paying the state $100,000, sought to have the receiver of the bank allow it to
deduct the $15,000 represented by the warrant, and to prove an unsecured
claim for the balance. Although the receiver would only accept proof of the
$100,000 as an unsecured claim, the Circuit Court of Appeals for the Fifth Cir-
cuit subsequently held that the surety was entitled to have the receiver transfer
and deliver to it the auditor’s warrant for $15,000.36 The reason why the surety
got the $15,000 warrant was not that he was subrogated to the rights of the
principal, for such a procedure would have been unfair to other creditors of the
insolvent bank who were entitled to their pro rata share of the bank’s assets.
The surety got the warrant because he should never have been required to pay
the $15,000 which it represented. When the bank became insolvent, it owed the
state of Mississippi $100,000; the state owed the bank $15,000 on the warrant.
Since the function of the surety is to protect the creditor from loss in the event
that the principal does not perform, it would seem that the surety’s duty to pay
the state might reasonably be limited to $85,000. The Circuit Court of Appeals
explained that “. . . the debts existing between the bank and the state were
mutual, notwithstanding that the indebtedness represented by the warrant was
incurred by the hospital commission. The right of set off, even though it did not
exist at law, will be recognized and enforced in equity, in view of the bank’s in-
solvency.”37
It is thus apparent that in some cases where subrogation of the surety to the
rights of the principal will be unfair to other creditors of the principal, equitable
set-off of the principal’s claims against the creditor may be used by the surety.
While the same result may be reached in specific cases, the theories of the two
means are diverse. Where one line of reasoning will appeal to one’s sense of fair-
ness, the other may not.
In the case which gave rise to this discussion, the proposition announced—
that of enabling the surety to be subrogated to the rights of his principal against
third parties—would be needed most when the contractor becomes insolvent.
Inasmuch as application of the proposition in such a situation appears unfair to
other creditors of the contractor, and inasmuch as there is no justification for
the result on the basis of equitable set-off, and in view of the fact that the propo-
sition appears to be without precedent, there seems little justification for the
rule announced in this case.

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**EFFECT OF INSURANCE BINDER RECEIPT ON APPLICANT’S INTERIM COVERAGE**

The plaintiff sued to recover on a contract for life insurance. Liability of the
insurance company turned on the construction of these words in the application:
“if the Company is satisfied that on the date of the completion of Part B of this
application I was insurable . . . . and if this application, including said Part B,

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36 Ibid., at 840.
37 Ibid.
is, prior to my death, approved by the Company at its Home Office, the insurance applied for shall be in force as of the date of completion of said Part B.” At the time of signing the application on August 3, the applicant paid the first premium and the defendant’s agent gave him a receipt, both the application and the receipt being forms prepared by the defendant for use by its solicitors. From August 3 to August 26, the “Home Office” ordered a series of medical examinations and investigations, all of which were favorable to insurability. On August 26 one of the doctors of the company’s medical department approved the application “from a medical standpoint.” On the same day the “Home Office” received news of the applicant’s death at the hands of an assailant, and the application was never finally approved. The trial judge found that the applicant and the defendant’s agent intended that the former should be covered from the date of the completion of Part B, and that if the deceased had lived, approval would have been given. On appeal to the Second Circuit Court of Appeals it was held that the binder clause was ambiguous; according to well-settled principles, the ambiguity was resolved against the insurance company. Judge Learned Hand believed that an ordinary man would understand the clause as putting the policy into effect on the completion of Part B, and refused to adopt the interpretation indicated by strict construction of the language. In a concurring opinion, Judge Clark, citing a law review comment, urged that the effect of such binder agreements should not turn on a possible finding of ambiguity but on the inequities which might result from the unique nature of the transaction and the relationship of the parties. Gaunt v. John Hancock Mutual Life Ins. Co.

Binder receipts are given to the applicant after payment of the first premium, which insurance companies attempt to collect before issuance of the policy in order to obtain some measure of protection against the applicant’s arbitrary withdrawal of his offer during the company’s expensive investigation of his insurability. Advance collection affords twofold protection: the applicant usually feels contractually obliged to perform, and, should he withdraw his application, it is unlikely that he would resort to a law suit to recover the relatively small sum paid.


2 Operation of Binding Receipts in Life Insurance, 44 Yale L.J. 1223 (1935). In that article the problem of binder receipts was carefully explored, and the prediction was then made that binders of the type in the Gaunt case would fall into disuse. During the past twelve years, however, few important changes in the use or judicial treatment of binder receipts have appeared.

3 160 F. 2d 599 (C.C.A. 2d, 1947), cert. den. 37 S.Ct. 1736 (1947). The case is noteworthy in that there was no Connecticut case clearly in point. Under the doctrine of Erie R. Co. v. Tompkins, 304 U.S. 64 (1938), the court faced the problem of finding the local law, and Judge Clark’s opinion seems to be directed at improving the local law as well. Hence, Judge Clark did not feel justified in abdicating the judicial role for that of “ventriloquist’s dummy” as to state law.
Although insurance companies are reluctant to give the applicant coverage before "Home Office" approval, they feel that in relating the effective date of the policy back to the date of application they are giving the applicant certain advantages which he would not enjoy if the effective date were the date of final approval. The insurer contends that these advantages are expressly or impliedly embodied within the restrictive terms of the binder receipts, and it is there that most courts have searched for the intent of the contracting parties. In doing so they have anachronistically regarded insurance contracts as typical bargained-for agreements, complete in themselves as integrated writings. It is apparent, however, that the insurance contract is not the result of individual bargaining between the applicant and the insurance company. The printed contract forms are prepared in advance by company lawyers, who devise clauses which lead the applicant to believe that he is covered from the date of application or medical examination and payment of the first premium. An applicant cannot bargain as to the terms of one of these mass-produced forms; he must "take it or leave it," usually with no assistance in interpreting the contract except the information given him by an agent.

The inevitable inequities resulting from the nature of this transaction have prompted some courts to afford the applicant protection by exercise of the judicial prerogative of interpretation. The binder has frequently been found ambiguous and construed against the insurer. Cases cited supra note 5; 3 Williston, Contracts §§ 604, 606, 631 (rev. ed., 1936); Rest., Contracts §§ 228, 230 (1932).

4 "The defendant suggests six possible 'advantages' to the insured which will satisfy the phrase, 'the insurance ... will be in force,' (1) The policy would sooner become incontestable. (2) It would earlier reach maturity, with a corresponding acceleration of dividends and cash surrender. (3) It would cover the period after 'approval' and before 'issue.' (4) If the insured became uninsurable between 'completion' and 'approval' it would still cover the risk. (5) If the insured's birthday was between 'completion' and 'approval,' the premium would be computed at a lower rate. (6) When the policy covers disability, the coverage dates from 'completion.'" Gaunt v. John Hancock Mutual Life Ins. Co., 160 F. 2d 599, 601 (C.C.A. 2d, 1947).


7 "The clause seems to be a mere trick on the part of the insurance company to deceive the applicants into the belief that they have temporary insurance." Francis v. Mutual Life Ins. Co., 55 Ore. 285, 292, 106 Pac. 323, 327 (1910).

8 The representations of the agent usually have no effect on the terms of the binder agreement. Londo v. Integrity Mutual Ins. Co. 249 Wis. 281, 24 N.W. 2d 628 (1944); Braman v. Mutual Life Ins. Co., 73 F. 2d 391 (C.C.A. 8th, 1934); Chamberlain v. Prudential Ins. Co., 109 Wis. 4, 85 N.W. 128 (1901).

of the agent or pamphlet material are invoked as aids in resolving the ambiguity. The desire to find ambiguity leads to uncertainty as to the validity of any binder containing the condition precedent of "Home Office" approval, and encourages, when the ambiguity is construed against the insurer, renewed efforts of the insurers' lawyers to find the magic combination of words. Although satisfactory results may be obtained in individual cases by use of the ambiguity technique, the uncertainties fostered by this type of construction render it an undesirable judicial device. Whether an ambiguity exists, in fact, is the paramount question confronting the courts in dealing with these cases, and the ambiguities are frequently discovered by devious means. Indeed, in the Gaunt case, Judge Learned Hand seems to be enlarging the area in which ambiguity may be found by finding it where the words used, considered in the full context of the negotiations, would not be understood by a layman to have the meaning attributed to them by insurance underwriters. A willingness to base a finding of ambiguity on terms other than those found within the express words of the binder agreement itself seems to be a fair recognition of the inequitable positions of the parties and makes it appear likely that Judge Hand and Judge Clark were approaching the problem with similar premises.

The great amount of litigation involving binder receipts points up the fact that the methods of dealing with contracts of adhesion have been largely unsatisfactory. A satisfactory solution can be reached only by the open recogni-


12To an insurance underwriter the meaning of the phrase "as of the date of the completion of Part B" might be quite clear. But, as indicated by Judge Hand, "the application was not to be submitted to underwriters; it was to go to persons utterly unacquainted with the niceties of life insurance, who would read it colloquially. It is the understanding of such persons that counts; and not one in a hundred would suppose that he would be covered, not 'as of the date of completion of Part B,' as the defendant promised, but only as of the date of approval." Gaunt v. John Hancock Mut. Life Ins. Co., 160 F. 2d 599, 601 (C.C.A. 2d, 1947).

13"The contract is drawn up by the insurer and the insured, who merely 'adheres' to it, has little choice as to its terms." Patterson, The Delivery of a Life Insurance Policy, 33 Harv. L. Rev. 198, 222 (1919).

14"All the technical doctrines resorted to by the courts in the insurance cases denying liability are in the last analysis but rationalizations of the court's emotional desire to preserve freedom of contract." Kessler, Contracts of Adhesion—Some Thoughts About Freedom of Contract, 43 Col. L. Rev. 629, 639 (1943).
tion that the courts must adapt "to the modern form-pad bargain . . . . older rules based on the individualized writings of an earlier day . . . . Where bargaining is absent in fact, the conditions and clauses to be read into a bargain are not those which happen to be printed on the unread paper, but are those which a sane man might reasonably expect to find on that paper." The sensible intentions and expectations of the negotiating parties themselves, and not the unilaterally-drawn wording of the binder and policy, should be controlling. The applicant who pays his premium expects to be protected immediately, and is customarily led to believe so by the agent. Since the effective date is said to be the date of the application once "Home Office" approval is given, but the applicant is not covered until the application is approved, the applicant is actually paying for a period during which he may not be covered. Although a literal interpretation of the standardized contract form may yield this result, it cannot be said that the bonus received by the insurance company from the applicant under his mistaken belief that he was receiving immediate and complete protection represents freedom of contract.

Where a binder of the type in the principal case is used, the question of whether the insurance was in effect might arise i) where the applicant dies or suffers some other change of condition immediately after the application is submitted, 2) where there is a change of condition during the period of medical and financial investigation, 3) where there is a change of condition before final approval, but after the completion of the investigation, and 4) where there is a change of condition after approval.

A recognition of the inequity of this type of contract of adhesion will enable courts more easily to conclude that the agreement between the insurer and the applicant contemplated temporary coverage, pending final action by the insurer. This idea has been used to good advantage in a few cases. Duncan v. John Hancock Mutual Life Ins. Co., 137 Ohio St. 441, 31 N.E. 2d 88 (1940); Hart v. Travelers' Ins. Co., 236 App. Div. 309, 258 N.Y. Supp. 711 (1932), aff'd 261 N.Y. 563, 185 N.E. 739 (1933); Albers v. Security Mutual Life Ins. Co., 41 S.D. 270, 170 N.W. 159 (1918); Patterson, Essentials of Insurance Law § 20, at 74 (1935).


"Satisfaction" means an honest judgment based on facts sufficient "to satisfy a reasonable man in the promisor's position." Rest., Contracts § 265 (1932); 1 Williston, Contracts § 44 (rev. ed., 1936); 3 ibid., at § 675A.
sumption of coverage might have the salutary effect of causing insurance companies to clarify the provisions as to the effective date; i.e., the agent would be instructed to be certain that applicants understand the effective date to be after the medical examination. The applicant would be covered in situations 3 and 4 if the agreed effective date were either the date of the application and premium payment or the date of satisfactory completion of the medical examination.

As Judge Clark points out in his concurring opinion in the Gaunt case, "a result placed not squarely upon inequity, but upon interpretation, seems sure to produce continuing uncertainty in the law of insurance contracts." His position points the way to more expeditious handling of a perplexing problem.

EFFECT OF ROBINSON-PATMAN ACT ON QUANTITY DISCOUNTS

In a proceeding initiated under the Robinson-Patman amendment to Section 2 of the Clayton Act, the Federal Trade Commission charged the Morton Salt Company with illegal discriminations in price between different customers. The company had established openly announced quantity and cumulative discounts: 1) a quantity discount of $.10 per case from the list price of $1.60 granted to all customers who purchased Blue Package Table Salt in carload lots; 2) an additional $.10 per case cumulative rebate to customers purchasing 5,000–50,000 cases of Blue Package salt in any consecutive 12-month period, or a $.15 rebate to purchasers of more than 50,000 cases; 3) a 5 per cent cumulative rebate on all table salt other than the Blue Package varieties to customers whose total salt purchases during a 12-month period exceeded $50,000. After a full hearing, the Commission ordered the company to cease and desist from discriminating in price between customers. On petition for review, the Seventh Circuit Court of Appeals set aside this order and dismissed the complaint. Morton Salt Co. v. FTC.

A major weakness of the Clayton Act's prohibition of price discrimination prior to 1936 was the express exception of quantity discounts from the statute's sanctions, even though such discounts might reflect a windfall for favored large

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18 160 F. 2d 599, 603 (C.C.A. 2d, 1947).
2 Quantity discounts are granted on individual orders exceeding the base quantity, so that they may normally be determined when the order is placed. Cumulative discounts are based on the total volume of a buyer's purchases over a given period of time, and are therefore usually given in the form of retroactive rebates.
3 39 F.T.C. 35 (1944).
4 162 F. 2d 949 (C.C.A. 7th, 1947), cert. granted 68 S. Ct. 355(1948), noted in Quantity Discounts Under the Robinson-Patman Act, 42 Ill. L. Rev. 556 (1947); 60 Harv. L. Rev. 1167 (1947).