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Starting Over: Policy Rescission In New York Vs. The UK

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It is an unfortunate fact of life for insurers and insurance coverage defense attorneys that courts often lean the insured's way in matters of policy interpretation. This axiom also carries through in many jurisdictions when insurers accuse the insured of concealing or misrepresenting information during the underwriting process. It is therefore extremely important that insurers know all of the important information about an insured when choosing whether — and on what terms — to underwrite a policy. One way for insurers to ensure that they are not left holding the bag if an insured misrepresents information on its insurance application is to rescind the policy, which voids the contract ab initio. But, what are the circumstances where an insurer can take such measures?


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This important topic has recently been addressed under both New York law and the law of the U.K. Interestingly, these jurisdictions both tend to favor the insurer but take different approaches to policy rescission. While an insurer subject to New York law may rescind a policy for material misrepresentation regardless of whether the insured's misrepresentation was intentional, U.K. law now provides different remedies based on both the insured's conduct and what actions the insurer would have taken had it properly been informed of all of the circumstances surrounding the misrepresentation.


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New York

New York Insurance Code § 305 provides that "[n]o misrepresentation shall avoid any contract of insurance or defeat recovery thereunder unless such 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 such a contract."

In H.J. Heinz Co. v. Starr Surplus Lines Insurance Co., 15cv0631 (W.D. Pa. Feb. 1, 2016), the United States District Court for the Western District of Pennsylvania, applying New York law, set forth the proper standard for rescission of an insurance contract where material facts were omitted from the insured's application. This case was recently affirmed by the Third Circuit Court of Appeals.

Heinz sued Starr Surplus Lines Insurance Company for $25 million for breach of contract, declaratory judgment and bad faith, based on Starr's denial of Heinz's claim under its product contamination policy.

Starr counterclaimed seeking, inter alia, rescission of the policy. The basis of the counterclaim was that Heinz knowingly and in bad faith omitted from its insurance application material information regarding its loss history. Namely, Heinz stated that it had not been the subject of any regulatory complaints within the prior 12 months and had not had any fines assessed it by a regulatory body in the prior three years. It also failed to inform Starr of a 2014 Chinese recall involving its baby cereal products, a 2013 recall involving baby food contaminated with mercury and other smaller losses.

Heinz argued both that the alleged misrepresentations were not material, and that Starr had "actual notice" of the allegedly falsely represented or withheld information.

In December 2015, the court conducted a trial on Starr's counterclaim for rescission. The advisory jury found that there was a material misrepresentation of facts in the insurance application, but that Starr did not prove by clear and convincing evidence that Heinz deliberately omitted material information during the insurance application process. The jury also found that Starr had waived its right to assert a rescission claim by agreeing to sell the policy despite having sufficient knowledge of the misrepresentation.

After the jury reached its conclusions, the district court ruled that the "extraordinary equitable remedy" of rescission was appropriate. It stated that "New York case law instructs that both intentional and unintentional misrepresentations will void a contract of insurance if the misrepresentation is material." The court agreed with the jury that Heinz made material representations of fact, and upheld the jury's conclusion that Heinz did not deliberately omit or remain silent with respect to the information.

The court found, however, that Starr had not waived its right to assert a rescission claim. According to the court, "[w]hile Starr was not 'perfect' in its assessment and underwriting practices, perfection is not the standard," and "Starr acted more than reasonably under the circumstances." The amount of material in the underwriting file that referred to the relevant information "without more, would not trigger a reasonably prudent insurer to follow-up further."

Other New York courts have made clear that a "misrepresentation is material, and thus could warrant rescission by an insurer, if 'had [the fact] been revealed, the insurer or reinsurer would either not have issued the policy or would have only at a higher premium.'" U.S. Underwriters Insurance Co. v. Novel Home Health Care Servs. of N.Y., Corp., No. 14CV3715ARRCLP (E.D.N.Y. Jan. 14, 2016) (citations omitted); see also, Andrew Amer & Linda H. Martin, The Standard of Materiality for Misrepresentations Under New York Insurance Law - A State of Unwarranted Confusion, 17 Conn. Insurance L.J. 415 (2011) (A misrepresentation "is material where it appears that a reasonable insurer would be induced by the misrepresentation to take action which he might not have taken if the truth had been disclosed") (citation omitted). In other words, "the insurer does not have to prove that it would not have issued any policy to the insured, but rather that it would not have issued the specific policy in question. Novel, 2016 WL 5339358, at *4.

United Kingdom

The law of rescission in the U.K. is now governed by the Insurance Act 2015, which received royal assent on Feb. 12, 2015, and applies to all U.K. insurance policies entered into on or after Aug. 12, 2016, including renewals.

Unlike the rule set forth by the Heinz court, the act provides different remedies depending on both the conduct of the insured and what the insurer would likely have done had it known the full facts.

Under the duty of fair presentation portion of the act, which applies only to nonconsumer insurance contracts, "the insured must make to the insurer a fair presentation of the risk." A fair presentation of the risk is one which: 1) discloses "every material circumstance which the insured knows or ought to know," or "failing that, gives the insurer sufficient information to put a prudent insurer on notice that it needs to make further enquiries for the purpose of revealing those material circumstances"; 2) makes the disclosure "in a manner which would be reasonably clear and accessible to a prudent insurer"; and 3) all material representations with respect to facts are "substantially correct," and all material representations "as to a matter of expectation or belief [are] made in good faith." If the insurer does not inquire, however, the insured need not disclose circumstances that diminish the risk, that the insurer knows, ought to know, or is presumed to know, or circumstances as to which the insurer "waives information."

The act defines material circumstances as ones that "would influence the judgment of a prudent insurer in determining whether to take the risk and, if so, on what terms." The act provides examples of material circumstances, including "special or unusual facts relating to the risk," "any particular concerns which led the insured to seek insurance cover for the risk," or "anything which those concerned with the class of insurance and field of activity in question would generally understand as being something that should be dealt with in a fair presentation of risks of the type in question."

The act provides remedies for "qualifying breaches" where the insurer can show that, if not for the breach, the insurer either would not have entered into the contract at all, or would have entered into the contract but only under different terms. A qualifying breach is either: 1) deliberate or reckless (i.e., the insured knew that it was in breach of the duty of fair presentation, or did not care whether or not it was in breach of the duty of fair presentation); or 2) neither deliberate nor reckless.

Schedule 1 of the act provides the insurers' remedies for qualifying breaches. Where the qualifying breach was deliberate or reckless, the insurer may avoid the contract and refuse all claims, and is not required to return any of the premium paid.

The act then considers several circumstances concerning qualifying breaches that were neither deliberate nor reckless. If the insurer would not have entered into the contract at all if it were aware of the true facts, it may avoid the contract, but must return all premium. If the insurer would have entered into the insurance contract on different terms — other than terms relating to the premium — the contract is to be treated as though it had been entered into on those different terms, if the insurer so requires. If the insured would have entered into the contract but charged a higher premium, the insurer is permitted to reduce proportionately the amount to be paid on a claim, using the formula provided by the act.

Which Approach is More Favorable, and to Whom?

The New York approach is simpler in application than that of the U.K., as only two requirements need be met: first, the misrepresentations must be material, and second, knowledge of the misrepresented facts would have led to the insurer's refusal to enter into the contract. Once those requirements are established, the court need not undertake an analysis as to whether the misrepresentations were intentional. Additionally, the Heinz decision makes clear that even where an insurer is imperfect in its underwriting of the policy, as long as it acts reasonably with respect to ascertaining all of the available facts, it will not be deemed to have waived its right to rescind.

On the other hand, policy rescission under U.K. law now requires an analysis both of whether the insured's misrepresentations were intentional, and what actions the insurer would have taken had it been aware of all of the material facts. The various remedies available under the act require courts to undertake a detailed analysis of the intentions of the parties and then a calculation of the proper claim payment.

In both jurisdictions, the burden is on the insured to accurately convey information. For the insurer, however, it appears that New York law is a bit more favorable overall. This is because the insurer need not show whether the breach was intentional. Moreover, under New York law a policy can be rescinded if the insurer can establish that it would not have entered into the contract as written if it were aware of all of the material facts. On the other hand, the new U.K. law provides different remedies based on the insurer's reaction to the misrepresentation, i.e.: 1) the insurer would not have entered into the contract at all; 2) the insurer would have entered into a contract but on different terms; or 3) the insurer would have entered into the contract but charged a higher premium.

The one circumstance in which U.K. law may be more favorable than New York law is where an insured intentionally misrepresents the facts, and the insurer would not have entered into the insurance contract at all had the full facts been known. Under both New York and U.K. law, the policy would be void ab initio; under New York law, however, the insurer would have to return the premium to the insured, while under the new U.K. law, the insurer would not have to return the premium. If an insured unintentionally misrepresented the facts, and the insurer would not have entered into the insurance contract at all had the full facts been known, under both New York and U.K. law the policy would be void ab initio and the insurer must return the premium.

The more favorable attributes of New York law are illustrated in circumstances in which the insurer would still have entered into the contract had it known the correct facts, but would have charged a lower premium or would have changed the terms. In such instances, different remedies are available under U.K. law, whereas in New York, the insured would be entitled to rescission.

The bottom line for insurers is to pay close attention to the application process and to be prepared to articulate the effect and ramifications of a material misrepresentation by an insured. And while both New York courts and U.K. courts can be favorable to an insurer in these situations, there are still issues of proof that an insurer must be prepared to discuss in order to seek rescission of a policy.

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