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## PHENOMENOLOGY OF INSURABLE INTEREST IN LIFE ASSURANCE

SCIENTIFIC PAPER

### Abstract

Subjective attitude towards tangible or intangible possessions is the driving force of the person's will to seek the means of their protection. In this paper, the institute of interest is generally analysed through the philosophy of enlightened self-interest and economics, while in the field of law, "interest" is compared to the subjective right and condition in law. Subsequently, the subject of research is the position of legal theory in relation to the need for interest in personal insurance, also explored through the analysis of the characteristics of certain types of life assurance and rationales for effecting such assurance. The current circumstances are briefly addressed in comparative legal systems, with a special focus on English law. At the end of the paper, an example of legally regulated obligations of insurance sales agents to act in the best interest of policyholders and insured persons is presented at the level of the European Union, together with the example of French law regulating conflicts of interest in life assurance.

**Keywords:** *insurance, life, interest, subjective right, condition in law, insurance beneficiary*

### I. Theoretic Considerations of the Insurable Interest

Depending on their initial premises, philosophy and psychology provide different answers to the question of what "interest" is.<sup>2</sup> In the field of social relations,

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<sup>2</sup> For example, to the concept of interest in the evolutionary biology the theory of reciprocal altruism may be applied whereby an organism acts in a manner that temporarily reduces its fitness while increasing

for the philosophy of ethics, it is important to note what the French historian, lawyer, philosopher, and sociologist Alexis de Tocqueville pointed out. Namely, he claimed that the general principle in the emergence of democracy in America is that man serves himself in serving his fellow creatures and that his private interest is to do good.<sup>3</sup> He thus became the founder of the philosophy of enlightened self-interest in the philosophy of ethics, according to which persons who act to further the interests of others in the same group ultimately serve their own self-interest. This interest, in the narrowest sense, is manifested in family relations where parents and children mutually support one another, whereas one of the goals of contracting life assurance is to ensure a certain financial security of the spouse and children after the death of the insured. A personal interest that is identical with the interests of other individuals creates in their lives a community of interests expressed through the general, public interest of society.<sup>4</sup> Thus, the members of the community are timely and efficiently provided for, evading social benefits and the burden on public social security funds.

The economics of enlightened self-interest includes narrow self-interests (which focus on individual possessions), shared interests (which focus on relationships, community, and social values), and altruistic interests (which focus on interests that are solely others', which one pursues only out of a sense of stewardship, ethics, or morality).<sup>5</sup> Economically determined interest is a subjective relationship expressed in the desire to achieve or avoid certain conditions or to preserve or acquire certain possessions.<sup>6</sup> In legal relationships, interest is an important subject of law that gives various means for expression, implementation and protection, which is why a subjective right is constituted thereon.<sup>7</sup> According to Professor Andrija Gams, interest is, in fact, a conscious relationship between the need and the means (goal) of its satisfaction, and in civil law it represents a certain economic relationship.<sup>8</sup> That is why it is said that a person who has a legally relevant interest enters into a legal relationship in which his interest and the interest of his contracting party are

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another organism's fitness, with the expectation that the other organism will act in a similar manner at a later time (Robert, L. Trivers, "The evolution of reciprocal altruism", *Quarterly Review of Biology*, 46(1), 1971, pp. 35–57).

<sup>3</sup> Alexis de Tocqueville, "How the Americans combat individualism by the principle of self-interest rightly understood" (500–503) in: *Democracy in America*, Vol. II, Chapter VIII, The University of Chicago Press, Chicago and London, 2002, pp. 500.

<sup>4</sup> Snežana Radovanović, "Slobodni građani, demokratija – Pretpostavke primene rimskog prava", *Mega-trend Review*, 17(4), 2020, pp. 41–48, pp. 43.

<sup>5</sup> John Ikerd, "Rethinking the Economics of Self-Interests", Lecture at the Seminar, September 1999, University of Missouri. Retrieved from: <http://web.missouri.edu/ikerdj/papers/Rethinking.html>, 20. 3. 2019.

<sup>6</sup> Vladimir Janković, Mirjana Milosavljević, (editors), *Mala enciklopedija Prosveta – Opšta enciklopedija*, fourth edition, A–J, Prosveta, Beograd, 1986, pp. 898.

<sup>7</sup> Borislav T. Blagojević, (Editor-in-Chief), *Pravna enciklopedija*, volume 1, Savremena administracija, Beograd, 1989, pp. 496.

<sup>8</sup> Andrija Gams, *Uvod u građansko pravo*, Naučna knjiga, Beograd, 1988, pp. 90.

satisfied. Accordingly, legal theory states that civil subjective law is a set of powers aimed at satisfying certain interests that the state recognizes and guarantees to one party in a civil law relationship, as opposed to the coexistent obligation of the other party.<sup>9</sup> However, the interest of a person can also be satisfied through unilateral legal transactions, based on a unilaterally expressed will. One such example in life assurance is determining the insurance beneficiary. According to the generally accepted legal theory, the act by which the insurance beneficiary is appointed is a unilateral statement of will, and the insurance beneficiary's statement of intent to exercise that right is irrelevant to the creation of the right itself,<sup>10</sup> whether the beneficiary is named at the time of concluding the life assurance contract or after its conclusion.<sup>11</sup> By appointing the insurance beneficiary, the insured person realises the interest for which the contract for insurance of his own life was concluded.

From the perspective of economics, enlightened self-interest is a product of balance between the abovementioned types of interests which does not allow us to simply maximize or minimize any one particular aspect or dimension of our lives,<sup>12</sup> whereas from the legal perspective, the interest enjoys protection only if it is recognised or allowed by law. In this regard, in life assurance, as in other types of insurance, insurable is only a legitimate interest. However, another question could be raised here regarding the circumstances under which the insured person had lost his life. For example, does insurance cover the death of an insured person due to a terrorist act? The answer to this question will largely depend on the provisions of the insurance terms and conditions, as some of them exclude such events from life assurance cover, while others cover them.<sup>13</sup> On the other hand, an insured person, who is a wrongdoer, cannot be protected by life assurance. Such a solution derives from the general rule on the nullity of insurance in respect of harmful events that would occur from illegal, immoral or prohibited actions of the insured, such as escape from prison, evasion of military service, etc.<sup>14</sup> In Serbian law, if the insured event occurred during the war operations, unless agreed otherwise, the insurer shall be liable to pay only the mathematical reserve (and not the sum insured),<sup>15</sup> while

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<sup>9</sup> Nikolić, Dušan, *Uvod u sistem građanskog prava*, seventh edition, Faculty of Law in Novi Sad, Novi Sad, 2006, pp. 235–236.

<sup>10</sup> Šulejić, Predrag, *Pravo osiguranja*, Dosijske, Beograd, 2005, pp. 490.

<sup>11</sup> Jovan Slavnić, Slobodan Jovanović, „Zakonsko regulisanje osiguranja života u korist trećeg lica u savremenim evropskim pravima i u pravu Srbije“, *Pravni život*, tom LXIV, no. 11/2015, pp. 135–152, pp. 144.

<sup>12</sup> J. Ikerd, 1999.

<sup>13</sup> Hilary Osborne, “Insurers ‘will consider claims resulting from attack’”, *The Guardian*, 8 July 2005. Retrieved from: <https://www.theguardian.com/business/2005/jul/08/insurance.terrorism>, 20. 3. 2019.

<sup>14</sup> P. Šulejić, 2005, pp. 310–311.

<sup>15</sup> Law of Contract and Torts, *Official Gazette of SFRY*, no. 29/78, 39/85, 45/89 – decision of CCY And 57/89, *Official Gazette of FRY*, no. 31/93 (ZOO) and *Official Gazette of Serbia and Montenegro*, no. 1/2003 – Constitutional Charter, Article 952, paragraph 1.

English law takes into account various circumstances regarding the status of the policyholder / insured, as well as the interests of British citizens. Thus, in the event of the insured person's death during the service in the enemy army engaged against Great Britain, the insurance contract will be null and void. In the event of death during war operations, the insurer's obligations will exist if the insured dies on the enemy's side, provided that he was not engaged in war operations against Great Britain. In the case of a life assurance policy of an insured person who is an enemy, where the insurance beneficiary is a British citizen as the creditor who granted such insured the loan, the insurance shall take effect in the event of the death of such an insured person during or as a result of hostilities.<sup>16</sup>

Subjective right often does not have to coincide with the existence of an interest. In this case, there is a legally protected interest due to the existence of a certain *condition in law*.<sup>17</sup> Condition in law is a situation in which some of the legally prescribed conditions for acquiring a civil subjective right are missing.<sup>18</sup> It is a situation in which to create a subjective right, it is necessary to fulfil one or more legally relevant facts. In the field of life assurance, the insurance beneficiary is in the condition in law until the condition for acquiring the right to indemnity under the life assurance policy is met. Thus, the insurance beneficiary acquires the right to collect the insured amount after the death of the assured.

Although a large part of legal theory, as well as the Serbian Law of Contract and Torts refers to property insurance when considering the existence of interest,<sup>19</sup> there is also a perception that the interest, as the driving force behind the conclusion of the insurance contract, also exists in the personal insurance.<sup>20</sup> Those who think that the existence of interest is not necessary in the insurance of persons, ignore the fact that the personal insurance also includes a whole range of personal insurance lines where compensation is represented. This is the case with health and accident insurance, which reimburses the costs incurred by treatments and medical aid, as well as daily benefits. When it comes to life assurance in the event of death or survival, the insurer's interest is reflected in some other rationales for concluding this type of insurance, and thus its effects are different. In such case, the interest may be reflected in the financial security of the relatives after the death of the insured person or in the savings. Therefore, the interest in life assurance is reflected in the will of the insured persons to achieve financial security for themselves or their relatives in the future.

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<sup>16</sup> Nicholas Legh-Jones (General Editor), *MacGillivray on Insurance Law*, Ninth Edition, Sweet & Maxwell, London, 1997, pp. 351.

<sup>17</sup> A. Gams, 1988, pp. 88; Ilija Babić, *Osnovi imovinskog prava – Uvod u građansko pravo i stvarno pravo*, Official Gazette, Beograd, 2008, pp. 117.

<sup>18</sup> D. Nikolić, 2006, pp. 235.

<sup>19</sup> P. Šulejić, 2005, pp. 312.

<sup>20</sup> Nikola V. Nikolić, *Ugovor o osiguranju*, Državni osiguravajući zavod, Beograd, 1957, pp. 57.

Thus, it seems wrong to take the generally accepted view that life insurance does not have a compensatory character because it does not aim to compensate for the damage suffered, and therefore the interest in life insurance does not have the same significance as in property insurance.<sup>21</sup> However, while it is true that the property insurance is an interest of a material nature, it is wrong that the personal insurance has no such interest. From the times of slavery and the Hammurabi Code to the early Anglo-Saxon law, there was evidence of the application of the theory of the value of human life used to determine compensation to the relatives of a person who kills a third person. In modern times, it is also important to determine the value of human life in proceedings for compensation of damage caused by a murder (manslaughter or premeditated – author’s comment).<sup>22</sup> According to the US insurance economy, the value of human life (today – author’s comment) is a measure of future earnings or the value of individual services, i.e. the capitalized value of an individual’s future income less his or her own subsistence, such as food, clothing, and accommodation. From a dependent’s point of view, the value of the human life of the breadwinner is the value of the benefits that the dependent can expect.<sup>23</sup>

Legal theory points out that the insurance of a person in connection with life, health, bodily integrity does not have a compensatory character, nor is characterised by insurance interest,<sup>24</sup> although, as we have seen, there is an interest in personal insurance, but it depends on the goal to be achieved by concluding a particular type of personal insurance. Therefore, the interest in insuring a person has its material component which is related to particular expenses, while in other cases it is related to the payment of a certain amount of money (insured amount) which is not compensatory, because the value of damaged or destroyed material property (object) is not compensated. Thus, the rationale for concluding a contract on personal insurance arises from caring for tomorrow and the desire to provide yourself, children, wife or any other relative with protection against accidents and death or protection in the event of a certain occurrence that causes higher expenses (wedding, schooling), or affects the reduction of the insured’s earnings, or simply stems from the desire to improve living conditions (survivorship).<sup>25</sup> As indicated in economic theory, advances towards a better understanding of future developments and their consequences can greatly contribute to the establishment of a “ready society”.<sup>26</sup> However, an insurance

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<sup>21</sup> P. Šulejić, 2005, pp. 312–313.

<sup>22</sup> Kenneth Black III, Harold D. Skipper, *Life Insurance*, 15th Ed., Lucretian, LLC, Atlanta, 2015, pp. 26.

<sup>23</sup> K. Black, H. Skipper, 2015, pp. 27.

<sup>24</sup> P. Šulejić, 2005, str. 313; Jovan Slavnić, *Privredno / trgovinsko pravo sa osnovama građanskog prava*, Belgrade Business School, Beograd, 2006, pp. 403.

<sup>25</sup> N. Nikolić, 1957, pp. 57–58.

<sup>26</sup> Mirjana Radovic-Markovic, Sladjana Vujcic, “Prediction in social sciences”, *International Review*, No. 1-2, 2021, pp. 15–20.

premium, actuarially determined on a scientific basis to be paid by the insurer, should be distinguished from the mere selling price of different items in sales contracts where individual consumers have an interest in keeping the sales price as low as possible, while the distributor has an interest in achieving the highest possible selling price for his product.<sup>27</sup>

In comparative law, there is no agreement on the compulsory existence of an insurable interest in life, property and transport insurance. There are legal systems that prescribe the mandatory existence of an insurable interest in the insurance of persons, property and transport under the threat of insurance nullity, such as Great Britain and China, while in Australia, the existence of an interest in life assurance has been abandoned since 1995.<sup>28</sup> However, a number of legislations do not accept the concept of interest in personal insurance, but instead require the consent of the insured person (the person in whose life the insured event is to occur) in order for the insurance to operate.<sup>29</sup>

From the emergence of insurance as an activity of great interest in maritime transport and trade, and even after the discovery of the fundamental mathematical principles of modern personal insurance methods and the first mortality tables in England, insurance has often served as means for betting and a gambling that, at one point, the law had to forbid. Thus, in the 18th century England, it was common for policies to be taken out on the lives of public figures, distant family members, and acquaintances until the complaints were made when newspapers started to print the odds of survival of public figures.<sup>30</sup> To put a stop to this phenomenon, the Life Assurance Act 1774 was adopted and is still in force. It stipulates the existence of insurable interest under threat of nullity. Because of the situation determined by the mentioned law, which due to the development of personal insurance became unclear in certain matters, as well as obsolete and restrictive in some other aspects, insurers were prevented from insuring certain types of demands. In 2008, English, Welsh and Scottish proponents of the amendments to the Law initiated the procedure for drafting the Insurable Interest Bill (in life assurance, author's comment). The draft Insurable Interest Bill of June 2018 covers almost all possible situations and statuses of the person who is a party to the life-related insurance contract. In view of the above and according to the provisions of the said Bill, the insured will have an insurable interest if there is a reasonable prospect that it will suffer an economic loss if the insured event occurs. In English law, the insurable

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<sup>27</sup> Milica Stojković, Violeta Jeremijev, "Price formation in trade companies", *International Review*, 3-4, 2021, pp. 62-66, pp. 63.

<sup>28</sup> Zheng Jing, "Insurable interest in life insurance: a Chinese perspective", *Journal of Business Law*, 5/2014, pp. 337-359.

<sup>29</sup> P. Šulejić, 2005, pp. 312.

<sup>30</sup> Law Commission & Scottish Law Commission. (March 2015). *Insurance Contract Law: Insurable Interest*, Extract from LCCP 201 / SLCDP 152 (Post Contract Duties and other Issues), pp. 105.

interest of the policyholder in insuring the life of another person is reflected in the blood relationship between spouses, children, parents and other relatives on the basis of: (1) obligations to bear the funeral costs, (2) the obligation to bear the costs of support or education of the insured, (3) the cost of hiring a home-care worker if the insured performed important household chores, (4) the insured's contribution to the common family fund, and (5) legal obligations to support the insured in case of his illness, incapacity for work, old age, or poverty.<sup>31</sup> The persons in whom the insured may have an insurable interest are: the policyholder who is also the insured, the spouse or common-law partner of the insured, children and grandchildren of the insured, a person who is a member of a pension plan or other scheme managed by the insured, and the person in whose favour the insurance is concluded (insurance beneficiary). All legal systems are also characterised by the situations when another person, beyond the circle of the mentioned persons, may have an interest in insuring someone else's life. This will be the case with the life assurance of the person taking the loan, when the bank, as one of the conditions for securing the loan, requires the conclusion of that person's life assurance policy against the risk of accident and death. This is the material interest of the bank which, in the event of the borrower's death or incapacity for work, uses an insurance policy to collect the remaining loan amount. This protects not only the bank as a creditor, but also the heirs of the deceased debtor who are in such case protected from the obligation to pay the debt of the testator. In the above example, there are excluded interests, because the heirs would not have the right to keep the insured compensation based on the inheritance. However, if they collected it from the insurer, they have the obligation to pay it to the creditor. This arises from the legal obligation according to which the heirs, in addition to the property, inherit the debts of the testator up to the value of the inherited property.<sup>32</sup> A similar situation is the case of insuring the life of a key person in a business entity whose knowledge, skills, and contacts directly influence the sustainability and success of business operations. In such case, the (material) interest in insuring life of the key person has the business entity in which that person is employed or holds an important office. In that case, the value of the key person's life represents the value of the services he or she provides to the business entity, due to which that person may have a larger number of life sums (depending on the range of services and jobs he or she performs or provides to the business entity -author's comment).<sup>33</sup>

In addition to national laws, the legislative activity of the European Union significantly affects the development of the law of member states, because it introduces certain obligations in the field of equalization of rights. As the protection of

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<sup>31</sup> N. Legh-Jones, 1997, pp. 38.

<sup>32</sup> Law on Inheritance, *Official Gazette of RS*, nos. 46/95, 101/2003 – Decision of CCRS and no. 6/2015, Article 222.

<sup>33</sup> K. Black, H. Skipper, 2015, pp. 27.

insurance service users improves, the obligations of insurance distributors/insurers, intermediaries, and insurance agents increase. New obligations and standards of conduct in legal transactions are established with the aim of implementing certain development policies. Thus, in insurance industry, in addition to acting honestly, fairly and professionally, which is otherwise their obligation under the national laws, insurance service providers are obliged to act in the best interests of the policyholders.<sup>34</sup> This standard applies to their obligations concerning information, advisory activities, insurance proposals, and preparation of the text of the insurance contract, conclusion of the insurance contract, and participation in the management and execution of the insurance contract, especially when the policyholder is to collect the insured benefit. However, the standard of “best interest” of the insured person remained undefined and consequently, the duty was imposed on the insurance distributors to act, in addition to taking into account their commercial interests, in the best interests of the insurance customers. This means that with their decisions and actions, the insurance service distributors are obliged to achieve and maintain a certain balance of their interests and the interests of insurance beneficiaries. To that extent, the regulations protecting the rights of insurance customers do not refer to the insurable interest as a *conditio sine qua non* validity of the insurance contract, but to every conceivable interest of the policyholder / insured person in terms of its legally recognised interests such as full and accurate information on the insurance product, the method of premium payment, profit sharing, moment when the sum insured is paid out, exercising the right to payment of the insurance redemption value, movement of assets which determines the life assurance unit-linked sum insured, and other legal rights.

In some cases, comparative legal systems also regulate situations where there is a conflict of interest regarding life assurance. As an example, legal theory cites French law according to which, the beneficiary of a life assurance contract, who manages the business of the insured person or is his or her guardian, is considered to be in a conflict of interest with the incapacitated person, and the insurance beneficiary may not be replaced without the approval of the court or the family council from the moment when the guardianship has been established in relation to the right to contract or redeem life assurance policy.<sup>35</sup>

## II. Conclusion

Finally, it can be said that throughout history, the institute of interest was created and developed in accordance with the given social relations and specificities

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<sup>34</sup> Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast), *Official Journal of the European Union*, L 26, 2. 2. 2016, Article 17, paragraph 1.

<sup>35</sup> J. Slavnić, S. Jovanović, 2015, pp. 147.



of individual markets. There is a noticeable difference between the Anglo-Saxon tradition in which interest has been and remains to this day one of the important insurance institutes that influences its validity, while in continental (European) legal systems there is generally no such importance in personal insurance. However, the denial of the existence of interest in personal insurance is unfounded and should not be interpreted as inherent to property insurance. The institute of compensation, which is characteristic of property insurance, is also inherent to all types of personal insurance where the purpose of insurance protection is achieved through the reimbursement of certain costs or amounts due. On the other hand, the interest in life assurance is related to one's own material security in old age or the security of one's relatives, as well as to covering particular expenses. Therefore, although the subject of personal insurance is an intangible value (life and health of a person or costs related to a particular person as a beneficiary or insured), personal insurance has its own material basis that coincides with the interest for which this type of insurance is concluded. The institute of contract law interests thus explained should be distinguished from the application of the presumed best interest of the policyholders and insured persons as a supervisory and regulatory obligation of all life assurance distributors when advertising, offering insurance, informing policyholders and insured persons, concluding and executing life assurance contracts.

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