court house, asylum, or any other public structure. Likewise, such specifications shall be supplemented by full and complete drawings or models in all other cases where the same are needful or desirable to completely and definitely define the work so proposed to be undertaken. Upon the filing of said specifications and drawings in the office of said auditor, said board shall cause a brief notice to be published once time in each of two leading newspapers of general circulation, published in the county, if there be such, representing respectively the two political parties casting the highest number of votes in such county at the last preceding general election, informing the public of the general nature of the proposed undertaking, and of the fact that drawings and specifications are on file at such office, and calling for sealed proposals for such work by a day fixed in said publication, but not earlier than two weeks after said publications. In all cases where the amount involved exceeds two thousand ($2,000) dollars, such advertisement shall be published twice in each of such newspapers, and the time for receiving bids shall be not earlier than four weeks after the first of such publications. Further publications may also be made when deemed for the public interest.” (Our italics.)

INSURANCE COMMISSIONER: Reinsurance contract—liability thereunder of company to policyholders.

May 5, 1933.

Hon. Harry E. McClain,
Commissioner of Insurance,
Indianapolis, Indiana.

Dear Sir:
I have before me your letter of April 17th, which reads as follows:

“The Fort Dearborn Insurance Company, a fire and casualty company, licensed to do business in the State of Indiana, under date of December 31, 1932, reinsured all outstanding policies in the State of Indiana with the Central Mutual Insurance Company of Chicago, also licensed to do business in the State of Indiana.
Copy of this reinsurance agreement is attached hereto for your full information.

"Due to the failure of the Fort Dearborn to make the payments to the Central Mutual on such reinsurance contract and in accordance with the terms thereof the Central Mutual on the 5th day of April proceeded to send notices of cancellation to all policyholders, formerly insured in the Fort Dearborn, which policies the Central Mutual had assumed as of December 31, 1932. These notices of cancellation did not provide for the return of the unexpired portion of the premium to the policyholder. Policy obligation provides that where cancellation is made there shall be a tender of the unexpired portion of the premium or same will be refunded upon demand. This tender of the return premium has been refused by the Central Mutual.

"May we respectfully request an opinion upon the attached contract as to whether or not under the terms of the contract the Central Mutual assumed the liability on policies issued in Indiana by the Fort Dearborn to the extent that they are liable for the return premium on policies canceled by them prior to the expiration term of such policy."

It is a general rule of law that in the absence of statute a reinsurer is liable to the policyholder only when there were promises, acts or agreements on its part with knowledge of which, and in consideration of which, the policyholder made a payment or promise, or performed some act, or relinquished some right by which a contract, express or implied, was established between the policyholder and the reinsurer; or by which the policyholder agreed to a novation—a substitution of the reinsurer for the original insurer.

The liability of the Central Mutual Insurance Company, if any, to the policyholder must be on the theory of a novation, or else upon the theory of a new and independent contract created between itself and the original insured. To constitute a novation, there must be an acceptance or consent by the insured; and to constitute a new contract there must appear to have been a meeting of the minds of the reinsuring company and the policyholder sufficient to constitute an agreement. Whether or not either of these things occurred de-
pends upon the facts respecting each individual policy of the Fort Dearborn company and the relation established thereon between the Central Mutual and the policyholder.

A novation is a form of assignment in which, by the consent of all the parties, a new contract is substituted for an existing contract. There must be an agreement between the parties that the original debtor should be released and the assignee accepted in his stead. (46 C. J., Sec. 6; In re Bank, 268 Fed. 1012; Stowell v. Gram, 69 N. E. (Ill.) 342.)

There are four essentials to a novation, as follows:

(1) A previous valid obligation.
(2) The agreement of all the parties to the new contract.
(3) The extinguishment of the old contract.
(4) The validity of the new one.

(Cox v. Baltimore, etc., R. Co., 180 Ind. 495, and cases cited.)

The novation, if any, in the case presented by your inquiry was one by which a new debtor was substituted for an old one. (Kelso v. Fleming, 104 Ind. 180, 182.) As in the case of all agreements, the contract of novation is the result of, and springs from, an offer and acceptance, and hence is subject to be defeated by a withdrawal of the offer or a modification thereof before acceptance. (Durham v. Bischof, 47 Ind. 211.) Whether or not, in each case, the cancellation by the Central Mutual of the contract between itself and the Fort Dearborn was effected before acceptance of its terms by the policyholder, is largely a question of fact in each particular case.

If the reserve which the policyholders had each helped to create and in which each had an interest had all been actually transferred and paid to the Central Mutual by the Fort Dearborn, in accordance with the terms of their reinsurance contract, then probably the Central Mutual would be liable to the policyholders on the theory of the reserve being a trust fund for their benefit, or upon the theory of conversion. (Fed. Life Ins. Co. v. Kerr, 173 Ind. 613.) But it appears that that portion of the reserve which had actually been paid to the Central Mutual under the reinsurance contract up to the time of the purported cancellation of such contract, and more than such amount, was actually earned by the Central Mutual by their assumption of liability during the period between execution of the contract and cancellation thereof. The balance of
the reserve, representing unearned premiums proportionate to the terms of the respective policies remaining after the purported cancellation between the two insurance companies, I assume has never been turned over to the Central Mutual and presumably still remains in the custody of Fort Dearborn. In fact, the cancellation of the contract of reinsurance purportedly was based upon the failure of the Fort Dearborn to pay over this portion of the reserve in accordance with the terms of such contract.

A statute prescribing the terms by which one insurance company may reinsure and take over the business of another company will be considered as entering into and forming a part of the contract of reinsurance. (Fed. Life Ins. Co. v. Kerr, 173 Ind. 613.) But here the reinsurance was not effected pursuant to the authority of any statute of the State of Indiana. Our only statutes pertinent to this subject are sections 9155-9157, inclusive. Unfortunately, they relate only to domestic insurance companies, authorizing such companies to reinsure in joint-stock insurance companies authorized to do business in this state. Clearly, these statutes are not applicable to the case at bar.

"In the absence of a statute requiring a reinsuring company to assume all the obligations and conditions contained in the policy of the company reinsured, and in the absence of such a provision in the contract of reinsurance, we know of no authority holding that a reinsuring company is bound by the provisions of the policies issued by the company whose policies are reinsured. The measure of a reinsuring company's liability under such circumstances is measured by the contract of reinsurance and the policies thereafter issued by it." (Our italics.) Western Life Indemnity Co. v. Bartlett, 84 Ind. App. 589, 610.

If a contract of reinsurance is incomplete owing to failure of consideration, the general rule is that the original policyholder has no right of action against the reinsurer. (33 C. J., Sec. 736; Hoffman v. North British, etc., Ins. Co., 70 N. Y. S. 106.) And in the instant case, the Fort Dearborn Company failed to make its payments provided for in the contract, and the Central Mutual acted under a clause of the contract expressly authorizing cancellation of the same.
It has been held that a company that takes over the business of another, in consideration of payments to be made, and thereby renders the reinsured company unable to carry out its contracts, cannot relieve itself from liability to the original policyholders by avoiding its contract because of the reinsured company's failure to pay subsequent installments of the consideration. (33 C. J., Sec. 736; Rushe v. Traders Fire Ins. Co., 111 Tenn. 405, 102 Am. S. R. 790.) But in the case presented by your question, that portion of the business and assets of the Fort Dearborn represented by the reserve created by premiums unearned as of the date of cancellation of the reinsurance agreement, apparently has not been turned over to the Central Mutual. This being true, it seems inconceivable that the Central Mutual has "rendered the reinsured company unable to carry out its contracts", or that it has reduced the ability of such insurer below that which existed prior to the execution of the reinsurance agreement.

Of course, if in any individual case the policyholder has paid premiums under the original policy to the reinsurer, or has in fact lost or relinquished any material right under the original policy in reliance upon a representation made to him by the reinsurer or his agents that the reinsuring company has assumed the risk unqualifiedly, then there is a sufficient consideration to support a contract of insurance between the policyholder and the reinsurer, based upon the policy. (13 C. J., Sec. 736.)

This was a contract executed without the knowledge or consent of the policyholder, and to which he was not a party. Such a contract cannot bind the policyholder (Fed. Life Ins. Co. v. Barnett, Admr., 71 App. 613), nor could it deprive him of any of his vested contract rights; similarly, neither can it increase his rights unless it is shown that a contract, either express or implied, was created between himself and the reinsurer.

The case of Fed. Life Ins. Co. v. Barnett, Admr., supra, is authority for the proposition that where a policy of reinsurance is not issued to the assured, the reinsurer is liable to the assured, if at all, upon the terms of the reinsurance contract between the reinsurer and the original insurer. The liability, if any, is not on the original policy, but on the promise and agreement to assume the risk. The court makes
the statement that the general rule is that the liability of the reinsurer is solely to the insured; but that it is competent for the reinsurer to make the reinsurance contract inure directly to the benefit of the party originally insured, and in jurisdictions where a third party is allowed to maintain an action on a contract made for his benefit he may, in such case, recover directly from the reinsurer.

The Fort Dearborn Company could not cancel its policy liability without tender of the return of the unearned portion of the premium. No more could the Central Mutual cancel its liability on a policy issued by the Fort Dearborn without such tender, if the Central Mutual had in fact assumed such liability by novation or subrogation or otherwise. And the mere notice of cancellation without tender of the unearned premium, even though intended to effect a cancellation, nevertheless would not operate as a cancellation unless so treated by the policyholder.

In conclusion, unless the policyholder has assented to the cancellation, liability on the policy, and liability for the return of unearned premium, would still attach, either to the Central Mutual or to the Fort Dearborn. Which company would be liable depends upon the facts in each particular case. But it is sufficient that one or the other of the companies must tender a return of unearned premium before the purported cancellation can be effective.

ADJUTANT GENERAL: Armory board—authority and jurisdiction in its duties in connection with maintenance and operation of Indianapolis armory.

May 6, 1933.

Hon. Elmer F. Straub,
Adjutant General,
Indianapolis, Indiana.

Dear Sir:

I have before me a letter addressed to you by the secretary of the Indianapolis armory board under date of April 25, which you have referred to this office with a request for an official opinion regarding the matters therein contained.

The questions set out by said letter are as follows: