

## MISREPRESENTATION AND RESCISSION OF INSURANCE CONTRACTS

(FORC Journal: Vol. 18 Edition 3 - Fall 2007)

Angela Ables, Esq.  
(405) 272-9221

In today's hyper-litigious society, few insurers have escaped the challenge of bad faith litigation. Our insurance clients oftentimes find themselves facing allegations of bad faith and deceit relating to the denial of a claim for benefits made within the contestable period. Many states, Oklahoma included, have statutes relating to what constitutes "misrepresentation" of information contained in an application by a potential insured. Oklahoma's statute, 36 O.S. § 3609, allows an insurance company to avoid payment on a life insurance claim if the policy was issued based upon a material misrepresentation of a health condition by the insured.

The pertinent portion of Oklahoma's "misrepresentation" statute states:

A. All statements and descriptions in any application for an insurance policy or in negotiations therefore, by or on behalf of the insured, shall be deemed to be representations and not warranties. Misrepresentations, omissions, concealment of facts, and incorrect statements shall not prevent a recovery under the policy unless:

1. Fraudulent; or
2. Material either to the acceptance of the risk, or to the hazard assumed by the insurer; or
3. The insurer in good faith would either not have issued the policy, or would not have issued a policy in as large an amount, or would not have provided coverage with respect to the hazard resulting in the loss, if the true facts had been made known to the insurer as required either by the application for the policy or otherwise.

This seemingly straightforward and innocuous statute has been the subject of a great deal of discussion and interpretation by Oklahoma courts in recent years, particularly in the life insurance area. Insurers should be mindful of the body of law which has resulted from courts interpreting this statute before refusing to pay benefits to an Oklahoma claimant based on misrepresentation in the application.

### **History of the Misrepresentation Defense and the Development of the "Intent to Deceive" Standard in Oklahoma**

Prior to the enactment of 36 O.S. § 3609 in 1957, Oklahoma courts generally found that an insured's statements in his application for insurance had to be construed as "representations and not warranties." <sup>1</sup> The Oklahoma Supreme Court held that the untruth of any material representation relied on by the insurance company in making the contract would avoid the contract, wholly irrespective of the insured's intent, whether innocent or fraudulent, with which such misrepresentation was made. <sup>2</sup>

After the enactment of 36 O.S. § 3609, the first Oklahoma Supreme Court opinion dealing with the subject of an insurer avoiding payment of benefits to an insured based on a material misrepresentation was the 1965 case of *Massachusetts Mutual Life Insurance Co. v. Allen*. <sup>3</sup> According to the court, under 36 O.S. § 3609,

A 'misrepresentation' in insurance is a statement as a fact of something which is untrue, and which the insured states with the knowledge that it is untrue and *with an intent to deceive*, or which he states positively as true without knowing it to be true, and which has a tendency to

## FEDERATION OF REGULATORY COUNSEL, INC.

mislead, where such fact in either case is material to the risk. 4

In its syllabus in *Massachusetts Mutual* concerning a discussion of the definitions of "omission" and "incorrect statement" the Court stated as follows:

An "omission" in negotiations for a life insurance policy under 36 O.S. 1961 § 3609, is an *intentional omission* to disclose a fact or condition which is material to the acceptance of the risk or the hazard assumed....(emphasis supplied).

An "incorrect statement" in negotiations for a life insurance policy under 36 O.S. 1961, § 3609, is a statement of fact which is untrue and known to be untrue, or so carelessly made that an *intent to deceive may be inferred*. 5

The Oklahoma Supreme Court's interpretation of 36 O.S. § 3609, as enunciated in *Massachusetts Mutual*, informed insurers, albeit subtly, that a finding of an insured's intent to deceive is required before a misrepresentation, an omission or incorrect statement in an application can avoid the policy under § 3609.

In three subsequent cases, the Oklahoma Supreme Court relied upon *Massachusetts Mutual* in further indicating that a finding of intent to deceive is required before a policy may be avoided due to false statements or omissions in a policy application. 6 7 8 These cases interpreted the holding in *Massachusetts Mutual* to require insurers relying on the defense of misrepresentation to bear the burden of proving the facts necessary to sustain this defense and that questions of the insured's intent in making false statements in a policy application were to be left to a jury. 9 10 11

The Tenth Circuit Court of Appeals has also visited the issue of "misrepresentation" under Oklahoma's statute and has determined that a finding of an insured's intent to deceive is required to deny policy benefits under 36 O.S. § 3609. 12 13 In *Hays v. Jackson Nat'l Life*, the Tenth Circuit stated:

When *Massachusetts Mutual*, *Brunson*, and *Claborn* are considered together, we are persuaded that section 3609 requires a finding of intent to deceive before an insurer can avoid the policy.

The court in *Hays* rejected the lower court's finding that an insured's intent was irrelevant and again reiterated that the question of intent was a material issue of fact for the jury that precluded summary judgment. 14

In *Vining v. Enterprise Financial Group, Inc.*, the Tenth Circuit found that the insurer could not rely on the affirmative defense of misrepresentation under 36 O.S. § 3609 where the insurer admitted that the insured did not willfully or intentionally misrepresent his health history. 15

In 2005, the Oklahoma Supreme Court had the opportunity to make a definitive ruling on the misrepresentation statute as a result of a certified question from the U.S. District Court for the Northern District of Oklahoma. The federal court asked the Oklahoma Supreme Court to answer the following certified question: "Whether Oklahoma law requires a finding that the insured intended to deceive the insurer before a misrepresentation, omission, or incorrect statement on an insurance application can serve as a ground to prevent recovery under the policy pursuant to Okla. Stat. Tit. 36 § 3609." The Oklahoma Supreme Court declined to answer the certified question, stating:

We have three times followed *Massachusetts Mutual's* requirement of a finding of an "intent to deceive" the insurer before a policy may be avoided by reason of the insured's false statement or omission in the application.

## FEDERATION OF REGULATORY COUNSEL, INC.

The "intent to deceive" standard has thus been unequivocally announced, and any insurer relying on the defense of misrepresentation under 36 O.S. § 3609 is required to prove that an insured intentionally deceived it before a policy may be avoided by reason of false statement or omission in the application.

### **Proving the "Intent to Deceive" Standard in the Context of Bad Faith Litigation**

The question for insurers is, how do they meet this burden of proving an "intent to deceive" on the part of the applicant/insured? Proving such an intent can be difficult for insurers, but to rescind a policy or deny a claim without doing so places the insurer at peril for bad faith tort claims. This hurdle is exacerbated by Oklahoma case law holding that the question of whether the insured intended to deceive the insurer is one for the trier of fact and may not be proved as a matter of law. **16** ("Where the evidence is conflicting as to either insured's state of health at the time of application, or the falsity of insured's statements in the application process, or the intent of the insured, the issues are properly tendered to the jury for resolution.") **17 18**

As the case law discussed herein holds, an insurer must take into consideration the intent of the insured before rescinding a policy based on 36 O.S. § 3609. The failure to consider the "intent" of the applicant when asserting the misrepresentation defense is fatal to the insurer's claim that it conducted a claims investigation reasonably appropriate and/or had a reasonable belief that the claim was factually or legally insufficient. **19 20**

Any insurer relying on a misrepresentation defense in Oklahoma should conduct a thorough investigation of the information asked and answered on the application, including the agent's recollection of the application process. A follow-up call to the insured, post-application, for the purpose of verifying the information on the application has been helpful in avoiding misrepresentations which could lead to litigated denials. Additional documentation as to what the insured actually knew at the time he or she made application for the insurance in question is a determination that must be made before a policy is rescinded.

Other possible methods of investigating and proving an insured's intent include: the dates and results of medical exams and tests, the subjects of conversations with various medical personnel, the extent of the insured's education and intelligence, the insured's conversations with friends and family, and any actions that the insured may have taken at relevant times which might indicate knowledge of serious medical problems, such as drawing or changing a will, or changes in personality or attitude. **21**

While Oklahoma courts have not spelled out directly what they expect of an insurer's investigation, some guidance may be gleaned from one case. In *Claborn v. Washington National Insurance Co.*, **22** in order to prove the insured intentionally misrepresented his health history, the insurer relied not only on the responses to the health questions contained in the policy application, but also on his affirmation that those answers were correct in a follow-up telephone interview conducted by the insurer. The Oklahoma Supreme Court ruled there was no conflicting evidence as to whether the insured intentionally misrepresented his health history because the insured admitted to the misrepresentation and his blatantly false answers to both the policy health questions and the follow-up phone interview. **23**

Opinions from courts in other jurisdictions provide additional insight into methods by which insurers can make a determination of the "intent" of the insured. Louisiana courts have stated that to determine whether there has been an intent to deceive on the part of an insured making representations in an application for insurance, courts look to surrounding circumstances indicating the insured's knowledge of falsity of representations and high recognition of their materiality, or from circumstances which create a reasonable assumption that the insured recognized materiality. **24 25** Strict proof of fraud was not required in these cases. **26** Courts have also allowed the intent of the insured to deceive the insurance company to be proven by circumstantial evidence. **27**

## FEDERATION OF REGULATORY COUNSEL, INC.

Additionally, an insured's intent to deceive can be established by extrinsic evidence that he or she actually and fully understood that an undisclosed medical condition was serious. A Federal Court in Louisiana held that an insured acted with intent to deceive by failing to report a malignant tumor where she clearly understood the gravity of her condition, as shown by the fact that she had discussed treatment options at length with her physician and had elected not to undergo further surgery. 28

The act of making the false representation with knowledge that it is false can give rise to the inference that the insured intended to deceive the insurer. 29 Since it is common knowledge that life insurance decisions are based in large part on the health of the applicant, it may be impossible to characterize an applicant's conduct as anything other than fraudulent where there is a willful and intentional failure to disclose health information which has been clearly and directly requested. 30 31 Factors such as the brevity of the time between the making of the representation and the occurrence of disability from disease may indicate that the insured unquestionably had knowledge at the time he or she made application for insurance that the insured was afflicted with such disease. 32

An additional problem for insurers to navigate is an application filled out by the insurer's agent which contains incorrect information relating to the insured's health history. This poses a hurdle for an insurer when misrepresentation is utilized as a defense to a claim because an agent's acts are imputed to the insurer. 33 Insureds will often blame any false information contained in their policy application on the insurance company's agent, effectively creating a material fact question as to who was responsible for the false information, precluding summary judgment.

Having the insured sign a post application acknowledgment of the information contained therein is one means of attempting to ensure that the information contained therein is accurate. In the Illinois case of *Marionjoy Rehabilitation Hospital v. Lo*, an insurance agent filled out an application for health insurance that failed to disclose the true health history of the applicant, which was known by the agent. 34 The court ruled that normally, in such situations, an insurer could not rely on misrepresentations contained in the application to refuse benefits because the agent's knowledge is imputed to the insurer for a proposed insured. However, in *Lo*, this rule did not apply. The insurer sent a letter to the insured requesting that he look over the application to verify the information contained therein. 35 The insured sent back the letter affirmatively indicating that the information contained in the application was indeed correct. The court ruled that this was an independent act by the insured that could not be imputed to the insurer via the agent and stated, in regards to the verification letter sent to the insured: "The communication at least in part is an attempt by the insurer to avoid any problems that might arise due to unscrupulous agents and as such should be encouraged." *Id.*

### **Conclusion**

Many insurance defense counsel have, in recent years, advised their clients that a "misrepresentation" which was "material to the loss" should be the standard in determining whether to rescind a policy. Juries are simply unsympathetic when an insurer denies a claim because the insured did not apprise the insurer on the application that he or she had been diagnosed or treated for a health condition that was material to the risk, but the death of the insured was actually caused by a traffic accident or some health condition not related to the undisclosed condition. If the misrepresentation was not "material to the loss," many insurers honored these types of claims, liberally construing the statutes to avoid bad faith litigation even in ostensibly "material to the risk" jurisdictions.

As all defense counsel know, when a trier of fact gets an opportunity to review almost any matter relating to insurers and their claims handling, the insurer will generally not prevail. Keeping insurers out of litigation is our goal, so we urge our clients to utilize caution before rescinding or denying a policy claim based upon misrepresentations, incorrect statements of fact or omissions in an application for insurance, as the standard of "intent to deceive" can be difficult, if not impossible, to meet.

**FEDERATION OF REGULATORY COUNSEL, INC.**

---

**Endnotes**

1. See, *New York Life Ins. Co. v. Strong*, 65 P.2d 194 (Okla. 1937), *certiorari denied* 57 S. Ct. 796, 301 U.S. 693, 81 L. Ed 1349.
2. *Tri-State Insurance Co., v. Herzer*, 279 P.2d 329, 332-333 (Okla. 1954); (quoting *United Benefit Life Ins. Co. v. Knapp*, 175 Okla. 25, 51 P.2d 963, 964).
3. 416 P.2d 935 (Okla. 1965).
4. *Id.*, at 941; quoting 29 Am. Jur., Insurance at § 698; (emphasis supplied).
5. *Id.*, at 936-937; (emphasis supplied).
6. *Whitlatch v. John Hancock Mutual Life Insurance Co.*, 441 P.2d 956 (Okla. 1968).
7. *Brunson v. Mid-Western Life Ins. Co.*, 547 P.2d 970 (Okla. 1976).
8. *Claborn v. Washington National Insurance Co.*, 910 P.2d 1046 (Okla. 1996).
9. *Whitlatch*, at 959.
10. *Brunson*, at 973.
11. *Claborn*, at 1049.
12. *Hays v. Jackson Nat'l Life Ins. Co.*, 105 F.3d 583 (10th Cir. 1997).
13. *Vining v. Enterprise Financial Group, Inc.*, 148 F.3d 1206 (10th Cir. 1998).
14. *Hays*, 105 F.3d at 586.
15. 148 F.3d at 1215.
16. See *Claborn v. Washington National Insurance Co.*, 910 P.2d 1046, 1049 (Okla. 1996).
17. Citing *Brunson v. Mid-Western Life Ins. Co.*, 547 P.2d 970 (Okla. 1976).
18. See also *Johnson ex rel. Johnson v. Forethought Life Ins. Co.*, 2006 WL 314446 (W.D. Okla. 2006).
19. See *Johnson ex rel. Johnson v. Forethought Life Ins. Co.*, 2006 WL 314446 (W.D. Okla. 2006).
20. See also *Matlock v. Texas Life Ins. Co.*, 404 F.Supp.2d 1307 (W.D. Okla. 2005).
21. *Couch on Insurance*, (6 Couch on Ins. § 87:22).

**FEDERATION OF REGULATORY COUNSEL, INC.**

22. 910 P.2d 1046, (Okla. 1996).
23. *Id.*, at 1049.
24. *See Parker v. Western Fidelity Ins. Co.*, 560 So. 2d 953 (La. App. 3 Cir. 1990).
25. *See also Henry v. State Farm Mutual Auto Ins. Co.*, 465 So. 2d 276 (La. App. 3 Cir. 1985).
26. (*Henry v. State Farm*, 465 So. 2d 276).
27. *Sharp v. Lincoln American Life Ins. Co.*, 752 S.W. 2d 673 (Tx. App. Corpus Christi, 1988).
28. *Watson v. United of Omaha Life Ins. Co.*, 735 F. Supp. 684 (M.D. La. 1990).
29. *See Monarch Life Ins. Co. v. Donahue*, 708 F. Supp. 674 (E.D. Pa. 1989).
30. 1 COA2d 1 § 20 (2005).
31. *Citing Mutual Benefit Life Ins. Co. v. Chisholm*, 329 N.W.2d 103 (Neb. 1983).
32. 6 Couch on Ins. § 87:22.
33. *See City Nat'l Bank and Trust Co. v. Jackson Nat'l Life Ins.*, 804 P.2d 463, 467 (Okla. Civ. App. 1990); (citations omitted).
34. 535 N.E.2d 1061 (Ill. App. 1989).
35. *Id.*, at 1064.