THE INCONTESTABLE CLAUSE IN LIFE INSURANCE POLICIES — A STATUTE OF LIMITATIONS, BUT NOT A CONFESSION OF JUDGMENT

The incontestable clause in its simplest form provides that: "This policy is incontestable after two years from date of issue, except for non-payment of premium."

The object of its incorporation in life insurance policies was to restrict the insurer to a definite time within which to discover any fraud or misrepresentation made by the insured in the application for insurance and to take appropriate action to cancel the policy.

"The general desirability of an incontestable clause is obvious, as much litigation is thereby avoided. Thus, a claim might be denied by the company on the ground of misstatements made by the insured in his application many years before death took place, and it might be difficult either to prove or to disprove the truth of the statements in question. It is, therefore, desirable that the application, which is the basis of the contract, be finally accepted as correct or rejected within a reasonable time after the contract goes into effect. This is the principal object of, and justification for, the incontestable clause."[1]

"It is customary to make life insurance incontestable after one or two years. This gives the company a limited period in which to ascertain whether the contract was secured by fraud. If it fails to do so within the stated period, then when death occurs it cannot go back a few years and use as a defense the fact that the policy was obtained by misrepresentation."[2]

"The purpose of the incontestable clause is to protect com-

1. LIFE INSURANCE, Maclean (Edition of 1929), 163.
2. THE RECORD, American Institute of Actuaries, 1931, Vol. 20, page 91.

panies and their honest policy-holders against fraud and misrepresentation."[3]

The actuary who first drafted an incontestable clause had all this in mind. Why did he incorporate therein the exception of non-payment of premium? The impossibility of ever carrying on a scheme of life insurance affording death and other benefits without the payment of premiums by the insured seems so obvious that no one could successfully contend that a clause in a policy making it incontestable after two years from date of issue really meant that after the expiration of that time the policy would entitle the insured to free insurance and no further premiums need be paid. But apparently that old-time actuary had experienced the mutilation of some of his most carefully-drawn clauses by astute lawyers intent upon gaining for their clients something to which they were not entitled according to actuarial principles. He feared that counsel learned in the law might be found to make this contention for free insurance after the expiration of the incontestable period and even that some court might uphold that contention. Perhaps some such case as *Kline v. Benefit Ass'n.*,[4] aroused his anxiety, as the court there stressed the necessity of a strict clause in a policy giving the right to declare a forfeiture thereof for non-payment of premium to justify such action by the insurer. It seemed wise to make use of this protection.

So the exception was added to the clause out of abundant caution and, though it may have removed the fear of any claim of free insurance, it has not prevented other interpretations of the incontestable clause not then foreseen.

"This clause contains several reservations. The generally accepted view appears to be that the companies made a mistake in the beginning by using any reservations, but this mistake was perpetuated when the statutes were enacted.

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3. *Id.*, page 99.
4. 111 Ind. 462, 11 N.E. 620.

"When the company thus qualifies the incontestable clause, it merely reiterates its privilege of relying on the terms of the policy. This raises an inference that it may be contesting its policy though it is merely seeking to have the terms enforced."[5]

"As Mr. W. M. String said in 1926, the exceptions . . . are extraneous and tend to befog the issue. In the first place, the exception as to non-payment of premiums is not necessary. The policy provides what happens in case premiums are not paid, and it is not a contest of the policy within the meaning of the incontestable clause for the company to decline payment because of non-payment of premiums."[6]

"The damage caused by these reservations is, however, of long standing and now the companies do not feel safe in eliminating such exceptions. They normally insert the stipulation regarding non-payment of premiums, and adjustment in case of misstatement of age."[7]

One or two exceptions, as indicated above, are not burdensome and do not unduly lengthen the clause; but they do give rise to unwarranted inferences which, if mutiplied and upheld, may eventually require substantially the entire policy to be incorporated in the incontestable clause. This repetition ought to be avoided. It would make the policy about twice as long as it is at present and would not contribute to its clarity, though it would afford protection from the claim that the incontestable clause enlarges the scope of the policy contract itself.

"The incontestable clause has been with us for more than fifty years. It will probably be with us in some form as long as there is life insurance, not only because it is required by statute

5. ACTUARIAL SOCIETY OF AMERICA, TRANSACTIONS, 1935, Vol. 36, p. 58.

6. RECORD OF AMERICAN INSTITUTE OF ACTUARIES, Vol. 15, page 246.

7. ACTUARIAL SOCIETY OF AMERICA, TRANSACTIONS, 1935, Vol. 36. page 58.

8. ACTUARIAL SOCIETY OF AMERICA, TRANSACTIONS, 1935, Vol. 36, page 54.

in more than thirty states, but also because it gives security to the policy-holder and, on the whole, is approved by the companies."[8]

"The incontestable clause is an anomaly in contract law. To a great extent it nullifies the well-established legal principle that fraud in the procurement of the contract vitiates that contract. It introduces a novel idea into the law, as it recognizes that one party may have secured the contract by defrauding the other, but the parties agree that nevertheless the contract shall be valid."

"The clause was voluntarily introduced by most companies and used for many years before it was required by law."[9]

"The first statute requiring an incontestable clause was enacted in New York in 1906 as part of the Armstrong legislation, and in the following decade similar legislation was taken in about half of the states."[10]

What is a contest of a policy by a life insurance company within the meaning of the incontestable clause? Does it include a proceeding to uphold the terms of the policy rather than an attempt to set them aside? Is a defense by a company to a suit on a policy, by which the defendant insists upon the validity of its provisions, and relies upon the language of the policy as defining its coverage, rather than an attempt to show that the policy is void because of fraud in its procurement, such a defense as is precluded by the incontestable clause after the expiration of the time limited thereby?

In a paper on the *Development of the Incontestable Clause* read before the Association of Life Insurance Counsel, December 8, 1920, Arthur I. Vorys, Esq., Associate Counsel of Western and Southern Life Insurance Company, in considering what does and what does not constitute the contest of a policy, suggested the following illustrative cases:

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9. *Id.*, page 56.
10. *Id.*, page 57.

"If a testator devise land to his brother, with a proviso that if the brother marry before the testator dies the land shall go to the testator's heirs; then in case the brother marries and the testator dies, and the heirs claim the land, no one would say they are contesting the will. The law, in providing for contests of wills, usually fixes a short period of a year or two within which an action to contest a will must be brought. If the heirs in this hypothetical case should commence an action against the brother to recover the land after the contestable period had expired, the brother certainly would not be heard to say that this is an action to contest the will and, therefore, could not be brought after the incontestable period had commenced to run. The action, and the title of the heirs, would not be to contest, or dispute, or to attack the validity of the wills, but to enforce the will according to its terms.

"If a building contract provides for a reduction in the price to be paid in case the construction is delayed beyond a fixed time, with a stipulation that the contract shall be incontestable after one year, then in case the contractor sue after the exipration of a year, no one would say that the owner cannot demand the reduction in the price upon proof of the delay."

To which the author added, with good reason one would think: "The principles involved in these illustrations are self-evident."

These principles are not perfectly self-evident to those who insist that after the time specified in the incontestable clause has expired, not only may the insurer not allege and prove that the applicant for the insurance was guilty of fraud in procuring the policy, which is what the clause was intended to accomplish; but also that the insurer may not deny liability, notwithstanding what the policy covers and what it does not cover by its terms, when the contestable period has expired, and especially when some exception of coverage is not made in the incontestable clause itself.

A leading and instructive case upon the matter of coverage is *Metropolitan Life Ins. Co. v. Conway, Superintendent of Insurance.*[11] An application by the insurance company was made to the Superintendent of Insurance for approval of a rider to be attached to life insurance policies. The rider provided that death as a result of service, travel or flight in any species of air craft, except as a fare-paying passenger, is a risk not assumed under this policy; but if death occurred as a result of such service, travel or flight, the company will pay to the beneficiary the reserve on this policy.

Approval was refused by the Insurance Department on the ground that the proposed rider was inconsistent with the Insurance Law of New York, providing that a policy shall be incontestable after it has been in force during the lifetime of the insured for a period of two years from its date of issue except for non-payment of premiums and except for violation of the conditions of the policy relating to military or naval service in time of war.

In holding that the rider and statute are consistent, the court, Cardozo, C.J., writing the opinion, said: "The provision that a policy shall be incontestable after it has been in force during the lifetime of the insured for a period of two years is not a mandate as to coverage, a definition of the hazards to be borne by the insurer. It means only this, that within the limits of the coverage the policy shall stand unaffected by any defense that it was invalid in its inception, or thereafter became invalid by reason of a condition broken."

Commenting upon the opinion of Holmes, J., in *Northwestern Mut. Life Ins. Co. v. Johnson,*[12] a case sometimes cited for the proposition that a clause in a policy not referred to in the incontestable clause is governed by the latter, Cardozo, C.J., states that the decision in the Northwestern case is not con-

11. 252 N.Y. 449, 169 N.E. 642 (1930).
12. 254 U.S. 96, 41 S. Ct. 47, 65 L. Ed. 155 (1920).

trary to that in the Conway case. "The clause there in question [Northwestern case] was not a limitation as to coverage. It was a provision for a forfeiture. In case of the suicide of the insured whether sane or insane, the policy was to be 'void'. This meant the forfeiture of the privilege to receive the surrender value of the policy or equivalent benefits, a privilege which would survive if there was merely a limitation of the hazards. Statutes there are indeed whereby the enjoyment of surrender values is preserved against forfeiture by the insurer for breach of a condition as to the payment of premiums, but not against conditions generally. What was said by Holmes, J., of the effect of the 'incontestable clause,' must be read in the light of the question before him. It is true, as he says, that with such a clause the death of the insured coupled with the payment of the premiums, will sustain a recovery in the face of the forfeiting condition. It is quite another thing to say that the same facts will prevail against a refusal to assume the risk. Later cases in the Federal courts develop the distinction clearly. 'A provision for incontestability does not have the effect of converting a promise to pay on the happening of a stated contingency into a promise to pay whether such contingency does or does not happen.' "[13]

The learned Chief Justice makes clear the distinction between a denial of coverage, which the insurer should always be permitted to assert in refutation of a claim on behalf of the insured not covered by the terms of the policy contract; and a defense by the insurer of invalidity of the policy because of fraud or misrepresentation by the insured in applying for it, or a suit by the insurer to cancel it for like reasons, either of which must be instituted within the time limited by the incontestable clause.

The incontestable clause is a self-imposed statute of limitations constituted for the purposes first set forth above. The

13. *Supra,* note 11.

expiration of the period of time provided therein prevents the insurer from raising certain questions concerning the validity of the policy in its inception but does not alter nor add to any of the terms, privileges, and provisions of the contract, which remain as they were when the policy was delivered. The company, by such lapse of time, may be prevented from alleging that the insured was afflicted with disease at the time when he stated in his application that he was in good health, and had received no medical treatment, although he had been attended by physicians, and therefore the policy was void; but in a suit to recover disability benefits, the company may always point to the provisions which define disability, total and permanent, as determining whether or not the proof submitted by the insured brings him within the terms of the policy which define the liability of the insurer.

The age of an applicant for insurance is important in determining the premium which must be required to mature the policy, and as bearing upon certain benefits included therein; so life insurance policies provide for adjustment for misstatement of age. This adjustment must be made whenever the true age is discovered, so that the correct premium will be paid, or the amount of insurance made to correspond with what the premium actually paid would have purchased at the true age of the insured, and thus all policy-holders of the same age and class, having similar policies, be treated alike and discrimination avoided as required by the statutes of the several States.

This is fundamental, and the incontestable clause has no bearing upon it. An adjustment for misstatement of age is not a contest of the policy, nor any attempt at avoidance of it, but a compliance with its terms. It has been in many instances incorporated in the incontestable clause as an exception, *viz.*, that the policy shall be incontestable after a specified period except for misstatement of age; and this because of the same fear which led to the incorporation of the exception of non-

payment of premiums. Neither exception is appropriate in the incontestable clause, and their inclusion therein and in statutes has caused confusion and contributed to the idea that a policy cannot be contested by the insurer on any ground not specified in the incontestable clause itself.

Clear and conclusive as the opinion in the case of *Metropolitan Life Ins. Co. v. Conway*[14] appears to be, it is not universally followed. *State ex rel. Republic National Life Ins. Co. v. Smrha et al.*,[15] was a case of refusal to approve a form of rider restricting liability in case of death as a result of engaging in aviation. The insurance company sought a peremptory writ of mandamus against the director of the department of insurance and against the department itself to compel the approval of a form of rider restricting liability in the event of the death of the insured as a result of engaging directly or indirectly in aviation—a not unreasonable demand as frequent accidents show.

It was not questioned that a life insurance company may lawfully restrict and limit the risk assumed by the insurer in the absence of statutory prohibition; but reference was made to the statutory incontestable clause making the policy incontestable after it shall have been in force during the lifetime of the insured for two years from its date, except for non-payment of premiums, and except for violations of the conditions of the policy relating to naval and military service in time of war. Also, reference was made to the statute preventing a provision by which the settlement at the maturity of any policy shall be of less value than the amount promised on the face of the policy plus dividend additions, if any, less indebtedness, and less any premium that may by the terms of the policy be deducted.

The court reached the conclusion in considering both statutes that, after the period of contestability has expired, with all

14. *Supra*, note 11.
15. 293 N.W. 375 (Neb. 1940).

premiums paid and no question of naval or military service involved, the sole issue is the death of the insured.

It is said that the Nebraska Insurance Department had approved such risk exclusion clauses for twenty-three years and then suddenly changed its ruling. The case shows the effect of the inclusion of the exception of non-payment of premiums, which raises the question whether the protection of the companies requires other exceptions, such as military or naval service in time of war. Then comes the question of disability benefits and the rest of the life insurance policy.

As to the case of *Metropolitan Life Ins. Co. v. Conway,*[16] the Nebraska court merely said that it and similar cases had been carefully examined and the conclusion reached that the better view is to the contrary. No serious attempt was made to controvert the reasoning of the New York Court of Appeals and, however strongly the Supreme Court of Nebraska may have felt itself controlled by the statutes to which it referred in making its decision, one is justified in assuming that, in general, the incontestable clause is not, and ought not to be, a mandate as to coverage, and that there is a distinction between a denial of coverage and a defense of invalidity.

The case of *Dibble v. Reliance Life Ins. Co. of Pittsburg, Pa.,*[17] decided by the Supreme Court of California in 1915, is often cited in support of the proposition that an incontestable clause, after the expiration of the contestable period, bars and precludes every defense to or any contest of the policy on any ground which is not specifically reserved or excepted in the incontestable clause itself.

The defense was ill-health of the insured at the time the policy was issued, and which was not disclosed in the application therefor.

The incontestable clause, after referring to the application,

16. *Supra,* note 11.
17. 170 Cal. 199, 149 Pac. 170 (1915).

a copy of which was attached to the policy, both constituting the entire contract between the parties, provided that the policy shall be incontestable after one year from its date, except for non-payment of premiums and except as otherwise provided in the policy. The defense was clearly one of fraud and the court gave consideration to section 1668 of the Civil Code of California to the effect that contracts exempting one from responsibility for his own fraud are against the policy of the law, and concluded that insurance policies are contracts, but do not exempt the insured from the consequences of his own fraud, but merely fix a reasonable limit to the time in which a defense of fraud may be urged. There was no exception of fraud in the clause, and the court said that there was nothing to suggest that a defense on the ground of fraudulent statements would not be barred by the lapse of time prescribed by the provision.

The statement for which the case is frequently cited as indicated above is broader than the decision required. What the court said was: "... the decisions in other states are practically unanimous in holding that a provision in a life insurance policy, to the effect that, after being in force the specified time, it shall be incontestable, precludes any defense after the stipulated period on account of false statements warranted to be true, even though such statements were fraudulently made, unless by the terms of the policy fraud is expressly or impliedly excepted from the effect of such provision."[18] This is not as comprehensive as the rule for which the case is cited as having established.

As the original object of the incontestable clause was to limit the time within which the defense of fraud in the application could be set up, and this was a case of fraud, and the time had expired, it would seem that this was a claim that might well have been paid without suit.

The *Dibble* case has led to the adoption of the comprehensive language by some of the courts. *Missouri State Life Insurance*

18. *Supra*, note 17.

Co. v. Cranford;[19] *Dorman v. John Hancock Mut. Life Ins. Co.;*[20] *Mutual Reserve Fund Life Ass'n. v. Austin;*[21] *Equitable Life Assurance Society v. Dean.*[22] "But now by the federal decisions without any noted exceptions, and in many State courts, the clause does not bar a contest over claims for loss not within the coverage of the policy."[23]

Certainly the language employed in stating and discussing the subject of incontestability of life insurance policies needs revision. The American Life Convention, Legal Section, in 1932, proposed this language: "After this policy of life insurance shall have been in force (during the lifetime of the insured) for a period of two years from the date borne by this policy it shall not be contested on any ground affecting its original validity."[24]

Forgery of a policy, or substitution of a healthy person to take a medical examination for a sick applicant ought to affect the original validity of the policy, and contest should be allowed even though the crime or fraud were successfully concealed for more than two years. Such cases might be handled on the theory that there was no policy at all.

If this proposal departs too much from that now existing in statutes and policies for practical adoption, it might be stated that: "This policy, within the limits of its coverage, is incontestable," etc., though this should not be necessary if the clause as originally drafted were reasonably interpreted. To say and intend that the language should be taken literally, that the

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19. 257 S.W. 66, 67.
20. 25 Fed. Supp. 889 at page 891.
21. 142 Fed. 398, at page 401, 6 L.R.A. (N.S.) 1064.
22. 91 Fed. 2d 569, at page 572.
23. 29 Am. Jur., INSURANCE, sections 880-900, especially 885 and 890, where the cases are collected.
24. ACTUARIAL SOCIETY OF AMERICA, TRANSACTIONS, 1935, Vol. 36, page 54.

time having expired, the incontestable clause bars and precludes every defense to or any contest of the policy on any ground which is not specifically reserved or excepted in the incontestable clause itself, opens such a wide field to unjust as well as honest claimants, that one is forced to the conclusion that it must be an over-statement; or at least to the hope that it will prove to be so.

Suppose that a suit is brought to recover disability benefits. The insured misrepresented his state of health in applying for the policy, but the time stated in the clause has expired. The insurer cannot defend on the ground of fraud. But the insured is not totally and permanently disabled. Disability benefits are not excepted in the incontestable clause. The fact is that the insured cannot by medical evidence bring himself within the coverage of the provisions of the policy relating to disability. Is the insurer barred and precluded from defending on the ground that the insured is not totally and permanently disabled within the language of the disability provisions? Should a motion to reject the offer of the insurer's evidence be granted? Indeed not! Then the language barring and precluding the company needs to be made less unrestrained.

And disability benefits are not the only provisions in life insurance policies. Already the statutes and policies add to the incontestable clause various exceptions in addition to non-payment of premiums, such as adjustment for misstatement of age, naval and military service in time of war, and disability benefits. Unless the incontestable clause receives a reasonable interpretation and unless its original meaning and purpose are restored to that of affording the companies a reasonable time in which to discover fraud and misrepresentation and to take appropriate action or defense, and preventing them from doing so after the time limit has expired, then the exceptions noted in the clause will have to be multiplied by statute and contract until the policy contract is substantially repeated in the incon-

testable clause. Then the clause will be defined, not by stating what it is, but by stating with innumerable exceptions what it is not. It should not be deemed a warrant to confess judgment.

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