

Lawyer's Policy Voided Due to Misrepresentation

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The U.S. District Court for the Western District of Virginia, applying Virginia law, held that an insurer may rescind a professional liability policy it issued to a law firm based on a material misrepresentation by the law firm in its renewal application. *TIG Ins. Co. v. Robertson, Cecil, King & Pruitt*, No. 1:01CV00143, 2003 WL 253167 (W.D. Va. Jan. 31, 2003).

The insurer issued a professional liability policy to a law partnership. When completing a renewal application, one of the partners checked "No Change" instead of "Yes" to a question inquiring whether "any attorney in [the] firm [was] aware of any claims made, wrongful acts, or errors or omissions that could result in a professional liability claim against any past or present attorney of the firm...." Subsequently, that same partner died of a self-inflicted gunshot wound. It was later determined that he was misappropriating client funds, and claims were made against the partnership because of his conduct. When the insurer was asked to cover the claims, it filed an action seeking rescission of the policy based on material misrepresentations.

The court first held that rescission was an available remedy to the insurer. The law firm argued that the cancellation clause of the policy entitled it to 30 days notice before cancellation of the policy, which it had not received. The court rejected this argument, reasoning that cancellation is a different remedy than rescission. The insurer, the court explained, did not want to cancel the policy sometime in the future; instead, it wanted to rescind the policy *ab initio*. The court therefore concluded that the insurer did not relinquish its right of rescission by including a cancellation clause in the policy.

The court rejected the law firm's argument that no misrepresentation had occurred. The court stated that the renewal application question "clearly asked the lawyer to disclose his own misconduct," and a reasonable attorney would know that misappropriating client funds would probably result in a claim. The court also rejected the law firm's argument that the misrepresentation was not material to the risk insured, noting that one of the insurer's underwriters had filed an affidavit stating that the insurer would not have issued the policy had it known the partner engaged in such conduct. Agreeing with the insurer, the court found it "unimaginable" that the partner's conduct would not be material to the risk being insured.

Next, the court held that the insurer was not estopped from rescinding the policy even though it had settled some of the claims that arose under the policy after the partner's death. The court reasoned that it was undisputed that the insurer issued a reservation of rights and preserved any defenses it had before handling the settled claims.

Finally, the court rejected the law firm's contention that the other partners were entitled to coverage because they did not commit wrongful acts or know of the deceased partner's wrongdoings. The argument that the "innocent partners" were entitled to coverage was based on the fact that the policy excluded claims arising from any "dishonest, fraudulent, criminal, malicious or knowingly wrongful act..." but provided an exception for "any Insured who did not commit, participate in, or have knowledge of any such act...." The court, though expressing sympathy for the innocent partners, held that the provision of the policy did not preclude the remedy of rescission. It stated that "[t]here is an obvious difference between affording coverage to an innocent insured under this Policy provision and rescinding the Policy because the Law Firm, through its authorized partner, lied on the application. Had [the partner] committed an act otherwise excluded under this provision of the Policy, without any misrepresentation in the application, his innocent partners would have had coverage."

For more information, please contact one of WRF's Professional Liability Attorneys at 202.719.7130