CLASSES OF INSURANCE*

DEFINITIONS, AND SOME RESULTS OF CLASSIFICATION

The matter of classifying types of insurance in the field other than life is a problem in itself, and of itself creates other problems in the business of insurance. May I for a moment survey those classes from the standpoint of their nomenclature as set out in the Dominion Insurance Act.

The sources of the names for the classifications are interesting and may be grouped as follows:

1. Some classifications are known by the hazard insured against: accident, sickness, earthquake, explosion, limited explosion, civil commotion, fire, forgery, hail, limited hail, theft, windstorm, falling aircraft, impact by vehicles, sprinkler leakage, water escape.
2. Some classes are known by the name of the antithesis of the hazard insured against: credit, surety, fidelity and yes even life insurance, since in these classes the perils are respectively the hazard of failure of credit, the failure of an undertaking, faithlessness in an employee and the inevitable hazard of death.
3. Some classes are known by the name of the thing insured: aircraft, automobile, plate-glass, livestock, boiler and machinery, personal property and real property insurance.
4. Some classes are known by very general terms such as public liability, employers' liability, weather, inland transportation and marine. None of the names in this group are adequate in themselves to do more than indicate the possible nature of the perils insured against or the persons or things insured.

It must be evident from the above grouping that considerable confusion and overlapping must exist since these named classes of insurance cannot be mutually exclusive. This point becomes evident again if the classes are put into the following categories:

(a) Where the cover provided is for loss from a *specific hazard* to which *any insurable property* may be exposed:

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Earthquake; explosion; limited explosion; civil commotion; fire; forgery; hail; sprinkler leakage; theft; weather; windstorm; falling aircraft; impact by vehicles; water escape;

(b) Where the cover provided is for loss from a *specific hazard* to which *certain specific property* may be exposed: limited hail; livestock;

(c) Where the cover provided is for loss from *any hazard* to which *certain named property* may be exposed: Aircraft (other than P.L. and P.D. cover); automobile (other than P.L. and P.D. cover); personal property; plate glass; real property (this definition excludes hazards specifically defined).

(d) Where the cover provided is for loss from *any hazard* to which *any insurable property* is exposed *if the loss occurs under certain circumstances:* Inland transportation; marine;

(e) Where the cover provided is for loss to *persons or property* caused by a *specific thing* or for which a *specific person is answerable:* Employers' liability; public liability (excludes insurance included in or incidental to some other class;) automobile P.L. and P.D.; aircraft P.L. and P.D.; boiler; machinery;

(f) Where the cover provided is for loss to a *specific person* from a *specific hazard:* Personal accident; credit (excludes insurance included in or incidental to some other class); fidelity; surety; sickness;

Thus if one takes the case of an automobile being destroyed by fire while on a dock awaiting shipment, insurance against such a claim might fall under any of the following three groups:

Group (a) i.e., It is a loss from the specific hazard of fire to which insurable property is exposed and comes within the scope of fire insurance.

Group (c) i.e., It is a loss from a hazard to which certain named property "an automobile" is exposed and comes within the scope of automobile insurance.

Group (d) i.e., It is a loss from a hazard to which insurable property is exposed and a loss occurring under certain circumstances and comes within the scope of marine insurance.

There are numerous other examples that might be cited. The question might be posed as to what kind of damage to a chattel might not be covered under a policy written as Personal Property Insurance.

Under these circumstances it is patent that the respective rights of the parties to an insurance contract will vary considerably in the event of a claim, depending, in the example which I have cited, upon whether the policy on the automobile was in fact a fire insurance contract, an automobile insurance contract or a marine insurance contract, and it is to be noted that the fire contract is statutory as is the automobile contract in all provinces but Quebec in which province this contract is subject to approval, while complete freedom reigns insofar as the marine insurance contract is concerned.

There appear to be several reasons why we should find such confusion in the orismology of the insurance business.

First, like Venus, insurance did arise from the sea, not full grown however, nor with perfection of form and symmetry nor was it even well proportioned in the detail. In spite of an age running to centuries, insurance is likely still in its swaddling clothes. With knowledge of astronomy, navigation developed because of trade; with the growth of trade a need for insurance arose. Once a method was conceived of affording indemnity for loss arising out of perils of the sea, the method was quickly adapted and applied to other perils that beset mankind. Coverages were designed to meet these perils, but there was a Topsy-like growth in each branch of the insurance business as each branch itself evolved. It is to be anticipated that as the ingenuity of man creates for the use of mankind new machines, new methods and as customs change, new forms and kinds of insurance will continue to arise and if nothing can be done about the existing confusion the confusion will undoubtedly become more confounded. The Dominion Insurance Act defined 21 classes in 1928; the present classifications in 1943 number 32 or 52% increase in 15 years. A continued multiplication of divisions will render the confusion more perplexing.

Secondly, whatever tendency there might have been among underwriters to maintain consistency in practice in the several fields of insurance, to some extend this tendency has been obstructed by legislative action in this and that jurisdiction. There are two outstanding examples of what I mean that readily come to mind:

(a) For some reason or other which I have not ascertained, the State of New York created an artificial barrier between what are commonly called Fire Companies and what are commonly called Casualty Companies. By limiting the charter powers of insurance companies incorporated in that state, it was anticipated that neither Fire nor Casualty Companies could interfere in the field occupied by the other. In conformity with this theory an attorney-general in New York State years ago ruled that a company incorporated in a foreign jurisdiction having broader charter powers would not be licensed in New York unless it formally agreed not to use anywhere in the United States powers other than those granted by New York to domestic companies. Had it been the State of Nevada that so ruled, the rule would have had little effect because the need to participate in the relatively small volume of business in Nevada would not warrant acquiescence in such a restriction. The volume of business available in New York, however, proved to be sufficient inducement and companies readily accepted the restriction and then proceeded to get around its effect by acquiring what are commonly called "running mates", that is a company operating in the field of insurance not occupied by the parent company. The rule proved ineffective too in preventing other kinds of encroachment in one field by the occupiers of the other due to the fact that classes of insurance as named are not mutually exclusive. Fire companies through their inland transportation department found a simple method to encroach on the casualty field, as I have previously mentioned, by giving burglary and other casualty covers in fact, though not in name, in the personal property floater policy.

In order to effect this segregation in the other than life insurance field, it was necessary for New York State to use names for the classes of insurance that a corporation was authorized to write so as to segregate the Companies into the two groups, *i.e.*, it was necessary to establish classes and call them by name so as to designate what business a Fire or a Casualty Company might each write.

(b) For the professed reason of protecting public interest, the legislature in Ontario, in 1875, appointed a commission under 38 Victoria, cap. 65, consisting of the Hon. William Buell Richards, afterwards Chief Justice of the Supreme Court; the Hon. John Godfrey Spragge, afterwards Chief Justice of the Court of Appeal; the Hon. John Hawkins Hagarty, afterwards Chief Justice of the Court of Appeal; the Hon. Samuel Henry Strong, former Chief Justice of the Supreme Court, and the Hon. Christopher Salmon Patterson, subsequently Puisne Judge of the Supreme Court.

The Commission reported on the fourteenth day of January 1876. It listed in the report twenty-one conditions which conditions they considered as fair and reasonable and ones which the Courts would accept as such and enforce as a matter of course. It was a short step for the legislature to take to enact that these conditions should form a part of every fire insurance contract in the province of Ontario allowing for a variation and modification of them if the Court should hold that such variation or modification was just and reasonable. The next short step was to eliminate the right to vary or modify and to make the contract to all intents and purposes a statutory one. For the most part, the statutory conditions in force in Canada are almost identical with the ones recommended by the Commission 68 years ago. While the conditions of the fire contract remain virtually unchanged through all these years, the conditions a fire insurance contract must meet have changed considerably.

I have already pointed out that whatever protection is afforded by these fire statutory conditions to a claimant who has suffered loss by fire only exists when the cover is granted by fire insurance policy and not when granted by an automobile or marine insurance policy and that possibly such protection does not exist when the cover is granted by a personal property floater policy although this latter point is still a moot question.

This innovation of a statutory policy will be more fully discussed anon. It suffices for the moment if one notes that on the presumption that there is freedom of contract in the field of personal property floater insur-

ance there has been an extensive development in this class of policy. The cover has been broadened to the advantage of the insured and the inland marine underwriters and to the disadvantage of fire underwriters whose policy conditions have been frozen by statute. The Dominion Government's Blue Book discloses the following premium volumes for Inland Transportation and Personal Property Insurance. (It is necessary to combine these premiums since a Personal Property Floater policy was in 1930 classified as Inland Transportation Insurance by those insurers who wrote this kind of contract).

1939	*1941*	*1942*
1,019,359.	3,895,961.	4,850,383.

This field of insurance has increased 375% in slightly over ten years while fire and burglary premiums on household effects have shown decline and this decline is undoubtedly due in part to the fact that fire and burglary cover is now being purchased under Personal Property Floater.

Thus the attempt of the legislature to create a statutory policy for the purpose of protecting the assured who suffers a fire loss has been thwarted by the birth and development of a new type of policy which has been classified as something other than fire insurance.

Thirdly, from the standpoint of protecting the public's interest by safeguarding the solvency of companies, the practice has been established of requiring deposits, Dominion or Provincial, on the basis of the classes of insurance that the corporation proposes to write. This "class consciousness" may I term it, tends to perpetuate a tendency to distort covers to make them fit snugly into pigeon holes and to circumscribe to some extent a trend towards comprehensive policies, which trend the public seems to encourage. To the extent that all risk covers, both as to property and as to liability insurance, increase, to that extend small and precise classifications fail in their purpose from the standpoint of both deposits and statistics.

It is not necessarily a sound conclusion to say that the chances of insolvency vary directly with the number of classes of insurance in which a company may interest itself. A company

writing only one class may easily jeopardize its existence by poor selection in that class, by unduly exposing itself to catastrophe hazard or by inefficient management or irresponsible investment.

The amount of deposit for any class of insurance is of necessity arbitrary which fact in itself is not a ground for any complaint but merely a ground for the argument that the same end, *i.e.* security against insolvency might as well be achieved by way of an arbitrary deposit requirement which would have no relationship to the number of classes an insurer intended to write.

The expansion of the fire policy by way of supplemental contract has required special treatment of those insurers who merely wish to write classes of hazard covered by the supplemental contract and limit their writings to risks on which they carry fire insurance. In such cases licences to so write are freely granted and no additional deposits are required. This is tantamount to arguing that the chance of insolvency increases as an insurer increases the number of classes he writes except when he writes these classes only with respect to risks on which he carries the fire cover.

Fourth and lastly, classifications in the insurance field serve a purpose with respect to statistics. Statistics, however, in the insurance business have to be considered with great care. The very existence of this overlapping and confusion in the classifications and classification nomenclature tends to distort the statistics and with the trend towards comprehensive cover it is quite possible that statistics with respect to individual classes will become more and more warped to such an extent that they may in fact actually become misleading.

To recapitulate, I might say that we have the insurance field divided up into numerous classes:

(a) Because it has grown up that way and tends to expand that way as new fields of insurance develop.

(b) Because legislatures here and there have treated the business as being one of many classes and have described or restricted the charter powers of companies by listing the classes of business which they might or might not write.

(c) Because legislatures have attenpted to control the terms of the insurance contract in certain named classes, *e.g.* Fire, automobile and health and accident.

(d) And because the business has been segregated into classes, these classes have been used for other purposes, such as the fixing of deposits, the issuance of licences and the accumulating of statistics.

Mr. Douglas Barlow, a member of the Quebec Bar, in a paper which was printed in *La Revue du Barreau* and in the CANADIAN BAR REVIEW, has stimulated some considerable interest in this subject and as a result the Association of Superintendents of Insurance for the Provinces of Canada has appointed a committee to give this matter consideration.

It seems to me that while the segregation of the business into classes may well be necessary for some purposes, it may not be essential or wise for all of the purposes for which classifications are now used.

For the purpose of delineating the charter powers of a company, the naming and defining of classes may be necessary to describe the field of insurance in which a company may operate. As each jurisdiction however may define a class as it sees fit, the word as defined is only usable in that sense in the jurisdiction which makes the definition. The corporation of a foreign jurisdiction may have powers under its charter to transact fire insurance and those powers may in its own jurisdiction be more extensive or restrictive than those described by the same words in the charter of a domestic corporation simply because of the difference in the scope of the definition.

Classifications are not essential in the administration of deposit requirements as it might be possible to establish some other satisfactory basis which would as readily assure solvency. It would seem that the balance sheet of a company and the location of its assets are pertinent factors while the type of insurer might likewise be an important item to consider when determining the amount and nature of a deposit that should be required from any underwriters at Lloyds, from Mutual Insurers or from Stock Insurers.

Classifications for the purpose of statistics may well be necessary but better classifications might be adopted for this purpose if the same classifications were not called upon to serve other ends such as a basis for deposit requirement and for legislation affecting insurance contracts.

For the purposes of licensing and of legislation affecting the insurance business, in the other than life insurance field, the

classifications might well be fewer in number. This field can be broken down readily into the following classes:

1. Marine
2. Insurance of person—health and accident
3. Insurance of property
4. Insurance against legal liabilities
5. Guarantee

The classifications of insurance of persons, of property and against liabilities are natural ones. The maintenance of a classification for marine and guarantee may easily be justified, the former because of the difference in its history, its growth and its practices, the latter because it is not in fact insurance.

From the standpoint of licensing, a company could be licensed for any or all of the said classifications subject to such limitations as might be found in its charter powers.

To illustrate what might be done with respect to legislation affecting insurance contracts, let us look for a moment at the fire statutory conditions. My arbitrary classification may in detail be open to question. On this point, I readily hold myself open to correction and conviction.

The fire statutory conditions can be said to fall into three groups.

1. Those that deal with what in fact is substantive law and the following statutory conditions might be so categoried. Using the Ontario side notes to the conditions to describe their nature, they are as follows:

	Ontario	Quebec
Misrepresentation	1	1
Form of Contract	2	2
Material Change	7	3
Other Insurance	8	8–9
Mortgagees and Payees	9	–
Entry, Control & Abandonment	13	5*
Fraud	16	15
Agency	21	21
Waiver of Conditions	22	20
Subrogation	24	Code

*Quebec condition 5 in part deals with abandonment, not entry and control.

It is suggested that most, if not all, of the above deal with what is really not a matter of contract but a matter of law and that these statutory conditions are not of the nature that the

interest of the insured would require that they should appear in the policy contract any more than other principles of law that govern contracts should be recorded in the policy for the information of the insured.

The statutory condition re "Replacement", Ontario S.C. 19, Quebec S.C. 18, also appears to be one of substantive law but it is one about which it might be said that it should appear in the policy for the information of the insured.

If it were possible to reach some agreement as to the statutory conditions that are in fact matters of law rather than of contract and then remove them from the contract, placing them in the statute, it would simplify the contract and create an opportunity to draft those sections of the Act so that they would be applicable to all forms of property insurance. Then insofar as the insured has rights and duties with respect to these subjects, those rights and duties would be common to any contract of property insurance. Uniformity in the substantive law governing all insurance of property on the one hand and all insurance of legal liabilities on the other, would simplify practice and should contribute to the interest of the insurer and insured alike.

I do not want it taken that I advocate the mere transposition of these statutory conditions from their present position to a position in the substantive law without considerable thought as to the principles covered by those conditions and the words in which these principles are stated. It is indeed possible that the principles need to be modernized and the phraseology improved. Most of them have served as we have noted since 1876.

2. There are to be found amongst the statutory conditions, conditions that deal with procedure and those, in my judgment, should appear in the policy so that an insured would have before him the steps that he and the insurer must take when dealing with each other.

Again using the Ontario headings, these conditions seem to be:

	Ontario	Quebec
Termination of Insurance	10	19
Salvage	11	5
Who to make Proofs of Loss	14	12–14
Requirements after Loss	15	13
Arbitration	17	16
When Loss Payable	18	17
Replacement	19	18
Action	20	22
Notice	23	23

There should be no difficulty in establishing reasonable conditions on the above mentioned subjects that would be universally applicable and universally acceptable.

3. The balance of the statutory conditions, namely Ontario Statutory Conditions 3, 4, 5, 6 and 12 and Quebec Statutory Conditions 4, 6, 10 and 11 are not so easily classified although many of them fall into one or the other of the above mentioned groups, but because of certain aspects I will deal with them individually.

(a) Ontario S.C. 6 and Quebec S.C. 11 expand the meaning of the term "fire" by saying that the insurer shall make good losses by lightning and certain types of explosion. What these statutory conditions do in effect is expand the normal meaning of the word "fire" and to this extent it is rather a matter of definition.

(b) Ontario S.C. 3 and Quebec S.C. 6 limit the scope of the policy by eliminating from the normal cover certain kinds of property such as money, books of accounts, etc. . . These statutory conditions effect by way of a term of the policy what amounts to a modification of the description of the risk. It is done of course on the ground that the type of property mentioned is not common to the normal risk and is not the type of property that the parties to the ordinary policy would have in mind when they entered into the contract.

(c) Ontario S.C. 4(b) and 4(d) and Quebec S.C. 10(b) and 10(d) limit the scope of the cover by eliminating certain causes of fire damage. The one eliminates what is commonly called War Risk and the other eliminates damage where goods are being processed by fire heat, whatever that is in this modern world where heat for processing is more often generated by electricity than by fire. These conditions eliminate something which is not considered a normal fire hazard just as such a restriction is effected by the courts in their consideration of the problem of the friendly fire, i.e., damage arising out of such fire hazards is not the kind of fire damage that the parties to the ordinary policy would have in mind at the time that they entered into the contract.

(d) Ontario S.C. 4(a) and 5(c) and Quebec S.C. 10(a) and 4, state or modify the rule of law with respect to the question of insurable interest and like the whole question

of insurable interest these conditions are aimed at what is termed "moral hazard."

(e) Another group of statutory conditions are aimed at the question of physical hazard, namely Ontario S.C. 4(c), 5(a), 5(b) and 5(d) and Quebec S.C. 10(c), 10(e) and 10(f) and they describe hazards that are not normal physical hazards in the average risk. They are hazards not contemplated in the normal rate and are for this reason excluded from the ordinary policy. That they serve a fire prevention purpose can well be argued and this is the considered view of the Association of Canadian Fire Marshals.

(f) Finally, Ontario S.C. 12 makes the cover effective at some place other than the descirbed premises if the removal was made for the purpose of safeguarding the goods from imminent damage from the spread of fire.

In conclusion may I say that it is the conditions in this last group that really affect the right of freedom of contract at the more essential points. On this question of freedom of contract there will be strong views on both sides and I would predict that the cleavage in viewpoint will not follow the division of interest as between insurer and insured.

There will be those who speak for the public who will say that the freezing of the fire cover by the enactment of statutory conditions has circumscribed the natural growth of the fire insurance business by preventing some improvements and hampering others and that the public has been denied the advantages that would naturally flow from the normal improvements that arise in a business that is highly competitive. They would further adduce as evidence of their contentions the cumbersomeness of the supplemental contract on the one hand and the growth and expansion of the personal property floater policy on the other, which growth in part they would attribute to the presumption that the personal property floater policy is at the moment free of the dead hand of the statutory conditions. With this view there will be many insurers who will agree.

On the other hand, among those who speak for the public there will be those who will refer to the conditions that were said to exist prior to the appointment of the Royal Commission in Ontario in 1876, which conditions were probably somewhat overstated by Chief Justice Wilson in a case reported in (1872), 33 U.C.R. 69. The Chief Justice made the following observations:

> The conduct of companies, when enforcing rigidly such conditions, has often been complained of by the Courts by reason of the number and nature and difficulty of the conditions they introduce into their policies; and the time perhaps has come when the legislature should interfere, and stand between them and those they insure or pretend to insure, or, in other words, the public, by limiting them to such conditions which the Courts shall determine to be reasonable.

Then too it may be admitted as a fact that in any field of endeavour there is bound to be a small minority which might be termed "smart operators", i.e. smart in the short view. Insurers appreciate the role that insurance plays in the present financial and commercial and industrial worlds and that Cain's questionable answer "Am I my brother's keeper" does not suffice since sharp practices in the business are charged to the business as a whole and are answerable for by all engaged in the industry. For this reason there will be some insurers who will support a statutory form of policy and a reasonable amount of administrative supervision, in the anticipation that such safeguards would keep "smart operators" within the bounds of fair practice.

It must be admitted that the indifference of the average insured as to the terms of his contract must be attributed either to sheer want of care or sheer abundance of faith based on an experience of fair dealing in insurance contracts since purchasers of insurance never seem to recall the maxim "caveat emptor."

The supporters of freedom of contract will of course point out in rebuttal to the supporters of government paternalism that the whole casualty field apart from automobile insurance is free from restriction and that the casualty business has so expanded in volume that it has now passed the mark set by the fire insurance business and that there is no evidence of abuse by insurers of the freedom of contract in the writing of casualty policies. It is quite probable that these same proponents would point out that the conditions that allegedly existed in 1876 do not and cannot exist today because in the interval the insurance business has reached a maturity so that those engaged in it appreciate that their own interests are best served by properly serving the public interest.

It will be interesting to follow this conflict in views; upon which school of thought prevails, much depends. That some via media may be found that will reasonably satisfy the contentions of the protagonists of both viewpoints is somewhat doubtful.

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