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NEWSLETTER

Policy Application Does Not Require Disclosure of Pending Claims Unless It Asks for Such Disclosure

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The United States District Court for the Middle District of Pennsylvania has held that an application for a management protection insurance policy did not require an insured to disclose any past, pending or future litigation and, therefore, the insured did not make any misrepresentations in its policy application when it failed to disclose information regarding an underlying lawsuit arising out of a traffic accident. *Westchester Surplus Lines Ins. Co. v. Safe Auto Ins. Group, Inc.*, 2010 WL 2640196 (M.D. Pa. June 30, 2010). The court also held that the insured did not make any misrepresentations in signing a higher limits warranty because the insured did not know and should not have known that the underlying lawsuit would exceed the policy's underlying limit.

The insured, an automobile insurance company, insured a driver who was involved in a traffic accident. The claimants offered to settle their claim with the insured for the insured driver's $15,000 policy limit. The insurer rejected this offer, and the claimant filed suit against the insured driver. The claimant later rejected settlement offers of $15,000 and $50,000, stating "that the case had a value in excess of $100,000." The claimants obtained a $3.5 million verdict against the insured driver and ultimately settled with the insured for $2.5 million.

The insured had applied for coverage while the underlying accident suit was pending but had not disclosed the underlying suit in its application. The insured had answered three sets of questions on the application pertaining to the insured's procedures for handling lawsuits and the threat of lawsuits. None of the questions asked about the existence of threatened or pending claims against the insured or any of its insureds. The insured also executed a higher limits warranty stating that the insured had no knowledge of a wrongful act, fact, circumstance or situation that it had reason to believe might result in a claim that could reasonably exhaust the policy's underlying limit, which was $2 million. The insurer filed a coverage action alleging that the insured had made material misrepresentations in the policy application by failing to disclose, in its answers, information about the underlying suit.

The court dismissed the insurer's complaint, holding that the application questions did not require the insured to disclose any information about past, pending or future litigation, including the underlying accident suit. The questions, the court explained, asked about policies and procedures for handling various types of claims, lawsuits and threats of lawsuits against the insured, and did not require it to list specific claims or lawsuits. Because the insured was never asked about any specific underlying claims or litigation, the court held, the insured did not make any misrepresentations in failing to disclose the underlying suit. The court further rejected the insurer's argument that "boiler plate" language appearing on the application's signature page required the insured to disclose the underlying claim. That language, the court explained, merely reflected the insured's promise "that the statements set forth in [the] application are true." Moreover, the court noted, the signature page language also expressly provided that nothing contained in the application "shall constitute notice of a claim or potential claim," contradicting the insurer's argument that the insured was required to list such claims.

The court also held that the insurer had failed sufficiently to allege that the insured made misrepresentations in signing the higher limits warranty without disclosing the underlying accident suit, which, the insurer argued, the insured knew or should have known would exhaust the $2 million underlying limit. The court held that the insurer's complaint failed to allege that any of the insured's senior executives or its general counsel knew or should have known that the underlying litigation would exceed $2 million in damages. The court noted that, at the time the warranty was signed, the underlying plaintiffs had recently stated only that the suit was worth more than $100,000. According to the court, "it strains credulity to suggest that [the insured] knew, or should have known, that the underlying case would exceed $2 million in damages simply because opposing counsel in the underlying case alluded that [t]he case was worth more than $100,000."