



Rescinding an Automobile Policy of Insurance in New Jersey - Episode #115

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Hosted by: John Czuba, Managing Editor

Guest Attorneys: Gina Stanziale and Allison Koenke of [Methfessel & Werbel](#)

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John Czuba: Welcome to the Insurance Law Podcast, the broadcast about timely and important legal issues affecting the insurance industry. I'm John Czuba, managing editor of *Best's Directory of Recommended Insurance Attorneys*.

We're pleased to have with us today attorneys Gina Stanziale and Allison Koenke from the law firm of [Methfessel & Werbel](#) in Edison, New Jersey with additional offices in New York City and in Philadelphia, Pennsylvania.

Gina is a member of the firm's counsel and has handled coverage, automobile liability, and premises liability cases. Gina was recently promoted to Co-Attorney Manager of the firm's property team along with Marc Dembling where she handles the defense of both first and third party claims from institution of suit to resolution, including the appeals process.

Allison is an associate attorney with the firm. She specializes in the defense of liability and personal injury protection cases. She also handles cases on PIP coverage and fraud issues and is experienced in the arbitration of PIP claims in the American Arbitration Association forum.

Allison also handles the defense of uninsured motorist and underinsured motorist coverage claims on behalf of insurance carriers.

We're very pleased to have them both with us today. Today's discussion is, "Rescinding an Automobile Policy of Insurance in New Jersey." We're going to lead off today with Gina for our first question.

Gina, under what circumstances can an insurance carrier void or rescind a policy in the state of New Jersey?

Gina Stanziale: Generally an insurance carrier can void or rescind a policy in New Jersey when a material misrepresentation has been made in either procuring insurance or in the submission of a claim otherwise known as a post loss misrepresentation.

A classic case of rescission involves a misrepresentation in the application for insurance. In the case of automobile insurance, potential policy holders will often withhold information they think will affect their insurance premium. Some examples are the failure to disclose residents of the household, failure to disclose regular operators of an insured vehicle, location of the vehicle, use of the vehicle such as commercial versus personal, or in cases of homeowners' insurance the owner occupancy status of the property.

If any of the withheld information is deemed material then a rescission is in order. A misrepresentation is material when it affects the premium. Thus, if the failure to disclose a resident of a household would have increased the insurance premium had he or she been disclosed a carrier is entitled to rescind the policy.

It is important to note that an increase of only \$150 is enough to deem it material to the risk. For proof purposes, underwriting must recalculate the premium and provide an affidavit to that effect as part of the carrier's proofs.

John: Allison, what is the effect of a voided or rescinded policy?

Allison Koenke: Once an insurance carrier decides to void or rescind the policy they must advise the insured and return the policy premium. At that point the policy is deemed to have never existed. The insurance carrier's obligations to their insured under the policy are extinguished. Any claims made by the insured for that policy period will not be honored by the insurance company.

However, the rescission does not extinguish the rights of recovery of innocent third parties. Insurance carriers are not given the same rights to rescind insurance policy benefits to a third party who is deemed innocent of any misrepresentation and who is injured through no fault of their own.

The innocent third party will be entitled to PIP as well as liability and property damage benefits. Innocent third parties include passengers in an insured vehicle at the time of the accident. It also includes parties who are occupants of vehicles involved in the accident with the insured vehicle.

Innocent parties do not include spouses, as they are deemed to be one and the same as in the appellate division decision of *Palisades Safety versus Bastien*. Courts have also applied the same theory to domestic partners in the unpublished decision of *GEICO versus Nelson*.

Generally, the status of a child as an innocent party would be dealt with on a case by case basis as in *Rutgers versus LaCroix*. The courts will consider whether a parent places a vehicle in his or her name to collect a lower premium. Was the child aware of the parent's actions? Did the child help pay for the insurance of a vehicle that is not in their name?

It is the insurance carrier's responsibility to establish that the innocent third party is not innocent.

John: Gina, when a policy is voided or rescinded what are the obligations of the insurance carrier to the insured?

Gina: When a policy is rescinded, the insurance carrier's obligation to the insured is twofold. First, the carrier must notify the policy holder of the rescission in writing. Second, the carrier must return the premium for the entire policy period, thus voiding the policy as if it never existed.

This differs from a cancellation where the return of a premium would be limited to the balance of the policy term. It is important to point out that rescission is an equitable remedy, thus the premium must be returned promptly. Under no circumstances may a carrier rescind a policy and keep the premium. Even in instances where the carrier paid out claims which exceed the premium prior to discovering the misrepresentation. The carrier is obligated to return the premium.

John: Allison, when a policy is voided or rescinded what are the obligations of the insurance carrier to an innocent third party under both a standard policy and a basic policy?

Allison: Prior to 1998, all New Jersey drivers were required to maintain a standard insurance policy with a mandatory bodily injury liability protection of \$15,000 per individual and \$30,000 per accident. This is the standard insurance policy and was the compulsory insurance requirement under NJSA 39:6a 3 and NJSA 39:6b 1a.

With regard to a standard policy, when an insurance policy is voided for a misrepresentation made by the insured New Jersey precedent provides that an insurer is liable to an innocent third party for the statutory minimum liability coverage of \$15,000 per person, \$30,000 per accident. The amount of coverage is mandated by New Jersey statute and the case of *New Jersey Manufacturers versus Varjabedian*.

In 1998, New Jersey passed AICRA, the Automobile Insurance Cost Reduction Act. This allowed a basic automobile insurance policy. This was an alternative to the mandatory coverage's previously required in New Jersey. The basic policy does not mandate liability insurance like the standard policy. It provides for optional liability coverage available at \$10,000.

In the recent case of *Citizen's United Reciprocal Exchange versus Perez* the Supreme Court evaluates what benefits are available to an innocent third party under a basic policy. Prior to this Supreme Court decision, it was accepted that innocent third parties under a basic policy were provided the minimum statutory limits of \$15,000 per person and \$30,000 per accident.

The appellate division relied in a 2-1 decision on the *New Jersey Manufacturers versus Varjabedian* case but here the Supreme Court overturned the appellate division and agreed with the dissenting judge below and found an insurance carrier with a voided basic policy was liable for the \$10,000 liability coverage because that is what the insured had contracted for.

The Supreme Court determined that the insured's fraud should not enhance recovery of an innocent third party. The innocent third party should be entitled to only what they would have gotten if there was no fraud and the policy was still in effect. The innocent third party should be entitled to only what was originally contracted for. No more, no less.

The Supreme Court made a point to explain that if the insured elects not to add the additional \$10,000 in liability coverage the insurance carrier would not be responsible for it to an innocent third party.

John: Gina, can an insurance carrier seek reimbursement of payments made on a claim prior to voiding or rescinding a policy?

Gina: When a policy is rescinded, as noted previously, it is deemed void ab initio back to the date of inception. It is as if there was never a contract between the parties. Thus, the carrier has no obligation to pay any claims that arise during that policy period.

To that end, although the returning of the premium when the policy is voided is unconditional it does not affect the insurer's right to seek reimbursement of payment made on behalf of an insured. Upon notifying the insured of the rescission, such right to seek reimbursement should be specifically reserved.

However, it must be noted that providers who have been paid prior to discovery of the misrepresentation are not obligated to return the payments to the insurance carrier. The liability for reimbursement is properly directed towards the insured not, for instance, the doctor or hospital that provided a service.

John: Allison, what is the difference between rescinding a policy and denying a claim?

Allison: A material factual misrepresentation made in an application for insurance may justify rescission if the insurer relied upon it to determine whether or not to issue the policy. When a policy is rescinded, it is considered void and never to have existed. Therefore, any claims made for the duration of the policy would not be covered.

When an insurance carrier chooses to deny a specific claim, the policy is still in full force and effect. The insurer is not required to return the premium. The insurer can utilize its right to deny a first party claim based on a post loss material misrepresentation made by an insured or any party making a claim.

The denial can be made based on the fraud or concealment provision of the policy. The policy can be rescinded or voided based on post loss misrepresentations as in the case of *Longobardi versus Chubb*.

The misrepresentation must be knowing. However, a motive to defraud does not have to be established. The statement must be material, such as padding a claim. The insurance carrier only needs to prove material misrepresentations by a preponderance of the evidence.

John: Gina, what are the insurance carrier's options when seeking to void or rescind a policy?

Gina: When a carrier discovers a misrepresentation that affects the premium, it may opt to continue with the coverage by seeking payment of the increased premium from the insured. However, if the carrier wishes to move forward with rescission there are two ways to proceed.

An insurance carrier's options when seeking to void or rescind a policy include simply notifying the policy holder of the rescission and returning the premium or, alternatively, filing for declaratory relief. The latter is clearly the more aggressive, proactive approach. The former places the ball in the insured's court, after which he or she may decide to either accept the consequences of rescission or file for declaratory relief.

Often times when there is no exposure to the insured, for instance when an insured is not actually seeking benefits, acceptance of the rescission without the necessity of court intervention makes more sense. However, where the exposure to the insured is great or where there are other claims, such as PIP, brought by providers by way of assignment, it might be worth the risk to retain counsel to bring an action for declaratory relief.

In that instance, the parties will ask the court to determine whether there are grounds for rescission. That is, is the rescission proper under the circumstances? Was there a misrepresentation? Was it material?

Keep in mind that these questions are generally decided by the court. However, under certain circumstances the question of whether or not a misrepresentation was made may be presented to a jury for consideration.

For instance, where residency is at issue in a circumstance where a policy holder neglected to disclose a person residing in the household, whether or not that person is a resident of the household may present an issue of fact sufficient for jury determination.

John: Allison, what investigatory tools are available to an insurance carrier when seeking to void or rescind a policy?

Allison: First, insurance carriers have to be able to identify policy misrepresentations. This requires that claims adjusters be able to identify issues such as undisclosed operators, use of the vehicle, such as personal versus commercial, residents of the household, and the garage location of the vehicle.

Identifying these red flags early in the claims process will allow for a strong investigation. Typical red flags include identifying who's driving the insured vehicle, what is an out of state auto accident with out of state passengers? Did the claimant or insured treat with out of state doctors? How many cars are on the policy and how many drivers?

Once a red flag is identified a carrier can conduct a statement of the parties involved. The SIU department can conduct an investigation and obtain facts and information such as a police report, medical records, E ZPass information, utility bills, cell phone records, and other proof of residency. The most effective way to establish a statement is an examination under oath.

The insured is required to cooperate with the investigation and to produce their documents. The examination under oath of an insured and claimants under the policy can be taken and witnesses should be sequestered during their testimony.



John: Thank you both very much for joining us today.

Allison: Thank you.

John: That was Gina Stanziale and Allison Koenke from the law firm of [Methfessel & Werbel](#), their Edison, New Jersey office. Special thanks to today's producer, Frank Vowinkel.

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If you have any suggestions for a future topic regarding an insurance law case or issue please email us at lawpodcast@ambest.com. I'm John Czuba, and now this message.

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