CASE NOTE: KOSMOPOULOS V CONSTITUTION INSURANCE CO OF CANADA

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[1] Introduction

The paper gives a brief introduction to the concept of insurable interest. It further dwells into the issue regarding whether shareholder’s have an insurable interest in the corporations property. The purpose of this paper, however, is to illustrate the fact that shareholders do have an insurable interest, regardless of the fact that the company is a separate legal entity. The paper would further analyse the contentious judgement delivered in Kosmopoulos v Constitution Insurance Co of Canada. ¹The case pertains to the ambit and scope of the concept of insurable interest and comprises one of the few instances where the Court has had the opportunity to grant shareholders the right to insure corporations assets. Additionally, the paper would provide an in-depth understanding of whether a bailee possess an insurable interest.


According to the facts mentioned in Kosmopoulos v Constitution Insurance Co of Canada, Mr. Kosmopoulos, the petitioner, had incorporated his leather goods business and became the sole shareholder and director of the company. However it is imperative to note that he leased the company office under his own name since he originally ran the business as a sole proprietor. Furthermore, the fire insurance policy taken for the office premises showed the insured as being the sole proprietor even though the insurance agency was well aware of the fact that the business was being carried on by the incorporated company. Subsequently, a fire in a neighbouring lot damaged his office, however, the insurance company refused to cover his damages on the grounds that Mr. Kosmopoulos lacked insurable interest.

Whether shareholders have an insurable interest in the corporation’s property.

It is settled law that the insured must have an insurable interest in the property at the time of the loss in order to recover on such an insurance policy. Furthermore, an individual is said to have an insurable interest in the subject matter insured if he has a relationship with it, and will derive monetary benefit or advantage from its preservation, and will suffer monetary loss from its destruction, termination, or injury as a result of the event insured against. It makes no difference whether the individual has a title to, a lien on, or ownership of the property if he suffers a loss as a result of its destruction.

The foregoing rules would appear to be broad enough to include the interest of a shareholder in the property held by his corporation. Because of his pecuniary relationship with respect to this property, it does not seem that the concept of a separate, title-holding corporate entity should preclude his having an insurable interest. Not only will the destruction of the corporation's property adversely affect the value of his holding in the company as such, but it will materially harm the prospects of a return on his investment through dividends. Moreover, because the total value of the corporate property would be diminished, his right to share in the net assets upon a subsequent dissolution would be impaired. It is to be recognized, therefore, that a shareholder has a direct and pecuniary interest in the preservation of the property of his corporation and consequently may legitimately require a means of indemnification with respect to his investment.

Nonetheless it is imperative to note that a stockholder, in a corporation, has no legal or equitable title to the organization’s assets that he may convert to a legal title. The company is the legal owner and can act with corporate property as if it were its own, subject to the charter's constraints. However, investors of a corporation have equitable rights of a monetary kind arising from their position as stockholders, which may be harmed by the loss of the corporate

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property in this case. The goal of business companies is to create money by exercising corporate franchises, and profits are distributed to stockholders according to their different interests. The right to "share in the profits" is the incentive for people to become shareholders. Similarly, when a corporation is wound up, the assets are divided among the investors after debts are paid. It is obvious that the destruction of the corporation may jeopardise both these stockholder rights, namely, the right to dividends and the right to partake in the eventual distribution of the corporation's assets.\(^5\)

It appears that the shareholder, as the sole natural person with a significant stake in the preservation of the corporation's property, should be permitted to safeguard that interest through the use of insurance. The above analysis clearly illustrates a shareholder's legitimate interest in his corporation's physical assets. With good cause, he may want to protect his investment against unforeseen destruction of his company's non-human, wealth-producing components. The limiting of reimbursement to the real loss he suffers will also help to eliminate what would otherwise appear to be the insurance's speculative nature.

According to the facts presented, Mr. Kosmopoulos was the sole shareholder in Kosmopoulos Leather Goods Limited. Furthermore, he used to conduct the company’s business in a leased premises, wherein the company’s assets were also stored. In this scenario, the leased premises and the assets were the mechanism through which profits were to be made, and their loss would, in the normal run of things, reduce the company’s ability to pay dividends and further reduce the stock value.\(^6\) From the analysis presented above we can reasonably conclude that since Mr. Kosmopoulos was the sole shareholder of the company, his relationship with the property led to the creation of a reasonable expectation of benefit from its ongoing existence, or loss from its destruction. Hence as a shareholder he had insurable interest in the property.

Additionally, it is imperative to note that in the present scenario, the insurance company was well aware of the fact that the business was being carried out by the incorporated company while the leased premises were in the name of Mr. Kosmopoulos. However, they raised no

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objection to him acquiring a means of indemnification for the probable loss or destruction of the corporation's non-human producing components. It would hence be irrational to insert the fiction of the corporate entity to prohibit him from claiming insurance. It is further argued that whether the shareholder wishes to cover his corporation's tangible property or not, he has a sufficiently valued interest in the preservation of the subject matter of his insurance. He not only has a monetary interest in the value of his stock, but he also has dual proprietary rights in his business, including the right to a share of declared dividends and the right to a portion of the company's net assets upon dissolution. Clearly, such insurance is not to be dismissed as a mere gamble. 7

The fee-simple title does not need to be vested in the insured to generate an insurable interest. It is sufficient that he possesses a direct, monetary interest that is vulnerable to destruction and is entitled to protection. 8 The destruction of the property unquestionably reduces the value of plaintiff's shares. He had a vested interest in the property's preservation, and it was an insurable interest. If the property was the corporation's entire property, the property's destruction effectively wiped out the value of his stock.

In the present case, the Court rightfully held that the shareholders have an insurable interest in the corporations property, in turn, overruling the restrictive definition of insurance laid down in *Macaura*, 9 which prevented individuals such as Mr. Kosmopoulos, who have suffered genuine pecuniary loss from obtaining indemnification for their losses.

[4] Whether bailee’s have an insurable interest.

Bailment is defined as the act of handing over commodities by the owner (bailor) to another (bailee) on the condition that they would be returned to the bailor, or according to his orders, as soon as the purpose for which they were bailed is answered10. As a result, the bailee is simply the individual who has been entrusted with the possession of items by the owner (the bailor), who retains title or ownership. A bailee does not own the items, but because he has custody of them, he may be legally liable for their safekeeping. As a result, bailees frequently seek insurance coverage.11

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8 William T. Vukowich, Insurable Interest: When It Must Exist in Property and Life Insurance, 7 WILLAMETTE L.J. 1 (1971).
In the present scenario, the Court dismissed the argument presented by the counsel for the respondents that since Mr. Kosmopoulos was in possession and control of the stock and merchandise for the corporation and was further responsible for its safekeeping he would be deemed a bailee of the assets for the corporation, hence giving him insurable interest.

The Court claimed that there appeared no evidence of an express bailment, however, it failed to take into consideration the fact that bailment can be implied. It is imperative to note that while the Kosmopoulos Leather Goods Limited owned the assets of the company, it was Mr. Kosmopoulos who possessed and utilized the goods as well as the leased premises to conduct his business. Furthermore, in *Lotan v. Cross*, the Court held that the servant of the bailor can be deemed a gratuitous bailee. In the present scenario, Since Mr. Kosmopoulos was the director and senior employee of the company, who was further in possession of the leased premises and the company assets stored within it, we can reasonably conclude that he was a gratuitous bailee.

Hence the question that arises is whether the bailee has insurable interest to insure the goods. In *Marks v. Hamilton*, it was determined that a person in possession as apparent owner, who is liable to the actual owners and may be brought to account for property, had insurable interest. This is because possessory title is a good root of title under common law, good against everyone save the legal owner, and therefore possession combined with a legal responsibility, such as a bailment, would result in insurable interest. As a result, even a gratuitous bailee would have insurable interest due to the personal liability that may emerge from his responsibility for the commodities and related need to account to the bailor.

When a bailee arranges for the insurance of goods, the law presumes that he is doing it as an agent for and on behalf of his principal, the bailor. However, the bailee does not need to have real authorization from the bailor to insure the items "without the owner's commands and even without telling him that such a policy existed." In line with agency principles, the bailee can get insurance coverage for a "disclosed" or "undisclosed" principal.

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14 Holt CJ in *Coggs v Barnard*, [1703] 2 Ld Raym 909.
Thus, in the present scenario, even if the company was not aware or did not consent to the fact that Mr. Kosmopoulos insured the leased premises, the same would not be deemed invalid.

However, the facts of the case are silent regarding whether Mr. Kosmopoulos was responsible for the loss of goods, hence the question here is whether a bailee who is not responsible for the loss of the goods has an interest that entitles him to claim insurance. The same was answered in Waters v. Monarch Fire and Life Assurance Co, wherein it was held that bailees could insure the items committed to them and still recover the entire worth of the damage in the case of loss, regardless of responsibility.\(^\text{16}\) Hence, bailee’s do possess insurable interest.

[5] Conclusion

In the case of Kosmopoulos v Constitution Insurance Co of Canada, the Court held that Mr. Kosmopoulos as sole shareholder of the company, was placed in a position with respect to the assets wherein benefit from their existence and prejudice from its destruction and hence had an insurable interest and is further entitled to recover the losses insured. While the Court refused to pierce the corporate veil, the judgement is instrumental for shareholders since it overruled the law laid down in Macaura, which offered an extremely restrictive definition of insurable interest. Nonetheless, it is imperative to note that the Court erred in considering whether there existed an implied bailment between Mr. Kosmopoulos and Kosmopoulos v Constitution Insurance Co of Canada.

\(^{16}\) Ibid