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Fred W. Catlett

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STATUS OF THE PROCEEDS OF LIFE INSURANCE UNDER THE COMMUNITY PROPERTY SYSTEM

The vast and increasing amount of money invested in policies of life insurance in the states having a community property system makes the status of the proceeds of such policies under that system of very general interest, and renders it highly desirable and important that the laws as to such contracts should be worked out with dispatch, definiteness and certainty The fact that there are in the community property states different theories as to the character and extent of the wife's interest and different statutes affecting the determination of the rights of the spouses has led to somewhat varying results. As the Supreme Court of Washington has not yet declared itself, with reference to contracts of insurance, upon a number of the questions raised, a discussion of the principles which would seem to be applicable to their solution should be timely

It is with considerable hesitation, however, that one ventures to discuss questions not yet specifically passed upon in this State and on which so many members of the Bar have opinions and ideas drawn from their own practice and experience. One can only proceed with proper humility and with care to avoid error and too much of prophecy as to the future action of our Supreme Court.

A contract of life insurance is like any other contract in that it is a valuable chose in action and property right.[1] As such, its character, whether community or separate, should be determined by the time of its acquisition[2] or by the character of the considera-

[1] *Hutson v. Merrifield*, 51 Ind. 24, 19 A. R. 722 (1875) *St. John v. American Mutual Life Ins. Co.*, 13 N. Y. 31, 64 Am. Dec. 529 (1855)) *Mutual Life Ins. Co. v. Allen*, 138 Mass. 24, 52 Am. Rep. 245 (1884) *In re Brown's Estate*, 124 Wash. 273, 214 Pac. 10 (1923) *Bundy v. Bundy*, 149 Wash. 464, 271 Pac. 268 (1928).

[2] Rem. Comp. St. of Wash., Sec. 6890, 6891, 6892; *In re Brown's Estate*, 124 Wash. 273, 214 Pac. 10 (1923), and many cases cited therein; *Neisz v. Neisz*, 152 Wash. 336, 277 Pac. 849 (1929)

tion given for it. If there is no actual evidence of the character of the consideration it will be determined presumptively by the marital status at the time the contract right is initiated.[3] The problem is complicated, however, because the contract of life insurance is ordinarily of such a character that the consideration is not all paid at the same time, but by installments. In one important respect the life insurance contract does differ from many other contracts. It is not a contract where a promise is exchanged for a promise. It is a contract where, in consideration of one act (payment of the first premium) and the performance of a similar act periodically, the company promises to pay upon the happening of a specified event or events. But there is no promise on the part of the insured to perform the periodic acts. He may neglect or decline to make subsequent payments and he thereby incurs no liability [4] It is not the case of the purchase of property for a consideration partly cash and partly promissory In the latter case the whole consideration is furnished at the very beginning. If, for instance, the contract is made prior to marriage the consideration may be said to be partly separate money and partly the separate promise of the person making it, the property right has been acquired without the use of any community asset. If community funds are used later in payment of this separate obligation, the character of the property acquired is not thereby changed. This principle may be said to be fairly well settled.[5] It ought to be applicable to the ordinary contract for the purchase of real estate, but the law in Washington in respect to such contracts has been warped by the view which the Supreme Court has taken of the interest acquired by the vendee under such contracts where there is a provision for forfeiture.[6]

The proper application of this principle of community property to life insurance contracts depends upon the nature of such a contract If it is to be regarded as a series of separate periodic contracts, then obviously its character will change with the char-

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[3] McKay on Community Property (2d ed.) Sec. 517 *In re Brown's Estate, supra, Blankenship v. Knox*, 105 Wash. 416, 178 Pac. 629 (1919).

I Cooley's Briefs on Insurance (2d Ed.) p. 116.

[5] *Katterhagen v. Meister* 75 Wash. 112, 134 Pac. 673 (1913). Here, as elsewhere in this article, no attempt is made to make the citation of cases exhaustive.

In re Kuhn's Estate, 132 Wash. 678, 233 Pac. 293 (1925) *Ashford v. Reese*, 132 Wash. 649, 233 Pac. 29 (1925) *Aylward v. Lally*, 147 Wash. 29, 264 Pac. 983 (1928) *Tieton Hotel Co. v. Manheim*, 75 Wash. 641, 135 Pac. 658 (1913) *Converse v. LaBarge*, 92 Wash. 282, 158 Pac. 958 (1916).

acter of each periodic payment, but if it be regarded as one continuous contract and the periodic payments be viewed as merely the performance of conditions necessary to keep alive rights already acquired and existing, then the character of the original consideration determines the status of the contract. Its character is not changed by the succeeding payments. They at most would create no more than a right to reimbursement. That the latter is the correct view of the nature of ordinary modern life insurance contracts is well settled.[7] The insurance company is bound on its promise if the periodic acts are performed. It canont terminate the contract by declining to receive the payment of a premium. On the other hand, many of the valuable rights of the insured date back to the date of his policy The size of the periodic payment, for instance, depends upon his age at that time and not upon his age at the time each succeeding payment is made.[8]

Applying this principle of community property logically then to contracts of life insurance, so viewed, it follows that the character of the property right which ultimately produces the proceeds of the insurance is determined at the time the contract is taken out and depends upon the character of the funds used. Ordinarily, a policy of life insurance is not in force until the first premium is paid either in cash or by note. The signing of the application, therefore, would not initiate the property right. But if the contract was completed before marriage by the payment of the first premium, and we are assuming at present that we have a policy where the proceeds are payable to the insured's estate, those proceeds should be separate property If subsequent premiums are paid out of community funds, the community estate should be entitled to reimbursements to the extent of the funds contributed, unless the facts furnish a basis for the presumption that it was intended to make

[7] *New York Life Ins. Co. v. Statham*, 93 U. S. 24, 23 L. ed 789 (1876).

[8] A similar question arises in connection with the re-instatement of a lapsed policy. Suppose a policy taken out prior to marriage lapses, and is re-instated after marriage by the payment of community funds. If the contract when re-instated is a new contract, it is community property. If it is merely the revival of an old contract, it would seem to be separate. The weight of authority holds it is not a new contract, but the revival of the old contract. *New York Life Ins. Co. v. Fecht*, 29 Fed. (2d) 318 (1928), *Mutual Life Ins. Co. v. Dreeban*, 20 Fed. (2d) 394 (1927) *Wastun v. Lincoln Life Ins. Co.*, 12 Fed. (2d) 422 (1926) *Reidy v. John Hancock Mutual Life Ins. Co.*, 245 Mass. 373, 139 N. E. 538 (1923) *Lovick v. Provident Life Ass'n.*, 110 No. Car. 93, 14 S. E. 506 (1892) *Reed v. Missouri Mutual Life*, 5 S. W (2d) 675 (1928) *New York Life Ins. Co. v. Rosen*, 236 N. Y. Sup. (1929).

a gift of those community funds to the separate estate of the spouse concerned. Of course, if the policy is taken out after marriage the presumption will be normally that community funds have been used in its purchase. It is also quite possible to have a case where a policy is contracted for after marriage and the first premium paid partly with separate and partly with community funds. If there were no other facts affecting the matter, the proceeds should be apportioned proportionately to the respective estates. As a practical matter, however, if it appeared that succeeding payments were made largely or entirely with community funds, courts would be very likely either to disregard the share of the separate estate in the first payment, particularly if comparatively small, or from very slight evidence to presume an intent to make a gift to the community of so much of the separate funds. This result would comport quite well in all probability with the real intent of the insured.

If the contract was originally separate, however, and the insured possessed separate funds or a separate income quite sufficient to enable him to pay the later premiums, and there was no clear proof that community funds were used in the payment of those premiums, it would be presumed that the subsequent premiums came also from the separate funds[9] This is perhaps only another way of saying that the burden of proving a right to reimbursement rests upon the estate claiming it.

The rule just laid down is the rule which has been established in Louisiana by the decisions of its Supreme Court.[10] It is not the view, however, which was taken in an early case in California.[11] There a policy of endowment insurance was taken out by the husband before marriage. It appeared that one-third of the number of premiums was paid from separate property and two-thirds from community funds, and the court held that the proceeds belonged to the respective estates in proportion to their contributions. That decision has been often cited and has been given more weight than it deserves. It has been severely criticized[12] and is wrong in prin-

[9] *Mutual Iife Ins. Co. v. Lundquist*, 140 Wash. 345, 248 Pac. 808 (1926). It should be said here that the most thorough and helpful discussion of the chief problem dealt with in this article is to be found in the excellent briefs of counsel in the Lundquist case. See also *Guye v. Guye*, 63 Wash. 340, 115 Pac. 731 (1911).

[10] *In re Moseman's Est.*, 38 La. Ann. 219 (1886) *In re Buddig*, 108 La. 406, 32 So. 361 (1902) *Succession of Verneuille*, 120 La. 605, 45 So. 520 (1908) *Succession of LeBlanc*, 142 La. 27, 76 So. 223 (1917)

[11] *In re Webb*, Myrick's Probate p. 93 (1875).

[12] McKay on Community Property (2d ed) Sec. 535.

ciple. The case itself is as old and very brief one, decided by an inferior court. There is no authority cited in it and no reasoning to support the conclusion. A subsequent California case cites it,[13] but no later case has been found which actually follows it, and in *In Re. Castagnola's Estate*[14] the California Supreme Court in language expressly approved the principle of the Louisiana decisions. The question has not been determined in Washington in any insurance case, although it was presented to the Supreme Court in the case of *Mutual Benefit Life Ins. Co. v. Lundquist.*[15] The decision of the question was rendered unnecessary there by the conclusion of the court on the facts that the premiums paid upon the policies in question were from the separate estate of the insured husband.

In our previous discussion, we have been assuming a policy of life insurance upon one of the spouses, payable to the estate of the insured. If the policy, however, is payable to the surviving wife, or to a mother or sister, a different set of problems is presented.

In the case of the policy payable to the wife, if there be no provision in the policy for a change of beneficiary, the interest of the wife is vested and cannot be taken away from her by the insured without her consent.[16] If, however, as is usually the case in the modern policy, the right to change the beneficiary is reserved to the insured, then the interest of the wife is not vested.[17] If she takes, however, it is generally held, that the proceeds are her separate property and do not fall into the community estate.[18] In some States, including Washington, that result is fixed by statute,[19] while in others it has been reached by the courts on the theory of a gift by the husband to the wife.[20] Since one spouse may convey his or her community interest in any property to the other, there is no impediment to such a gift, except in the case of existing cred-

[13] *New York Life Ins. Co. v. Bank of Italy*, 60 Cal. App. 602, 214 Pac. 61 (1923), *In re Stam* (1872). Myrick Probate p. 5, does not support the principle of *In re Webb.*

[14] 68 Cal. App. 732, 230 Pac. 188 (1924)

[15] 140 Wash. 345, 248 Pac. 808 (1926).

[16] *In re Heilbron's Est.*, 14 Wash. 536, 45 Pac. 153 (1896) *Thomas v. Grand Lodge*, 12 Wash. 500, 503, 41 Pac. 882 (1895). The interest of the beneficiary in a certificate in a mutual benefit society is not vested. See also *Cade v. Head Camp*, 27 Wash. 218, 67 Pac. 603 (1902).

[17] *Schade v. Western Union Life Ins. Co.*, 125 Wash. 200, 215 Pac. 521 (1923) *Buckner v. Ridgely Protective Ass.*, 131 Wash. 174, 229 Pac. 313 (1924).

[18] *Johnson v.* Cole (Tex.) 258 S. W 850 (1924).

[19] Rem. Comp. Stat. (1927 Sup.) Sec. 569-2.

[20] *In re Dobbel's Estate*, 104 Cal. 432, 38 Pac. 87 (1894).

itors, and the statute generally endeavors to take care of their interests.

In connection with this form of policy, very interesting and important questions have arisen in bankruptcy as to the right of the trustee to receive the cash surrender value of policies on the life of the husband, payable to the wife, but with a right reserved to change the beneficiary As the interest of the wife has not vested, a trustee of her separate estate obviously could not reach the cash surrender value. If the policy were taken out with community funds, the trustee of the husband's separate estate obviously could not reach the cash surrender value. The question remains whether or not the trustee of the community estate can reach it. It is an asset which the husband and wife can realize upon and it is difficult to see why it should not be community property and, except for the provisions as to exemption, pass to the trustee. Under the exemption provision, however, it may be saved by virtue of the State statutes. It was so held in *Holden v. Stratton*[21] with refer ence to the Washington Statute then in effect, but since repealed. A careful sudent of this problem has expressed the opinion that the last exemption statute of 1927[22] makes the law again doubtful.[23]

A similar question arises in case of divorce. Does the cash surrender value constitute community property? Or shall the policy be treated as community property? In Washington, where the interest of the wife is similar in quality to that of the husband, the policy is clearly community property It should be treated as having a value equal to its cash surrender value, at least. It is easily conceivable, however, that its real value may greatly exceed its cash surrender value, dependent upon the health of the insured. The policy might well be awarded wholly to one spouse,[24] who might thereafter pay the premiums and maintain the policy until the end, or take advantage of an option which policies frequently contain by which the cash surrender value is applied to the purchase of continued insurance for a specified term. In other words,

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[21] 198 U. S. 202, 49 L. ed. 1018, 25 Sup. Ct. R. 656 (1905).

[22] See note 19, *supra.*

[23] "THE EFFECT OF INSURED'S BANKRUPTCY ON POLICIES PAYABLE TO HIS WIFE BUT RESERVING THE RIGHT TO CHANGE"—Paper read before the Association of Life Insurance Counsel December 10th, 1929, at New York City by Francis B. Patten, Associate Counsel of the John Hancock Mutual Life Insurance Co. of Boston.

[24] *In Bundy v. Bundy*, 149 Wash. 464, 271 Pac. 268 (1928) the policy which was separate property of the husband, was awarded to him, although the wife was beneficiary therein.

if the community has chosen to speculate on the life of one of its members, the benefit of that speculation is a community asset.

But, suppose a divorce is granted and the decree fails to declare the rights of the spouses in the community property In Washington, in the case of other property the result is that the former spouses become tenants in common of the property formerly community Is there any reason why the same conclusion should not apply to the insurance contract?[25] In Texas "a wife's interest in a policy on her husband's life ceases upon obtaining a decree of divorce"[26], and "a judgment of divorce adjudging that all personal property of whatsoever kind and character mentioned in the pleadings belong to the community estate, even if construed as including a policy on the husband's life in favor of the wife, does not give her any interest in the policy after the divorce judgment goes into effect."[27]

The problem of the policy payable to mother and sister is equally important and more novel. The existence of such problem has been unobserved by many members of the bar. This question was also presented in the case of *Mutual Benefit Life Ins. Co. v. Lundquist, supra,* but was not determined in any of its difficult features. There the policies were taken out before marriage upon the life of the husband payable to the mother and sister. There can be no question that a bachelor may give his separate property to any one he pleases. If he chooses to take out a life insurance policy, payable to his mother, he may do so. After a man's marriage, however, his freedom to make gifts is very much limited by the community property system, at least as it exists in Washington.[28] In Texas it has been said that the husband is free to give away the community property as he sees fit, even to the impoverishment of the wife.[29] Even in California the interest of the wife in community personalty, prior to the death of the husband, is an expectancy merely [30] In Washington, however, the interest of the wife is of the same quality as that of the husband.[31] She is a half owner in the property The husband is the manager of the com-

[25] *In Mende v. Mende,* 148 Wash. 432, 269 Pac. 949 (1928), this interesting question was presented. It is submitted that the Company was right in refusing to pay over to the husband the cash surrender value without a legal proceeding to divest the interest or possible interest of the wife.

[26] *Hatch v. Hatch,* 35 Tex. Civ. App. 373, 80 S. W 411 (1904).

[27] *N. W Mutual Life v. Whiteselle* (Tex.) 188 S. W 22 (1916).

[28] But see *Cade v. Head Camp,* 27 Wash. 218, 61 Pac. 603 (1902).

[29] *Jones v. Jones* (Tex.) 146 S. W 265 (1912).

[30] *Blethen v. Pacific Mutual Life Insurance Co.,* 198 Cal. 91, 243 Pac. 431 (1926).

[31] *Olive v. Meek,* 103 Wash. 467, 175 Pac. 33 (1918).

munity, which is a sort of marital partnership and has been frequently by the Supreme Court, though probably incorrectly, referred to as a separate entity [32] At any rate, the Supreme Court has said that a husband as a manager of the community must use the community funds for the benefit of the community He cannot give those funds away in fraud of the wife.[33] This latter statement has been made in Texas, but the exact meaning of the phrase has not yet been worked out there and it may be that the Texas courts will yet come to the view which the Supreme Court of the State of Washington apparently holds, that any substantial gift of community funds to one outside of the community is presumptively a fraud upon the wife. In California (where the matter is affected by the statute) it has been held that a gift of community personalty by the husband is only voidable and not void, that the wife upon discovery of the gift may disaffirm it and recover her half interest.[35] If one is to judge from the present state of the Washington law, one would have to conclude that the husband cannot make a valid gift of community property in any substantial amount to one outside of the community, without the assent of the wife.[36] The application of that principle to life insurance policies at once restricts the right of the husband to designate any beneficiary, other than the wife, or to change the beneficiary to any other than the wife. It by no means follows, however, that such a thing can never be done. A community certainly owes obligations to the children of the spouses.[37] If a policy of insurance is taken out by the husband and father, upon his own life, for the benefit of an invalid or incompetent daughter, the policy can be easily supported as quite consistent with the principles laid down. It is not a gift, in any sense, in fraud of the wife. It is a case where the manager of the community personalty is using that personalty to meet the obligations of the community, and

[32] *Artheller v. Spokane & Inland Empire Ry Co.*, 107 Wash. 678, 182 Pac. 630 (1919) *Mattinson v. Mattinson*, 128 Wash. 328, 222 Pac. 620 (1924).

[33] *Stewart v. Bank of Endicott*, 82 Wash. 106, 143 Pac. 458 (1914) *Marston v. Rue*, 92 Wash. 129, 159 Pac. 111 (1916) *Parker v. Parker* 121 Wash. 24, 207 Pac. 1062 (1922) *Schramm v. Steele*, 97 Wash. 309, 166 Pac. 634 (1917).

[34] *Blethen v. Pacific Mutual Life Insurance Co.*, see note 30, *supra.*

[35] *Adams v. Black*, 6 Wash. 528, 33 Pac. 1074 (1893) *Litzell v. Hart*, 96 Wash. 471, 165 Pac. 393 (1917) *McAlpine v. Kohler & Chase*, 96 Wash. 146, 164 Pac. 755 (1917)

[36] But see remarks of Tolman J. in *Stevens v. Naches State Bank*, 136 Wash. at 144, 238 Pac. 918 (1925)

[37] *Rowlett v. Mitchell*, 52 Tex. Civ. Appj. 589 (1908) *Jones v. Jones* (Tex) 146 S. W 256, *Stevens v. Naches Bank*, 136 Wash. 137, 238 Pac. 918 (1925).

such a policy would be held valid even though the wife should dissent from the act of the husband. As he has been appointed by law the statutory manager of the community personalty, in case of difference of opinion as to the proper method of meeting community obligations, his judgment can properly be allowed to control. So a policy taken out after the second marriage, but for the benefit of the children of the husband by a former marriage, has been sustained in Texas as not in violation of the rights of the second wife.[38] Likewise a policy for the benefit of the aged father of the husband, where the community property was substantial and the community contribution to the premiums on the policy very small, has been sustained.[39] Nor does the principle we have discussed prevent the taking out of a policy by a husband upon his own life for the benefit of a relative who may have advanced money to the community, or who may have performed for the husband obligations owed to the husband, but unperformed by the wife. This is the principle of the case of *Union Mutual Life Insurance Co. v. Broderick.*[40] As the manager of the community the husband may certainly borrow money, and in connection with the making of a loan, he may give security, and if he originally makes the loan without security, there is the moral obligation to repay, and he may subsequently give security for that loan by way of insurance upon his own life.

If, however, the husband takes out a policy of life insurance after marriage, paying the first and subsequent premiums with community funds, and designates as beneficiary in the policy one outside the community, and to which the community has no financial or moral obligation, and the wife has in no wise assented to the gift, it seems probable that in Washington the proceeds of that policy can be claimed to be community property and the wife would be entitled to her interest in it.[41] Under such circumstances it is important for the insurance companies to know whether they are protected if they pay over the proceeds to the beneficiary other than the wife. In California it has been held that they are protected even though they have notice of the wife's existence and possible interest if payment is made prior to notice from the wife that she has elected to avoid the gift.[42] In Washington the company was

[38] *Rowlett v. Mitchell*, 52 Tex. Civ. App. 589, 114 S. W 846 (1908).

[39] *Jones v. Jones*, (Tex.) 146 S. W 265 (1912).

[40] 196 Cal. 497, 238 Pac. 1034 (1925).

[41] *Cade v. Head Camp, supra*, would seem to be contrary, unless it can be distinguished because concerned with a certificate in a mutual benefit society. The distinction, though often made, is not sound. The case, also, is an early case, decided long before the interest of the wife came to be regarded with such favor as today.

[42] *Blethen v. Pacific Mutual Life Ins. Co.*, see note 30, *supra.*

freed from liabilities where the husband had been given possession of the policy by the wife and he had changed the beneficiary to his estate and assigned his policies to a bank to secure loans previously made to the community [43] The courts will undoubtedly give weight to the practical necessities of the situation. The contract is a chose in action generally calling for the payment of money to a certain individual. Certainly if the company had no knowledge, as it generally would not, that any change constituted a gift in fraud of the wife, it would have no right to refuse the demand of the beneficiary for payment. There is no obligation upon it to go out and investigate as to the possible rights of the wife. It is her duty to be vigilant in asserting her own rights. Otherwise, the insurance company is justified in paying, and the wife is relegated to her right to proceed against the beneficiary who has collected.[44]

No attempt is here made to determine the proper result under all of the infinite variety of facts and circumstances which may exist in connection with the complicated modern insurance policy, added to the complexities of the community property system. It is hoped, however, that the foregoing discussion of principles may be of assistance in reaching the correct solution when once the exact facts have been ascertained. FRED W CATLETT.*

[43] *Schade v. Western Union Life Ins. Co.*, 125 Wash. 200, 215 Pac. 521 (1923).

[44] *Holmes v. Gilman*, 138 N. Y. 369· 20 L. R. A. 566 (1893) *Shaler v.* Trow bridge, 28 N. J. Eq. 545 (1877)

*Of the Seattle Bar.