CLAIM OF NOBORU SUMI

[No. 146–35–2023. Decided June 7, 1951]

FINDINGS OF FACT

This claim, in the amount of $215.55, was received by the Attorney General on March 28, 1949, and alleges loss through forced abandonment of a life insurance policy. Claimant was born in Seattle, Washington, of Japanese parents and has at no time since December 7, 1941, gone to Japan. On December 7, 1941, and for some time prior thereto, claimant actually resided at 1157 East 10th Street, Los Angeles, California, and he was living at that address when evacuated on May 9, 1942, under military orders pursuant to Executive Order No. 9066 to the Pomona Assembly Center and from there, later, to the Heart Mountain Relocation Center. At the time of his evacuation, claimant was the owner of a $3,000 life insurance policy which had been issued to him on January 18, 1941, by the Manufacturers Life Insurance Company of Toronto, Canada, on the 20-year endowment plan at a semiannual premium rate of $71.85. Claimant had made timely payment of the three premiums respectively due on January 18 and July 18, 1941, and January 18, 1942, paying a total of $215.55. He did not pay the premium due on July 18, 1942, however, but concluded to abandon the policy because he was then in the assembly center earning only $9 a month and had no funds other than these earnings. In consequence of claimant's default, on August 18, 1942, the 30-day grace period having expired, the policy was canceled by the company. Since the policy provided that no cash surrender value or other nonforfeiture provision should accrue until it had been in force for 3 full years, claimant received no refund or equivalent nonforfeiture benefit at the time of its cancellation. Claimant acted reasonably in the circumstances in defaulting on the premium payment due July 18, 1942, and in abandoning his policy. Claimant was still insurable on August 18, 1942, the date of cancellation, and the then fair market value of his policy was $184. Claimant was unmarried and sole owner of the policy at the time of loss and the loss has not been compensated for.

REASONS FOR DECISION

The instant case presents for original consideration an allegation of loss through forced abandonment of a life insurance policy. While the subject matter is new, the applicable criteria are, or course, well settled. As appears from the express provisions of Section 1 of the Statute, compensability thereunder rests upon a threefold basis. To assert a statutory cognizable right of recovery, a claimant must establish a transaction, occurrence, or conduct which (1) is "a reasonable and natural consequence" of his evacuation or exclusion, (2) relates to "real or personal property," and (3) has resulted in "damage * * * or loss" thereto. The issue presented, therefore, is whether or not claimant in the instant case has satisfied these requirements.

Of the three elements involved, the first two, "causation" and "property," offer no special problem. With respect to the first, "causation," as appears from the authorities cited in *Seiji Bando, ante,* p. 68, a "natural consequence" is one which ordinarily follows from an act and may reasonably have been anticipated or expected therefrom. Since evacuees were denied normal employment and income opportunities while in assembly and relocation centers, it obviously was to have been anticipated and expected that they would not be able to continue premium payments on their insurance policies. Furthermore, that this fact was fully recognized by the Congress is conclusively shown by the Statute's legislative history.

Thus, the Krug letter incorporated in the House Report on the bill (H. Rept. 732, 80th Cong., 1st sess.) specifically states:

> In relocation centers the only income opportunities for evacuees lay in center employment at wage rates of $12 to $19 per month, plus small clothing allowances. *Many felt compelled to discontinue payment of life insurance premiums.* Some found themselves unable to make mortgage or tax payments and lost substantial equities.
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> All of the foregoing examples of tangible loss to the evacuees are *directly attributable* to the evacuation and continued exclusion of these persons from their homes. [Emphasis supplied.]

Patently, then, claimant's failure to make the premium payment due on July 18, 1942, with resultant cancellation of his policy on August 18, 1942, was a "natural consequence" of his evacuation within the meaning of the Statute. Moreover, since it has been found as a fact that claimant acted reasonably in the circumstances, it is plain that the first of the three elements of statutory cognizability, namely, "a reasonable and natural consequence," has been fully satisfied.

Equally clear is the matter of "property." In this connection, it is appropriate to observe, initially, that while claimant's policy was on the so-called "endowment plan," it is well settled that such policies are in no wise different from other life insurance policies in contemplation of law. *Carr* v. *Hamilton,* 129 U. S. 252; *Cooley's Briefs on Insurance* (2d ed.), Vol. 1, pp. 32, 33. The question presented, therefore, is whether life insurance policies are "property" within the meaning of the Statute. That the answer is in the affirmative and that modern "level-premium" insurance policies are not mere indemnity contracts but property, having property values and being possessed of the ordinary characteristics of property, admits of no dispute. *United States* v. *Ryerson,* 312 U. S. 260; *Powers* v. *Commissioner,* 312 U. S. 259; *Guggenheim*

v. *Rasquin,* 312 U. S. 254; *Lucas* v. *Alexander,* 279 U. S. 573; *Chase National Bank* v. *United States,* 278 U. S. 327; *Grigsby* v. *Russell,* 222 U. S. 149; *Heiner* v. *Grandin,* 44 F. (2d) 141; *Frick* v. *Lewellyn,* 298 Fed. 803; *Ryerson* v. *United States,* 28 F. Supp. 265; *Billings* v. *Commissioner,* 35 B. T. A. 1147; cf. *Cooley, op. cit.,* Vol. 1, pp. 118–119; and see, also, *Griffin* v. *McCoach,* 116 F. (2d) 261, rev'd on other grounds in 313 U. S. 498. Moreover, it is pertinent to point out that as property modern level-premium insurance policies have two separate and distinct aspects. *Ryerson* v. *United States, United States* v. *Ryerson, Guggenheim* v. *Rasquin, Powers* v. *Commissioner, supra.* Thus, first, there is the ownership of insurance protection, i. e., the incident of insurance *per se. Idem.* Cf. *Speer* v. *Phoenix Mutual Life Ins. Co.,* 36 Hun. (N. Y.) 322; *Mutual Reserve Fund Life Ass'n.* v. *Ferrenbach,* 144 Fed. 342; *Caminetti* v. *Pacific Mutual Life Ins. Co.,* 23 Cal. 2d 94. Secondly, there is the element of "investment and self-compelled saving" indigenous to "level-premium" insurance and constituting its very essence. See authorities cited, *supra,* together with *Lovell* v. *St. Louis Mutual Life Ins. Co.,* 111 U. S. 264; *New York Life Ins. Co.* v. *Statham et al.,* 93 U. S. 24; cf. *Vance on Insurance* (2d ed.), pp. 26–27, 47. As appears from the authorities, insurance premiums are of two kinds: "natural" and "level." The former, i. e., "natural" premiums, relate to insurance only and are predicated on the precise risk involved, varying from year to year according to the age of the insured. "Level" premiums, on the other hand, are based upon the insured's calculated life expectancy and are therefore uniform and at a flat or level rate throughout the period of the policy. Because during a considerable portion of the term involved the amount paid exceeds the actual cost of the protection provided, under the "level-premium" plan an insured is able to accumulate a surplus, representing savings over and above the actual cost of his insurance *per se,* which the company keeps as a reserve. This reserve, together with the interest thereon, steadily accumulates so that on the expiration of the insured's life expectancy and maturity of the policy the total amount of the reserve equals the face amount of the policy. See *Mutual Reserve Fund* v. *Ferrenbach* and *New York Life Ins. Co.* v. *Statham et al., supra;* cf. *Vance, op. cit.,* pp. 51–52, 54, 56; and see, also, *Carr* v. *Hamilton* and *Lovell* v. *Insurance Co., supra.* As appears from the authorities, this reserve, i. e., the excess of the premiums over the actual cost of insurance, represents the insured's "equity" in his policy. *Idem.*[1] This well-recognized fact that an insured has an "equity" in a "level-premium" policy no doubt explains the joinder of discontinuance of payments in the portion of the Krug letter quoted above.

While "causation" and "property" then offer no difficulty, the third element, "loss," is of entirely different character and presents matter of exceeding complexity. The record discloses that the field determined claimant's loss to be in the amount of the legal reserve on the policy at the time of cancellation, apparently on the basis of the "value of the policy" principle applied in *Lovell* v. *St. Louis Mutual Life Ins. Co., supra.* The principle thus applied is one of the three rules applicable in cases of wrongful cancellation, termination, or repudiation of an insurance policy by the insurer, the other two being cost of similar insurance, i. e., replacement cost, and return of premiums with or without interest from the respective dates

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[1] Cf. *Mutual Reserve Fund Life Ass'n* v. *Ferrenbach,* 144 Fed. 342, at page 343: "In a policy issued upon what is termed the level premium plan, the insured has an equity arising from an excess of premiums paid above the current cost of insurance to the company. Under such a plan the natural premiums for the respective years, which steadily and progressively increase as the insured advances in age, are so adjusted and averaged among the years of his expectancy of life that they become flat or level, the same in amount in the beginning as at the end. In such a case it is apparent that the earlier level premiums contain an appreciable excess over the actual cost of insurance, which decreases, however, with the progress of the years. So it is said that in a level premium policy the insured has an equity, the excess of payment above cost of insurance * * *."

of payment. See annotations 48 A. L. R. 107; 107 A. L. R. 1233; cf. *Vance, op. cit.*, pp. 325–333; *29 Am. Jur.* §§ 314–317; *Watson* v. *Mass. Mut. Life Ins. Co.*, 140 F. (2d) 673. These three rules are applied where the insured is still insurable at the time of cancellation or repudiation. If the insured is then no longer insurable, a situation with which we are not here confronted, still a fourth rule is adopted, namely, maturity value of the policy less anticipated premiums determined on the basis of the insured's reduced expectancy, both amounts being duly discounted as of the time of cancellation. *Idem.* Cf. *Mutual Reserve Fund* v. *Ferrenbach, supra,* and *Capital City Ben. Soc.* v. *Travers,* 4 F. (2d) 290. Claimant has interposed objections to the principle applied by the field and, through brief of counsel, has offered three alternatives in lieu thereof, namely, (1) return of premiums with interest, (2) return of premiums without interest, and (3) premiums with interest less net cost of term insurance for the period that claimant's policy actually was in force.

That the claimant's alternatives are not here applicable is readily demonstrable. With respect to the first two, return of premiums with or without interest, examination of the authorities reveals that the principle advocated has, with but few exceptions, been generally rejected by the Federal courts. See, *Lovell* v. *Ins. Co., supra; Watson* v. *Mass. Mut. Life Ins. Co., supra; Capital City Ben. Soc.* v. *Travers, supra;* and *Mutual Reserve Fund Life Ass'n* v. *Ferrenbach, supra.* Moreover, the authorities reveal that not only is this principle punitive in concept (see *Vance, op. cit.*, p. 331; cf. *Watson* v. *Mass. Mut. Life Ins. Co., supra*), but its underlying rationale is contract rescission whereunder the parties are placed "precisely in the same situation they were in before the contract was made." *American Life Ins. Co.* v. *McAden,* 109 Pa. 399; cf. *Black* v. *Supreme Council, American Legion of Honor,* 120 Fed. 580, aff'd in 123 Fed. 650, *cert. den.* 191 U. S. 568; *Life & C. Ins. Co.* v. *Baber,* 168 Tenn. 347, 79 S. W. (2d) 36, 107 A. L. R. 1228, and annotations in 48 A. L. R. 107;

107 A. L. R. 1233. Obviously, this principle cannot be applied to the situation here involved, the issue being not rescission of contract, but valuation of property. As for claimant's third alternative, premiums with interest less net cost of equivalent term insurance, the basis of the contention apparently is the analogy of tortious interference with contract. As pointed out in *Mary Sogawa, ante,* p. 126, however, the validation of the evacuation by the Supreme Court in *Koromatsu* v. *United States,* 323 U. S. 214, renders principles of tortious recovery here inapplicable. Moreover, it is plain that the formula advanced is in any event untenable. Not only does the Statute make no express provision for recovery of interest (cf. *United States* v. *Hotel Co.,* 329 U. S. 585, 588), but it is equally clear that insurance is obtained at market price and not at net cost; furthermore, as already indicated, the problem here is not one of damage assessment, whether in contract or tort, but property valuation.

Equally inapplicable in the situation here postured is the principle of reserve value applied by the field. That this principle represents a recognized basis for valuation of insurance policies in a number of situations, cannot be disputed. As stated in the *Lovell* case, *supra,* the reserve value of a policy represents "what is called and known in the life insurance business as the value of * * * [a] policy." It likewise represents the "equitable" or "just" value of a life insurance policy and is undoubtedly the proper basis for equitable recission as between insurer and insured. *New York Life Ins. Co.* v. *Statham et al, supra;* cf. *Lovell* v. *Insurance Co., supra.* Again, it has been recognized as a proper basis for determining the "net" or "fair" value of a policy of the type here involved, i. e., one on which premium payments are still being made, for taxation purposes. See, e. g., *Lucas* v. *Alexander, supra;* cf. *Treasury Gift Tax Regulations 108,* Sec. 86.19 (i). The fact remains, however, that as pointed out in *George M. Kawaguchi, ante,* p. 14, the applicable standard under the Statute is "fair market value at the time of loss."

Moreover, as there observed, the "jurisdiction" conferred by the Statute is "to determine according to law." And it is elementary in law that the ascertainment of value is not a matter of formulas, but must be based upon proper consideration of all relevant factors. *Standard Oil Co.* v. *Southern Pacific Co.,* 268 U. S. 146. That the reserve value of a policy, though indubitably the proper basis for equitable recission, nevertheless does not and, from its very nature, cannot satisfy these requirements of law is irrefutable. As shown by the authorities, the reserve value of a policy is determined on the basis of "net premiums." *Fuller et ux.* v. *Metropolitan Life Ins. Co.,* 70 Conn. 647; *Cooley, op. cit.,* Vol. 2, p. 1628; *Vance, op. cit.,* p. 52; *Appleman's Insurance Law and Practice,* Vol. 1, p. 9. It is the "net" value of a policy, the amount which the company is required by law to set aside and accumulate in order to be able to discharge its obligation on the policy when it matures. *Ibid.* As further appears from the authorities, however, and as is indeed implicit in the very use of the term "net," as contradistinguished from "gross," insurance is not sold on the basis of "net premiums," but, rather, on the basis of such premiums plus "loading," the expense of writing the insurance. Thus, as stated in the *Fuller* case, *supra,* and emphasized by *Cooley, op. cit.,* p. 1628:

> The part of the premium intended to meet the cost of insurance, both current and future, is called the "net premium." It is the sum paid by each to furnish the stipulated protection for all. *But the policy holders must pay, not only for the cost of insurance, but also for the expense of management; so to the net premium is added a sum deemed sufficient to pay expenses and provide for contingencies. This is called the "loading." In this way, the policy holders pay the sum necessary for the cost of insurance and expense of management.* The amount of the net premium is calculated upon the basis of certain tables of mortality, and upon the as-

> sumption that the company will receive a certain rate of interest upon all its assets, and the amount of the loading is calculated upon a certain, assumed rate of expense. [Emphasis supplied.] [2]

Plainly, then, since insurance is sold on the basis of "net premiums" plus "loading" and the reserve on a policy represents the net premiums only and exclude the "loading," the reserve value principle satisfies neither the *Kawaguchi* "fair market value" standard nor the *Standard Oil Co.* v. *Southern Pacific Co.* requirement of "proper consideration of all relevant facts." It follows, there-

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[2] Cf. *Vance, op. cit.*, p. 48: "18. In cases of 'level premium' life insurance, the insurer must equate the sum payable under the terms of the policy with the present worth of all the premiums that may be received from the insured during the probable duration of his life, plus the proportionate part of the expense of management." Again, p. 49: "To this net premium—is added a certain amount of 'loading,' intended to cover the cost of administration, and to give a surplus from which any losses in excess of those anticipated may be paid." Finally, p. 52: "The premium charge, which will be *merely sufficient to discharge at maturity the obligation assumed to the insured under the policy,* is termed the 'net' premium; but, as has been said, the actuary must add to the net premium so fixed a sufficient amount, denominated 'loading,' to defray the expenses connected with the administration of the business of the company. The charge thus made, including this loading, is termed the 'office' premium." And see, also, *Id.*, pp. 51–52, 54, and 56, as to the meaning and function of the reserve fund.

See further, *Appleman, op. cit.*, p. 9: "To break down the principles of life insurance into more specific language, the insured pays what is known as a gross premium. This is, in turn, divided into two parts, the 'net premium' and the 'loading charge' or 'expense loading.' The net premium is set by law, the expense loading by the company's method of management. The net premium, in turn, is divided into two parts, the current year 'mortality element,' and the current year increase to 'policy reserve.' Since the reserve is built from the insured's own money, the company, therefore, uses the insured's own money plus interest accumulations thereon, to reduce his risk each year." Finally, for an indication of the "heavy initial expense incurred in writing new life insurance business incident to placing the business on the books of the company," see *Doty* v. *American National Insurance Co.*, 350 Mo. 192, 165 S. W. (2d) 862.

fore, that the reserve value principle, like claimant's alternatives, is not here applicable.[3]

Rejection of claimant's alternatives, including return of premiums with or without interest, and of the field's reserve value principle leaves for consideration the third of the three rules applied in the wrongful repudiation cases, namely, the "cost of comparable insurance" doctrine. That this principle satisfies the *Standard Oil Co.* v. *Southern Pacific Co., supra,* requirement of proper consideration of all relevant facts is obvious. Manifestly, the cost of comparable insurance necessarily reflects both elements involved in the situation, i. e., reserve value and "loading." As previously indicated, however, the problem here is one of property and not of contract. "Fair market value" is the test. *Kawaguchi, supra.* Necessarily, therefore, the question arises as to whether the "cost of comparable insurance" contract principle is susceptible of "fair market value" property adaptation. That this question can be answered in the affirmative is clearly shown by the cases involving taxation of single-premium insurance policies which have been the subject matter of gifts. See, *United States* v. *Ryerson, supra; Ryerson* v. *United States, supra; Parsons* v. *Commissioner,* 16 T. C. No. 34 (decided January 31, 1951). It is true, of course, that these cases involve fully paid-up

[3] That reserve value is not synonymous with fair market value and does not reflect all relevant valuation factors is recognized in Sec. 86.19 (i) of *Treasury Gift Tax Regulations 108,* which specifically states: "The value of a life insurance contract or of a contract for the payment of an annuity issued by a company regularly engaged in the selling of contracts of that character is established through the sale of the particular contract by the company, or through the sale by the company of comparable contracts. As valuation through sale of comparable contracts is not readily ascertainable when the gift is of a contract which has been in force for some time and on which further premium payments are to be made, *the value may be approximated,* unless because of the unusual nature of the contract such approximation is not reasonably close to the full value, by adding to the interpolated terminal reserve at the date of the gift the proportionate part of the gross premium last paid before the date of the gift which covers the period extending beyond that date." [Emphasis supplied.]

policies, whereas the policy in the instant case is one of continued payment. It is further true that there is a market practice for selling single-premium policies and that no such practice exists for the sale of policies already in force and on which further premium payments are to be made. That the principle applied in the gift tax cases is, nevertheless, likewise applicable here is manifest from the statement thereof in *Ryerson* v. *United States, supra,* specifically approved by the Supreme Court in *United States* v. *Ryerson, supra.* As stated by the District Court, 28 Fed. Supp. 267:

> The true value of a life insurance policy still in force can be ascertained only by the cost of duplicating that policy on the date of the gift.
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> The rule is the [same] price that any person of the same age, sex, and condition of health as the insured would have to pay for a similar policy in the same insurance company on the date the gift was made. This is a reasonable standard and one agreed upon by a willing buyer and a willing seller both of whom are acting without compulsion.

Substituting "loss" for "gift" in the above, the principle here applicable becomes transparently plain. The fair market value of claimant's policy on August 18, 1942, the time of loss, is the price which the insurer, Manufacturers Life Insurance Company of Toronto, Canada, would have charged him on that date for duplicating the property he then had, namely, a $3,000 endowment policty payable on January 18, 1961, or earlier in the event of claimant's death and at a semiannual premium rate of $71.85. Moreover, while such duplication cost would perforce be hypothetical due to the absence of any market practice for the sale of such a policy, the correct basis of computation is abundantly clear. Necessarily, it would be the reserve plus that portion of "loading" properly allocable thereto.

The "law" phase of the problem being thus resolved, there remains for consideration the evidential aspect. The matter requires but brief discussion. As already seen, the fair market value of claimant's policy at time of loss is its duplication cost on August 18, 1942, the date of cancellation. The record discloses, however, that claimant has adduced no evidence of such cost. The burden of proof is, of course, on claimant. Nevertheless, because, as in *New York Life Ins. Co.* v. *Statham et al, supra,* the matter is one of original impression, inquiry has been made of the insurer as to the charge it would have made claimant on August 18, 1942, the time of lapse, for the particular policy he had on that date were it then issuing it to him for the first time. In response to this inquiry, the insurer has advised that according to its calculations "the lump sum cost on August 18, 1942, for such a policy, on the assumption that Company rules and practice would have permitted its issue," would have been $184. It accordingly follows that the fair market value of claimant's policy at the time of loss must be found to have been in this amount.

In light of the above, it is clear that claimant is entitled to receive the sum of $184 as compensation for loss of personal property as a reasonable and natural consequence of his evacuation. In passing, it is appropriate to observe that inquiry discloses that information as to the legal reserve on an insurance policy is readily obtainable from insurance companies. Duplication cost, on the other hand, is not so easily available, requiring special computation. In view of this fact, practice may prove that claimants may not be able to provide the duplication cost of their insurance policies and may adduce evidence only as to reserve value. As previously indicated, the burden of proof is upon the claimant. Moreover, he must maintain that burden to the full extent of his demand. Hence, where a claimant is unable to obtain the necessary evidence as to duplication cost from the insurer and submits evidence of reserve value only, he will be deemed to have amended his claim downward and to be seeking the latter amount. Also it should be noted that to assure accuracy of application of the principle enunciated above, namely, the reserve plus properly allocable "loading," the evidence of claimant's proceeding on the duplication basis must set forth the respective elements of computaton involved, i. e., the amount of the reserve, on the one hand, and of the allocated "loading," on the other.