Volume 2 | Number 1 Article 6

3-1-1970

Antedated Contract of Property Insurance May Protect against a Loss Occurring Prior to Issuance of the Policy, Absent Fraud or Negligent Concealment.

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CASE NOTES

INSURANCE—ANTEDATED POLICIES—ANTEDATED CONTRACT OF PROPERTY INSURANCE MAY PROTECT AGAINST A LOSS OCCURRING PRIOR TO ISSUANCE OF THE POLICY, ABSENT FRAUD OR NEGLIGENT CONCEALMENT. *Burch v. Commonwealth County Mutual Ins. Co.*, 450 S.W.2d 838 (Tex. Sup. 1970).

Burch contacted an insurance salesman to obtain insurance on his automobile. The salesman notified him that he was covered, but did not specify a particular company. The salesman calculated the premium and accepted Burch's check. The following morning the salesman took the application to the general agent of the insurer. The salesman was not an agent of the insurer; rather, he was acting on behalf of Burch in procuring the policy. The general agent of the insurer accepted the application, cashed the check, and mailed the policy to Burch. The policy provided for antedated coverage from 12:01 a.m. of the previous day. Unknown to the salesman or to the general agent, the automobile had been destroyed in a collision that occurred after Burch had dealt with the salesman, but before the salesman had procured the policy from the general agent. Burch had tried to reach the salesman that morning to inform him of the collision, but he was unable to do so until two or three days later. Although the loss occurred within the stipulated policy period, the insurer sought to cancel. Burch filed a cross-action for his damages. The trial court granted Burch's motion for summary judgment, but the court of civil appeals reversed[1] on the theory that an insurance policy may never protect against a loss that occurred prior to the making of the contract. Held—*Reversed.* An antedated contract of property insurance may protect against a loss occurring prior to issuance of the policy, absent fraud or negligent concealment.

Insurance that covers existing losses is well known in the field of marine "lost or not lost" policies.[2] At an early date, the validity of promises to pay for existing losses was extended to the field of fire insurance as well, when the policy was antedated and the loss occurred between the date specified and the delivery of the policy.[3] These early

1 Burch v. Commonwealth County Mutual Ins. Co., 440 S.W.2d 410 (Tex. Civ. App.—Beaumont 1969), *rev'd*, 450 S.W.2d 838 (Tex. Sup. 1970).

2 M'Lanahan v. Universal Ins. Co., 26 U.S. (1 Peters) 170, 7 L. Ed. 98 (1828); Watson v. Delafield, 3 N.Y. Com. L. R. 474 (N.Y. 1807); Andrews v. Marine Ins. Co., 4 N.Y. Com. L. R. 656 (N.Y. Sup. 1811); Snow v. Mercantile Mut. Ins. Co., 61 N.Y. 160 (N.Y. 1874).

3 Hallock v. Commercial Ins. Co., 26 N.J. 268 (1857); Collins v. Phoenix Ins. Co., 21 Sup. Ct. N.Y. 534 (N.Y. Sup. 1878).

cases recognize that the basis of the insurance contract is risk.[4] They also recognize that this fundamental element is present when no loss is *known* to have occurred.[5] Thus, the courts had no difficulty in holding the insurer liable, even though a loss had occurred prior to the issuance of the policy,[6] provided the loss was unknown to both parties.[7] The risk was present in these cases because, as far as the parties knew, a loss may or may not have already occurred.[8] Thus, in the marine cases, the insurer was bound to pay for the loss even though the ship was lost prior to the issuance of the policy;[9] and the insured was required to pay the premium, notwithstanding the ship had safely arrived before the policy was issued.[10]

In 1938 Justice Black helped extend the validity of antedated policies into the general body of insurance law, when he observed that no legal obstacle prevents parties, if they so desire, from entering into contract of insurance to protect against losses that may have already occurred.[11] Such policies have since become widely recognized as being valid.[12]

At an early date, it appeared that Texas would follow the weight of authority in the United States. In *Blake v. Hamburg-Bremen Fire Ins. Co.*,[13] Justice Gaines seemed to recognize that it is the *knowledge* of the loss and not the *fact* of the loss that determines risk. In relieving a fire insurance company of liability on an antedated contract, he stated:

> It is not a case of two parties making a contract of insurance upon property already lost, agreeing to date it from a past day;

4 Kline Bros. Co. v. Royal Ins. Co., 192 F. 378, 388 (C.C.S.D. N.Y. 1911); *See also* Matlock v. Hollis, 109 P.2d 119, 132 A.L.R. 1325 (Kan. 1941).

5 Security Fire Ins. Co. v. Kentucky Marine & Fire Ins. Co., 70 Ky. 81 (1870).

6 Collins v. Phoenix Ins. Co., 21 Sup. Ct. N.Y. 534 (N.Y. Sup. 1878); Walker v. Lion Fire Ins. Co., 34 A. 736 (Pa. 1896).

7 Wales v. New York Bowery Fire Ins. Co., 33 N.W. 322 (Minn. 1887); Continental Casualty Co. v. Lanzisero, 181 A. 170 (N.J. App. 1935).

8 Security Fire Ins. Co. v. Kentucky Marine Fire Ins. Co., 70 Ky. 81 (1870).

9 Paddock v. Franklin Ins. Co., 28 Mass. 227 (1831).

10 Bradford v. Symondson, L. R. 7 Q.B.D. 456 (1881).

11 United States v. Patryas, 303 U.S. 341, 345, 58 S. Ct. 551, 554, 82 L. Ed. 883, 886 (1938).

12 Cases recognizing the validity of antedated insurance contracts—M.F.S. Mut. Ins. Co. v. Quinn, 295 S.W.2d 854 (Mo. App. 1953); Canadian Indemnity Co. v. Tacke, 257 F.2d 342 (9th Cir. 1958); National Indemnity Co. v. Smith-Gandy, Inc., 309 P.2d 742 (Wash. 1957); Pruitt v. Great American Ins. Co., 86 S.E.2d 401 (N.C. 1955); Ostroff v. Springfield Fire & Marine Ins. Co., 92 A.2d 899 (Pa. 1952); Ried v. Bankers Life Co., 28 N.W.2d 542 (Neb. 1947); Winecoff v. Nationwide Mut. Ins. Co., 444 S.W.2d 84 (Tenn. 1969); St. Julian v. Financial Indemnity Co., 77 Cal. Rptr. 843 (Cal. App. 1969); Dixon v. Western Union Assurance Co., 164 S.E.2d 214 (S.C. 1968); State Mutual Life Assurance Co. v. Heine, 49 F. Supp. 786 (W.D. Ky. 1943), *aff'd*, 141 F.2d 741 (6th Cir. 1944).

Cases denying recovery on antedated contracts where the loss was known to the insured—Matlock v. Hollis, 109 P.2d 119, 132 A.L.R. 1325 (Kan. 1941); Barry v. Aetna Ins. Co., 81 A.2d 551 (Pa. 1951); State Farm Mut. Auto Ins. Co. v. Calhoun, 112 So.2d 366 (Miss. 1959); Broome v. State Farm Mut. Automobile Ass'n., 152 So.2d 827 (La. App. 1963); Hunt v. Aetna Casualty and Surety Co., 387 P.2d 405 (Colo. 1963); Arley v. United Pac. Ins. Co., 379 F.2d 183 (9th Cir. 1967).

13 67 Tex. 160, 2 S.W. 368 (1886).

> both being, at the date of the contract, ignorant of the loss. When the notice was given, the fire was in progress, and the appellants knew it.[14]

Perhaps the case that started Texas down the path of error was *Norwich Union Fire Insurance Society v. Dalton*,[15] which contained this statement:

> Another elementary principle of the law of contracts applicable to insurance is that the property must be in existence at the time the policy is issued. As a corollary to this, the rights of the parties are fixed at the time the property is destroyed.[16]

The court relied on *Blake* as authority for this statement, but in so doing, it failed to perceive the distinction between the *fact* of loss and the *knowledge* of loss, which Judge Gaines had recognized.

If any doubt was created by this statement, it was resolved in a most unfortunate manner in *Alliance Ins. Co. v. Continental Gin*.[17] *Alliance* turned on the question of whether an insured who knew of an existing loss could ratify the unauthorized acts of an insurance agent. The agent had cancelled the policies issued by one company and substituted the policies of another company. In relieving the second company of liability, the court paraphrased an opinion written by the renowned Learned Hand in *Kline Bros. & Co. v. Royal Ins. Co.*[18] Judge Learned Hand was careful to draw the distinction between the fact and the knowledge of the loss; but this was lost in the transition.[19]

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14 Blake v. Hamburg-Bremen Fire Ins. Co., 67 Tex. 160, 165, 2 S.W. 368, 371 (1886).

15 157 S.W. 459 (Tex. Civ. App.—Austin 1914), *rev'd on other grounds*, 213 S.W. 230 (Tex. Comm'n App. 1919, jdgmt adopted).

16 *Id.* at 461.

17 285 S.W. 257 (Tex. Comm'n App. 1926, jdgmt adopted).

18 192 F. 378, 388 (C.C.S.D. N.Y. 1911).

19 Learned Hand, J.:

> . . . . An insurer's undertaking is a promise to pay upon a given event which either must happen in futuro, or if it have already happened must be still unknown. Were it not so, the promise would be merely to pay a large sum of money in consideration of a small one, which is an absurd intention to ascribe to anyone. In the case at bar, since the loss happened before the policy became binding, the promise could only be to pay for an existing loss. Such promises are common enough in marine insurance . . . and they have been held to be binding in the case of fire insurance when the policy was antedated and the loss occurred between the date and the delivery of the policy. . . . [I]n all such cases, however, the policy must . . . be construed as insurance of a risk, not as a certain agreement to pay. . . . Thus in a marine policy, though the loss may have in fact occurred, the fact is unknown, and there is the same aleatory element in the promise as though it might occur in the future. . . .[T]he element of some chance is a condition to the promise of the insured, and, if that element does not exist, his promise is made under a mistake of existing fact. It is of no consequence whether that fact be the actual loss, in a case where the insurance is of future loss, or of the insured's knowledge of the loss, in a case where the insurance is of an existing loss. In either case there must be some uncertainty as to the loss, or else the presupposition upon which the promise is made does not exist.

Compare with the opinion of the Texas Commission of Appeals in *Alliance*, note 20, *infra*.

The Texas Commission of Appeals completely failed to make this distinction and laid down broad dicta indicating that an insurance policy may never protect against a loss that occurred prior to the making of the contract.[20] The effect of this dicta was immediate. In several Texas cases following *Alliance*, the judges made sweeping statements to the effect that no insurance policy could protect property that was already destroyed, with or without the knowledge of the parties.[21] No less a jurist than Justice Norvell was swept up in the tide.[22] While sitting on the Texas Court of Civil Appeals in San Antonio, he was called upon to decide whether recovery could be had on an automobile collision policy, when the auto was destroyed prior to the time when the insured received a renewal policy. The learned Justice, relying on *Alliance*, said a recovery was precluded by a public policy that would inhibit the making or enforcement of an insurance contract in relation to imaginary property, even where both parties so intend.[23] True, an occasional case contained statements to the contrary; but these cases were ignored[24] or overruled.[25] The state of the law by 1956 was such that a federal court said:[26]

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20 Alliance Ins. Co. v. Continental Gin, 285 S.W. 257 (Tex. Comm'n App. 1926, jdgmt adopted):

> Property in esse . . . is the basis of a contract of or for fire insurance. A substantial element is the chance of loss. If either thing be absent (i.e., if there be no property originally or chance of loss be precluded by the certainty incident to preoccurring fire), the insurance company is in the absurd position of freely offering to pay a large and certain sum . . . if the insured will pay to it the comparatively insignificant amount of the premium. . . . Stated another way: In consideration of present payment by one party of the rate named, the other party agrees to pay a larger sum if, and when, a contingency happens; if the contingency does not happen, the one loses the small sum; if it does happen, the other loses a large sum . . . ; and it is entirely nonpermissible to assume that the parties intended to make, or did make, a contract requiring payment of the larger sum if either, or both, of them knew that the contingency, nominally in future, had already occurred. When good faith of both parties is assumed and the property does not exist, there is a mutual mistake of fact as to the very subject matter of the agreement; if the . . . insured knows of the previous destruction, there is present avoiding fraud. . . . [I]t is our opinion that public policy would inhibit the making or enforcement of an insurance contract in relation to imaginary property, even where both parties so intend.

21 United States Fire Ins. Co. v. Fife, 6 S.W.2d 211 (Tex. Civ. App.—Ft. Worth 1928, writ dism'd); American Central Ins. Co. v. Hulen, 30 S.W.2d 563 (Tex. Civ. App.—Ft. Worth 1930), *rev'd on other grounds*, 45 S.W.2d 570 (Tex. Comm'n App. 1932, jdgmt adopted); Trinity Universal Ins. Co. v. Rogers, 215 S.W.2d 349 (Tex. Civ. App.—Dallas 1948, no writ); Mallard v. Hardware Indemnity Ins. Co. of Minnesota, 216 S.W.2d 263 (Tex. Civ. App.—San Antonio 1948, no writ); *see also* U.S. Casualty Co. v. Rodriguez, 288 S.W. 487 (Tex. Civ. App.—San Antonio 1926, writ ref'd).

22 Mallard v. Hardware Indemnity Ins. Co. of Minnesota, 216 S.W.2d 263 (Tex. Civ. App.—San Antonio 1948, no writ).

23 *Id.*

24 Schubert v. McLain & McLain, 27 S.W.2d 846 (Tex. Civ. App.—Amarillo 1930, no writ).

25 Banker's Lloyds v. Montgomery, 45 S.W.2d 285 (Tex. Civ. App.—Eastland 1931), *rev'd* 60 S.W.2d 201 (Tex. Comm'n App. 1933, jdgmt adopted).

26 H. Schumacher Oil Works v. Hartford Fire Ins. Co., 239 F.2d 836, 841 (9th Cir. 1956); *see also* 4 APPLEMAN INS. LAW AND PRACTICE, § 2291, p. 145 (1941): "Texas has held, however, that property in esse and a chance of loss are necessary elements of in-

> Clearly there can be no recovery on those policies . . . written during the fire, whether as original or renewal policies, since such contracts are against the public policy of Texas, even if both parties are ignorant of the existence of the fire and even though all the damage has not yet occurred.

With this background, it is not surprising that the court of civil appeals would not enforce the contract in the principal case.[27] In reversing the decision, the supreme court "rediscovered" the distinction between the *fact* of loss and the *knowledge* of loss.[28] In so doing, the court has returned Texas to the mainstream of law in the United States. Justice Walker could see no reason for not allowing antedated policies. He recognized that the *sine qua non* of the insurance contract —risk—is present, provided neither of the parties know of a loss that has already occurred. Indeed, the court has gone a step further. In the principal case, the insured knew of the loss at the time the contract was entered into. Yet the court would not impute this knowledge to the agent, finding no fraud or neglect on the part of the insured. The court reasoned that since the insured believed he was already covered and since he did not know an insurance contract for his benefit was being made on the morning following the accident, his failure to notify the agent was neither fraudulent nor negligent.[29]

The logic of the court is perhaps best tested by considering the effect of an opposite decision. The enviable position in which such a decision would put the insurance company was recognized by Justice Vredenburgh in *Hallock v. Commercial Ins. Co.*:[30]

> [The insurance company] . . . intentionally made the year's risk commence from the 10th . . . . [T]hey . . . elected to take the premium from the 10th. They took their pay for the very time

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surance, and . . . no valid contract of insurance can be made unless the property is in being at that time."

27 440 S.W.2d 410 (Tex. Civ. App.—Beaumont 1969), *rev'd*, 450 S.W.2d 838 (Tex. Sup. 1970).

28 Burch v. Commonwealth County Mutual Ins. Co., 450 S.W.2d 838 (Tex. Sup. 1970).

29 *Id.* at 841. The court cites as authority Canadian Indemnity Co. v. Tacke, 257 F.2d 342 (9th Cir. 1958) and RESTATEMENT (SECOND) OF AGENCY § 256, Comment "e" (1957). The RESTATEMENT provides:

> A transaction is not affected by the knowledge of a principal which he cannot communicate to the agent, even though he knows that the agent is acting for him without such knowledge. It is only where the principal consciously or negligently fails to communicate with the agent that his knowledge affects the transaction. This is true whether the knowledge is acquired casually or is the result of a notification given by the other party to the transaction.

Several other insurance cases also support this proposition. *See* Pendergast v. Globe & Rutgers Fire Ins. Co., 159 N.E. 183 (N.Y. Sup. 1927); Andrews v. Marine Ins. Co., 4 N.Y. Com. L. R. 656 (N.Y. Sup. 1811); M'Lanahan v. Universal Ins. Co., 26 U.S. (1 Peters) 170, 7 L. Ed. 98 (1828); Cornfoot v. Fowke, 151 Eng. Rept. 450 (1840); *see also* VANCE, HANDBOOK ON THE LAW OF INSURANCE, § 66 (3d ed., 1951).

30 26 N.J. 268, 275 (1857).