
MISREPRESENTATIONS IN
APPLICATIONS FOR INSURANCE

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I. INTRODUCTION

This outline discusses the general rules applicable to cases involving misrepresentations made in applications for insurance.

II. GENERAL RULE

The general rule is that a material misrepresentation or omission made in an application for insurance will void the insurer's obligations under the policy. *Handbook on Insurance Coverage Disputes*, §3.01(a):

See, e.g., Metropolitan Life Ins. Co. v. Fugate, 313 F2d 788 (5th Cir. 1963); *Dennis v William Penn Life Assurance Co. of America*, 714 F Supp 1580, 1582 (W.D. Okla. 1989); *Viviano v Travelers Ins. Co.*, 533 F Supp 1, 6 (E.D. La. 1981); *Hatch v. Woodmen Accident & Life Co.*, 88 111. App. 3d 36, 409 NE2d 540, 543 (2d Dist. 1980); *Nationwide Mut. Ins. Co. v. Conley*, 156 W. Va. 391, 194 SE2d 170 (1972); *Unger v. Metropolitan Life Ins. Co.*, 103 111. App. 2d 150, 242 NE2d 907 (3d Dist. 1968); *Gardner v. North State Mut. Life Ins. Co.*, 163 N.C. 367, 79 SE 806 (1913). *See generally* 12A Appleman, *Insurance Law and Practice* §§7276, 7291-305 (1981). It has thus been held that a material misrepresentation in an insurance application permits the insurer to invalidate the policy and to avoid responsibility for losses claimed thereunder. *See Pedersen v. Chrysler Life Ins. Co.*, 677 F Supp 472, 474 (N.D. Miss 1988) ('[i]f a party applying for insurance makes a misstatement of a material fact in the application, the insurer is entitled to declare the policy issued in reliance thereon void *ab initio*.'); *INA Underwriters Ins. Co. v. D.H. Forde & Co.*, 630 F Supp 76, 77 (W.D.N.Y. 1985) (misrepresentations in the policy application render the policy void *ab initio*); *Shapiro v. American Home Assur. Co.*, 584 F Supp 1245, 1252 (D. Mass. 1984) (false statement in application that 'misrepresented the risk incurred' by the insurer relieved insurer of all liability under the policy).

Michigan appellate courts long have recognized this rule.

In *Life Insurance Co. v Woiciechowski*, 314 Mich 275, 281 (1946), the Michigan Supreme Court stated the general rule:

A false representation in an application for insurance which materially affects the acceptance of the risk entitles the insurer to cancellation as a matter of law. *Krajewski v Western & Southern Life Ins. Co.*, 241 Mich 396.

In *Wiedmayer v Midland Mutual Insurance*, 414 Mich 369, 375-76 (1982), the Michigan Supreme Court followed *Woiciechowski* and further clarified the rule:

Moreover, in *General American Life Ins Co v Woiciechowski*, 314 Mich 275, 281; 22 NW2d 371 (1946), we stated:

"A false representation in an application for insurance which materially affects the acceptance of the risk entitles the insurer to cancellation *as a matter of law*." (Emphasis supplied.)

The fact that the insurance policy did not affirmatively provide for cancellation under such circumstances does not operate as a bar to the insurer's ability to void the policy in the face of fraud. Common law has always permitted the avoidance of a contract procured by means of fraud. *New York Life Ins Co v Buchberg*, 249 Mich 317; 228 NW 770 (1930).

In *Government Employees Ins Co v Chavis*, 254 SC 507, 516-517; 176 SE2d 131 (1970), the South Carolina Supreme Court upheld the right of an insurer to rescind an automobile liability policy because of fraudulent statements made in the procuring of it, although the insurer had not secured the right to do so in the policy. In doing so, the Court observed:

"We know of no authority which requires the insurer to reserve the right to rescind its policy for fraud or material misrepresentation."

We agree with the South Carolina Supreme Court.

In *United Security v Insurance Commissioner*, 133 Mich App 38, 41 (1984), the Court of Appeals held:

In *Keys v Pace*, 358 Mich 74; 99 NW2d 547 (1959), the Court recognized that an insurance company may rescind a policy *ab initio* for an intentional misrepresentation of a material fact on the application.

A. RATIONALE FOR THE RULE

The rationale for the rule is the equitable notion that an insurer, in making underwriting decisions and in setting premiums has the right to rely on the information provided by the insured as true. 12A Appelman, Insurance Law & Practice §7292. According to well-settled contract law, when a contracting party's assent to a contract is induced by another's fraudulent or material misrepresentation upon which there is justifiable reliance, the contract is voidable.

Restatement 2d of Contracts §306(1). *Handbook on Insurance Coverage Disputes* §3.01[e].

In *Cunningham v Citizens Insurance Co.*, 133 Mich App 471 (1984), the Court of Appeals held that it would be unfair to the insurer to permit false and fraudulent applications:

To permit a false and fraudulent application to bind an insurance company will result in protective measures being taken by the insurance industry. If plaintiff's argument is accepted, one can readily foresee the day when agents will no longer be allowed to issue binders by the companies they represent. One who applies for insurance will have to wait until final acceptance and approval is received from the home office. This may take weeks. We do not believe that those who obey the law and are honest in their dealings should be forced to suffer adverse consequences because of a few wrongdoers' fraudulent acts. Public policy protects those who do right; the courts need not be overly solicitous of those persons who attempt to perpetrate fraud in their contractual relationships. [*Cunningham*, 133 Mich App at 478.]

B. THE REPRESENTATION MUST BE MATERIAL.

The general rule requires that the fact misstated or omitted is deemed "material" if it could reasonably be considered as affecting the insurer's decision to enter into the contract, or its evaluation of the degree or character of the risk, or its calculation of the premium to be charged. *Handbook on Insurance Coverage Disputes* §3.01[d].

Thus, if the misstatement or omission is not material to the risk insured and has been made in good faith, courts will usually permit the insured to recover under the policy. 12A Appleman Insurance Law & Practice §7293.

In *Oade v Jackson National Life Insurance Co.*, 465 Mich 244 (2001), the Michigan Supreme Court dealt with issues involving a life insurance policy and MCL 500.2218. MCL 500.2218 deals with false statements made in applications for disability insurance. It provides, in part:

The falsity of any statement in the application for any disability insurance policy covered by Chapter 34 of this code [MCL 500.3400 *et seq.*] may not bar the right to recovery thereunder unless such false statement materially affected either the acceptance of the risk or the hazard assumed by the insurer.

(1) No misrepresentation shall void any contract of insurance or defeat recovery thereunder unless the misrepresentation was material. No misrepresentation shall be deemed material unless knowledge by the insurer of the facts misrepresented would have led to a refusal by the insurer to make the contract.

* * *

(3) In determining the question of materiality, evidence of the practice of the insurer which made the contract with respect to the acceptance or rejection of similar risk shall be admissible . . .

The decedent completed an application for a “preferred” life insurance policy. The application obligated the decedent to provide the insurer with updated health information between the time the original application was completed and the date the policy was issued. On the application, plaintiff denied having experienced chest pains or being hospitalized, both which were true at the time. However, between the application date and the date the policy was issued, he went to the hospital emergency room because he experienced chest pains. He failed to provide this information to the insurer. On January 4, 1994, the insurer approved a “standard” life insurance policy to the decedent, not a “preferred” policy, as the decedent had expected. The decedent paid the policy premium and the policy was delivered on January 6, 1994. The decedent died on September 1, 1994 from a sudden heart attack. The insurer refused to pay on the policy because of the decedent’s failure to provide it with updated information. *Oade*, 456 Mich at 247-249.

The plaintiffs, the named beneficiaries, sued the insurer for its refusal to pay. The Circuit Court held that the insurance policy never took effect because the decedent failed to communicate the “material changes” to the insurer in writing. The Court of Appeals reversed on the basis of MCL 500.2218(1), finding that the decedent’s misrepresentation was not “material”, because the insurer would have issued a policy anyway had the decedent provided updated information, albeit a different policy at a higher rate.

The Supreme Court reversed, citing its earlier decision in *Keys v Pace*, 358 Mich 74, 82 (1959):

Our decision in *Keys v Pace*, 358 Mich 74, 82; 99 NW2d 547 (1959), made clear that a fact or representation in an application is ‘material’ where communication of it would have had the effect of ‘substantially increasing the chances of loss insured against so as to bring about a rejection of the risk or the charging of an increased premium.’ *Keys*, in turn, is consistent with the plain language of MCL § 500.2218(1), which defines materiality in terms of the insurer’s refusal ‘to make *the* contract’ (emphasis added), not ‘a’ contract. [*Oade*, 456 Mich at 254.]

The Supreme Court noted that the undisputed evidence established that the correct information would have lead the insurer to charge an increased premium ‘hence a different contract.’ The court thus ordered summary disposition in favor of the insurer. Thus, the test is whether the insurer, if it had known the truth, would have refused to enter *the* contract it executed, not just *any* contract of insurance. *Id.* at 254.

In reaching its decision, the Michigan Supreme Court reversed the Court of Appeals

decision in *Zulcosky v Farm Bureau Life Ins Co of Michigan*, 206 Mich App 95 (1994). *Zulcosky* had ruled that a change in facts is “material” only where the correct information would cause the insurer to reject the application altogether. The Supreme Court made clear that this is not the case because MCL 500.2218 defines materiality in terms of the insurer’s refusal to make the same contract as issued without the misrepresentation. *Oade*, 465 Mich at 253-254.

In *Keys v Pace*, 358 Mich 74 (1959), the applicant for automobile insurance gave a false answer to the question whether his license had been revoked, suspended or refused within the past three years. The Supreme Court cited several quotes from 29 Am Jur Insurance including:

The generally accepted test for determining the materiality of a fact or matter as to which a representation is made to the insurer by the applicant for insurance is to be found in the answer to the question whether reasonably careful and intelligent underwriters would have regarded the fact or matter, communicated at the time of effecting the insurance, as ***substantially increasing the chances of loss insured against so as to bring about a rejection of the risk or the charging of an increased premium.*** [*Keys*, 358 Mich at 82 (Emphasis supplied)(citation omitted).]

This is the quote which is cited by the Supreme Court in *Oade*. *Oade* dealt with the application of MCL 500.2218. But it relied on *Keys* as a correct statement of the law regarding the determination of a material misrepresentation. *Keys* did not deal with MCL 500.2218. Therefore, *Keys* is the controlling authority for the definition of a material misrepresentation in cases other than those dealing with MCL 500.2218. *Keys* indicated that a misrepresentation is material when it would bring about a rejection of the risk “***or the charging of an increased premium.***” *Keys*, 358 Mich at 82 (emphasis added).

The United States Court of Appeals for the Sixth Circuit concluded that this was the law when applying Michigan law. *Old Life Ins Co of America v Garcia*, 411 F3d 605 (CA 6, 2005). “Michigan law permits rescission of an insurance policy when the insured makes a material misrepresentation in the application for insurance. A misrepresentation is material if the insurer would have charged a higher premium or not accepted the risk had it known the true facts.” *Id.* at 611 (citation omitted).

In *Auto Club Insurance Ass’n v Juncaj*, 2002 WL 1804030 (Mich Ct App, Aug 6, 2002), the defendant Juncaj submitted an application for automobile liability insurance. After the policy was issued, the defendant’s daughter while operating one of the insured’s vehicles was involved in an accident. After the accident the insurer rescinded the policy on the ground that Juncaj had made material misrepresentations by giving a St. Clair Shores address when he lived in Hamtramck, and by failing to include his daughter on the policy as a principal driver of the van. The court held that if the insured makes a material misrepresentation in an application for insurance, the insurer is entitled to rescind the policy and declare it void *ab initio*. The court further held that once an innocent third party is injured in an accident that is subject to coverage provided by the policy, the insurer is estopped from asserting fraud to rescind the policy with respect to the required coverage. The court found that there was no evidence that had the insurer

been timely informed that the daughter was driving or that the insured had moved to Hamtramck, it would have determined that he was not eligible for coverage. Thus, the court determined that rescission was not justified. The Court of Appeals further rejected the argument that *Oade v Jackson National Life, supra*, justified rescission on the basis that the misrepresentation would have resulted in charging a higher premium. However, the court's reasoning on this issue is somewhat suspect. The court held first that the *Oade* case dealt with MCL 500.2218, which is specifically applicable to life insurance and thus did not apply to the current case. It is correct that the statute only applies to life and disability insurance, but the statutory language was previously being used to **limit** the ability to rescind not create it. The court further stated that nothing in *Oade* indicated that the holding in *Lake States v Wilson*, 231 Mich App 327, 331 (1998), was no longer viable. The holding in *Wilson* stated:

Rescission is justified without regard to the intentional nature of the misrepresentation, as long as it is relied upon by the insurer. Reliance **may** exist when the misrepresentation relates to the insurer's guidelines for determining eligibility for coverage. (emphasis added)

Thus, the holding did not indicate that reliance **only** existed when the misrepresentation related to guidelines for determining coverage but it indicated that reliance **may** exist in this situation. Further, in her concurring statement to the order denying leave to appeal in *Juncaj*, Justice Kelly noted that the Court of Appeals really did not address the materiality issue because it found no misrepresentation at all. *Auto Club Ins Ass'n v Juncaj*, 468 Mich 923 (2003) (Kelly, J., concurring). Thus, this supports the conclusion that the Court of Appeals discussion of the material misrepresentation issue was nothing more than dictum. Subsequent courts have not followed *Juncaj* on this issue. They have followed the binding precedent contained in *Keys*.

In *Wojciechowski v Franklin Life Insurance*, 2002 WL 1803918 (Mich Ct App, Aug 6, 2002), the plaintiff applied for group credit life insurance in connection with the purchase of a car. In the application she falsely indicated that she had not been diagnosed or treated for cancer and degenerative disc and joint disease. After her death, the insurer sought to rescind the policy upon discovering the misrepresentation. Once again, because this was a policy of credit life insurance, the applicable statute was MCL 500.2218(1). The Court of Appeals reversed judgment for the plaintiff and ordered summary disposition in favor of the insurer holding that regardless of the plaintiff's claim that the plaintiff did not know the representations were false, the representations were material and the insurer proved that it relied upon them through an affidavit that it would have denied the application had it known the correct medical history.

Several subsequent cases have stated that a misrepresentation is material if the insurer would have charged an increased premium. See: *Sterling Heights v United National Ins Co*, 2005 WL 5955829 (ED Mich, February 11, 2005) (liability policy); *Chicago Ins Co v Wiggins*, 2005 WL 2179384 (ED Mich, September 9, 2005) (professional liability policy); *Williams v MEEMIC Ins Co*, 2006 WL 547834 (Mich Ct App, March 7, 2006) (auto policy); *Blundy v Secura Ins*, 2008 WL 2596603 (Mich Ct App, July 1, 2008) (no fault policy); and *Steadfast Ins Co v Prime Title Services, LLC*, 2008 WL 5216021 (WD Mich, December 11, 2008) (escrow agent's error and omission liability policy).

Thus, in cases involving application of MCL 500.2218, the Supreme Court has ruled that charging a higher premium is sufficient to establish material misrepresentation. However, for cases to which MCL 500.2218(1) does not apply, the law is stated by *Keys*, which also provides that a misrepresentation is material if it would have resulted in a higher premium.

1. Cases in which the courts found that the misrepresentations were material.

Numerous cases have found a material misrepresentation. Examples include:

(1) *Cunningham v Citizens Ins.*, 133 Mich App 471 (1984), where the applicant in applying for a no fault policy denied that he had been convicted of any drunk driving offense within the last five years when he had been so convicted.

(2) *Auto-Owners v Insurance Commissioner*, 141 Mich App 776 (1985), where the applicant failed to disclose speeding tickets and that her license had been suspended.

(3) *Farmers Insurance v Anderson*, 206 Mich App 214 (1994), where the applicant, Joyce Anderson, represented that she would be the primary driver, and failed to indicate that her son, Dillon, whose driver's license had been revoked, would be the primary driver.

(4) *Auto-Owners v Johnson*, 209 Mich App 61 (1995), where the insured represented that he had not been involved in any accident and had not been convicted or paid a fine for a moving violation in the last three years when he had been involved in an accident the day he made the application in which two occupants of the vehicle he struck were killed.

(5) *Lash v Allstate Insurance*, 210 Mich App 98 (1995), where the applicant for a no fault policy denied he had traffic citations over the last three years when he had a citation for operating a motor vehicle while impaired.

(6) *Massachusetts Casualty v Love*, 1996 WL 426530 (E.D. Mich, Jan. 10, 1996), where the applicant, a chiropractor, seeking a disability insurance policy, misrepresented his earnings on his application.

(7) *Zeer v Lake States*, 1996 WL 33362126 (Mich Ct App, Aug. 2, 1996), where the insured listed only himself and his wife as household drivers and checked "no" regarding moving violations, when the record revealed that there were other drivers, all of whom except one, had incurred moving violations in the last three years.

(8) *American Fellowship v Bojaj*, 1996 WL 33347491 (Mich Ct App, Dec 30, 1996), where the insured failed to disclose on the application that her son was a resident of the household.

(9) *Hammoud v Metropolitan Property & Casualty*, 222 Mich App 485 (1997), where under "Driver Information" and "All Residents Not Previously Indicated" there was no mention of the plaintiff who was the owner of the vehicle and a resident of the household.

(10) *Lakes State Insurance Co. v Wilson*, 231 Mich App 327 (1998), where the insured listed only herself as a "Resident and driver" when there were five persons living in the household, including the injured claimant.

(11) *State Farm Mut Auto Ins Co v Wilson*, 2005 WL 356292 (Mich Ct App, Feb 15, 2005), where insured misrepresented information on her insurance application that there were no other drivers in the household, including an uninsurable driver with a lengthy history of traffic offenses who later was involved in an accident. The court permitted the insurer to reform the policy based on misrepresentation and fact that insurer could not easily ascertain that the other driver resided in the household.

(12) *Farm Bureau Ins Co v Auto Owners Ins Co*, 2005 WL 1224701 (Mich Ct App, May 24, 2005), where insurer properly rescinded policy because insured falsely had represented that the property was titled in his name and that he had not been past due on the mortgage or taxes within the preceding five years.

(13) *Rodgers v North American Ins Co*, 2005 WL 1683548 (Mich Ct App, July 19, 2005), where insured failed to mention his bone spur on his left heel or his osteoarthritis in response to disability application's question of whether he had been treated for any "condition/disease/disorder of the bones," and insurer was entitled to rescind policy based on misrepresentation.

(14) *Montgomery v Fidelity & Guaranty Life Ins Co*, 269 Mich App 126 (2006), where insured did not disclose his smoking habit on life insurance policy, although he died in a car accident. The court held that the material misrepresentation warranted rescission of the policy.

(15) *Wheatonn v Geico Gen'l Ins Co*, 2006 WL 740080 (Mich Ct App, March 23, 2006), where insured either misrepresented the location of his vehicle on his auto policy application or misrepresented his extent of coverage on his claim for benefits and, either way, the insurer was permitted to rescind auto policy.

(16) *Auto Club Insurance v Grandberry*, 2006 WL 1360405 (Mich Ct App, May 18, 2006), where the court held that a misrepresentation as to the insured's address would be a material fact in an application for insurance, but held there was a question of fact whether there was a misrepresentation. If the material misrepresentation existed, the insurer would be entitled to reform the contract to the statutory minimum limits of \$20,000/\$40,000 due to a claim by an innocent third party.

(17) *Key v Great West Life & Annuity Ins Co*, 2006 WL 2000756 (Mich Ct App, July 18, 2006), where insured failed to reveal that he had received treatment for diabetes during the ten years before he applied for insurance; insurer would not have issued policy had it known true information and rescission allowed.

(18) *NCMIC Ins Co v Dailey*, 2006 WL 2035597 (Mich Ct App, July 20, 2006), where insurer could rescind legal malpractice policy because attorney (through his agent) had

materially misrepresented items on the application; insurer had to refund policy premiums.

(19) *Home Owners Ins Co v Reed*, 2006 WL 2708669 (Mich Ct App, Sept. 21, 2006), a widow planned to purchase a vehicle from her nephew Reed for her husband and added the vehicle to her Home Owners' policy. When her husband passed away before the sale was complete, Reed continued to drive the vehicle. The court held that insurer could rescind automobile insurance policy where there was no intention under widow's policy that Reed would be covered. Fact that misrepresentation was unintentional or related to a future occurrence was irrelevant.

(20) *Vernor's Dollar Discount, Inc v Fremont Mut Ins Co*, 2008 WL 541146 (Mich Ct App, February 28, 2008), where the sole shareholder of the applicant corporation failed to list a prior fire occurring at her prior incarnation of the business. The Court of Appeals concluded that the shareholder did not take the corporation's separate existence seriously or observe any corporate formalities. Therefore, the court concluded that the shareholder wrongfully used the corporation's separate existence to obtain insurance without having to disclose her prior history with fire losses. The court concluded that the history of fire loss was a material misrepresentation.

(21) *Manier v MIC Gen Ins Corp*, 281 Mich App 485 (2008), where the court found a material misrepresentation when the insured misrepresented the location of where her son lived and garaged the insured vehicle. The Court of Appeals rejected the insured's argument that the insurer could have easily ascertained the true location of the vehicle and the insured's residence. The court noted that there was no duty to investigate or to perform further research regarding the insured's residence. The court also upheld a household exclusion containing a stepdown provision that reduced coverage to the minimum required by MCL 257.520(b)(2).

(22) But see *Fountain v. Amex Assurance Co*, 2004 WL 2451937 (Mich Ct App, Nov 2, 2004), where the insured informed the insurer that she had worked at a business "on and off" and a question of fact existed as to whether the insured accurately answered the application while she was working from home.

(23) But see *Buckner v Old Republic Life Ins Co*, 2006 WL 664348 (Mich Ct App, March 16, 2006), where the insurer was barred from contesting validity of disability insurance policy on basis that insured's material misrepresentations regarding preexisting medical problems rendered policy void, where two-year period policy's incontestability clause had lapsed.

(24) But see *Williams v Allstate Ins Co*, 2007 WL 284514 (Mich Ct App, Feb 1, 2007), where insurer failed to prove material misrepresentations despite the fact that the insured, who was married but had separated and had five children, indicated on her application that she was single, had no dependants, and that there were no other licensed drivers in her household. No evidence presented that any of insured's children over sixteen were licensed drivers or resided with insured. There was also no evidence that insured's husband, who had a suspended license, was a member of her household or had access to her vehicle.

(25) But see *Blundy v Secura Ins*, 2008 WL 2596603 (Mich Ct App, July 1, 2008), where the insurer failed to show a material misrepresentation in spite of the fact that the insured misrepresented the fact that he owned the insured vehicle when it was actually owned and registered by his son. The Court of Appeals concluded that the insured did not make a representation in the application with the intent that the defendant would rely on it. The insured was straightforward as to who would be driving the vehicle and the insured's son was available during the application process and was actually paying the insurance premiums. Therefore, the insurance premiums reflected the risk posed by the son being the principal driver. The Court of Appeals stated that there was nothing in the record to support a conclusion that the insured was attempting to take advantage of a multi-vehicle discount or that he was even aware that he was receiving one. The court also concluded that the son was an innocent third party because there was no evidence of any collusion to misrepresent his ownership of the vehicle or to obtain a discount premium

Notably, the only case cited above involving rescission based on an insurer's argument that it would have increased the premium was *Wheatonn, supra* [No. 15]. The remaining misrepresentation cases either involved an insurer's claim that it would have refused the risk completely or did not provide the rationale behind the insurer's argument to rescind the policy.

C. IF THERE HAS BEEN A MATERIAL MISREPRESENTATION, THE INSURER MAY VOID OR REFORM THE POLICY.

If there has been a material misrepresentation in the application for insurance, the insurer may consider the policy void from its inception. *Farmers Insurance v Anderson*, 206 Mich App 214, 218 (1994); *Auto-Owners v Insurance Commissioner*, 141 Mich App 776, 779-80 (1985).

However, an insurance company may also have the option of reforming the policy in the event of a material misrepresentation. *Lake States Ins Co v Wilson*, 231 Mich App 327, 331-32 (1998). In *Lake States Ins Co, supra*, the insurance company was permitted to reform the policy to provide for coordinated benefits [instead of the "optional" noncoordinated no-fault and health insurance coverage] where the insured failed to disclose other drivers in the household on her application. As the Court explained in *Auto Club Ins Assoc v Grandberry*, 2006 WL 1360405 (Mich Ct App, May 18, 2006):

Once an innocent third party is injured in an accident, the insurer is estopped from asserting fraud to rescind the insurance contract. [*Lake States Ins Co, supra* at 331-32]; *Farmers Ins Exch v Anderson*, 206 Mich App 214, 220; 520 NW2d 686 (1994). However, ***an insurer is not precluded from reforming the policy to eliminate any "optional" insurance coverage***, MCL 257.520(g), as that optional coverage relates to an innocent third party, unless the insurer could easily ascertain the fraud or misrepresentation. *Id.* at 332; *Farmers Ins Exch, supra*, at 219. The financial responsibility act defines "optional" coverage as "any lawful coverage in excess of or in addition to the [mandatory minimum] coverage specified for a motor vehicle liability policy."

MCL 257.520(g); *Lake States Ins Co, supra* at 332. ***In sum, an insurer is entitled to reformation of an insurance policy if (1) there was a material misrepresentation, (2) the coverage the insurer wishes to rescind is "optional," and (3) the fraud or misrepresentation could not have been easily ascertained by the insurer at the time that the insurance contract became effective.*** *Lake States Ins Co, supra* at 332. [Footnote omitted, emphasis added.]

The Court of Appeals reached the same conclusion in *Manier v MIC Gen Ins Corp*, 281 Mich App 485 (2008):

In *Lake States Ins Co v Wilson*, 231 Mich App 327, 331-332, 586 NW2d 113 (1998), we held that although an insurance company is estopped from asserting fraud to rescind coverage applicable to an innocent third party, “an insurer is not precluded from rescinding the policy to void any ‘optional’ insurance coverage[.]” “Optional” coverage includes “any lawful coverage in excess of or in addition to the [mandatory minimum] coverage specified for a motor vehicle liability policy.” *Id.* at 332 n 2, 586 NW2d 113, quoting MCL 257.520(G).

D. THE MISREPRESENTATION NEED NOT BE INTENTIONAL.

It is generally held that if the fact misrepresented or the undisclosed information is material, it does not matter whether the misrepresentation or a non-disclosure was intentional or by mistake.

Handbook on Insurance Coverage Disputes §3.01[c] states:

The insurer will be relieved of liability even though the material misrepresentation was not made knowingly, willfully, or with an intent to deceive. See *Michael v. World Ins. Co.*, 254 F2d 663, 664 (6th Cir. 1958); *In re Epic Mortgage Ins. Litig.*, 701 F Supp 1192, 1242-43 (E.D. Va. 1988); *Hatch v. Woodmen Accident & Life Co.*, 88 111. App. 3d 36, 409 NE2d 540, 543 (2d Dist. 1980); *Barrera v. State Farm Mut. Auto. Ins. Co.*, 71 Cal2d 659, 659 n.4, 456 P2d 674, 679 n.4, 79 Cal. Rptr. 106, 111 n.4 (1969); *Modisette v. Foundation Reserve Ins. Co.*, 77 N.M. 661, 427 P2d 21, 25 (1967); *Anaheim Builders Supply, Inc. v. Lincoln Nat'l Life Ins. Co.*, 233 Cal. App. 2d 400, 43 Cal. Rptr. 494 (5th Dist. 1965); *Metropolitan Life Ins. Co. v. Becraft*, 213 Ind. 378, 12 NE2d 952 (1938); *Piccininni v. Aetna Life Ins. Co.*, 250 A.D. 498, 294 NYS 880 (2d Dep't 1937). See generally R. Long, *The Law of Liability Insurance* § 19.08, at 19-21 (1986); 17 *Couch on Insurance* 2d §67:343(1983).

Michigan appellate courts have recognized this rule.

In *U. S. Fidelity & Guaranty v Black*, 412 Mich 99 (1981), the Supreme Court held that in cases involving parties to a contract, there is no necessity to prove intent to deceive, in order to show misrepresentation:

Therefore we hold that independent proof of intent to induce reliance is unnecessary to maintain an action in deceit under the doctrine of innocent misrepresentation inasmuch as the material statement made in the course of contractual negotiations is presumptively made with the intention that it should be relied upon. [*Black*, 412 Mich at 120.]

In *Legel v American Community Mutual Insurance*, 201 Mich App 617 (1993), the Court of Appeals affirmed summary disposition to the defendant insurer holding on this issue:

However, it is unnecessary for an insurer to show fraudulent intent in order to cancel an insurance policy where an applicant makes a material misstatement concerning prior medical history. [*Legel*, 201 Mich App at 618 (citation omitted).]

In *Lash v Allstate*, 210 Mich App 98 (1995), the issue involved whether the applicant was mistaken as to the date of his previous citation for operating a motor vehicle while impaired. The Court of Appeals held that whether the misrepresentation was innocent or intentional was irrelevant to void the policy of insurance *ab initio*:

Rescission is justified in cases of innocent misrepresentation if a

party relies upon the misstatements, because otherwise the party responsible for the misstatement would be unjustly enriched if he were not held accountable for his misrepresentation. *Britton v Parkin*, 176 Mich App 395, 398-399; 438 NW2d 919 (1989). This is true, even as in this case, if it was a mutual mistake of fact. [*Lash*, 210 Mich App at 103.]

In *Lakes State Insurance v Wilson*, 231 Mich App 327 (1998), the Court of Appeals ordered summary disposition for the insurer on appeal holding:

It is the well-settled law of this state that where an insured makes a material misrepresentation in the application for insurance, including no-fault insurance, the insurer is entitled to rescind the policy and declare it void ab initio. *Lash v Allstate Ins. Co.*, 210 Mich App 98, 101, 532 NW2d 869 (1995). Rescission is justified without regard to the intentional nature of the misrepresentation, as long as it is relied upon by the insurer. Reliance may exist when the misrepresentation relates to the insurer's guidelines for determining eligibility for coverage. [*Wilson*, 231 Mich App at 331.]

E. THE INSURER MUST RELY ON THE MISREPRESENTATION.

The insurer may not assert a misrepresentation as a basis to void a policy of insurance if the insurer has not relied upon the misrepresentation.

In *Darnell v Auto-Owners Insurance Co.*, 142 Mich App 1 (1985), the plaintiff applied for a no fault insurance policy on April 1, 1980 and denied that any drivers in her household had their licenses revoked, restricted or suspended within three years. The insurer then obtained the plaintiff's driving record and learned that the applicant's husband had a restricted license. Despite having this information, the insurer issued the policy. The Court of Appeals held that the insurer could not later rescind the policy on the basis of the misrepresentation:

. . . Mrs. Darnell's misrepresentation as to plaintiff's driving record, as a matter of law, was not material since Auto-Owners' very action of issuing the policy with knowledge of plaintiff's record belies any contention that it would have rejected the risk or charged an increased premium. Accordingly, the misrepresentations of Mrs. Darnell were not material, based upon Auto-Owners' actions. [*Darnell*, 142 Mich App at 10.]

In order to void a policy for material misrepresentation, the insurer must have justifiably relied upon the misrepresentation. If the insurer was not justified in relying upon the misrepresentation, it may not assert the misrepresentation to void the policy.

In *Farmers Ins Exch v Anderson*, 206 Mich App 214 (1994), Joyce Anderson applied for

an auto insurance policy but did not disclose that her son Dillon, whose driver's license had been revoked, would be operating the insured vehicle. Joyce Anderson represented that she would be the primary driver in spite of the fact that she knew that Dillon would be the primary driver. *Id.* at 215-216. The Court of Appeals concluded that the misrepresentation regarding Dillon could not be easily ascertained by the insurance company. Dillon's name was nowhere to be found on the application for insurance completed by Anderson. Therefore, the Court of Appeals concluded that it would have been virtually impossible for Farmers to know that it should obtain Dillon's driving records, because it had no reason to believe that he would be operating the subject vehicle. *Id.* at 220-221. The Court of Appeals in *Anderson* distinguished the case from the facts of *Ohio Farmers v Michigan Mut Ins Co*, 179 Mich App 355 (1989). In *Ohio Farmers*, Ohio Farmers issued an insurance policy covering Francis E. Carter's Buick. Later, Carter gave the Buick to her son, Charles Seratt. Seratt then traded the Buick for another car, a Chevrolet, and obtained title to the Chevrolet in his own name. Although Seratt did not live with his mother, he listed Francis Carter's address on the car registration and on his driver's license. Francis Carter requested Ohio Farmers change the insurance coverage to the Chevrolet. Ohio Farmers did not know that Seratt owned or was the principal driver of the Chevrolet. It also did not know that Seratt did not reside with his mother. Seratt then loaned the Chevrolet to his brother-in-law, Ronald Maples, and while Maples was driving the car he was involved in an accident resulting in injuries to a third person. In *Anderson*, the Court of Appeals stated that *Ohio Farmers* involved a situation where fraud relied on by the insurer was readily ascertainable at the time the contract for insurance was formed.

In *Hammoud v Metropolitan Property & Casualty*, 222 Mich App 485 (1997), the court held that the insurer does not owe a duty to investigate or verify the insured's representations or to discover intentional material misrepresentations. *Id.* at 489.

However, in *Lake States v Wilson*, 231 Mich App 327 (1998), the court held that there could be an issue whether the misrepresentations could have been "ascertained easily" by the insurer. The court determined that the insurer could not have easily ascertained the fact that other persons and drivers resided in the insured's household.

In *Manier v MIC Gen Ins Corp*, 281 Mich App 485 (2008), the court noted no duty to investigate:

In *Hammoud v Metropolitan Prop & Cas Ins Co*, 222 Mich App 485, 489; 563 NW2d 716 (1997), this court held that "an insurer does not owe a duty to the insured to investigate or verify" a policy applicant's representations "or to discover intentional material misrepresentations." Here, Alice Burton advised defendant that Manier resided in her home, and claims to have no awareness of Manier's driver's license number. Burton also failed to advise defendant that Manier's girlfriend drove the Silhouette. Reviewing the issue *de novo*, we conclude that defendant could not have "easily ascertained" Burton's misrepresentations at the time she made them. Because no duty of investigation compelled defendant to perform further research regarding Manier's

residence, [*Farmers Ins Exch v Anderson*, 206 Mich App 214 (1994)] does not control this case, and the circuit court correctly determined that Burton's misrepresentation entitled defendant to reform the policy. [*Manier*, 281 Mich App at 490.]

For cases involving insurance policies governed by MCL 500.2218, which pertains to life and disability insurance, in *Smith v Globe Life Insurance Co.*, 460 Mich 446, 460-62 (1999), the Supreme Court held that if the misrepresentation deals with the "hazard assumed" then the insurer is not required to establish reliance under MCL 500.2218 in order to void the policy. The court referred to the language of the statute which provides:

The falsity of any statement in the application for any disability insurance policy covered by Chapter 34 of this code may not bar the right to recovery thereunder unless such false statement materially affected *either the acceptance of the risk or the hazard assumed by the insurer*. (MCL 500.2218, emphasis added)

In the *Smith* case, the misrepresentation dealt with a misrepresentation that the applicant did not have a heart condition. He had a heart condition and died of a heart attack. The court thus held that the misrepresentation was causally connected to the loss and thus the misrepresentation materially affected the hazard assumed regardless of whether the defendant actually relied upon the misrepresentation.

F. THE INSURER'S REQUEST FOR INFORMATION MUST BE CLEAR AND UNAMBIGUOUS.

The material misrepresentation by the insured must be clear and unambiguous.

Where the insurer asks an ambiguous question on the application, the ambiguity will be construed against the insurer. For example, in *Cook v Auto-Owners*, unpublished Michigan Court of Appeals decision docket number 168780 (1995), Cook applied for insurance when her son resided with her and the son's license had been suspended three times during the previous three years and was suspended at the time the application was completed. The claim resulted when the son, Albert Cook, was a pedestrian when struck and killed by a vehicle that had been struck by an uninsured motorist. The application failed to disclose that her son's license had been suspended three times in the previous three years, but the insured claimed that this information was not clearly asked for:

Cook claims (1) that the form itself was ambiguous, and (2) that the agent who filled out the form asked her only for information regarding any other persons that would drive her vehicle. Plaintiff told the agent that she was the only person that would be driving her vehicle. The agent who filled out the insurance application indicated that she asked each question on the insurance application. According to the agent, she specifically asked plaintiff to identify any other drivers in her household and whether any

driver had a license suspension or revocation in the previous three years.

The application contained a section headed 'DRIVER INFORMATION,' which was followed by a heading 'PROVIDE APPLICABLE INFORMATION FOR ALL HOUSEHOLD MEMBERS.' Under these headings are columns asking for the state in which the driver is licensed, the driver license number, the person's name as it appears on the license, and whether the driver is a principal or occasional driver of the insured vehicle. The application also asks whether 'any driver had a license suspension or revocation during the past 3 years.'

Ambiguities in insurance contracts must be construed in favor of the insured and against the insurer, the drafter. *Michigan Mutual Ins Co v Dowell*, 204 Mich App 81, 87; 514 NW2d 185 (1994). Where the provision is clear and unambiguous, its terms must be construed according to their plain, ordinary, and popular meaning. When the terms may reasonably be understood in different ways, the contract is deemed ambiguous. *Id.*

We find the form to be ambiguous. The form can be read so as to lead an applicant to understand that it requests information only as to household members that will drive the insured vehicle. That the form specifically asks for an indication as to whether a household member is either a principal or occasional driver of an insured vehicle creates a question as to whether a person who will not be driving an insured vehicle must be listed. Moreover, the form includes questions pertaining to 'driver', such as whether a driver has had a license suspended within the past three years, and separate questions referring to 'any household member[s].'

Because the application is ambiguous, there is a question of fact as to whether Cook made intentional misrepresentations on the application. Therefore, summary disposition pursuant to MCR 2.116(C)(10) was improperly granted on this issue.

The Court of Appeals addressed the issue in light of a medical condition on an application for mortgage life insurance in *Frost v Minnesota Life Ins Co*, 2007 WL 914627 (Mich Ct App, March 27, 2007). Plaintiff's decedent wife described herself as bulimic, but she was never diagnosed as bulimic. During her pregnancy, she was referred to a psychologist due to the failure to experience normal weight gain, but she never actually went to the appointment. After the pregnancy, the plaintiff and the decedent purchased mortgage life insurance. Question 3 on the application asked whether the decedent had ever had, or been treated for, mental disorders. The decedent answered no to this question. Three months later, the decedent died due to heart problems, potassium deficiency, and bulimia nervosa. The insurer denied coverage

claiming a misrepresentation of the decedent's mental health in the application. The insurer relied on the fact that the Diagnostic and Statistics Manual of Mental Disorders (4th Ed, 1994), a treatise regarding the diagnosis of mental disorders, indicated that eating disorders were mental disorders. Because bulimia is an eating disorder, the insurer argued that this amounted to a mental disorder under the medical treatise. The Court of Appeals rejected this because:

It is unlikely that the average lay person is familiar with the provisions of the DSM-IV, and there is no evidence that the decedent was familiar with the treatise. Further there is no evidence that the decedent had ever been diagnosed by a qualified health professional as having a recognized eating disorder before her death and, regardless of how we may view the decedent's behavior in light of the diagnosis criteria for eating disorders, lay persons are not qualified to make medical diagnoses. Thus the mere fact that an eating disorder qualifies as a mental disorder under the DSM-IV does not itself prove that the decedent's condition constituted a mental disorder or that she believed it to be a mental disorder. [*Id.* at slip op p 2.]

The court also noted that the fact that the decedent was referred to a psychologist for counseling does not prove that she had or believed she had a mental disorder. Therefore, under the facts, the court found a question of fact regarding whether the decedent made a false representation in her application for insurance.

G. THE INSURER MAY BE BARRED OR ESTOPPED FROM VOIDING THE POLICY WHEN THERE HAS BEEN AN INJURY TO AN INNOCENT THIRD PARTY.

The Michigan appellate courts have held that in cases where the insured has made a misrepresentation in the application, and there is an intervening accident involving an innocent third party before the time the insurer voids the policy, then the insurer is then estopped or barred from voiding the policy.

The Michigan appellate court rulings are in accord with the Michigan Financial Responsibility Act, §520, MCL 257.520 which provides in pertinent part:

- (f) Every motor vehicle liability policy shall be subject to the following provisions which need not be contained therein:
 - (1) The liability of the insurance carrier with respect to the insurance required by this chapter shall become absolute whenever injury or damage covered by said motor vehicle liability policy occurs; said policy may not be cancelled or annulled as to such liability by any agreement between the insurance carrier and the insured after the occurrence of the injury or damage; no statement made by the insured or on his behalf and no violation of said policy shall defeat or void said policy, and except as hereinafter

provided, *no fraud, misrepresentation, assumption of liability or other act of the insured in obtaining or retaining such policy* or in adjusting a claim under such policy, and no failure of the insured to give any notice, forward any paper or otherwise cooperate with the insurance carrier, *shall constitute a defense as against such judgment creditor.*

* * *

(g) Any policy which grants the coverage required for a motor vehicle liability policy may also grant any lawful coverage in excess of or in addition to the coverage specified for a motor vehicle liability policy *and such excess or additional coverage shall not be subject to the provisions of this chapter.* With respect to a policy which grants such excess or additional coverage the term “motor vehicle liability policy” shall apply only to that part of the coverage which is required by this section. [Emphasis added.]

Thus, pursuant to the statute, no fraud or misrepresentation may be asserted to cancel or annul the coverage required by the Financial Responsibility Law, but this prohibition does not apply to any excess coverage or coverage in addition to that specified by the Financial Responsibility Law.

In *Ohio Farmers v Michigan Mutual*, 179 Mich App 355, 364-65 (1989), the Court of Appeals held on this issue:

Therefore, we conclude that basic public policy considerations require that, once an innocent third party is injured in an accident in which coverage is in effect on the automobile, an insurer will be estopped from asserting rescission as a basis upon which it may limit its liability to the statutory minimum. Accordingly, the trial court was correct in determining that plaintiff failed to state a claim upon which relief can be granted.

In *Katinsky v Auto Club*, 201 Mich App 167, 170-71 (1993), the Court of Appeals held:

A false representation in an application for no-fault insurance that materially affects the acceptance of the risk entitles the insurer retroactively to void or cancel a policy. See *Auto-Owners Ins Co v Comm'r of Ins*, 141 Mich App 776, 779-780; 369 NW2d 896 (1985). However, this right to rescind ceases to exist once there is a claim involving an innocent third party. *Darnell v Auto-Owners Ins Co*, 142 Mich App 1, 9; 369 NW2d 243 (1985). Public policy requires that an insurer be estopped from asserting rescission when a third party has been injured. *Ohio Farmers Ins Co v Michigan Mutual Ins Co*, 179 Mich App 355, 364-365; 445 NW2d 228 (1989). Therefore, any misrepresentation McBride may have made on an insurance application regarding the validity of the check

cannot result in rescission of the policy with respect to plaintiff's claim.

However, in *Farmers Insurance Exchange v Anderson*, 206 Mich App 214 (1994), the Court of Appeals held that the estoppel to void the policy would only apply to the statutorily mandated minimum coverage of \$20,000/\$40,000. In *Anderson* case, the policy provided liability limits of \$100,000/\$300,000 and the court held that the insurer would be able to rescind the policy to the extent of the coverage in excess of the statutorily mandated minimum coverage.

In cases where the injured party is the party who made the misrepresentation, there is no bar. *Cunningham v Citizens Insurance Co*, 133 Mich App 471 (1984); *Auto-Owners v Insurance Commissioner*, 141 Mich App 776 (1985). Similarly, in *Hammoud v Metropolitan Property & Casualty Ins. Co.*, 222 Mich App 485 (1997), the court held that where the injured plaintiff was the owner of the insured vehicle, even though he was not the party who filled out the application, he was still actively involved in the fraud and thus was not an innocent third party.

The Michigan Court of Appeals further held that the estoppel to assert rescission does not apply to any "optional" coverage which the court defined as "any lawful coverage in excess of or in addition to the [mandatory minimum] coverage specified for a motor vehicle liability policy." See MCL 257.520(g). In *Lakes State Insurance Co. v Wilson*, 231 Mich App 327 (1998), the Court of Appeals held:

Once an innocent third party is injured in an accident in which coverage was in effect with respect to the relevant vehicle, the insurer is estopped from asserting fraud to rescind the insurance contract. MCL 257.520(f)(1); MSA 9.2220(f)(1); *Auto-Owners Ins. Co. v Johnson*, 209 Mich App 61, 64, 530 NW2d 485 (1995). However, an insurer is not precluded from rescinding the policy to void any 'optional' insurance coverage, MCL §257.520(g); MSA 9.2220(g), unless the fraud or misrepresentation could have been 'ascertained easily' by the insurer. 231 Mich App at 331-32.

One unpublished case from the Michigan Court of Appeals further suggested that an "innocent third party" includes only those third parties injured or killed by a vehicle and excludes a lienholder. See *GMAC v Titan Ins Co*, 2004 WL 2256170 (Mich Ct App, Oct 7, 2004).

In *Continental Gen Ins Co v Gershonowicz*, 2008 WL 1733363 (Mich Ct App, April 15, 2008), the Court of Appeals concluded that the innocent third party exception to rescissions for material misrepresentation did not apply to health insurance. The court noted that the insurer's right to rescind a health insurance policy is not limited by statute as the right to rescind auto insurance policies is by MCL 257.520.

H. THE INSURER MUST RESCIND AND MAY NOT PROCEED AS A CANCELLATION.

Where the insurer has a right to rescind the policy for a misrepresentation and void the

policy from the inception of the policy, the insurer must take steps to do so. However, if the insurer learns of the misrepresentation and then chooses to cancel the policy, then the policy is not void from the inception, and the rules of cancellation apply.

For example in *Burton v Wolverine Mutual Insurance*, 213 Mich App 514 (1995), the insured learned of the misrepresentation but chose to retain the earned portion of the premium and then cancelled the policy. Before the effective date of cancellation, the accident occurred. The court held that the insurer was barred from claiming that the policy was void:

The remedy that defendant seeks is untenable. Defendant wishes, upon the discovery of a misrepresentation in the application, to have the right to collect a premium and provide coverage as long as there are no losses and yet remain entitled to choose rescission and deny coverage if a loss occurs. In short, defendant wishes to be able to earn a premium without having to provide coverage. That, however desirable it may be to defendant, is not an available option. Rather, it must either rescind the policy upon discovery of the misrepresentation and refund the premium or cancel the policy, retaining the premium earned until the effective date of the cancellation and provide coverage until the effective date of the cancellation. But it cannot have its premium and deny coverage too.

In sum, defendant was entitled upon discovery of the misrepresentation to rescind the policy issued to plaintiffs. Instead, it chose to continue coverage for approximately three weeks longer and to retain a premium for that period. Having chosen to do so, defendant was obligated to provide coverage for that period and to pay the loss that happened to have occurred. [*Burton*, 213 Mich App at 519-520.]

Similarly in *Hill v Pioneer State Mutual*, 2001 WL 1353655 (Mich Ct App, Nov 2, 2001), the insureds failed to mention to the defendant's agent that their son was living with them and driving their vehicles at the time of the application. Subsequently, the agent learned that the son was residing with them and obtained a motor vehicle report and learned that he had nine points. Despite this knowledge the insurer issued the policy covering the insureds and their son. One day later, the insurer issued a cancellation notice effective December 15, 1997. However, on November 19, 1997 the son was involved in an accident. When the insurer became aware of the accident, it then sent a letter on December 20, 1997 seeking to rescind the policy and return the premium. The Court of Appeals relied upon the decision in *Burton*, holding that the insurer had the option to rescind the policy *ab initio* once it determined that misrepresentation had occurred but instead chose to cancel the policy and keep the premium payment. Thus, the defendant was barred from later attempting to rescind the policy:

Like the defendant in *Burton*, defendant in the instant case had the option to rescind plaintiffs' policy *ab initio* once it determined that

misrepresentation occurred; instead, defendant chose to cancel the policy and keep plaintiffs' premium payment. Like the plaintiff in *Burton*, Gregory was in an accident during the covered period before a cancellation notice was to take effect. Defendant in the instant case, like the defendant in *Burton*, attempted to rescind plaintiffs' policy once it learned of the accident. As in *Burton*, defendant is not entitled to do so. Indeed, defendant had already chosen its remedy by canceling plaintiffs' policy instead of rescinding it, and it cannot 'have its premium and deny coverage too.' *Id.* at 520. The trial court did not err by relying on *Burton* to rule for plaintiffs.

See also *NCMIC Ins Co v Dailey*, 2006 WL 2035597 (Mich Ct App, July 20, 2006), in which the court held that the insurer could rescind the legal malpractice policy because attorney (through his agent) had materially misrepresented items on the application, but the insurer had to refund policy premiums to put the parties back to the status quo since the policy was void *ab initio*.

I. RETENTION OF INSURANCE PREMIUMS WHERE POLICY IS RESCINDED FOR MISREPRESENTATIONS

Where an insurer seeks to rescind a contract for insurance on the basis of misrepresentation the general rule is that the insurer must return all premiums paid by the insured. *Burton v Wolverine Mut Ins Co*, 213 Mich App 514, 520 (1995); *NCMIC Ins Co v Dailey*, 2006 WL 2035597 (Mich Ct App, July 20, 2006). The rationale behind this rule is that the parties will be restored to their pre-contract status quo. *NCMIC, supra*.

Although there are no cases on point in Michigan, other states have noted an exception to this general rule. Specifically, these cases have held that if an insured makes material misrepresentations in the application and an insurance company pays claims under the policy, the insurance company is entitled to a setoff and need not return the full premium to rescind the policy.

In *American Standard Ins Co v Durham*, 403 N.E.2d 879 (Ind Ct App, 1980), citing 6 Couch on Insurance (2d ed. 1961) § 34:35 at 779, the Court held:

Notwithstanding the general rule that, in order to avoid liability on a policy there must be a prompt tender of premiums, such a tender is not necessary where . . . the insurer has paid a claim thereon which is greater in amount than the premiums paid.

Though not cited by the parties, directly on point is a 60 year old Indiana case, *Great Eastern Casualty Co v Collins* (1920), 73 Ind App 207, 126 NE 86. Collins sued Great Eastern for failure to pay on an insurance policy. As a defense, Great Eastern asserted a material misrepresentation in the policy application, entitling the

company to a rescission of the contract. Over the six months the policy had been in effect, Collins had paid \$16 in premiums, but had received \$16.67 on a previous claim. . . .

On appeal, this court held that when an insurance company has already paid out more in claims than had been paid in premiums, there is no need to tender premiums into the court. The court summarized:

We are not unmindful of the rule in this state, so well established that we do not need to cite authorities, that in order to avoid liability there must be a seasonable and prompt tendering back of premiums received. . . . (But) the law, as well as equity and good conscience, does not require appellant to return the premiums where appellee was appellant's debtor for more than the amount thereof. [*Durham*, 403 NW2d at 881-882 (internal citations omitted).]

Likewise, in *Gutting v Shelter Mut Ins Co*, 905 SW2d 550 (Mo Ct App, 1995), the insurance company was allowed to offset losses by retaining the insured's premium upon rescission. In *Gutting, supra*, the insured brought a claim to recover for losses from a fire. The insurer denied plaintiff's claim and rescinded the policy on grounds that plaintiff failed to disclose prior insurance claims on her application. Because the insurer had already made a \$2,500 advance payment for the loss, it refused to tender back any of the premium and requested reimbursement from the insured for money advanced in excess of the premium. The Court held that "where, as here, the insurer has paid money to the insured under the policy which is subsequently rescinded by reason of the insured's knowingly false application, and the money paid exceeds the premium received by the insurer, the insurer has a right of offset, and return of the premium is not a condition precedent to rescission." *Id.*

In *Borden v Paul Revere Life Ins Co*, 935 F2d 370 (CA 1, 1991), the Court determined that an insurance company was not in breach of contract and could rightfully rescind a policy for the insured's misrepresentations where the insurer had paid close to \$65,000 in benefits as compared to the insured's \$1,500 in premium payments:

The function of rescission, after all, is to restore the status quo ante--a feat which will customarily involve returning the consideration originally paid. But the rule--like most rules--is not without its exceptions. We think it is good law that, when an insurer has paid a claim to an insured under a policy which is subsequently rescinded by reason of the insured's knowingly false application, and the monies paid are in excess of the premiums received, the insurer has a right of offset; hence, return of the premium is not a condition precedent to rescission. *Accord American Standard Ins Co v Durham*, 403 NE2d 879, 881 (Ind Ct

App 1980); *Mincho v Bankers' Life Ins Co*, 129 AD 332, 113 NYS 346, 348 (1908); see also 6 *Couch on Insurance 2d* [§34.35], at 892- 93 [(1985)]; 3A J. Appleman, *Insurance Law & Practice* § 1832 (1979); 2 *Black on Rescission* § 483, at 1219-20 (1929). A contrary rule – requiring an insurer which has already overpaid a scalawag insured to throw good money after bad in order to set aside a policy obtained by the insured's deceit – would make no sense. [*Borden*, 935 F2d at 379.]

J. MISREPRESENTATIONS BY THE INSURED MAY NOT AFFECT THE INSURER'S LIABILITY TO THE LIENHOLDER.

There are generally two types of loss payable clauses. The first type, known as an ordinary loss payable clause, directs the insurer to pay the proceeds of the policy to the lienholder, as its interest may appear, before the insured receives payment on the policy. Under this type of policy, the lienholder is simply an appointee to receive the insurance fund to the extent of its interest, and its right of recovery is no greater than that of the insured. In such case, a breach of any condition of the policy by the insured would prevent recovery by the lienholder. See *GMAC v Titan Ins Co*, 2004 WL 2256170 (Mich Ct App, Oct 7, 2004).

The second type of loss payable clause is known as the standard loss payable clause. Under this type of clause, a lienholder is not subject to the exclusions available to the insurer against the insured because an independent or separate contract of insurance exist between the lienholder and the insurer. In other words, there are two contracts of insurance within the policy, one with the lienholder and the insurer and the other with the insured and the insurer. The Michigan Supreme Court held in *Foremost Insurance v Allstate Insurance*, 439 Mich 378 (1992), that any defense against the insured under a standard loss payable clause would **not** serve as a defense against the lienholder.

K. FRAUDULENT INSURANCE ACT

MCL § 500.4503 defines fraudulent insurance acts which include acts or omissions committed by any person who knowingly and with intent to injure, defraud or deceive:

(a) Presents, causes to be presented, or prepares with knowledge or belief that it will be presented to or by an insurer or any agent of an insurer any oral or written statement knowing that the statement contains any false information concerning any fact material to an application for the issuance of an insurance policy.

(b) Prepares or assists, abets, solicits, or conspires with another to prepare or make an oral or written statement that is intended to be presented to or by any insurer in connection with, or in support of, any application for the issuance of an Insurance policy, knowing that the statement contains any false information concerning any fact or thing material to the application.

(c) Presents or causes to be presented to or by any insurer, any oral or written statement including computer-generated information as part of, or in support of, a claim for payment or other benefit pursuant to an insurance policy, knowing that the statement contains false information concerning any fact or thing material to the claim.

(d) Assists, abets, solicits, or conspires with another to prepare or make any oral or written statement including computer-generated documents that is Intended to be presented to or by any insurer in connection with, or in support of, any claim for payment or other benefit pursuant to an insurance policy, knowing that the statement contains any false information concerning any fact or thing material to the claim . . .

MCL 500.4511 provides the penalty making a person who commits a fraudulent insurance act guilty of a felony punishable by imprisonment for not more than four years or a fine of not more than \$50,000 or both. The person shall be ordered to pay restitution.