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Equitable Conversion as Affecting Purchaser's Rights to Vendor's Insurance Policy

Harry I. Stegmaier

NOTES

EQUITABLE CONVERSION AS AFFECTING PURCHASER'S RIGHTS TO VENDOR'S INSURANCE POLICY

The majority rule in America holds that where a contract to sell land has taken place the vendee thereafter, being regarded as the equitable owner, must bear the risk of loss to the property, provided such loss was not caused through the fault of the vendor, and the vendor was not in default so as to be entitled to a decree of specific performance.[1] Kentucky is fully in accord with this view.[2]

In England at common law the vendee after the sale of the property was held to have no rights to insurance money on a policy taken out on the vendor's interest[3] even though the risk of loss doctrine is there universally recognized.[4] The opposite stand has been taken in most of the jurisdictions of the United States, which hold that an insurance policy issued after an executory contract of sale of the property accrues to the benefit of the purchaser, even though the contract of insurance existed only with the vendor, and no assignment, express or implied, had been effected.[5] The English view has been followed in a few

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[1] *Hough* v. *City Fire Ins. Co.*, 29 Conn. 10 (1860) (dictum); *Parcell* v. *Grosser*, 109 Pa. 617, 1 Atl. 909 (1885); *Snyder* v. *Murdock*, 51 Mo. 175 (1872).

[2] *Cottingham* v. *Fireman's Fund Ins. Co.*, 90 Ky. 439, 14 S. W. 417 (1890); *Marks* v. *Tichenor*, 85 Ky. 536, 4 S. W. 225 (1887); *Martin* v. *Carver*, 8 K. L. R. 56, 1 S. W. 199 (1886); *Johnston* v. *Jones*, 12 B. Monroe 326 (1851).

[3] *Rayner* v. *Preston*, 18 Ch. Div. 1 (1881); *Poole* v. *Adams*, 12 W. R. 683 (1864); *West of England Fire Ins. Co.*, v. *Isaacs*, 1 Q. B. 226 (1897); *Phoenix Ins. Co.* v. *Spooner*, 2 K. B. 753 (1905).

[4] *Paine* v. *Mellor*, 6 Ves. Jr. 349 (1801); *Minchin* v. *Nance*, 4 Beav. 332 (1841).

[5] *Baker* v. *Rushford*, 91 Vt. 495, 101 Atl. 769 (1917); *Gilbert* v. *Post*, 28 Ohio St. 276 (1876); *Williams* v. *Lilley*, 67 Conn. 50, 34 Atl. 765 (1895); *Wm. Skinner Co.* v. *Houghton*, 92 Md. 68, 48 Atl. 85 (1900); *Hill* v. *Cumberland Valley Co.*, 59 Pa. St. 474 (1861) (dictum); *Kauffman* v. *All Persons*, 16 Cal. App. 388, 117 Pac. 586 (1911); *Russell* v. *Elliott*, 45 S. D. 184, 186 N. W. 824 (1922); *Milleville Aerie* v. *Weatherby*, 82 N. J. Eq. 455, 88 Atl. 847 (1913); *Standard Oil Co.* v. *Dye*, 223 Mo. App. 926, 20 S. W. (2d) 946 (1929); *McGinley* v. *Forrest*, 107 Neb. 309, 186 N. W. 74 (1921); *Brady* v. *Welsh*, 200 Iowa 44, 204 N. W. 235 (1925).

states.[6] Kentucky, following the majority opinion, allows the purchaser to recover.[7]

The right of the vendee to secure the proceeds of an insurance policy taken out by the grantor has been justified by the courts on three grounds. (1) Most of the cases go on the theory that where the vendor receives insurance money after a loss he holds it in trust for the benefit of the vendee.[8] This view seems erroneous. Because the vendee is entitled to specific performance of the executory contract does not of itself make the vendor a trustee. No trust exists here in any form as the vendor has a personal interest in the res—the property. He holds the land as security for the debt owing by the purchaser, he is entitled to the rents and profits until title has passed, and he cannot be held to an accounting as a trustee can be. No valid grounds exist for the imposing of a constructive trust on the vendor since no fraud has been practiced by him on the purchaser, and even though it may be inequitable for the vendor to retain this money since he has suffered no detriment, it does not follow that the vendee has a right to it. It rightfully belongs to the insurer.[9] (2) A number of jurisdictions, including Kentucky, lay down as the reason for the rule that the insurance money is to be treated as a substitute for the property destroyed.[10] This theory contemplates that a policy taken out on the vendor's interest follows the propery covered without the necessiy of an assignment or other express agreement. This view is completely at odds with a fundamental principle of insurance law that a policy is a personal contract of indemnity.[11] Therefore, insurance does not run

[6] *Remington* v. *Sabin*, 132 Minn. 372, 157 N. W. 504 (1916); *King* v. *Preston*, 11 La. Ann. 95 (1856); *Wilson* v. *Hill*, 3 Metc. 66 (1841); *McCutcheon* v. *Ingraham*, 32 W. Va. 378, 9 S. E. 260 (1889).

[7] *Mattingly* v. *Springfield F. & M. Ins. Co.*, 120 Ky. 768, 83 S. W. 577 (1904); *Godfrey* v. *Alcorn*, 215 Ky. 465, 284 S. W. 1094 (1926).

[8] *Phoenix Ins. Co.* v. *Mitchell*, 67 Ill. 43 (1873); *Brewer* v. *Herbert*, 30 Md. 301 (1868); *Peoples Street Ry. Co.* v. *Spencer*, 156 Pa. 85, 27 Atl. 113 (1893); *Brakhage* v. *Tracy*, 13 S. D. 343, 83 N. W. 363 (1900); *Wm. Skinner Co.* v. *Houghton*, 92 Md. 68, 48 Atl. 85 (1900).

[9] *King* v. *Preston*, 11 La. Ann. 95 (1856).

[10] *Doty* v. *Rensselaer Ins. Co.*, 176 N. Y. S. 55 (1919); *Mattingly* v. *Springfield F. & M. Ins. Co.*, 120 Ky. 768, 83 S. W. 577 (1904); *Williams* v. *Lilley*, 67 Conn. 50, 34 Atl. 765 (1895); *Callahan* v. *Linthicum*, 43 Md. 97 (1875); *Brownell* v. *Board of Education*, 204 N. Y. S. 150 (1924) (dictum).

[11] *Place* v. *Norwich & N. Y. Transp. Co.*, 118 U. S. 468 (1885); *Lucena* v. *Crawford*, 2 B. & P. (N. R.) 269 (1802); *Cromwell* v. *Brooklun Fire Ins. Co.*, 44 N. Y. 42 (1870).

with the land since it is the vendor's interest alone which is protected and not the property itself.[12] (3) *Insurance Co.* v. *Updegraff*[13] enunciates the view that since the parties at the time of making the contract of insurance intend that the insurance cover the whole interest and, therefore, that the purchaser's interest be protected, the courts should give legal effect to this intention, even though no express assignment be made. Attributing such an intention to insurers lacks an essential basis of fact. It seems that such a business custom does not exist among them for the reason that many vendees realize that they are not entitled to the benefit of the vendor's insurance on the property. This is evidenced by numerous contracts which expressly stipulate for the benefit of the grantor's insurance, or that he bear the risk of loss until the date of performance. Likewise, the fact that vendees often insure their interest indicates that no such idea exists among insurance companies.[14] It seems, therefore, that the courts do not have a sufficient legal basis for their holding.

The minority view, which holds that a vendee under an executory contract to sell property is not entitled to the insurance money on a policy taken out by the vendor on his interest even though the risk of loss be on the purchaser, is sound. It must be remembered that the policy constitutes a personal contract between the insurer and the vendor to indemnify any loss which the vendor may suffer by reason of the partial or total destruction of the property.[15] If the vendee is allowed to recover it would mean that the insurance company would be insurer of the interests of both the vendor and the vendee for which it has been paid in premiums only for the interest of the vendor. No presumption, then, can be invoked that the insurer meant to protect both interests. The fact that the purchaser is recognized as equitable owner and, therefore, affected by any deterioration of the property and that the vendor has insurance on the property are two entirely distinct matters, and since the

[12] *Rayner* v. *Preston*, 18 Ch. Div. 1 (1881).

[13] 21 Pa. St. 513 (1853).

[14] See the following cases in which the rights of a vendor to insurance taken out by the purchaser on his interest have been adjudicated. *Hammer* v. *Johnson*, 44 Ill. 192 (1867); *G. & B. Coal Co.* v. *Southern Elkhorn Coal Co.*, 217 Ky. 827, 294 S. W. 792 (1927); *Cetkowski* v. *Knutson*, 163 Minn. 492, 204 N. W. 528 (1925).

[15] Note (11), *supra*.

purchaser is a stranger to the contract of insurance he secures no rights thereunder which entitle him to the fund. The position of the insurance company is not considered in these cases. There is no doubt that if the risk of destruction falls on the vendee before title passes the vendor is not damnified by the loss and, therefore, the insurer would be within its rights in refusing to make any sort of a payment,[16] or, if it had, in recovering it back from the vendor.[17] The insurance companies should not be forced to bear these losses for which they are not compensated just because they may be financially better able to stand them than the purchaser who has not the benefit of insurance. Likewise, the courts should not at the present time try to hold insurers accountable on doubtful grounds as was formerly done in many instances, since the object of the courts to relieve from hardship caused by the unfair methods of dealing with the public indulged in by insurance companies has been largely done away with by the insurers themselves, or has been eliminated by statutes. The fact that the insured vendor receives a fund, which in fact really belongs to the insurance company because he has not suffered any loss, does not give the purchaser any rights to it even though the vendor may be able to get specific performance with full compensation from the purchaser and thus profit by the destruction of the property.[18] If the insurer sees fit to pay to the vendor a sum it is not legally bound to pay, it is not the vendee's affair.

It might be added that the vendee has suffered no hardship against which the courts should relieve in view of the fact that several convenient and simple ways are at his disposal in order to alleviate the loss which the law imposes upon him. He might insure his own interest since he as well as the vendor has an insurable interest.[19] He could have stipulated in the contract

[16] *Mahan* v. *Home Ins. Co.*, 205 Mo. App. 592, 226 S. W. 593 (1920); *Gottingham* v. *Fireman's Ins. Co.*, 90 Ky. 439, 14 S. W. 417 (1890).

[17] *Castellain* v. *Preston*, [1883] 11 Q. B. 380; *Davidson* v. *Hawkeye Ins. Co.*, 71 Iowa 532, 32 N. W. 514 (1887); *Aetna Ins. Co.* v. *Tyler*, 16 Wend. (N. Y.) 385 (1836); *Woodruff* v. *Ins. Co.* 26 N. J. L. 541 (1857); *Phoenix Assurance Co.* v. *Spooner*, [1905] 2 K. B. 753.

[18] *King* v. *Preston*, 11 La. Ann. 95 (1856).

[19] *O'Brien* v. *Paulsen*, 192 Iowa 1351, 186 N. W. 440 (1922); *Elliott* v. *Ashland Ins. Co.*, 117 Pa. St. 548, 12 Atl. 676 (1888); *Ayres* v. *Hartford Ins. Co.*, 17 Iowa 176 (1864); *Hamilton* v. *Ins. Co.*, 98 Mich. 535, 57 N. W. 735 (1894).

of sale that the risk of loss should remain on the vendor until the property had been transferred to him.[20] He could have demanded that he have the benefit of the grantor's insurance.[21] He, too, could have had the policy assigned to him in the contract.[22] He, likewise, could have secured the benefit of the insurance by a stipulation that he would be responsible for the payment of premiums during the period between the date of the execution of the contract and the date of transferring the property.[23] From the ease with which the purchaser could protect himself he should be classed as negligent if he has not taken at least one of the opportunities afforded, and, therefore, the courts should not give him access to a fund to which he has no legal claim on the ground of hardship.

It is submitted, then, that the courts should change their attitude and should refuse a purchaser relief where he is attempting to secure insurance money to be derived from a policy taken out on the vendor's sole interest. If there is felt to be a need for change it should be done by legislative enactment as in England,[24] and Germany.[25]

In closing it might be mentioned that the judicial legislating by the courts in this matter points to the fundamental unfairness and injustice existing in the practice of placing the risk of loss on the vendee as a result of the theory of a conversion of land in equity. Courts instinctively realize the hardship on the vendee in consequence of their enforcement of this rule, and they endeavor to protect him as much as possible. But in relieving him from the harshness of the doctrine, they have not become aware that they are shifting the burden to another equally innocent party, the insurer. The better practice would be to do away with the doctrine of equitable conversion as to

[20] *Brownell* v. *Board of Education*, 239 N. Y. 369, 146 N. E. 630 (1925); *Phinizy* v. *Guernsey*, 111 Ga. 346, 36 S. E. 796 (1900).

[21] *Doty* v. *Renssellaer Fire Ins. Co.*, 176 N. Y. S. 55 (1919).

[22] *Reed* v. *Lukens*, 44 Pa. St. 200 (1863); *Zenor* v. *Hayes*, 228 Ill. 626, 81 N. E. 1144 (1907); *Allyn* v. *Allyn*, 154 Mass. 570, 28 N. E. 779 (1891).

[23] *Naquin* v. *Texas Savings & Real Estate Investment Assoc.*, 95 Tex. 313, 67 S. W. 85 (1902); *Persico* v. *Guernsey*, 220 N. Y. S. 689 (1927); *Fanning* v. *Equitable F. & M. Ins. Co.*, 46 Ill. App. 215 (1892); *Baker* v. *Rushford*, 91 Vt. 495, 101 Atl. 769 (1917); *Scott* v. *Crinnian*, 43 Ont. Law Rep. (1918).

[24] 12 & 13 Geo. 5, Chap. 16, Sec. 105 (1922); amended, 15 Geo. 5, Chap. 5, Sec. 3 (1925).

[25] German Private Ins. Law, Sec. 69 (1).

risk of loss altogether, since it is probably contra to the intention of the parties at the time of making the contract, and since it creates an unwarranted hardship on the vendee, he being subjected to this risk without having a corresponding right to possession, or to the benefits accruing from the use of the property in most cases.

HARRY I. STEGMAIER.