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TOPIC: Court Holds Misrepresentation in Life Insurance Application is Jury Issue

CITATIONS: *Mitchell v. Modern Woodmen of America*, 2014 WL 6983293, No. 2:10–cv–00965–JEO. (United States District Court, N.D. Alabama, Southern Division Dec. 10, 2014); Federal Rules of Civil Procedure No. 56(a).

SUMMARY: In a case involving a life insurer's denial of claims for misrepresentations on the application and subsequent statements made to a telephone interviewer for the insurer, the trial court held that the misrepresentations were issues to be decided by a jury, and not by a judge.

RELEVANCE: This decision reminds life insurance professionals how important it is for insureds to provide complete and accurate information to underwriters regarding the insured's financial details. The insured's failure to provide complete financial underwriting information in the application led to the litigation over Modern Woodman's liability for the death benefit.

The case also is a reminder that generally courts grant motions for summary judgment on a very conservative basis. If the motion is denied, the result is a jury trial where the issues are litigated. Since if a motion is granted no trial occurs, a court in tight fact patterns will almost always deny the motion.

Courts generally feel it is better to err in favor of a decision to go to trial. Either party may ultimately win at the trial, and a denial of the motion for summary judgment does nothing to ultimately decide the relevant merits of the parties' claims.

FACTS: This case involves two insurance certificates [life policies] issued by Modern Woodmen of America on the life of Stephanie Mitchell in 2008. The first provided $1 million in life insurance coverage and $350,000 in accidental death coverage. The second provided an additional $1 million in life insurance coverage.

In March 2009, less than a year after Modern Woodmen issued the certificates, Stephanie Mitchell died from gunshot wounds to the head. Her death was ruled a homicide. Tom Mitchell, Stephanie's husband, was the principal beneficiary of both insurance certificates. In May 2009, he submitted a claim to Modern Woodmen for benefits under both certificates.

Because Stephanie's death occurred within two years of the issuance of the certificates, Modern Woodmen conducted a claim review. After nearly a year passed with no payment of the claim, Tom Mitchell and Brittany Allred, the contingent beneficiary of both certificates, filed this action against Modern Woodmen for breach of the insurance certificates and for bad-faith refusal to pay the claim for benefits.

Modern Woodmen answered the complaint and asserted a counterclaim seeking a declaratory judgment to allow them to deny the death claims. The basis of the counterclaim was that Stephanie Mitchell failed to give "accurate and complete" answers to the questions on her insurance applications. Fifteen months later, Modern Woodmen issued a second denial citing additional alleged "material misrepresentations" by Stephanie Mitchell.

This action came before the court on three principal motions:

1. The beneficiaries' motion for summary judgment in their favor on their claims against Modern Woodmen for breach of the insurance policies.

2. Modern Woodmen's motion for summary judgment in its favor on all of the claims in Plaintiffs' complaint and on its counterclaim for a declaratory judgment as to whether benefits are payable under the insurance policies.

3. The beneficiaries' motion for a judgment holding that Modern Woodmen proceeded on their claim in bad faith.

The insured worked with her husband in two unincorporated businesses. According to federal income tax records, total income for the business, in 2008, was $4,521. According to state sales tax records, the business had no sales from June 2008 until its closing in November 2008. The plaintiffs contend, however that the business operated on a cash system and that the tax returns are not dispositive of the business's inventory value or sales.

On the first application for life insurance, Stephanie, the insured, stated that she was employed by Mitchell Marine, that her occupation was secretary/housewife, that she kept the books for her husband's businesses, and that she had a "shared income" with her husband. The amount of the shared income was not reflected on the application.

However, Stephanie's husband Tom had also applied for life insurance from the insurer and filed a financial statement in which he represented that he had salary or wages of $280,000 in 2007 and salary or wages of $40,000 to $50,000 year to date. He further represented that he had net business or professional income of $60,000 to $70,000 in 2007 and that his net worth was $3,150,000.

In a telephone interview, Stephanie stated that she performed managerial duties for the companies and worked over 40 hours per week. The interviewer listed her salary as $70,000+ and her husband's income as $80,000+. She also stated she had a "small" insurance policy that she was keeping but did not recall the amount of the policy or the name of the insurance company.

In the second application for coverage, Stephanie answered "No" to the following questions: "Have you applied for life insurance that is currently pending or are you planning on purchasing life insurance with another company?" and "Have you had life or health insurance rejected, rated, postponed, modified, or cancelled?" In reality, she had $1.71 million in life coverage and $500,000 accidental death coverage in force with another insurer.

Within three days of the application in question, she applied for *additional* coverage with other life insurers.

RESULT: On the misstatement of income issue, the court held:

> As noted above, and as both parties acknowledge, the question whether a fact is or is not material is generally a jury question. After carefully reviewing the record, the court concludes that the materiality of Stephanie Mitchell's income and her failure to disclose the "whole truth" about her income in her application is a matter for the jury to decide.

On the misrepresentation of existing and pending coverage issue, the court held:

> Although the materiality of a misrepresentation is generally a jury question, Modern Woodmen's own evidence and argument establish that the misrepresentations in Stephanie Mitchell's first application regarding her other life insurance (existing and applied for) were not material as a matter of law. As previously noted, Modern Woodmen asserts that the maximum amount of life insurance Stephanie Mitchell would have qualified for, given her true income, was $113,025. Therefore, accepting Modern Woodmen's argument in its entirety, Stephanie's representations in her application that she had only $200,000 in existing life insurance and had not applied for any other insurance were not material. Even as represented in her application, she already had more life insurance than she qualified for.

On the matter of bad faith in paying the claim, Modern Woodmen won and received a motion for summary judgment in their favor. The court reached this decision on both the life policy and also the accidental death rider:

> First, to the extent Plaintiffs allege that Modern Woodmen is liable for bad-faith refusal to pay their claim for accidental death benefits, their bad faith claim fails as a matter of law because…. Modern Woodmen had a valid, lawful reason to deny accidental death benefits-namely, Stephanie's representation on her insurance application that she had no existing accidental death coverage when in fact she had $500,000 in accidental death coverage in force with American General, more coverage than Modern Woodmen's underwriting guidelines allow.
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> Second, to the extent Plaintiffs' bad-faith claim is based on Modern Woodmen's refusal to pay their claim for life insurance benefits under the [life policy], Modern Woodmen had a legitimate, debatable reason not to pay those benefits. Because Modern Woodmen had, at the very least, a

> debatable reason to deny Plaintiffs' claim for life insurance benefits under the [life policy], Plaintiffs' bad-faith claim for refusal to pay those benefits—whether couched as "normal" bad faith or "abnormal" bad faith—fails as a matter of law.

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