

UPDATE ON TEXAS LAW ON THE RESCISSION OF INSURANCE POLICIES

INTRODUCTION

Texas courts have long applied a five-factor test in determining whether an insurer can rescind an insurance policy. To rescind a policy, the insurer must prove: “(1) the making of the representation; (2) the falsity of the representation; (3) reliance thereon by the insurer; (4) the intent to deceive on the part of the insured in making same; and (5) the materiality of the representation.”¹

In 1963, the Texas Legislature “charged the Texas Legislative Council with the task of planning and executing a permanent statutory revision to ‘clarify and simplify the statutes and to make the statutes more accessible, understandable, and usable.’”² As part of this ongoing effort, the Texas Legislature adopted Title 5 to the Texas Insurance Code, effective April 1, 2005.³ The 2003 session law states that it “is intended as a recodification only,” with “no substantive change in law . . . intended.”⁴ However, in *Fleming Foods of Texas, Inc. v. Rylander*, the Texas Supreme Court held that “clear, specific language” in a recodified statute that changes prior law must be applied as written.⁵ In the event of a conflict, the latter enactment controls: “We are compelled to conclude that when, as here, specific provisions of a ‘nonsubstantive’ codification and the code as a whole are direct, unambiguous, and cannot be reconciled with prior law, the codification rather than the prior, repealed statute must be given effect.”⁶

The recodified rescission requirements are located in Chapter 705, entitled “Misrepresentations by Policyholders.” Chapter 705 includes three subchapters: general provisions applicable to all insurance policies (sections 705.001-.005); special provisions applicable to life, accident, and health insurance policies (section 705.051); and special provisions applicable only to life insurance policies (sections 705.101-.105). As explained below, the recodified statutes have potentially changed the contours of the five-factor *Mayer* test and arguably eliminated one factor—intent to deceive—altogether. Since numerous courts have applied the *Mayer* test to policies issued after the April 1, 2005 effective date of the recodification,⁷ some with little or no discussion, this article addresses the recodified statutes under the rubric of those five factors.

ELEMENTS OF A RESCISSION CLAIM

Misrepresentation. Not surprisingly, sections 705.004, 705.005, 705.051, and 705.104 all require a rescission-seeking insurer to show that the insured made a misrepresentation in his application.⁸ This is typically the threshold issue for an insurer. If it cannot readily establish a misrepresentation, it has no business seeking rescission.

The reported decisions on this element tend to turn on the specific terms of the application question(s) at issue. For example, in *RLI Insurance Co. v. Gracia*,⁹ the insured applied in 2005 and 2006 for two personal umbrella liability policies.¹⁰ He denied that he had ever “had a citation/conviction for driving under the influence of alcohol or drugs, reckless driving, careless driving . . . , or negligent driving.” As it turned out, the insured had been arrested in 2001 after police officers observed him driving above the speed limit and weaving between lanes. While in police custody, he received both a “Statutory Warning,” which stated that he had been arrested and explained the consequences of his refusal to provide a breath and/or blood sample for examination, and a “Notice of Suspension,” which stated that his driver’s license would be suspended in forty days because of his refusal. The insured was charged with driving under the influence and obstructing a street or highway accessible by the public. The former charge was dismissed when he pled guilty to obstructing a highway.

The insurer filed suit to rescind the policies, and the insured sought summary judgment on the ground that he had not made a misrepresentation. The court granted the insured’s motion, finding that his arrest for driving under the influence was not a “citation” (as he never received “an official summons to appear” or other document requiring him to appear at a certain time and place to defend himself), the application did not inquire about whether he had been “charge[d]” with a driving offense, and he was not “convicted” of “reckless driving” (as he was convicted only of obstructing a highway, which did not require the use of a vehicle).¹¹ *Gracia* thus indicates that courts will carefully scrutinize the questions in the application (which were, after all, selected and drafted by the insurer) to confirm that the insured actually made a misrepresentation.

Reliance. Although reliance is not expressly addressed in Chapter 705, courts have nonetheless continued to require insurers to establish that element under the five-factor *Mayes* test.¹² This element has historically been one of the easiest elements for an insurer to satisfy, as one of its underwriters can testify that the insurer relied on the information it received during the application process and was not aware of any contrary information.¹³ Of course, as earlier decisions made clear, actual knowledge of falsity of the representation is fatal to a showing of reliance.¹⁴

Intent to Deceive. As the author has previously observed, an argument can be made that the recodification eliminated “intent to deceive” as an element of a rescission claim.¹⁵ Section 705.004, entitled “Misrepresentation in Policy Application,” and section 705.051, entitled “Immaterial Misrepresentation in Life, Accident, or Health Insurance Application,” both set forth the elements of a rescission claim, yet neither section mentions intent.¹⁶ In turn, section 705.104 (which applies only to life insurance policies) permits an insurer to rescind such a policy more than two years after its issuance by showing either: (1) it gave notice to the insured of its intent to rescind; or (2) the misrepresentation was material to the risk and “intentionally made.”¹⁷ Since the Texas Legislature clearly knew how to impose an intent requirement, its refusal to include one in the statutes setting forth the elements of a rescission claim—sections 705.004 and 705.051—provides further evidence that intent to deceive is no longer an element of a rescission claim during the first two years a life insurance policy is in force.¹⁸

As section 705.104 permits the rescission of a life insurance policy that has been in force for more than two years upon a showing that the misrepresentation was “intentionally made,” it could be argued that a showing of intent is not required to rescind a policy that has been in force for less than two years. Admittedly, the Texas Supreme Court rejected a comparable argument with respect to an accident and sickness insurance policy in *Union Bankers Insurance Co. v. Shelton*.¹⁹ Importantly, however, the second paragraph of the now-repealed Texas Insurance Code article 3.70-3(A) (2)(a), which was the provision at issue in *Shelton*, stated that the fraud exception in the first paragraph “shall not be construed as to affect any legal requirement for avoidance of a policy . . . during such initial two-year period.”²⁰ Here, on the other hand, none of the current rescission statutes contain a comparable savings clause. Moreover, *Shelton* pre-dates not only the 2003 recodification, which arguably eliminates intent as an element, but also *Fleming Foods* and the other cases cited above which hold that an unambiguous statute must be applied as written, even if it changes the law.

Similarly, insurers can argue that the elements of *Mayes* (including intent to deceive) are not independent of and in addition to these statutes. First, the Texas Legislature was presumably aware of *Mayes* when it enacted the 2003

recodification, yet it neglected to include intent to deceive as an element in the sections governing rescission.²¹ Second, the purpose of the recodification process is to make Texas law more accessible and understandable for all interested parties.²² It is unfair and illogical to require the parties to research prior law and then revive a common-law requirement that the Texas Legislature easily could have included (but elected not to) in a newly enacted statute.²³ Simply stated, it would defeat the purpose of a recodification to require parties to retrieve a common-law requirement that is not within the four corners of a recently recodified statute.

Importantly, however, a post-recodification case squarely addressing the issue held that intent to deceive is still an element of a rescission claim.²⁴ In *Medicus Insurance Co. v. Todd*, the defendant insured submitted a two-page application for medical malpractice insurance in which he denied that he had ever been the subject of an investigation by a licensing authority and represented that he had been a party only to four malpractice actions in the past five years. In fact, the insured had been investigated twice by the Texas Medical Board and had been a party to six lawsuits at the time of his application. Although the underwriter recommended denying coverage due to the insured’s claims history, the insurer’s chief underwriter and president rejected the recommendation, and the insurer issued a one-year policy.

In connection with the renewal of this policy, the insurer requested the insured to complete its official 19-page application, which included a question about his claims history that was not limited to the last five years, and pre-filled the information it had on the insured. The insured did not supplement the application with the eight additional lawsuits that had been filed against him or the three pre-suit demand letters he had received, and the insurer renewed the policy for another year. In a subsequent lawsuit, the attorney for one of the insured’s patients asserted that the insured had been a party to 15 lawsuits and the subject of two investigations by the Texas Medical Board. The insurer then informed the insured it was rescinding the policy and filed a declaratory-judgment action to confirm that the policy was void. The jury found in the insured’s favor and awarded him his attorney’s fees.

On appeal, the insurer contended that it had two alternative remedies to rescind the policy: (1) the common-law remedy, which required a showing of intent to deceive; and (2) the statutory remedy under section 705.004, which did not require a showing of intent.²⁵ The insurer claimed that it invoked only the statutory remedy and, thus, was not required to establish the common-law requirement that the insured intended to deceive it into issuing the policy.²⁶ The court of appeals disagreed, finding that the insurer was required to prove intent.²⁷

As part of its analysis, the court acknowledged that, even

though section 705.004 and its predecessors did not expressly require a showing of intent to deceive, the Texas Supreme Court had imposed (and continued to impose) that requirement.²⁸ The court then observed:

Section 705.004, in its different codifications, is now 110 years old. Although the statute has never expressly required the insurer to prove the insured intended to deceive the insurer with a misrepresentation in the policy application, the courts of Texas have consistently held that an insurer may not rescind a policy due to a misrepresentation in an insurance application unless the insurer proves the insured intended to deceive the insurer with the misrepresentation. We cannot vary from this long history of case law imposing this duty upon insurers. We conclude “the intent to deceive on the part of the insured in making” a misrepresentation in an application for insurance is an element the insurer must prove to obtain a declaratory judgment that a policy is void due to the misrepresentations.²⁹

Although it acknowledged that section 705.004 did not expressly require a showing of intent to deceive, the *Todd* court did not address *Fleming Foods* or any of the other statutes enacted as part of the recodification that included an intent requirement, and its reliance on section 705.004’s predecessors was likely misplaced.³⁰

In *Hinna v. Blue Cross Blue Shield of Texas*, the application at issue had been completed after the effective date of the recodification. The application provided that “fraud or any intentional misrepresentation of a material fact” could result in rescission, which may explain why the court applied the five-factor test from *Mayes*, without further discussion.³¹ Since the defendant insurer was unable to satisfy either of the two previously recognized situations in which intent may be established as a matter of law—when the insured warrants the facts in the application or has colluded with the insurance agent—the court declined to enter summary judgment on the insured’s intent to deceive.³²

In *Halsell II*, the federal district court took the rather rare step of finding intent to deceive as a matter of law. In that case, the insurer sought summary judgment on its rescission claim and the beneficiary’s counterclaims. The beneficiary did not file a response, presumably because his counsel withdrew after the issuance of *Halsell I*. (*Halsell I* is addressed below). As a result, the court entered summary judgment in the insurer’s favor. Even though the policy at issue was issued on February 1, 2008, the court applied the five-factor test from *Mayes* without any analysis; it then proceeded, however, to find intent to deceive as a matter of law:

Here, United of Omaha presents Halsell’s misrepresentations on three occasions to show

his intent to deceive United. Specifically, United of Omaha notes that Halsell made his declaration that he had not received treatment for drug/substance abuse below a statement that read that an affirmative answer to such a question would mean that the applicant “is not eligible for Term Life Express coverage.” Furthermore, Halsell declared: “All answers in this application are true and complete and will be relied on by United of Omaha to determine insurability.” In addition, United of Omaha notes that Defendant James D. Halsell sold his son Justin the policy, paid for the policy himself, and received a commission of 130% of the policy’s first year premium. United of Omaha has presented evidence of Justin Halsell’s intent to deceive the insurer, while Defendant Halsell has provided no evidence on summary judgment to create an issue of material fact on this issue. The Court notes that Defendant has done nothing to negate United of Omaha’s evidence that the insured intended to deceive the insurer in light of the limited circumstances under which the Court may find an intent to deceive as a matter of law.³³

Although it is not clear from the opinion, the court may have relied on the “collusion with the insurance agent” exception³⁴ to the general rule that intent to deceive cannot be found as a matter of law. Somewhat surprisingly, three other courts have recently found intent to deceive as a matter of law, with one decision based on procedural grounds, one decision bereft of any analysis as to the insured’s intent, and one decision based on seemingly uncontroverted deposition testimony.³⁵

In sum, an insurer should argue that intent to deceive is no longer an element of a rescission claim. Nonetheless, the insurer should be prepared to establish that such element is satisfied.

Materiality. Section 705.004 provides that, to establish a policy is void or voidable, the insurer must show the matter misrepresented: “(1) was material to the risk; or (2) contributed to the contingency or event on which the policy became due and payable.” Both of these tests are questions of fact.³⁶ Section 705.004(b) is in the disjunctive, meaning that an insurer need only prove one of the two tests.³⁷

In *Hinna*, the court found that the insured’s failure to disclose her history of migraine headaches was material as a matter of law, even though a report from the insurer’s risk management committee indicated that the insurer would have issued coverage with an exclusion for migraine headaches, meaning that the liver-related claims at issue would have been covered:

The summary judgment record conclusively

establishes that plaintiff's misrepresentations were material to the risk because defendant assumed the risk associated with plaintiff's history of migraines when it issued the policy. See *Robinson*, 569 S.W.2d at 30. While defendant very well may have issued plaintiff a policy that would have covered the claims relating to plaintiff's liver condition even if it had known of her history of migraines, it would not have issued the particular policy it did issue. To accept plaintiff's argument that her misrepresentations were not material because, had they been known, only migraine headaches would have been excluded, the court would have to read the "or" out of section 705.004(b) of the Texas Insurance Code. Plaintiff's reading of section 705.004(b) would require an insurer seeking to establish the defense of misrepresentation to show *both* that the misrepresentation was material to the risk *and* that it contributed to the contingency or event on which the policy became due and payable. The Texas Supreme Court has squarely rejected such a reading of section 705.004(b). See *Robinson*, 569 S.W.2d 28. Thus, defendant has established that plaintiff's misrepresentations were material to the risk.³⁸

In *Gouverne v. Care Risk Retention Group, Inc.*, the defendant insurer sought to rescind a medical malpractice insurance policy due to the plaintiff insured's failure to disclose a potential malpractice claim on his application. The insurer sought summary judgment on the ground that the plaintiff's misrepresentation satisfied both of the tests in section 705.004. The court nonetheless applied the five-factor *Mayes* test, noted that fact issues "generally exist" on materiality and intent to deceive, and found a fact issue on intent based on an email from the patient that purportedly led the plaintiff to believe she would not sue him.³⁹

Section 705.004 does not apply to a life insurance policy "(1) that contains a provision making the policy incontestable after two years or less; and (2) on which premiums have been duly paid."⁴⁰ Thus, if section 705.004 is inapplicable, the materiality element emanates from section 705.051, which applies only to life, accident, and health insurance policies. Section 705.051 provides:

A misrepresentation in an application for a life, accident, or health insurance policy does not defeat recovery under the policy unless the misrepresentation:

- (1) is of a material fact; and
- (2) affects the risks assumed.⁴¹

risk." Therefore, if an underwriter testifies that the insurer would not have issued the policy at issue if it had known the true facts, then the insurer can presumably establish materiality under both section 705.004 and section 705.051.

Moreover, the requirement in subsection (2) that the misrepresentation "affects the risks assumed" may have an impact in those cases in which the insurer would have issued coverage but charged a higher premium or (in the disability or health insurance context) included exclusions for one or more conditions. In line with this reasoning, a handful of Texas courts have found that a misrepresentation is not material if the insurer would have issued the policy but charged a higher premium.⁴² Section 705.051(2), however, permits an insurer to argue that a rating or exclusion is material because the underlying misrepresentation "affects the risks assumed."

Two recent cases have addressed section 705.051.⁴³ In *Vasquez v. ReliaStar Life Insurance Co.*, the insured and the trustee of the trust that was to own the policy asserted in the application that the insured's net worth was \$2.4 million, that her annual income and interest totaled \$150,000, and that she had never declared bankruptcy. Following the insured's death, the insurer conducted its contestable investigation, which revealed that the insured had previously declared bankruptcy, had no assets, and did not receive any income other than Social Security payments. In response to the sole question in the charge, which tracked section 705.051, the jury found that the application at issue contained misrepresentations that were of a material fact and affected the risk assumed. The plaintiff trust appealed, contending that the insured's false statements did not have any bearing on her health or death. In response, the insurer asserted that nothing in the plain language of section 705.051 required that the misrepresentation involve the insured's health or life expectancy, and the court of appeals observed:

We agree. Had the Legislature intended to limit the meaning of the "affects the risks assumed" prong in section 705.051, it would have utilized similar language as it used in subsection 705.004(b)(2), which permits the insurer to void a policy pursuant to a misrepresentation provision if, among other results, the insurance applicant's misrepresentation "contributed to the contingency or event on which the policy became due and payable." Compare TEX. INS. CODE. ANN. § 705.051, with *id.* § 705.004(b)(2) (West 2009).⁴⁴In *Nguyen*, the insured (who did not speak, read, or write English) denied any adverse health history, and the defendant insurer issued the policy as requested on June 9, 2008. The insured was diagnosed with lung cancer eight days later, and she died from the cancer on September 8, 2008. The insurer conducted a contestable investigation, found that the insured had a history of lung problems dating to September 2007, and elected to rescind the policy. The beneficiary sued the insurer and the agent who took the application. The insurer sought summary judgment on (among other grounds) its entitlement pursuant to

26 Subsection (1) is consistent with the requirement in section 705.004(b)(1) that the misrepresentation be "material to the

section 705.051 to rescind the policy based on the insured's misrepresentations. The trial court sustained the insurer's procedural objections to the summary-judgment evidence of the beneficiary, who had failed to specifically reference where a material issue of fact could be found in the 650 pages of evidence she submitted.

The court of appeals affirmed, finding that the trial court did not abuse its discretion in refusing to consider any of the beneficiary's evidence.⁴⁵ Since the insurer nonetheless had the burden of establishing its entitlement to summary judgment, the court briefly examined the insurer's claim that section 705.051 authorized it to rescind the policy based on the insured's misrepresentations in the application. The court ruled that the beneficiary's invocation in her reply brief of the five-factor *Mayer* test was too late, and in light of the beneficiary's failure to show how the insurer did not meet its burden, the court of appeals affirmed the trial court's ruling.⁴⁶

OTHER RESCISSION-RELATED ISSUES

Notice of Intent to Rescind. Section 705.005 provides that the insurer may use a misrepresentation defense "only if the defendant shows at trial that before the 91st day after the date the defendant discovered the falsity of the representation, the defendant gave notice that the defendant refused to be bound by the policy" to the insured or his beneficiaries.⁴⁷ If section 705.005 is applicable, unless the issue is established as a matter of law, an insurer must submit a special issue to the jury regarding this notice requirement. For example: "Do you find from a preponderance of the evidence that the Insurer gave notice to the Insured that it refused to be bound by the Policy on or before the 91st day after discovering the falsity of the representation?"

Courts interpreting section 705.005's predecessor held that the failure to satisfy this requirement prevented an insurer from obtaining judicial approval of its rescission.⁴⁸ Thus, in those situations in which section 705.005 applies, an insurer must give notice that it is refusing to be bound by the policy to the insured or his beneficiary within 91 days of its receipt of documents or other information showing that the insured made a misrepresentation.⁴⁹

Importantly, however, Subchapter C to Chapter 705, entitled "Special Provisions Related to Life Insurance Policies," includes a statute rendering section 705.005 inapplicable to certain life insurance policies:

Subchapter A [which includes section 705.005] does not apply to a life insurance policy:

- (1) that contains a provision making the policy incontestable after two years or less; and
- (2) on which premiums have been

duly paid.⁵⁰

Therefore, if a life insurance policy provides it is incontestable after two years or less, an insurer need not provide the 91-day notice required by section 705.005. Otherwise, an insurer must give notice within 91 days of discovering the falsity of the insured's representation that it will not be bound by the policy.

The question then becomes whether the contestable clause at issue satisfies section 705.105 by "making the policy incontestable after two years or less." Section 705.005 and section 705.105 both took effect on April 1, 2005. Two cases have examined the interplay between these two sections.⁵¹

In *Halsell I*, the relationship between section 705.005 and section 705.105 was squarely at issue.⁵² The defendant beneficiary sought summary judgment on the ground that the insurer did not comply with the 91-day notice requirement in section 705.005, yet the court excused the insurer's failure to do so based on a contestable clause stating:

Except for non-payment of a premium, we will not contest the validity of this policy after it has been in force during the lifetime of the insured for two years from the issue date.⁵³

Thus, the court ruled that, since the insurer had contested its obligations within two years of its issuance of the policy, it could assert its rescission claim.⁵⁴

In *Myers*, the beneficiary of a life insurance policy sued the insurer, and the insurer asserted a counterclaim to rescind the policy. The trial court entered judgment in the insurer's favor, and the beneficiary contended on appeal that the trial court improperly refused to submit a jury instruction on whether the insurer had complied with the 91-day notice requirement in section 705.005.⁵⁵ After acknowledging that "[s]tatutory notice is an essential element of a defense based on misrepresentation or rescission," the court of appeals reversed, finding that there was evidence in the record that the insurer's notice was given almost two months too late.⁵⁶ *Myers* does not, however, include any indication that the insurer had argued that the policy at issue included a two-year contestable clause that rendered the 91-day notice requirement inapplicable, and since the appellate briefs for that case are not available online, it is unclear whether the insurer: (1) had failed to include a compliant contestable clause; or (2) did not recognize the potential applicability of section 705.105.

Subchapter A of Chapter 1101 of the Texas Insurance Code includes a listing of the provisions that insurers must include in all life insurance policies issued or delivered in Texas.⁵⁷ Section 1101.006 is entitled "Incontestability." It provides:

- (a) Except as provided by Subsection
- (b), a life insurance policy must provide

that a policy in force for two years from its date of issue during the lifetime of the insured is incontestable, except for nonpayment of premiums.

(b) At the option of the company, a life insurance policy may provide that the policy may be contested at any time for violation of policy conditions relating to naval and military service in a time of war.⁵⁸

This statute is still in force, and there do not appear to be any cases addressing the interplay between section 705.105 and section 1101.006.

Perhaps the key case interpreting the predecessor statute to section 705.105 is *Protective Life Insurance Co. v. Russell*.⁵⁹ In *Russell*, the trial court had entered summary judgment in the beneficiary's favor. On appeal, she sought to uphold the judgment on the ground that the insurer had failed to give her timely notice of its rescission. The Tyler Court of Appeals affirmed, stating:

[The beneficiary] argues that article 21.35 [i.e., the predecessor to section 705.105] is inapplicable to the case at bar because [the insurer's] policy failed to include the express language required by article 21.35. The incontestability clause [the insurer] included in the policy stated “[w]e cannot bring any legal action to contest the validity of this policy after it has been in force two years, except for failure to pay premiums, unless fraud is involved.” [The beneficiary] contends that this clause is illegal because it purports to reserve a right to assert fraud more than two years after the date of the policy. In support of this argument, [the beneficiary] relies on *American Nat'l Insurance Company v. Tabor*, 111 Tex. 155, 230 S.W. 397 (1921) and *National Life & Accident Insurance Company v. Taree*, 8 S.W.2d 291 (Tex. Civ. App.—El Paso 1928, writ dism'd w.o.j.).

In *Tabor*, the incontestability clause at issue stated “[t]his policy shall be incontestable after two years from its date of issue for the amount due provided premiums have been duly paid, except for fraud.” *Tabor*, 230 S.W. at 398. The incontestability clause in *Taree* stated “[a]fter this policy shall be in force for two full years from the date hereof, it shall be incontestable, except for nonpayment of premiums, fraud, or misstatement of age, subject to the restrictions as to military or naval service as contained herein.” *Taree*, 8 S.W.2d 291-92. The *Tabor* and *Taree* courts held that because the statutes provided that an incontestability clause must

be absolute, the incontestability clauses in those cases were invalid and ineffective; therefore, the statute which exempted life insurance companies from providing notice within ninety days was inapplicable.

The same rules apply to this case. The incontestability clause [the insurer] chose to use in its policy was not absolute because it allowed [the insurer] to contest a claim after two years for fraud; therefore, it was invalid and ineffective. Since [the insurer] did not comply with the time constraints regarding notice of [the insured's] alleged misrepresentation as a defense to the claim, [the insurer] waived its right to assert misrepresentation as a defense.⁶⁰

Thus, unless and until section 1101.006 is amended to include a fraud exception, an insurer should give notice of its rescission of a policy, including a fraud exception within 91 days of its discovery of the falsity of the material misrepresentation at issue.

Contest Requirement. Like the majority of jurisdictions, Texas requires an insurer to actually bring an action to rescind the policy or raise the misrepresentation defense within the contestable period. The rule is set forth in *Trevino v. American National Insurance Co.*,⁶¹ in which the Texas Supreme Court stated:

The language of the incontestable clause and of the statute in the use of the words “contested” and “incontestable” contemplates and intends to require the institution within the specified period of a proceeding in court to cancel the policy on account of original invalidity or the filing, within that period in a suit brought on the policy, of an answer setting up a ground of original invalidity to defeat recovery.⁶²

Two courts have recently recognized, however, that the inclusion of “during the lifetime of the insured” in the 1963 amendment of section 1101.006(b)'s predecessor means that a life insurance policy *never* becomes incontestable where the insured dies within two years of the policy's issuance.⁶³

Attachment of Application. Section 705.103, which applies only to life insurance policies, states that such a policy “must be accompanied by a copy of: (1) the policy application; and (2) any questions and answers given in connection with the application.”⁶⁴ There do not appear to be any recent opinions addressing the attachment requirement. However, suffice it to say that the application answers on which the rescission claim is based must be attached to the policy at the time it is delivered to the insured. Misrepresentations in other documents (such as the paramedical examiner's form, the broker's statement, or the telephone interview with the insured) that are not attached to the policy cannot serve

as the basis of the rescission claim, although they may be admissible on other issues, such as intent to deceive.

Rescission After Two Years. As noted above, section 705.104 by its terms permits the rescission of a life insurance policy that has been in force for more than two years upon a showing that the misrepresentation was “material to the risk” and “intentionally made.” There are two recent cases citing section 705.104.⁶⁵ In *Federated Life Insurance Co. v. Jafreh*, an insurer attempted to rescind a life insurance policy for fraud outside the two-year contestable period. Although the opinion is not entirely clear, the insurer’s declaratory-judgment claim for rescission failed in the district court, and the beneficiary ultimately recovered the policy proceeds, 18% penalty interest, pre- and post-judgment interest, attorney’s fees, and costs.

On appeal, the insurer argued that section 705.104 allowed it to contest the policy for fraud even after the expiration of the contestable period. After observing that section 705.104 “allows the insurer to contest a life insurance policy two years after its date of issue provided the insurer shows the misrepresentation was material and intentionally made,” the Fifth Circuit nonetheless determined that section 705.104 was inapplicable because it did not take effect until April 1, 2005, meaning that the policy at issue was incontestable after two years.⁶⁶

In *Massachusetts Mutual Insurance Co. v. Mitchell*, the court addressed the beneficiary’s motion to dismiss, and cited section 705.104 and *Jafreh* in support of its conclusion that the insurer had stated a claim for relief:

If [the insured] applied or consented to the policies at issue, the Texas Insurance Code explicitly allows insurers to rescind life insurance policies even after two years if the insurer proves material, intentional misrepresentations were made in obtaining the policy.⁶⁷

The contestable clause required by section 1101.006(a) is not fatal to this analysis. If a life insurance policy contains the required contestable clause, the insured will likely argue the terms of his agreement with the insurer (i.e., his life insurance policy) prevent the insurer from rescinding the policy after the premiums have been paid for two years, regardless of the effect of section 705.104. If the contestable clause is construed as an absolute bar to any challenge to a life insurance policy that has been in force for two years, then section 705.104 (which applies to only life insurance policies) is thereby rendered meaningless, as its application is limited to situations in which a policy has been in force for over two years. To give section 705.104 some meaning, it must be interpreted as constituting an exception to the contestable clause.⁶⁸

CONCLUSION

Even though Chapter 705 sets forth the applicable standards for the rescission of an insurance policy, many Texas courts have continued to apply the five-factor *Mayer* test, including the application of one element—intent to deceive—that cannot be found in the four corners of either section 705.004 or 705.051. This continued reliance on a common-law test creates unnecessary uncertainty for both insurers and insureds in cases involving a rescission claim. In order to effectuate the stated purpose of the recodification process, the purpose being to make Texas law more accessible and understandable for all interested parties, courts should derive the required elements of a rescission claim from the provisions of Chapter 705 as written and without resort to common-law elements that are not identified in that chapter.

1 *Mayer v. Mass. Mut. Life Ins. Co.*, 608 S.W.2d 612, 616 (Tex. 1980). Although *Mayer* was not the first case to articulate these factors, it is perhaps the most oft-cited case associated with them.

2 TEX. GOV’T CODE § 323.007(a).

3 Act of May 22, 2003, 78th Leg., R.S., ch. 1274, §§ 1-28, 2003 TEX. SESS. LAW SERV. 3611-4139 (Vernon).

4 Act of May 22, 2003, 78th Leg., R.S., ch. 1274, § 27, 2003 TEX. SESS. LAW SERV. 3611, 4139 (Vernon).

5 6 S.W.3d 278, 284 (Tex. 1999). After *Fleming Foods* was decided, the Texas Legislature amended the Tax Code provision at issue. See *Levy v. OfficeMax, Inc.*, 228 S.W.3d 846, 849 (Tex. App.—Austin 2007, no pet.) (citing Act of June 2, 2003, 78th Leg. R.S., ch. 1310, § 86, 2003 TEX. GEN. LAWS 4748, 4782).

6 6 S.W.3d at 286. Although the Texas Legislature disagreed with this result and passed a bill in 2001 that would have overruled *Fleming Foods*, Governor Rick Perry vetoed it. See Veto Message of Gov. Perry, Tex. H.B. 2809, 77th Leg., R.S. (2001).

7 See, e.g., *Medicus Ins. Co. v. Todd*, 400 S.W.3d 670, 678 (Tex. App.—Dallas 2013, no pet.); *Tex. Farm Bur. Mut. Ins. Co. v. Rogers*, 351 S.W.3d 103, 107 (Tex. App.—San Antonio 2011, pet. denied); *Temcharoen v. United Fire Lloyds*, 293 S.W.3d 332, 341 (Tex. App.—Eastland 2009, pet. denied); *Benbow v. Liberty Mut. Fire Ins. Co.*, No. A-12-CV-1164 LY, 2014 WL 690621, at *2 (W.D. Tex. Feb. 21, 2014); *United of Omaha Life Ins. Co. v. Halsell*, No. SA-08-CV-1007-XR, 2010 WL 376428, at *3 (W.D. Tex. Jan. 25, 2010) (*Halsell II*); *Great Lakes Reins. (UK) PLC v. S. Marine Concepts, Inc.*, No. G-07-276, 2008 WL 6523861, at *3 (S.D. Tex. Oct. 21, 2008); *Gouverne v. Care Risk Retention Group, Inc.*, No. 2-07-206, 2008 WL 2065835, at *4 (S.D. Tex. May 13, 2008); *Hinna v. Blue Cross Blue Shield of Tex.*, No. 4:06-CV-810-A, 2007 WL 3086025, at *3 (N.D. Tex. Oct. 22, 2007).

8 TEX. INS. CODE §§ 705.004(b), 705.005(b), 705.051, 705.104.

9 No. 3:06-CV-1447-M, 2007 WL 2428599 (N.D. Tex. Aug. 28, 2007).

10 Even though the insured applied for at least one (if not both) of these policies after the April 1, 2005 effective date of the recodification, the court did not discuss any of the recodified statutes in its opinion.

11 *Id.* at *3-4. Not surprisingly, however, other courts have found a misrepresentation where the answer is indisputably false. See, e.g., *Perez v. Old Am. County Mut. Fire Ins. Co.*, No. 14-09-00456-CV, 2010 WL 3168389, at *2 (Tex. App.—Houston [14th Dist.] Aug. 12, 2010, pet. denied) (finding that the insured had made a misrepresentation in failing to disclose his 17-year-old daughter in response to the insurer's questions about possible drivers and household residents over the age of 15).

12 See, e.g., *Halsell II*, 2010 WL 376428, at *4 (“Reliance is established when the insurer does not know the representations are false.”).

13 See *id.* (finding evidence of reliance as a matter of law).

14 See *Koral Indus. v. Sec.-Conn. Life Ins. Co.*, 802 S.W.2d 650, 651 (Tex. 1990) (noting that an insurer's fraud defense is destroyed by “actual knowledge of the misrepresentations”).

15 See Andrew C. Whitaker, *Rescission of Life Insurance Policies in Texas—Time to Correct Some Old Errors*, 59 BAYLOR L. REV. 139 (2007); Andrew C. Whitaker, *Rescission of Life, Accident and Health Insurance Policies in Texas—The Rules Have Changed*, 9 J. TEX. INS. LAW 2 (2008)

16 Further support for the conclusion that intent need not be shown to rescind a life insurance policy may be found in the differences between section 705.004 and section 705.003, which is entitled “Misrepresentation in Proof of Loss or Death.” Both of these sections establish a general rule that a policy provision stating that a misrepresentation makes the policy void or voidable has no effect and is not a defense in a suit brought on the policy. TEX. INS. CODE §§ 705.003(a), 705.004(a). With respect to a misrepresentation in proof of loss or death, the general rule is inapplicable if the insurer establishes that the misrepresentation was (among other requirements) “fraudulently made.” *Id.* § 705.003(b); see also *Gotham Ins. Co. v. Warren E&P, Inc.*, ___ S.W.3d ___, No. 12-0452, 2014 WL 1190049, at *5 (Tex. Mar. 21, 2014) (noting that section 705.003 “allows misrepresentation clauses to render insurance policies void or voidable only for fraudulent, material misrepresentations that mislead insurers into waiving or losing defenses”). In contrast, section 705.004(b) does not expressly require a showing of fraud with respect to a misrepresentation in an application for an insurance policy.

17 TEX. INS. CODE § 705.104.

18 See *Iliff v. Iliff*, 339 S.W.3d 74, 81 (Tex. 2011) (“Because section 154.066 is unambiguous, we decline to read into the statute an extra proof requirement that the Legislature did not express.”); see also *Meritor Auto., Inc. v. Ruan Leasing Co.*, 44 S.W.3d 86, 90 (Tex. 2001) (“Ordinarily where the Legislature has used a term in one section of a statute and excluded it in another, we will not imply the term where it has been excluded.”); *Smith v. Baldwin*, 611 S.W.2d 611, 616 (Tex. 1980) (observing that, where proof of intent was required by some sections of the DTPA but not by others, intent would not be implied where it had been excluded).

19 889 S.W.2d 278, 281 (Tex. 1994).

20 TEX. INS. CODE Art. 3.70-3(A)(2)(A) (repealed).

21 See *Gen. Servs. Comm'n v. Little-Tex Insulation Co.*, 39 S.W.3d 591, 596 (Tex. 2001) (observing that “the Legislature is presumed to be aware of case law relevant to statutes it amends or enacts”); *McCullough v. McCullough*, 212 S.W.3d 638, 642 (Tex. App.—Austin 2006, no pet.) (“We also are to presume that the legislature enacted a provision with knowledge of the background law and awareness of existing law.”); see also *Iliff*, 339 S.W.3d at 80 n.3 (citing *Fleming Foods* in support of the proposition that “the doctrine of legislative acceptance is inapplicable when courts are presented with an unambiguous statute”).

22 See TEX. GOV'T CODE § 323.007(a) (providing that the purpose of the statutory revision program “is to clarify and simplify the statutes and to make the statutes more accessible, understandable, and usable”).

23 See *Fleming Foods*, 6 S.W.3d at 284 (noting that “the citizens of Texas must be able to look with confidence to existing law as written”); see also *Fitzgerald v. Advanced Spine Fixation Sys., Inc.*, 996 S.W.2d 864, 866 (Tex. 1999) (noting that “ordinary citizens should be able to rely on the plain language of a statute to mean what it says”).

24 See *Todd*, 400 S.W.3d at 679.

25 *Id.* at 676-77.

26 Somewhat curiously, however, the insurer asserted on page 15 of the Appellant's Brief (which is available on the court of appeals' website) that it “sought to void the policy issued to [the insured] on two separate grounds: the common law basis for voiding a policy and the statutory basis for voiding a policy provided by TEX. INS. CODE § 705.003.”

27 *Id.* at 679 (observing, based largely on its analysis of *Shelton*, that “there is only one cause of action for rescinding a policy due to misrepresentations in the application; that is, by application of both the relevant statutes and the common law, which includes the insured's intent to deceive”).

28 *Id.* at 677-78.

29 *Id.* at 679.

30 See *Cont'l Cas. Ins. Co. v. Functional Restoration Assocs.*, 19 S.W.3d 393, 399 (Tex. 2000) (concluding that, where statutes enacted as part of the ongoing statutory revision program were unambiguous, “we need not look to the prior law in determining legislative intent; instead, we may presume that the Legislature intended the plain meaning of its words”).

31 2007 WL 3086025, at *3.

32 *Id.* at *4-5.

33 2010 WL 376428, at *4 (record citations omitted).

34 See *Washington v. Reliable Life Ins. Co.*, 581 S.W.2d 153, 160 (Tex. 1979) (noting that “strong evidence of collusion” between an insured and the agent might serve to establish intent to deceive as a matter of law).

35 See, e.g., *Perez*, 2010 WL 3168389, at *2 (finding intent to deceive as a matter of law on the basis of deemed admissions); *Benbow*, 2014 WL 690621, at *2 (entering summary judgment on the insurer's rescission claim where a convicted felon had obtained homeowners' coverage on a house he did not own); *Great Lakes Reins.*, 2008 WL 6523861, at *3 (granting summary judgment on intent based on the deposition testimony of the insured's captain).

36 TEX. INS. CODE § 705.004(b)-(c).

37 See *Hinna*, 2007 WL 3086025, at *6. This conclusion is consistent with the analysis of the courts interpreting section 705.004's predecessor. See, e.g., *Bettes v. Stonewall Ins. Co.*, 480 F.2d 92, 95 (5th Cir. 1973) (rejecting the plaintiff's claim that a misrepresentation must both be material and contribute to the loss); *Robinson v. Reliable Life Ins. Co.*, 569 S.W.2d 28, 28 (Tex. 1978) (finding that the misrepresentation was material to the loss even though it did not contribute to the event causing the loss).

38 *Hinna*, 2007 WL 3086025, at *6 (emphases in original).

39 2008 WL 2065835, at *4. The court also found that, even though the insurer included warranty language in the application and the policy incorporated the application into the policy and conditioned coverage on the truthfulness of the statements in the application, a fact issue existed based on the insured's subjective belief that a suit "may" not be brought against him. *Id.* at *4-5.

40 TEX. INS. CODE § 705.105. The contours of section 705.105 are addressed below in the analysis of the 91-day notice of intent to rescind requirement set forth in section 705.005.

41 *Id.* § 705.051.

42 See *Harrington v. Aetna Cas. & Sur. Co.*, 489 S.W.2d 171, 177-78 (Tex. Civ. App.—Waco 1972, writ ref'd n.r.e.). *Harrington* has been followed on this issue in at least one case and cited as dicta in three others. See *Horne v. Charter Nat'l Ins. Co.*, 614 S.W.2d 182, 185 (Tex. Civ. App.—Fort Worth 1981, writ ref'd n.r.e.) (following *Harrington*); see also *Bundick v. Nat'l Life & Acc. Ins. Co.*, 509 F. Supp. 584, 585 (W.D. Tex. 1980), *aff'd*, 636 F.2d 311 (5th Cir. 1981); *Bowie v. Ranger Ins. Co.*, 563 S.W.2d 394, 396-97 (Tex. Civ. App.—Eastland), *rev'd on other grounds*, 574 S.W.2d 540 (Tex. 1978); *Westchester Fire Ins. Co. v. English*, 543 S.W.2d 407, 412 (Tex. Civ. App.—Waco 1976, no writ).

43 See *Vasquez v. ReliaStar Life Ins. Co.*, No. 14-12-01115-CV, 2014 WL 1267171, at *2-3 (Tex. App.—Houston [14th Dist.] Mar. 27, 2014, no pet.); *Bich Ngoc Nguyen v. Allstate Ins. Co.*, 404 S.W.3d 770, 780 (Tex. App.—Dallas 2013, pet. denied).

44 2014 WL 1267171, at *3.

45 404 S.W.3d at 777.

46 *Id.* at 781-82.

47 TEX. INS. CODE § 705.005.

48 See *Womack v. Allstate Ins. Co.*, 296 S.W.2d 233, 235-36 (Tex. 1956) (reversing a summary judgment in the insurer's favor where the record did not show when the insurer discovered the falsity of the representation); *Sanders v. Jefferson Nat'l Life Ins. Co.*, 510 S.W.2d 407, 408 (Tex. Civ. App.—Dallas 1974, no writ)

(reversing a summary judgment in the insurer's favor because of its failure to plead and prove that it gave notice of its rescission within 90 days of learning of the falsity of the insured's representations).

49 It is not enough for an insurer to notify the insured that it believes he has made a misrepresentation or to seek an explanation for his nondisclosure; rather, it must give notice that it refuses to be bound by the policy. See *Nat'l Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 780 S.W.2d 417, 425 (Tex. App.—Texarkana 1989) (finding that the insurer's letter that it was investigating the claim did not satisfy the notice requirement in section 705.005's predecessor), *aff'd*, 811 S.W.2d 552 (Tex. 1991).

50 TEX. INS. CODE § 705.105.

51 See *United of Omaha Life Ins. Co. v. Halsell*, No. SA-08-CA-1007-XR, 2009 U.S. Dist. LEXIS 65693 (W.D. Tex. July 16, 2009) (*Halsell I*); *Myers v. Mega Life & Health Ins. Co.*, No. 07-06-0233-CV, 2008 WL 1758640 (Tex. App.—Amarillo Apr. 17, 2008, pet. denied). In *In re VarTec Telecom, Inc.*, Bankr. No. 04-81694, 2007 WL 2142499, at *2-4 (Bankr. N.D. Tex. July 23, 2007), the bankruptcy court ruled that section 705.005 was inapplicable to a policy that was not issued in the course of the insurer's Texas business. Thus, the interplay between section 705.005 and section 705.105 was not at issue in that case.

52 In this case, the plaintiff insurer was unable during the claim process to acquire medical records regarding the insured, so it filed a declaratory-judgment action, used discovery to obtain the medical records showing the misrepresentations, and then gave notice of its intent to rescind, amending its complaint to assert a rescission claim. 2009 U.S. Dist. LEXIS 65693, at *3. An insurer may want to consider this approach when it encounters an insured or beneficiary that is unwilling to cooperate during the claim process.

53 *Id.* at *7.

54 *Id.* at *10. The "contest" requirement is addressed below.

55 The court relied on section 705.005 even though the insurer had issued the policy at issue years before the April 1, 2005 effective date of that section. 2008 WL 1758640, at *2.

56 *Id.* at *3-4. The court also rejected the insurer's argument that the 91-day notice period did not begin to run until the insurer had determined that the misrepresentation was material. *Id.* at *5.

57 TEX. INS. CODE § 1101.001.

58 *Id.* § 1101.006.

59 119 S.W.3d 274 (Tex. App.—Tyler 2003, pet. denied).

60 *Id.* at 284.

61 168 S.W.2d 656 (Tex. 1943).

62 *Id.* at 658 (citation omitted). Indeed, the *Trevino* court held that an insurer which initially filed a general denial in response to a beneficiary's suit could not amend its answer after the expiration of the contestable period to seek rescission or raise the misrepresentation defense. *Id.* at 660; see also *Patton v. Am. Home Mut. Life Ins. Co.*, 185 S.W.2d 420, 422 (Tex. 1945) (finding that

an insurer's fraud defense was barred by the policy's contestable clause where the defense "was not presented in court within the stipulated period of two years"); *Universal Life & Acc. Ins. Co. v. Murphy*, 368 S.W.2d 878, 880 (Tex. Civ. App.—Fort Worth 1963, no writ) (holding that the contestable clause barred the insurer's assertion of a misrepresentation defense more than two years after the issuance of the policy, even though the insurer initially asserted but later withdrew or waived the defense in an earlier action filed within the contestable period). Thus, a contestable clause which establishes a time limit to allege a misrepresentation defense requires the assertion of a rescission claim in a lawsuit, not mere notification to an insured or beneficiary, within the prescribed time period.

63 See, e.g., *Cardenas v. United of Omaha Life Ins. Co.*, 731 F.3d 496, 502 (5th Cir. 2013); *Mut. of Omaha Life Ins. Co. v. Costello*, 420 S.W.3d 873, 877-78 (Tex. App.—Houston [14th Dist.] 2014, no pet.). In *Cardenas*, the Fifth Circuit also found that section 1101.006 applies to reinstatements and establishes a two-year incontestability time limit, provided that the insured survives for two years following the reinstatement. 731 F.3d at 504-05.

64 TEX. INS. CODE § 705.103.

65 See *Federated Life Ins. Co. v. Jafreh*, 392 Fed. Appx. 280, 283 (5th Cir. 2010); *Mass. Mut. Ins. Co. v. Mitchell*, 859 F. Supp. 2d 865, 870 (S.D. Tex. 2012).

66 392 Fed. Appx. at 283.

67 *Mitchell*, 859 F. Supp. 2d at 870. The *Mitchell* court subsequently entered summary judgment in the insurer's favor on its imposter claim and thus did not reach the rescission claim. *Mass. Mut. Ins. Co. v. Mitchell*, 942 F. Supp. 2d 652, 656-58 (S.D. Tex. 2013).

68 See *Ex parte Pruitt*, 551 S.W.2d 706, 709 (Tex. 1977) ("Statutes should be read as a whole and construed to give meaning and purpose to every part."); *In re Azle Manor, Inc.*, 83 S.W.3d 410, 414 (Tex. App.—Fort Worth 2002, orig. proceeding) (noting that, where statutes may be in conflict, the court should harmonize them to give effect to both by assigning each a meaning that will permit each to stand); see also TEX. GOV'T CODE § 311.021 ("In enacting a statute, it is presumed that . . . the entire statute is intended to be effective.").