Insurance On Expected Profits

By JOSE A. UNSON *

I. PRELIMINARY CONSIDERATIONS

A. *History and Development*

The practice of insuring expected profits had its real beginning in England and was at first peculiar to marine insurance. This is so because for several years after its introduction into England, insurance was largely confined to marine risks. Consequently, the law of marine insurance was first developed in English courts, and in its early forms, the law of insurance itself was derived from the maritime law.[1] "It is well known that the contract of insurance sprang from the law maritime and derived all its material rules and incidents therefrom." [2]

Although insurance on expected profits was at first peculiar to marine insurance, yet it was not exactly contemporaneous with the latter—for, while the practice of insurance in the early days was already in full swing, insurance on expected profits was still unknown and only made its appearance quite recently. This may appear surprising for if it is true that property insurance is indemnity insurance (a principle acknowledged from the beginning), and since the owner of property may lose the profits of a resale because of the destruction of the property, it would seem that a policy insuring the owner of goods *might* have been construed to cover lost profits within the limits of the policy. As a matter of fact, such a result was precluded in the early days of marine insurance by the rule then prevailing that the property is to be valued at the port of departure rather than at the port of destination, for the purpose of measuring the loss under an unvalued marine policy.[3]

This hard and fast rule was later on relaxed, and the next step in the development of insurance on expected profits was the recognition of the principle that the parties to a marine contract might value the goods at any amount within reason and that the valuation might include the enhanced value of the goods at the port of destination. From this, it was an easy step to the recognition of insurance on profits expected to proceed from property. Thus, as early as 1781, insurance on expected profits was given definite judicial recognition when Lord Mansfield, said to be the father of insurance law, upheld such a policy against the contention that it was a wager.[4] With rare economic insight, the English courts encouraged insurance on profits in maritime adventures, in order "that men of small fortunes should be encouraged to engage in commerce by their having the means to preserve their cap-

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[1] Vance, Law of Insurance (1930), pp. 18, 23.

[2] New England Marine Ins. Co. v. Dunham, 11 Wall. 1, 20 L. Ed. 90, 96.

[3] Patterson, Essentials of Ins. Law (1935) p. 103.

[4] Grant v. Parkinson, 3 Douglas 16; Patterson, Essentials of Insurance Law (1935), p. 103.

itals entire." [5] The right to insure expected or contingent profits is now settled in England and has received repeated and elaborate confirmation.[6]

Since the development of the practice of insurance has followed the same lines in the United States as in England, the principles on this branch of the law, as evolved by the English courts, have been largely adopted in the United States. Consequently, American courts have accorded equal recognition of insurance on expected profits.[7]

In the Philippines the same thing is true, since Act No. 2427 (otherwise known as the Insurance Act) was copied almost verbatim from the insurance laws of California and New York, and its provisions are nothing more than a collection of the generally accepted principles of insurance in the United States. As a matter of fact, Section 98 of the Insurance Act expressly authorizes insurance on expected profits.

In other countries, however, the story is different. In Spain, Italy, France, and Holland every kind of interest that rests in expectancy only is not a proper subject of insurance.[8] "Several of the commercial tribunals (in Spain and France) wished . . to adopt the practice of the English and give a greater extension to the liberty of insurance. To this it was answered that risk was the essence of the contract, and that there was no real loss of that which is a nonentity, and had no future existence, as future contingent freight and profits." [9] Kent, however, relying on the views of Santerna, Straccha, and Roccus says that in Italy, Portugal, and the Hanse Towns insurance on expected profits is valid.

B. *Our Law on the Subject—Sources*

In this connection it is enough to state that our law of insurance on expected profits is found in Act No. 2427 (otherwise known as the Insurance Act). The specific parts or sections of the law related to the subject of this work will be discussed in detail later.

Act No. 2427, enacted on December 11, 1914, took effect on July 1st of the following year. It is almost an exact copy of the insurance law of California, with the exception of Chapter V, entitled Insurance Companies, which was likewise copied almost verbatim from the insurance law of New York. Heretofore, our law on insurance was found in the Code of Commerce, the Civil Code and the Corporation Law, but Section 204 of the Insurance Act expressly repealed Sections 147-153 of the Corporation Law, Title VIII of Book II and Section III of Title III of Book III of the Code of Commerce, as well as "all laws or parts of laws in conflict or inconsistent with this Act." Our law on insurance is consequently now found in the Insurance Act and the Civil Code, the latter with respect to life annuities, which may be considered as a form of insurance not treated by nor inconsistent with the Insurance Act.

It is significant that since the taking effect of Act No. 2427 our courts have had no occasion to pass upon a case on insurance on

[5] Barclay v. Cousins, 2 East 544.
[6] Kent's Commentaries, Vol. 3, p. 439.
[7] Ibid.
[8] 38 C. J. 1913; Barclay v. Cousins, supra.
[9] Kent's Commentaries, Vol. 3, p. 439.

expected profits. In the discussion of this work, therefore, resort must be had to other sources in the search for principles and materials. "As the Philippine Law (Act No. 2427) was taken verbatim from the law of California, in accordance with the settled cannons of statutory construction, the courts should follow in fundamental points, at least, the construction placed by California courts on a California Law.[10]

It is unfortunate that there is a similar dearth of California jurisprudence on the subject of insurance on expected profits, so guidance must be sought in the general principles prevailing on the subject. "The Philippine Law of Insurance should be supplemented by the general principles prevailing on the subject. The purpose should be to have the Philippine Law of Insurance conform as nearly as possible to the modern Law of Insurance as found in the United States proper." [11] English jurisprudence on marine insurance should also not be disregarded, since "the law on marine insurance was first developed in English courts and in its early forms the law of insurance was derived in maritime law, and as such was a part of the general law merchant, and international in its character." [12] "It is well known that the contract of insurance sprang from the law maritime and derived all its material rules and incidents therefrom." [13]

II. Is Expectation of Profits Insurable Interest?

A. *General Principles*

In order to provide a basis of discussion, it is well to recall some of the fundamentals of the contract of insurance. It is here proposed to briefly discuss only those that are necessary for the proper treatment of the subject of this work.

Every student of law who has had occasion to study the subject of insurance is, of course, familiar with the legal requirement of "insurable interest". This is one of the characteristic elements of insurance which distinguishes it from other forms of contracts. This requirement is so indispensable that no insurance contract can exist without it. "The sole object of insurance is the indemnity of the insured, and if he has no insurable interest, the contract is void." [14] The absence of this requirement will transform the contract into a mere wager, the prevention of which is precisely one of the objects of the requirement of insurable interest. "A wager is an agreement between two parties by which one (at least) agrees to pay to the other money (or other thing of value), dependent upon the happening of a contingent event in which neither party has any interest other than the one created by the agreement.";[15] or, as applied to insurance, "one where, independent of the policy, the party insured has nothing to lose".[16]

In England, wagering contracts are declared void by statute [17] and

[10] Ang Giok Chip v. Springfield Fire and Marine Ins. Co., 56 Phil. 375.

[11] Gercio v. Sun Life Ass. Co. 48 Phil. 53.

[12] Vance, Law of Insurance (1930) p. 23.

[13] New England Marine Ins. Co. v. Dunham, 1 Wall. 1, 20 L. ED. 90, 96.

[14] Sec. 17, Act No. 2427.

[15] Patterson, Ess. of Ins. Law (1935) p. 88.

[16] Samuel Putnam v. Mercantile Marine Ins. Co., 5 Met. 396.

also considered so in the United States by judicial decisions, except in some states like New York where it is declared void expressly by statute, on the grounds that wagering contracts of any sort are against public policy.[18] It was the general impression of American and English courts that, at common law, a policy in which the insured had no interest and which was in fact nothing more than a mere wager or bet between the parties, was a valid contract.[19] But these courts were all talking through their hats, if we are to believe the case of Ruse v. Mutual Life Ins. Co. (23 N. Y. 516), which maintains that the common belief of English and American courts that, at common law, a policy in which the insured had no interest was valid, is a misconception. The decision explains how through such misapprehension this erroneous doctrine first crept into the law, and finally concludes that at common law, independent of any statute, this class of contract was illegal as against good morals and public policy.

B. *Insurable Interest in General*

The decisive question around which the discussion of this work revolves is whether profits expected to proceed from a thing is an insurable interest, and for this purpose it becomes necessary to know the nature and meaning of the term "insurable interest" and see if expectation of profits may be embraced therein.

As understood in English and American law, "insurable interest", stated in its broadest sense, "is applied to that interest which the law requires a person making a contract of insurance to have in the thing or person insured, in order that contracts creating rights and duties so highly dependent upon chance may escape the condemnation visited upon wagers";[20] or "the relation between the insured and the event insured against, such that the occurrence of the event will cause substantial loss or damage to the insured." [21] These definitions are broad enough to cover insurable interest in life and property insurance, but this discussion will be confined to the latter, for, it is hardly conceivable that profits may be expected on human life.

The real meaning of insurable interest in property is well expressed in the admirable opinion of Laurence, J., in the leading case of Lucena v. Craufurd (2 Bos. & P. N. R. 269), which "not only is characterized by eminent good sense, but also has the sanction both of antiquity and the enthusiastic approval of subsequent judges and text-writers," [22] "A man is interested in a thing", says the great judge, "to whom advantage may arise or prejudice happen from the circumstances which may attend it. * * * Interest does not necessarily imply a right to the whole or a part of the thing * * * but *the having some relation to or concern in the subject of the insurance; which rela-*

[17] 19 Geo. II, c 37.

[18] Vance, Law of Insurance, 2nd Ed. (1930) p. 119.

[19] Juhel v. Church, 2 Johns. Cases, 333; Abbott v. Sebor ib., 39; Chudining v. Church, 3 Caines 141; Buchanan v. Ocean Ins. Co., 6 Cowen, 318; Craufurd v. Hunter, 8 T.R. 13; Good v. Elliott, 8 T.R. 693.

[20] Vance, Law of Insurance (1930) p. 118.

[21] Patterson, Essentials of Ins. Law (1935) p. 87.

[22] 1 Arnold, Marine Ins. 11th Ed. (1924) p. 254.

tion or concern, by the happening of the perils insured against, may be so affected as to produce damage, detriment, or prejudice to the person insured."

Insurable interest, therefore, is not limited to the ownership of or title to property, but embraces a variety of interest connected with the same, for according to the same case, "the property of a thing and the interest derivable from it, may be different. Of the first, the price (of the thing) is generally the measure; but by interest in a thing, every benefit and advantage arising out of and depending on such thing may be considered as being comprehended." "It may be said that one may insure * * * property when he stands in such relation thereto that he will be benefited by its continued existence and damnified by its destruction." [23] The interest may be a special or limited interest, disconnected from any title, lien, or possession. "If the holder of the interest is deprived of * * * certain benefits growing out of or depending upon it, he has an insurable interest." [24]

1. *Section 12, Act No. 2427*

It is in Section 12 of Act No. 2427 that the law makes a general definition of "insurable interest." This section is found in Chapter I of the Insurance Act, entitled Insurance in General, and is, therefore, applicable to property insurance in general. Section 12 provides: "Every interest in property, whether real or personal, or any relation thereto, or liability in respect thereof, of such nature that a contemplated peril might directly damnify the insured, is an insurable interest." This definition of insurable interest by our law seems to stand on all fours with the nature and meaning of insurable interest given in the case of Lucena v. Craufurd, which has just been discussed. The phrase "every interest in property" speaks for itself, and is almost all-embracing. The "relation" or "liability" with respect to the thing which the law speaks about gives rise to an interest in the property, for if his relation or liability in relation to the property is of such nature that the peril contemplated might directly damnify him, he must be conceded to have an interest in the property. And that interest comprehends every benefit and advantage arising out of and depending on such thing.

a. *Is Expectation of Profits Embraced Within Section 12 of Act No. 2427?*

The next point of inquiry is whether expectation of profits to proceed from a thing is an insurable interest within the definition given in Section 12. Is such expectation "an interest in the property, or relation thereto, or liability in respect thereof, of such a nature that a contemplated peril might directly damnify the insured?" It can be readily seen that one who expects to receive profits out of a thing, because of such expectation, must be related to it somehow, for it is hard to see how a person who has no relation at all with the thing may expect to get profits out of it. Therefore, because of such expectation (relation), he may fairly be considered to possess an interest in the thing, whatever denomination might be given to such interest. The word

[23] Vance, Law of Insurance (1930), p. 119.

[24] German Insurance Co. v. Hepman 34 Neb. 704; 52 N.W. 401.

"interest," as has been shown, includes every benefit or advantage arising out of and depending on such thing, and surely profits expected of a thing are a distinct benefit or advantage, if realized; a benefit or advantage which, in the ordinary course of things would probably have vested absolutely in the insured, but for the intervention of the perils contemplated. The destruction of the thing destroys all hope of realizing profits from it and to that extent damnifies whoever is interested in the thing.

The conclusion, therefore is that expectation of profits is an insurable interest within the definition given in Section 12.

C. *Insurable Interest—Qualified*

The question, however, does not end here. So far, benefit or advantage has been spoken of in general terms. But what must be the character of the benefit expected or the loss that is feared? Must the expected benefit (profits) have such a legal basis that its conferring is recognized or compelled by law, or the loss be such that would entitle the insured to damages against a tortfeasor, if any? It should be remembered that not every valuable economic relation is founded upon, or protected by, a legal right. On this point, reference must again be made to decided cases. According to Professor Vance, Justice Lawrence's statement in Lucena v. Craufurd is too broad and must be qualified, because not all benefit expected or detriment feared is an insurable interest. It is necessary that the benefit or advantage expected, or detriment feared, must have a legal basis.[25]

This point was made clear by Andrews, J., in Riggs v. Commercial Mutual Ins. Co.,[26] where the following language is used: "It would seem, therefore, that whenever there is a real interest to protect and a person is so situated with respect to the subject of insurance that its destruction would or might reasonably be expected to impair the value of that interest, an insurance of such interest would not be a mere wager within the statute, whether the interest was an ownership in, or a right to the possession of, the property, *or simply an advantage of a pecuniary character having legal basis*, but dependent upon the continued existence of the thing. It is well settled that a mere hope or expectation, which may be frustrated by the happening of some event is not an insurable interest." So in the case of Baldwin v. State Insurance Co.,[27] it was held that "an expectation of benefit to be derived from its continued existence, however likely or morally certain of realization it may be, will not afford a sufficient interest, "unless that expectation has a basis of legal right." As specially applied to insurance on expected profits, "the insured must have a real interest in the subject matter from which the profits are expected. There must be a substantial basis for the hope or expectation of profits." [28] If such interest exists, an expected benefit constitutes an insurable interest, even though the possibility of injury to the in-

[25] Vance, Law of Insurance (1930), p. 94.

[26] 125 N.Y. 7; 25 N.E. 1058; L.R.A. 684; 21 Am. St. Rep. 716. [27] 60 Iowa 497; 15 N.W. 300.

[28] Kent's Commentaries, Vol. 3, p. 441.

sured by the happening of the peril insured against is very remote.[29]

The case of Lucena v. Craufurd (supra) clearly illustrates what is meant by an expectation supported by a legal basis. The holding of the court was that while the commissioners (who were appointed by an Act of Parliament, with power to take possession and dispose of certain vessels that might be brought into English ports) had no present legal right to the vessel themselves, yet they might expect to acquire such right in case the vessels made the voyage in safety. All this interest was based upon an Act of Parliament, which must operate if the vessel came into port. Hence, by the destruction of the vessels at sea, they (the commissioners) were prevented from acquiring a legal right in them, and were, therefore, damnified.[30] While it is true that "courts always lean in favor of insurable interest," [31] because the legitimate subjects of insurance are thereby enlarged and business greatly improved, nonetheless the courts insist that the expectation of benefit or advantage must have a "legal basis," otherwise the policy will fall into a wagering contract.

1. *Sections 13 and 15 of Act No. 2427*

The next question to be considered is whether or not our law recognizes this "legal basis requirement. The definition of "insurable interest" in Section 12 is rather too general and to remedy this defect the law enlarges and amplifies on that definition by providing in Section 13 of what insurable interest may consist in. Section 13 provides: "An insurable interest in property may consist in: (a) an existing interest; (b) an inchoate interest founded on an existing interest; (c) an expectancy, coupled with an existing interest in that out of which the expectancy arises." Subsection (c) more properly concerns this work, for the subject is insurance on expected profits, something which has as yet no present existence. An existing interest or an inchoate interest (the latter being an existing interest also, although just begun and still incomplete) are beyond the scope of this thesis.

Section 13, in express and positive language, recognizes the insurability of an interest in property which merely consists of an "expectancy." According to Section 13, an expectancy is an interest in property, and interest comprehends every benefit or advantage derivable from the property. Expectancy therefore, as used in Section 13, means expectancy of benefit or advantage in property. Profits by itself constitute a distinct benefit or advantage, hence expectation of profits is expection of benefit or advantage, and as such is apprehended within Section 13, Subsection (c).

But Section 13, Subsection (c), is not satisfied with an interest which consists of a simple expectancy, but imposes the additional requirement that such expectancy must be "coupled with an existing interest in that out of which the expectancy arises." The language of the law is not difficult to understand and means exactly

[29] Vance, Law of Insurance, pp. 136-137.

[30] Ibid.

[31] Stock v. Inglis, 10 A. C. 263.

what it says. A hope or expectation not founded on an existing interest is nothing less than a wild hope or expectation, which in general is unacceptable as insurable interest. The expression of Subsection (c) may be said to be the stand of the law that the expectation must rest on a legal and substantial basis, thus confirming what seems to be a settled rule in the United States in general. Knowing the history of the Insurance Act, this is, of course, to be expected. Whatever doubt there is in this regard is dispelled by Section 15, when it provides that "a mere contingent or expectant interest in anything, not founded on an actual right to the thing, nor upon any valid contract for it, is not insurable."

This rule of law, as applied to expectation of profits that is insurable, means nothing more than that expectation of profits, however morally certain, will not afford a sufficient insurable interest, unless such expectation has a legal basis. Of expectancy founded on a legal basis, and a mere hope or expectation—illustrations of the former have been given and that of the latter in the later pages.

It seems clear then that under Sections 13 and 15 of the Insurance Act, expectation of profits, to be insurable, must rest on a legal basis.

D. *Expectation of Profits in Marine Insurance*

In Chapter II of the Insurance Act, entitled Marine Insurance, the law makes provisions for specific kinds of interest that may be insured, among them that of expected profits.

At this juncture, it is well to point out the technical distinction between property insurance in general and what is usually known as marine insurance. The impression should not be gotten that there is a basic difference between the two—since marine insurance, just like ordinary property insurance, has for its subject matter property or any interest therein. It is however distinguished from the latter in that it has reference to risks connected with navigation, or as more explicitly stated in Section 92 of the Insurance Act, "marine insurance is an insurance against risks connected with navigation, to which a ship, cargo, freightage, profits, or other insurable interest in movable property may be exposed during a certain voyage or a fixed period of time." Another distinction, as can be gathered from Section 98, is that only personal or movable property may be insured in marine insurance.

1. *Section 98, Act No. 2427*

Whatever doubt there is as to the insurability of expected profits in maritime adventures is removed by Section 98 of the Insurance Act, which provides that "one who has an interest in the thing from which profits are expected to proceed, has an insurable interest in the profits." This section is the only part of the law which gives express recognition of insurance on expectation of profits. It may be said that the law also recognizes this kind of insurance in Section 92 (supra), where the word profits is used in connection with the legal definition of marine insurance, but then in not very explicit terms.

Because of this and the further fact that insurance on expected profits was at first peculiar to marine insurance, it was thought at

first to begin the discussion of this work with Section 98, but since the ultimate question to be decided is whether expectation of profits is insurable interest or not, it was thought wise to discuss first Section 12, where insurable interest is defined. As it is, upon reading Section 98, expectation of profits is undoubtedly a proper subject of insurance; but after the discussion of insurable interest and its qualifications, it is believed that even in the absence of Section 98, profits may be properly insured under a marine policy, since Sections 12, 13, and 15 of the Insurance Act are applicable to all kinds of insurance. Section 98 is nothing more than a reaffirmation by our law of a practice which is quite established. All its concommitant rules and principles must also be observed. As a matter of fact, it will be observed that Section 98 itself requires that the expectation of profits must possess a legal basis when it grants that profits may be insured only by "one having an interest in the thing from which profits are expected to proceed * * *" The law has thus imposed this requirement to every interest resting on expectancy, in all kinds of risks.

E. *Factual Expectation of Benefit or Advantage*

Not every valuable economic relation is founded upon, or protected by, a legal right. Particular individuals may stand in such a relation to other individuals that the destruction of the one's property may cause damage to the other's business. Professor Patterson gives an interesting example. "Suppose, for example, that A owns a gasoline filling station near B's large roadhouse in the open country; the burning of the roadhouse, though it leaves the filling station physically unharmed, will lessen A's income from guests in the roadhouse. A clearly has no legal claim against B on his loss. Has he a sufficient insurable interest in B's hotel to enable him to recover under such a policy covering the loss of profits due to its destruction? Such an insurable interest, based upon no legal right or legal liability may be called factual expectation of loss." [32]

This factual expectation, as can be readily seen, falls short of the requirement that the expectation must have a "legal basis", because it is based on no legal right. Judicial recognition of this type of interest is highly doubtful. The controversy over factual expectation goes back as far as 1872 when Lord Mansfield in the case of Le Cras v. Hughes (3 Douglas 81), upheld the insurability of such kind of interest. Justice Lawrence approved Lord Mansfield's view [33] in his statement already quoted and which we have qualified. This view was relied upon by the Supreme Judicial Court of Massachussetts in holding that a firm of commission merchants had an insurable interest in commissions which they had reasonably expected to earn from goods consigned to them on commission, though they had no property right in the goods and no legal right to prevent the consignee's changing their destination at any time before the arrival.[34]

In another case, the holder of a patent on an oil refining process gave Ellis and Co. an exclusive

[32] Patterson's Essentials of Ins. Law (1935) p. 94.

[33] Lucena v. Craufurd, 2 Bos. & P.-N.R. 269.

[34] Putnam v. Mercantile Marine Ins. Co., 5 Met. 396.

license to use the process, in exchange for a promise to pay royalties, measured by the amount of oil refined. The holder of the patent then procured fire insurance on "diminution of royalties" caused by fire in the works and was held to have an insurable interest, which the court measured by comparing the royalties before and after the fire.[35] It can be seen that the destruction of the plant did not terminate the contract for the use of the license by the company, yet such destruction did diminish the royalties payable. In a Louisiana case which held that a mercantile (unsecured) creditor of a small storekeeper had no insurable interest in the debtor's stock of goods and the store building, the court relied on the actual probability of loss to the creditor rather than the legal claim, as the basis of the decision.[36]

These decisions indicate that eminent courts are prepared to go to considerable lengths in upholding the insurable interest arising from factual expectation.

Yet, the statements of Lord Mansfield and Justice Lawrence, upon which the preceding decisions were premised, were rejected by Lord Eldon in the very same case of Lucena v. Craufurd. "If moral certainty be a ground of insurable interest, there are hundreds, perhaps thousands, who would be entitled to insure. First the dock company, then the dock master, then the warehousekeeper, then the porter, then every other person who to a moral certainty would have anything to do with the property and of course get something by it. Suppose A to be possessed of a ship limited to B in case A dies without issue; That A has 20 children, the oldest of whom is 20 and B is 90 years of age; if it is a moral certainty that B will never come into possession, yet it is a clear interest. On the other hand, suppose the case of an heir at law of a man who has an estate worth £20,000 a year, who is 90 years of age, upon his death bed intestate and incapable from incurable lunacy of making a will; there is no man who will deny that such an heir at law has a moral certainty of succeeding to the estate; yet the law will not allow that he has any interest or anything more than a mere expectation." His view is confirmed in the case of Farmers' Mutual Ins. Co. v. New Holland Turnpike Co., (122 Pa. 37, 15 A. 563). In this case, a private turnpike company obtained a fire insurance on a county-owned bridge, which was so located in reference to the turnpike that the destruction of the bridge would greatly diminish the turnpike tolls. The company had previously contributed one third of the cost of an earlier bridge erected at the same point. The court held that even though the destruction of the bridge damnified the turnpike company to the extent of the diminution of profits pending the rebuilding of the bridge, there was no sufficient insurable interest. On the real basis of the decision, there seems to be a conflict of opinions. It seems that the court acted on the premise that such profits constitute but a mere expectation, lacking the legal requirement of insurable

[35] National Filtering Oil Co. v. Citizens Ins. Co., 106 N.Y. 535; 13 N.E. 337.

[36] A. Ross & Co. v. Merchants Mut. ns. Co., 27 La Ann. 409. Similar statements made in Tischendorf v. Lynn Mut. Fire Ins. Co., 190 Wis. 33, 40; Donavin v. Thurston, 190 App. Div. 48,179 N.Y. Supp. 473.

interest, and Professor Vance, talking of the same case, believes that this is the real basis of the decision.[37] But professor Patterson, (after quoting an excerpt from the decision) says that the court confuses the question of insurable interest with that of interpretation of the terms of the policy. "The last sentence quoted (referring to the statement in the decision that "such is not the contract of the parties") is sufficient to dispose of the claims for lost tolls, since it is well settled that a fire policy covers only replacement value, not profits or use and occupancy, unless the policy so stipulates."[38] In other words, the reason why the court decided against the insured in the claim for lost profits was that the parties never intended to include such in the contract; and not that such interest was a mere factual expectation, the court leaving that question aside.

Therefore, although most of the courts insist that the insured's expectant interest must have a "legal basis", as has been shown, this requirement is *not absolute.* Few courts are satisfied with a factual expectation of benefit. The only difference, of course, is that the law recognizes an expectation of benefit supported by a legal basis, while it does not accord the same treatment to factual expectation. The certainty in one is legal, in the other moral. In both cases, the degree of probability that the expectation of benefit will be realized is more or less the same, which is, that in the ordinary course of events, the expected benefit would have vested in the insured but for the intervention of the perils insured against.

In view of this state of authorities, the role of the legal prophet is extremely difficult, and there is no telling to what extent some courts will go to sustain a policy not supported by a legal basis. This type of interest represents the border line between a real insurable interest and a mere wager, and has more than fancied grounds for its justification. In fact, Professor Patterson confidently asserts that "a carefully drawn policy, expressly covering a genuine factual expectation interest, valued by the policy at a fair sum or measured by any fair scale clearly defined, would not be declared unenforceable on the ground of wagering."[39]

III. Similar Kinds of Interests

Expectation of profits is an interest which has no present existence. There are many such interests, and they bear a close resemblance to expectation of profits. They, too, are proper subjects of insurance.

A. *Commissions.*

Benecke considers commission as species of profits expected to arise from the sale of property consigned to an agent, and that they are insurable interest in England and in other countries whree insurance on profits are valid.[40] In the case of Samuel Putnam v. The Mercantile Marine Ins. Co.,[41] it was assumed that insurance on expectation of profits is valid, the court praising the opinion of Justice Lawrence in Lucena v. Craufurd as "sound and sagacious," in-

[37] Vance, Law of Insurance (1930) p. 137

[38] Patterson, Essentials of Insurance Law, p. 95

[39] Patterson, Ess. Of Ins. Law (1935), p. 97

[40] Benecke on Indemnity p. 35.

[41] 5 Met. 286.

troducing no novel principles into the law, advancing no position hazardous to trade, "though its tendency is to enlarge the legitimate subjects of insurance." The claim for expected commissions insured was justified on the ground that "the case, in its essential features, is is like that of an insurance on profits." In French v. Hope Ins. Co.,[42] the right of a consignees to effect insurance on his commission is mentioned without expressing any doubt in regard to it. It was held that the plaintiff had a substantial interest at risk, "for if the ship had arrived safely, he would have been entitled to profits, and they depended on her arrival."

B. *Freightage.*

Freightage equally with profits and commissions, is a proper subject of insurance. It bears a striking resemblance to expectation of profits in that it has no present existence at the time the policy is taken out. The Insurance Act expressly recognizes this type of interest when mention of it is made in Section 96 as among the specific kinds of insurable interest.

Section 96 provides: "The owner of a ship has an insurable interest in expected freightage which according to the ordinary and probable course of things he would have earned but for the intervention of the perils insured against or other peril incident to the voyage." Freightage has a restricted meaning in marine insurance, and is only used to mean "all the benefit derived by the owner, either from the chartering of the ship or its employment for the carriage of his own goods or those of others." [43] "It signifies the earnings or profits derived by the owner or the hirer of a ship * * * and has always been considered a proper subject of insurance in the United States and England, but not in France and Italy, so far as it rests on expectancy. The right to freight results from the right of ownership, and therefore the owner is the only person having an insurable interest, and he has such interest * * * *although it has been prepaid, if there is no agreement that it is to be retained by the ship-owner at all events.*" [44] "Ordinarily, passage money is not included in the term freight as used in the policy." [45]

One who has paid advanced freight on cargo being shipped, when such freight is not repayable in the event of loss, has an insurable interest in respect of such advance. In cases also where the contract of affreightment provides that the freight shall be payable, "ship lost or not lost", that is, where the ship-owner is entitled to the payment of freight whether or not the ship arrives at its destination, this also gives the merchant an insurable interest in respect of the freight.[46]

C. *Future Crops.*

As its name indicates, this is a kind of interest that has no present existence, and in that respect it acquires a common characteristic with expectation of profit.

"It is well settled that a farmer may insure future crops, if they are to be grown on land owned by him at the time of the issue of the policy; but such a limitation is without reason. He may

[42] 16 Pick. 397.
[43] Section 95, Act No. 2427.
[44] 38 C. J. 1913-1914.
[45] Danon v. Home etc. Assur. Co., 1 R. 5 C.P. 155
[46] 38 C.J. 1007-1013.

just as properly insure the crops to be raised by him as cropper" on the land of another, provided the crops will belong to him when produced." [47] In Sawyer v. Wedge County Mutual Ins. Co. (37 Wis. 503), an insurance upon crops to be grown during a period of five years was held to cover grain that was properly within the description of the policy, and which had been raised on land not owned by the insurer at the time of the execution of the policy. Professor Vance is full of praise of this decision as "eminently sound", although he adds that "the court was at much needless pains to reconcile its holdings with the accepted rules as to what constitutes insurable interest." [48]

D. *Liability Insurance.*

The insured under a legal liability policy has an insurable interest in something closely akin to profits. The courts usually take for granted the existence of this interest and dispose of it in general terms.[49] When analyzed, it is found to lie in the vague "economic return" which the insured expected to realize from the impairment of his estate or from the uninterrupted sale of his services, or from the successful outcome of some aleatory venture.[50]

Insurance against loss of the *expected economic return* from ventures in which factors wholly beyond human control are important elements have become common. Thus, Swarthmore College in Aug., 1923, purchased a $10,000 policy to cover the risk of possible failure to obtain satisfactory solar eclipse pictures by an expedition sent to Durango, Mexico for that purpose. Here, the College had an insurable interest in the economic return expected from the successful outcome of the expedition.

IV. Difficulties of the Practice of Insuring Expected Profits

It is an established rule in England and America that "there can be no recovery for loss of profits unless such profits are specifically covered by the policy. Expected profits cannot be proved as an element of loss suffered under a general policy upon the subject out of which the profits are expected to arise.[51] The reason given is that the possible profits that might have arisen if the loss had not occurred is merely an incidental part of the loss, and recovery is confined to the direct loss of the property. Profits are excluded unless mentioned *eo nomine.*

Hence, the necessity of inserting the clause "on profits * * * valued at" so much. The purpose of inserting the clause "profits * * * valued at" so much is to relieve the insured of proving the amount of profits that he would have made in the insured goods had they arrived at the destination (or had they not been destroyed); such proof, especially at a distant

[47] Vance, Law of Insurance, p. 140.
[48] Vance, Law of Insurance, p. 140.
[49] Phys. Def. Co. v. Cooper, 118 C.C.A. 50, 199 Fed. 576; but see Vredenburgh v. Phys. Def. Co., 126 Ill. App. 509; Phys. Def. Co. v. Laylin 73 Ohio St. 90, 76 N.E. 567; 25 Harv. Law Rev. 390; Lexington Grocery Co. v. Phila. Cas. Co., 157 N.C. 116, 72 S.E. 870; Fidelity & Guaranty Co. v. 1st Nat'l Bank, 233 Ill. 475.
[50] Vance, Law of Insurance, pp. 142, 143.
[51] Niblo v. Insurance Co., 1 Sandf. (N.Y.) 551; Matter of Wright & Pole, 1 Adol. & E. 621; Niagara Fire Ins. Co. v. Heflin, 6 S.W. 393; Stock v. Inglin, L.R. 9 Q.B. Div. 708.

market, would be difficult if not impossible to obtain.[52]

But even if there is such a clause in the policy, the rule is not always the same. The English courts long ago established the rule that even in such cases, "the insured must prove that some profits would have been made had the goods reached their destination" or that "recovery may be had only to the extent of probable profits proved." [53] In the United States, however, such is not the rule, for the American courts do not require such proof to be made and hold that "the valuation (of profits) is conclusive on the insurer in the absence of fraud", and they even go to the extent of holding that "the insured may recover the valued policy even though he sent the goods to a losing market." [54] In any event, the valued policy does not relieve the insured of the burdens of proving an insurable interest in the goods.[55]

The American view seems more reasonable, for there is no reason why the parties cannot contract and agree beforehand on the amount of profits covered by the policy. It must be presumed that the insurer did not close his eyes to the probable profits expected, but on the contrary, it is reasonable to believe that he considered that precisely in fixing with the insured the amount of profits to be covered by the insurance. Precisely, the purpose of making a valuation of the profits, according to Professor Patterson, is "to relieve the insured of proving the amount of profits that he should have made * * * Such proof, especially at a distant market, would be difficult, if not impossible to obtain." [56]

The English courts, by the doctrine they enunciate, defeat this very purpose, and impose unjustifiable hardship on the insured. The only result is the discouragement of insurance of this kind and the field of insurance is thereby most unreasonably narrowed. For reasons already well known, the American rule would most probably be followed in the Philippines.

The rule that there can be no recovery for loss of profits unless such profits are specifically covered by the policy is eminently sound, so far as it goes. But it should be remembered that the insured may take out a valued policy—and this is universally recognized. A valued policy is one where the thing insured is valued at a specified sum by the mutual agreement of the insured and the insurer.[57] And "a valuation in a policy of marine insurance is *conclusive* between the parties thereto in the adjustment of either a total or partial loss, if the insured has some interest at risk, and there is no fraud on his part. * * *" [58]

The expectation of profits may enhance or increase the value of the property—at least, in the eyes of the insured, and may be considered as part of the value of the thing itself. Now, what will prevent the insured from including the expected profits in the valuation of the property, instead of taking out a separate policy for

[52] Patterson, Ess. of Ins. Law, p. 109.
[53] Hodgson v. Glover, 6 East 316; 1 Arnold Marine Ins. (11th Ed. 1924) 287.
[54] Patapsco Ins. Co. v. Coulter (3 Peters) 222; Loomis v. Shaw, 2 Johns. Cases (N.Y.) 36.
[55] Patterson, Essentials of Insurance Law, p. 109 (1935).
[56] Ibid.
[57] Section 58, Act. No. 2427.
[58] Section 149, Act No. 2427.

the profits? If such valuation is conclusive between the parties (which is the rule obtaining in the United States and the Philippines), then expectation of profits may very well be protected under a valued policy, without its being mentioned *eo nomine*, nor a separate policy taken out on it. The fundamental idea is that the realization of profits is so certain in most cases that whoever is to be the recipient of it already adds it to the value of the thing from whence it is expected to proceed even before it is actually realized.

V. CONCLUSION

Needless to say, every contract of insurance must satisfy the legal requirement of "insurable interest" if it hopes to stand before a court of law. So indispensable is this requirement that no insurance contract can exist without it. It is no wonder, therefore, that a large part of this work has been devoted to answer one simple query: Is expectation of profits an insurable interest?

All doubt in this regard is removed by section 98 of the Insurance Act, which authorizes insurance on expected profits in plain and unmistakable language. This section is found under that portion of the law dealing with marine insurance. The question, therefore, arises: Is insurability of expected profits limited to maritime ventures? The question is reduced as to whether or not expectation of profits is insurable interest within Section 12 of the Insurance Act. Attempt has been made to show that expectation of profits is easily comprehended in the general definition of insurable interest given in Section 12. Further, Section 13 generously provides that an insurable interest in property may consist of "an expectancy." As a matter of fact, it is believed that even in the absence of Section 98, expectation of profits is still an insurable interest in marine insurance, since Sections 12 and 13 apply to property insurance in general.

The conclusion, therefore, is that expectation of profits is embraced within Sections 12 and 13 of the Insurance Act and merely reaffirmed in Section 98.