Prior to Issuance of Life Policy*, 10 ARK. L. REV. 499, 499-500 (1956).

³⁷ 424 F.2d at 1007.

³⁸ *Id.* at 1012 (dissenting opinion).

³⁹ *Id.* at 1010.

⁴⁰ *E.g.*, Bray v. North Carolina Police Voluntary Benefit Ass'n, 258 N.C. 419, 424, 128 S.E.2d 766, 770 (1963); Widows Fund of Sudan Temple v. Umphlett, 246 N.C. 555, 560, 99 S.E.2d 791, 794 (1957).

⁴¹ Phoenix Life Ins. Co. v. Raddin, 120 U.S. 183, 190 (1887).

knowledge that some of the statements in an application are incorrect does not of itself put the insurer on inquiry, and charge it with knowledge of all the facts that an inquiry, would disclose."⁴² Rather, it is the character of the information possessed by the insurer which is determinative.⁴³

From the facts disclosed in the application, the insurer would have no occasion to suspect that the physician's recent discovery of the applicant's physical defects indicated an uninsurable condition. Instead, the more reasonable inference was that the affirmative answers in question 11 pertained to the applicant's only previous illness disclosed in the application, namely, the appendectomy in 1964. Such an inference is clearly supported in light of *Barden's* assertion of good health at the time of the application. These facts being insufficient to impose a duty of inquiry⁴⁴ and an investigation being unlikely to yield the vital information, it is difficult to justify the court's decision on the waiver issue. Waiver, being the voluntary relinquishment of a known right,⁴⁵ necessarily requires knowledge of the existence of that right and an intent to surrender it.⁴⁶ Without the requisite character of information (and no reason to obtain it), the insurer could hardly be held to have intentionally relinquished his equitable right to rescind.

Such a result-oriented decision as *Barden* is particularly difficult to reconcile with the basic notion of *uberrima fides*. Since the parties deal at arms length, the insurer must of necessity rely upon the applicant's good faith for its knowledge of the facts.⁴⁷ Prior to *Barden* a prime deterrent against a breach of this good faith was the knowledge on the part of the insured that should his misrepresentations be discovered within the contestable period, his wager with the insurer would yield no more than his total investment. The decision in *Barden*, however, effectively reduces the time allowed for the insurer's challenge and, in so doing, serves notice upon the clever but uninsurable applicant that the odds in his favor have been increased. By removing several questionable issues from the

⁴² *Provident Life & Accident Ins. Co. v. Hawley*, 123 F.2d 479, 482-83 (4th Cir. 1941) (applying North Carolina law).

⁴³ *Id.* at 483.

⁴⁴ In *Hawley* the insurer inquired and learned that the insured had been cured of an affliction prior to the application but was not precluded from establishing a defense of a related illness that was undisclosed by both the insured and the prior investigation.

⁴⁵ 16A J. APPLEMAN, *INSURANCE LAW AND PRACTICE* § 9081 (1968).

⁴⁶ *Brady v. Funeral Benefit Ass'n*, 205 N.C. 5, 7, 169 S.E. 823, 824 (1933).

⁴⁷ Comment, *Material Misrepresentation As a Requirement For Rescission of Insurance Contracts*, 73 DICK. L. REV. 250 (1969).

consideration of the jury, the policy manifested by section 58-30 of the North Carolina General Statutes has been stretched to an extreme.

WILLIAM W. MAYWHORT

Landlord and Tenant—Retaliatory Evictions and Housing Code Enforcement

The low income tenant in North Carolina must rely primarily upon municipal housing codes to ameliorate substandard housing conditions.¹ Although enforcement of code regulations has to some extent elevated the quality of existing urban housing, the process of repair under the codes, particularly for the benefit of the low income tenant, is hampered by the probability of considerable delay.

There may be delay between the first appearance of the defect and the inspector's knowledge of the defect. Since a limited number of inspectors must inspect not only those dwellings suspected of being substandard but also all other housing in the city,² a general program of area inspections is tedious and time consuming. Therefore, inspectors are forced to rely upon reports of code violations from interested parties as an additional means of discovering violations. A tenant of adequate means, having a bargaining power equal to that of the landlord, is likely to repair himself or prompt his landlord to repair a serious defect rather than reporting it and awaiting municipal action under the enforcement process. But a low income tenant can seldom undertake repair; furthermore, a paucity of decent housing³ may discourage him from antagonizing his landlord by reporting code violations.

The landlord might also retard the process of repair after the defect has been discovered by the inspector. A recalcitrant landlord of slum property will hesitate to expend money for repair of premises of only tenable value⁴ and may take advantage of methods available under the

¹ Enabling legislation for municipal housing codes is found in N.C. GEN. STAT. § 160-182 (Supp. 1969).

² For example, there are six building inspectors to implement a program of city-wide housing inspection for the city of Durham. When the program is completed, it will have taken about ten years. Interview with Building Inspector for the City of Durham, North Carolina, Dec. 10, 1970.

³ The North Carolina General Assembly has recognized that the state suffers from a housing shortage and that a substantial number of existing dwellings are in a substandard condition. N.C. GEN. STAT. § 157-2 (1966) (legislation enabling the establishment of municipal housing authorities).

⁴ See *Symposium—Enforcement of Municipal Housing Codes*, 78 HARV. L. REV. 801 (1965).