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Rescission of Life, Accident and Health Insurance Policies in Texas – *The Rules Have Changed*

I. INTRODUCTION

For over 70 years, Texas courts have required an insurer seeking to rescind a life, accident, or health insurance policy to show (among other elements) that the insured had the "intent to deceive" the insurer into issuing the coverage.[1] In adopting this requirement, Texas courts have followed the minority view; in most states, it is enough if the misrepresentation (provided it was material) was negligent or careless.[2] Intent to deceive is obviously a high standard to meet, and Texas courts have generally held it cannot be established on summary judgment.[3]

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.'"[4] As part of this effort, the Texas Legislature recently completed a recodification of the Texas Insurance Code. Although the 2003 session law states that it "is intended as a recodification only," with "no substantive change in law… intended,"[5] the Texas Supreme Court has held that "clear, specific language" in a recodified statute that changes prior law must be applied as written.[6] If the new statutes on misrepresentations by policyholders, which are codified at Texas Insurance Code sections 705.001-.105, are applied as written, then insurers have an excellent argument that significant changes have been made to the elements an insurer must establish to rescind a life, accident, or health insurance policy. These revised statutes give Texas courts the opportunity to rectify their improper imposition of an intent-to-deceive requirement during the first two years a life, accident, or health insurance policy is in force.

II. THE COMMON-LAW REQUIREMENT OF INTENT TO DECEIVE

The requirement of intent to deceive is not a creature of Texas statutory law; instead, it resulted from judicial rulemaking.[7] As the Texas Supreme Court noted in *Union Bankers Insurance Company v. Shelton*, the first case to impose this requirement was the 1888 decision in *Lion Fire Insurance Company v. Starr*.[8] *Starr* was a suit for benefits under a personal property fire insurance policy that contained the following provision: "Any fraud, or attempt at fraud, or any false swearing, on the part of the assured, shall cause a forfeiture of all claim under this policy."[9] The insurer alleged (among other defenses) that the policy was rendered void because the insured committed fraud in submitting his claim.[10] After a jury verdict in favor of the insured for the face amount of the policy, the insurer appealed and alleged error in the trial court's refusal to charge the jury that the policy by its terms was void if the insured's claim was fraudulent.[11] The Texas Supreme Court reversed, finding the parties had expressly agreed that fraud, attempted fraud, or false swearing would result in a forfeiture under the policy.[12] Consequently, the fraud requirement in *Starr* was a creature of the parties, contract, not common law, and the supreme court's actual holding was merely that the insurer was entitled to submit that contractual defense to the jury.

Westchester Fire Insurance Company v. Wagner involved a similar contractual provision.[13] The fire insurance policy at issue in *Wagner* provided it "shall be void… in case of fraud or false swearing by the insured touching any matter relating to this insurance."[14] The insurer denied the named insured's claim on the ground the destroyed goods belonged to a third party, even though the insurer's agent knew of the third party's interest.[15]

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After concluding that the insurer was bound by the agent's knowledge, the *Wagner* court rejected the insurer's argument that the named insured's sworn statement it owned the destroyed property annulled the policy.[16] Without citation to any authority, the *Wagner* court observed: "It is the settled rule that false statements, to avoid a policy, must have been willful, and with design to deceive or defraud."[17] Since the named insured had informed the insurer's agent of the third party's ownership interest, the *Wagner* court found the trial court did not err in refusing to submit the requested issue.[18]

The intent-to-deceive requirement eventually made its way from the finding of a forfeiture due to an intentional misrepresentation during the claim process[19] to the rescission of an insurance policy due to a misrepresentation in the application process.[20] In *American Central Life Insurance Company v. Alexander*, the insurer denied liability on the ground the insured had made misrepresentations in his application for coverage, and the beneficiary specially excepted to the insurer's failure to allege the misrepresentations were intentionally made.[21] The trial court sustained the special exceptions and entered judgment in the beneficiary's favor, and the court of civil appeals affirmed.[22] In its analysis, the Texas Commission of Appeals cited *Cooley's Briefs on the Law of Insurance*[23] and *Wagner*[24] in support of its assertion that the misrepresentation must have been willful or made fraudulently with the intent to deceive, even though neither of those authorities necessarily compelled that result.[25]

Over time, the intent-to-deceive requirement became increasingly entrenched in Texas law. In *Clark v. National Life & Accident Insurance Company*, the insurer sought to rescind a life insurance policy within two years of its issuance on the ground the insured had made fraudulent misrepresentations in his application.[26] The jury found the insured was in sound health at the time the policy was issued, and the insurer did not request the submission of any issues on its rescission defense.[27] The trial court entered judgment in the beneficiary's favor, but the court of civil appeals reversed, finding that the insurer's fraud defense was established as a matter of law.[28] The Texas Supreme Court disagreed and affirmed the trial court's judgment.[29] As part of its analysis, the supreme court cited *Alexander* and *Wagner* in support of its assertion that "[i]t is the settled rule that, in order to avoid a policy, false statements must have been made willfully and with design to deceive or defraud."[30] After *Clark*, the Texas Supreme Court repeatedly relied on these cases in requiring insurers seeking rescission to prove intent.[31]

For the most part, these courts did not predicate their imposition of an intent requirement on the Texas statutes governing rescission, which is not surprising in light of the fact that those statutes did not expressly require such a showing. For example, Texas Insurance Code article 21.16, which was entitled "Misrepresentation by Policyholder," required a showing of materiality but was silent on the issue of intent:

> Any provision in any contract or policy of insurance issued or contracted for in this State which provides that the answers or statements made in the application for such contract or in the contract of insurance, if untrue or false, shall render the contract or policy void or voidable, shall be of no effect, and shall not constitute any defense to any suit brought upon such contract, *unless it be shown upon the trial thereof that the matter or thing misrepresented was material to the risk or actually contributed to the contingency or event on which said policy became due and payable,* and whether it was material and so contributed in any case shall be a question of fact to be determined by the court or jury trying such case.[32]

In turn, Texas Insurance Code article 21.17 was entitled "Notice of Misrepresentation" and did not require a showing of intent:

> In all suits brought upon insurance contracts or policies hereafter issued or contracted for in this State, no defense based upon misrepresentations made in the applications for, or in obtaining or securing the said contract, shall be valid, unless the defendant shall show on the trial that, within a reasonable time after discovering the falsity of the representations so made, it gave notice to the assured, if living, or, if dead, to the owners or beneficiaries of said contract, that it refused to be bound by the contract or policy; provided, that ninety days shall be a reasonable time; provided, also, that this article shall not be construed as to render available as a defense any immaterial misrepresentation, nor to in any wise modify or affect Article 21.16 of this code.[33]

On the other hand, Texas Insurance Code article 21.19, which was entitled "Misrepresenting Loss or Death" and addressed misrepresentations made during the claim process, expressly required that the misrepresentation be both material *and* "fraudulently made":

> Any provision in any contract or policy of insurance issued or contracted for in this State which provides that the same shall be void or voidable, if any misrepresentations or false statements be made in proofs of loss or death, as the case may be, shall be of no effect, and shall not constitute any defense to any suit brought upon such con-

> tract or policy, *unless it be shown upon the trial of such suit that the false statement made in such proofs of loss or death was fraudulently made and misrepresented a fact material to the question of the liability of the insurance company* upon the contract of insurance sued on, and that the insurance company was thereby misled and caused to waive or lose some valid defense to the policy.[34]

As such, neither article 21.16 nor article 21.17 (both of which addressed misrepresentations in the *application* process) required an insurer to prove intent, whereas article 21.19 (which addressed misrepresentations in the *claim* process) expressly required a showing of fraud. As noted above, however, both the Texas Supreme Court and the Fifth Circuit imposed an intent requirement for rescissions.[35]

Similarly, these courts did not predicate the intent-to-deceive requirement on the express terms of the incontestable clause. Like many states, Texas requires that life, accident, and health insurance policies contain certain provisions,[36] including a clause addressing when and how an insurer may seek to void the policy.[37] *Union Bankers Insurance Company v. Shelton* involved an insurer's rescission of a health insurance policy,[38] and at the time of the policy's issuance, all Texas accident and sickness policies had to contain the following provision:

> Time Limit on Certain Defenses: (a) After two years from the date of issue of this policy no misstatements, except fraudulent misstatements, made by the applicant in the application for such policy shall be used to void the policy or to deny a claim for loss incurred or disability (as defined in the policy) commencing after the expiration of such two-year period.
>
> (The foregoing policy provision shall not be so construed as to affect any legal requirement for avoidance of a policy or denial of a claim during such initial two-year period, nor to limit the application of Section 3(B), (1), (2), (3), (4), and (5) in the event of misstatement with respect to age or occupation or other insurance).[39]

On the application, the insured denied he had ever been treated for or had any known indications of any disorders of his skeletal or muscular systems.[40] Seven months after the policy was issued, the insured underwent total hip replacement surgery to correct necrosis in his left hip joint, and the insurer cancelled the policy due to his failure to disclose his hip problems.[41] The jury answered all of the questions against the insured, except it failed to find he intended to deceive the insurer.[42] The trial court nonetheless entered judgment in the insurer's favor, but the court of appeals reversed and remanded the case for a new trial on the insured's bad-faith claim.[43]

In its appeal to the Texas Supreme Court, the insurer sought to avoid the jury's no-intent finding by arguing that the first paragraph of article 3.70-3(A)(2)(a) implied an insurer could cancel a health insurance policy within two years of its issuance on the basis of innocent (i.e., non-fraudulent) misrepresentations.[44] The Texas Supreme Court disagreed, finding (in a plurality decision) that the second paragraph of article 3.70-3(A)(2)(a), by its terms, meant that the first paragraph did not affect the determination of whether the insurer must prove intent during the first two years a policy was in force.[45] The supreme court then held, in reliance on *Starr, Clark, Allen*, and *Mayes*, that the common law of Texas required a showing of intent during the first two years.[46]

In *Alexander*, the Texas Commission of Appeals found support for the imposition of an intent-to-deceive requirement in Texas Revised Civil Statutes article 4732, which required all life insurance policies to contain a provision stating that "all statements made by the insured shall, in the absence of fraud, be deemed representations and not warranties."[47] Prior to the adoption of this statute's predecessor in 1909,[48] Texas courts applied the strict obligations of warranties, which permitted an insurer to avoid a policy where *any* statement of the insured identified as a warranty was not literally and exactly true.[49] Not surprisingly, insurers sought to use this doctrine to void coverage on the basis of misstatements that were irrelevant to the issue of whether the coverage would have been issued in the first place.[50] For example, in *Blackstone v. Kansas City Life Insurance Company*, the insurer sought to rescind two life insurance policies on the ground the insured had misrepresented his place of birth and residence and the number of his brothers and sisters, none of which had anything to do with his insurability.[51]

Upon scrutiny, however, this provision does not support the imposition of the intent-to-deceive requirement. In effect, this provision equated the making of a fraudulent representation with a breach of a warranty, both of which permitted an insurer to avoid the policy. Importantly, if an insured's statement was treated as a warranty, its falsity served to void the policy without regard to whether the statement was material.[52] Properly read, article 4732 thus permitted an insurer to rescind a life insurance policy on the basis of a fraudulent statement that was *not* material. In turn, the rescission statutes in force at the time (such as Texas Revised Civil Statutes article 5043) permitted a rescission on the basis of a material misrepresentation (without expressly requiring a showing of intent).[53] By allowing rescissions upon a showing of either a fraudulent, non-material representation (which was effectively a warranty pursuant to article 4732) or a material misrepresentation

(which under article 5043 need not have been intentionally made), Texas law would have been consistent with the majority rule, which has long permitted rescissions on the basis of a misrepresentation that was fraudulent *or* material.[54] Texas courts nonetheless adopted, on the basis of questionable analysis, the minority position that an insured's misrepresentation must be both fraudulent *and* material before an insurer could rescind his coverage.

III. THE RECODIFICATION OF THE TEXAS INSURANCE CODE

By virtue of the recent recodification of the Texas Insurance Code, significant changes have been made to Texas law on the rescission of insurance policies. In 2003, the Texas Legislature completed its revision of the Texas Insurance Code, and the session law containing this recodification states: "This Act is intended as a recodification only, and no substantive change in law is intended by this Act."[55] Notwithstanding this admonition, the Texas Supreme Court has held that courts must give effect to a recodified statute that is unambiguous, even if it results in a change in the law.[56] 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."[57] If the recodified statutes are given their plain meaning, insurers have an excellent argument that a showing of intent is not required to rescind a life, accident, or health insurance policy that has been in force for less than two years.

Effective April 1, 2005, the Texas Legislature adopted Title 5 to the Texas Insurance Code.[58] Indicative of the concern with fraud in the insurance area,[59] Subtitle F is entitled "Insurance *Fraud*," and its first four chapters (chapters 701-704) are entitled "Insurance *Fraud* Investigations,"[60] "Motor Vehicle Theft and Motor Vehicle Insurance *Fraud* Reporting,"[61] "Covered Entity's *Antifraud* Action,"[62] and "*Antifraud* Programs."[63] In contrast to these repeated references to fraud, chapter 705 (which contains the recodified rescission requirements) is entitled "*Misrepresentations* by Policyholders."[64]

Chapter 705 contains three subchapters: general provisions applicable to all insurance policies,[65] special provisions applicable to life, accident, and health insurance policies,[66] and special provisions applicable to only life insurance policies.[67] The recodified statutes establish the following requirements with respect to all insurance policies:

> • 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 which are questions of fact;[68] and
>
> • 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.[69]

These requirements do 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."[70] As such, if a life insurance policy provides it is incontestable after two years or less, the insurer need not give the 90-day notice required by section 705.005; otherwise, and always with respect to non-life insurance policies, the insurer must give notice, within 90 days of discovering the falsity of the insured's representation, that it will not be bound by the policy.

In turn, section 705.051 (which applies to only life, accident, and health insurance policies) 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.[71]

Since neither this section nor any of the other sections articulating the rescission requirements expressly refer to intent, an insurer seeking to rescind a life, accident, or health insurance policy can argue that a material misrepresentation that was made negligently or carelessly is enough.[72] If intent was to be required, the Texas Legislature could have easily so stated, and it would defeat the purpose of a recodification to require parties to analyze the common law to retrieve this requirement.[73]

Finally, section 705.103 (which applies to only 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."[74] In turn, section 705.104 provides:

A defense based on a misrepresentation in the application for, or in obtaining, a life insurance policy on the life of a person in or residing in this state is not valid or enforceable in a suit

brought on the policy on or after the second anniversary of the date of issuance of the policy if premiums due on the policy during the two years have been paid to and received by the insurer, unless:

> (1) the insurer has notified the insured of the insurer's intention to rescind the policy because of the misrepresentation; *or*
>
> (2) it is shown at the trial that the misrepresentation was:
> (A) *material to the risk; and*
> (B) *intentionally made*.[75]

By its terms, section 705.104 permits an insurer to rescind a life insurance 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. By permitting the rescission, upon a showing of an intentionally made misrepresentation, of a life insurance policy that has been in force for over two years, section 705.104 is consistent with (albeit stated differently than) Texas Insurance Code section 1201.208(a), which is the successor statute to the provision at issue in *Shelton* and permits the rescission of an individual accident and health insurance policy that has been in force for two years upon a showing of "a fraudulent misstatement."[76]

In addition, section 705.104 (with its express reference to intent), when read together with section 705.051 (which is silent on the issue of intent), strongly suggests that intent need not be shown to rescind a life, accident, or health insurance policy that has been in force for less than two years. Admittedly, the Texas Supreme Court rejected a comparable argument with respect to a health insurance policy in *Shelton*; 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."[77] On the other hand, section 705.051 now sets forth the "legal requirement[s] for avoidance of a [life, accident, or health insurance] policy… during the initial two-year period"[78] and does not requiring a showing of intent. Simply put, the Texas Legislature is capable of imposing an intent requirement where it sees fit, and its decision to require intent in section 705.104 (which applies only to life insurance policies that have been in force for two years) but not in section 705.051 must be acknowledged and given meaning.[79]

Further support for the conclusion that intent need not be shown to rescind a life, accident, or health insurance policy that has been in force for less than two years may be found in other recent enactments. For example, both section 705.003, which concerns misrepresentations in proof of loss or death, and section 705.004, which concerns misrepresentations in a policy application, establish a general rule that a policy provision stating a misrepresentation makes the policy void or voidable has no effect and is not a defense in a suit brought on the policy.[80] With respect to a misrepresentation in proof of loss or death, the general rule is inapplicable if the insurer establishes the misrepresentation was (among other requirements) "fraudulently made."[81] Tellingly, a showing of fraud is *not* required with respect to a misrepresentation in a policy application; rather, it is enough if the insurer establishes the misrepresentation was "material to the risk" or "contributed to the contingency or event on which the policy became due and payable."[82]

In turn, section 1201.272, which is entitled "False Statements," provides:

> The falsity of a statement in an application for an individual accident and health insurance policy does not bar a right to recovery under the policy unless the statement materially affected the acceptance of the risk of the hazard assumed by the insurer.[83]

Tellingly, this provision (which applies to the application process) does not impose an intent requirement, whereas section 1202.051(c)(2) (which applies to the cancellation of an individual health insurance policy) permits an insurer to decline to renew or continue an individual health insurance policy "for fraud or intentional misrepresentation."[84]

All told, if the terms of chapter 705 are applied as written, a showing of intent is not required to rescind a life, accident, or health insurance policy that has been in force less than two years.

IV. CONCLUSION

Many actions have unintended consequences.[85] Although the Texas Legislature may not have intended to change Texas law on the rescission of life, accident, and health insurance policies, the recodification of the Texas Insurance Code has had that effect. If courts follow the Texas Supreme Court's admonition that recodified statutes are to be applied as written, even if the resulting interpretation changes the law, then the plain language of chapter 705 of the Texas Insurance Code confirms that an insurer no longer must establish an insured's intent in seeking to rescind a life, accident, or health insurance policy that has been in force for less than two years. In this recodification, the Texas Legislature has moved Texas law in line with that of the majority of other jurisdictions, which permit the rescission of an insurance policy on the basis of a misrepresentation that is either material *or* fraudulent.

1. *See Union Bankers Ins. Co. v. Shelton*, 889 S.W.2d 278, 281-82 (Tex. 1994) (observing that "[t]he proposition that an insured's intent to deceive is likewise required is well established in the common law of this state"). In *Shelton*, the Texas Supreme Court cited *Lion Fire Insurance Co. v. Starr*, 12 S.W. 45, 46 (Tex. 1888), which involved a personal property fire insurance policy, as the first case to announce this rule, and in 1933, the Texas Commission of Appeals extended this requirement to life insurance policies. *See American Cent. Life Ins. Co. v. Alexander*, 56 S.W.2d 864, 866 (Tex. Comm'n App. 1933, judgm't adopted). Both the Texas Supreme Court and the Fifth Circuit have held that an insurer seeking to rescind an insurance policy must plead and prove five elements: (1) the making of a 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. *See Mayes v. Massachusetts Mut. Life Ins. Co.*, 608 S.W.2d 612, 616 (Tex. 1980); *Lee v. National Life Assur. Co. of Canada*, 632 F.2d 524, 527 (5th Cir. 1980). These requirements were apparently first articulated in this manner in *General American Life Insurance Company v. Martinez*, 149 S.W.2d 637, 640-41 (Tex. Civ. App. – El Paso 1941, writ dism'd judgm't cor.).

2. *See Shelton*, 889 S.W.2d at 285 (Phillips, C.J., concurring) (observing that Texas has "adopted the minority position that intent to deceive is required for cancellation of an insurance policy on the ground of a misrepresentation"); *see also Tingle v. Pacific Mut. Ins. Co.*, 837 F. Supp. 191, 192 (W.D. La. 1993) (noting that the majority rule is that "'a material misrepresentation need not have been made fraudulently in order to be available to avoid a policy'") (quoting 45 C.J.S. INSURANCE § 548 (1993)); William H. Danne, Jr., *Modern Status Regarding Materiality and Effect of False Statement by Insurance Applicant as to Previous Insurance Cancellations or Rejections*, 66 A.L.R.3d 749, 781-82 (1975) ("The prevailing view in the absence of a statute to the contrary is that a materially false warranty or representation by an insurance applicant will defeat recovery on the policy even if made in good faith or as the result of inadvertence or ignorance."). Similarly, federal common law under the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. §§ 1001-1461 (2000), does not require that the misrepresentation be fraudulent; rather, it is enough if the misrepresentation was material. *See Tingle*, 837 F. Supp. at 193.

3. *See Cartusciello v. Allied Life Ins. Co. of Tex.*, 661 S.W.2d 285, 288 (Tex. App. – Houston [1st Dist.] 1983, no writ); *see also Flowers v. United Ins. Co. of Am.*, 807 S.W.2d 783, 786 (Tex. App. – Houston [14th Dist.] 1991, no writ) (noting that knowledge of one's health condition is insufficient to presume intent as a matter of law); *Estate of Diggs v. Enterprise Life Ins. Co.*, 646 S.W.2d 573, 576 (Tex. App. – Houston [14th Dist.] 1982, writ ref'd n.r.e.) (reversing summary judgment where the court determined it could not "presume an intent to deceive from the fact that [the insured], with a long history of heart ailments, made false statements on his application for insurance"). Texas courts have suggested, however, that intent may be established as a matter of law where there is strong evidence of collusion between the insured and the agent. *See Lee*, 632 F.2d at 528; *Washington v. Reliable Life Ins. Co.*, 581 S.W.2d 153, 160 (Tex. 1979).

4. *Fleming Foods of Tex., Inc. v. Rylander,* 6 S.W.3d 278, 283 (Tex. 1999) (quoting TEX. GOV'T CODE § 323.007(a)).

5. Act of May 22, 2003, 78th Leg., R.S., ch. 1274, § 27, 2003 Tex. Gen. Laws 3611, 4139.

6. *Fleming Foods*, 6 S.W.3d at 284; *see also State Farm Life Ins. Co. v. Martinez*, 216 S.W.3d 799, 804 (Tex. 2007) (noting that, "[w]hile we generally presume the Legislature accepts judicial interpretations of a statute by reenacting it without substantial change, we do not make that presumption when there have been substantial changes, or when it would contradict the statute's plain words" (footnotes omitted)).

7. *See S. Leigh Moore, A Promising Alternative to Intent to Deceive: Intent to Induce Issuance*, 48 BAYLOR L. REV. 273, 278 (1996) (observing that "[t]he intent to deceive requirement was not born out of any certain case; rather, the requirement is a creature of misunderstandings and misconstruction that grew into accepted law through the desire of courts to uphold lower courts' decisions if at all possible").

8. *Shelton*, 889 S.W.2d at 281-82 (citing *Starr*, 12 S.W. at 46).

9. *Starr*, 12 S.W. at 46.

10. *Id*. at 45.

11. *Id*. at 45-46.

12. *Id*. at 46.

13. 57 S.W. 876, 877 (Tex. Civ. App. 1900, writ ref'd).

14. *Id*.

15. *Id*.

16. *Id*.

17. *Id*.

18. *Id*. at 878.

19. *Starr*, 12 S.W.at 46.

20. *American Cent. Life Ins. Co. v. Alexander,* 56 S.W.2d 864, 866 (Tex. Comm'n App. 1933, judgm't adopted).

21. *Id*. at 865-66.

22. *Id*. at 865 (citing *American Cent. Life Ins. Co. v. Alexander,* 39 S.W.2d 86, 86, 90 (Tex. Civ. App. – Amarillo 1931, writ granted)).

23. *Id*. at 866 (citing 3 ROGER W. COOLEY, BRIEFS ON THE LAW OF INSURANCE 1988 (1905)).

24. *Id*. (citing *Westchester Fire Ins. Co. v. Wagner,* 57 S.W. 876 (Tex. Civ. App. 1900, writ ref'd)).

25. *See* Moore, *supra* note 7, at 279-81 (analyzing *Wagner*, 57 S.W. at 877; *Alexander*, 56 S.W.2d at 866).

26. 200 S.W.2d 820, 821 (Tex. 1947).

27. *Id*. at 822.

28. *Id*. at 821.

29. *Id*. at 824.

30. *Id*. at 822.

31. *See Shelton,* 889 S.W.2d at 281-82 (citing *Clark*); *Mayes*, 608 S.W.2d at 616 (citing *Clark*); *Allen v. American Nat'l Ins. Co*., 380 S.W.2d 604, 607-08 (Tex. 1964) (citing *Clark, Alexander*, and *Wagner*). Although this element is typically characterized as the "intent to deceive," the Texas Supreme Court observed in *Shelton* that "the utterance of a *known* false statement made with intent to induce action ... is equivalent to an intent to deceive." *Shelton*, 889 S.W.2d at 282 n.7 (emphasis and omission in original); *see also Haney v. Minnesota Mut. Life Ins. Co*., 505 S.W.2d 325, 328 (Tex. Civ. App. – Houston [14th Dist.] 1974, writ ref'd n.r.e.) (stating that "[t]he jury findings of the making of known false statements, with intent to induce action on the part of the insurance company, amounted to findings of an intent to deceive"). Intent to induce action represents an easier test for an insurer to satisfy, as the jury is more likely to find the insured intended to induce the insurer to act than he intended to deceive it. Moreover, the insurer can argue that language in the application stating the insured is requesting the insurer to issue coverage on the basis of his disclosures enables the insurer to establish intent as a matter of law.

32. TEX. INS. CODE art. 21.16 (repealed 2003). In the same vein, TEXAS INSURANCE CODE article 21.18 was entitled "Immaterial Misrepresentation" and provided:

> No recovery upon any life, accident or health insurance policy shall ever be defeated because of any misrepresentation in the application which is of an immaterial fact and which does not affect the risks assumed.

Id. art. 21.18, *repealed by* Act of May 20, 2003, 78th Leg, R.S., ch. 1274, § 26(a)(1), 2003 Tex. Gen. Laws 3611, 4138.

33. *Id*. art. 21.17 (repealed 2003).

34. *Id*. art. 21.19 (repealed 2003).

35. *See Lee*, 632 F.2d at 527; *Mayes*, 608 S.W.2d at 616.

36. *See generally* TEX. INS. CODE §§ 1101.001-.013 (life insurance policies); *id*. §§ 1201.201-.227 (individual accident and health insurance policies).

37. *See id*. § 1101.006(a) (life insurance policies); *id*. § 1201.208(a) (individual accident and health insurance policies).

38. 889 S.W.2d 278, 281-82 (Tex. 1994).

39. Act of June 6, 1955, 54th Leg., R.S., ch. 397, § 3(a)(2), 1955 Tex. Gen. Laws 1044, 1046, *amended by* Act of Sept. 19, 1969, 61st Leg., C.S., ch. 11, § 1, 1969 Tex. Gen. Laws 118, 118, *repealed by* Act of May 22, 2003, 78th Leg, R.S., ch. 1274, § 26(a)(1), 2003 Tex. Gen. Laws 3611, 4138 (current version at TEX. INS. CODE § 1201.208(a)). Although life insurers have not been allowed to include a comparable incontestable clause, they arguably could have rescinded, upon a showing of fraud, a life insurance policy that had been in force for over two years if courts had given meaning to the latter part of article 21.35, which applied by its terms to "every contract or policy of *life* insurance" and provided:

> The provisions of Articles 21.16, 21.17, and 21.19 of this code shall not apply to policies of life insurance in which there is a clause making such policy indisputable after two (2) years or less, provided premiums are duly paid; provided further, that *no defense based upon misrepresentation made in the application for, or in obtaining or securing, any contract of insurance upon the life of any person being or residing in this State shall be valid or enforceable in any suit brought upon such contract two (2) years or more after the date of its issuance, when premiums due on such contract for the said term of two (2) years have been paid to, and received by, the company issuing such contract, without notice to the assured by the company so issuing such contract of its intention to rescind the same on account of misrepresentation so made, unless it shall be shown on the trial that such misrepresentation was material to the risk and intentionally made*.

Act of May 22, 1989, 71st Leg., R.S., ch. 656, § 1, 1989 Tex. Gen. Laws 2163, 2163 (repealed 2003).

40. *Shelton*, 889 S.W.2d at 279.

41. *Id*.

42. *Id*.

43. *Id*.

44. *Id*. at 279-80.

45. *Id*. at 281.

46. *Id*. at 281-82.

47. 56 S.W.2d at 866 (quoting Act of March 22, 1909, 31st Leg., R.S., ch. 108, § 22, 1909 Tex. Gen. Laws 192, 200 (current version at TEX. INS. CODE § 1101.007)).

48. Act of March 22, 1909, 31st Leg., R.S., ch. 108, § 22, 1909 Tex. Gen. Laws 192, 200.

49. *See, e.g., Supreme Lodge Knights & Ladies of Honor v. Payne*, 108 S.W. 1160, 1162 (Tex. 1908) ("The fact warranted, being untrue, rendered the certificate void."); *Kansas Mut. Life Ins. Co. v. Pinson,* 63 S.W. 531, 531 (Tex. 1901) (noting "the general rule that the breach of warranty in an insurance policy works a forfeiture of the contract").

50. *See, e.g., Pinson*, 63 S.W. at 531-32 (finding that a policy was void for breach of warranty where the insured misstated the ages of his five sisters by a few years).

51. 174 S.W. 821, 821-23 (Tex. 1915).

52. *See Brotherhood of R.R. Trainmen Ins. Dep't of Cleveland, Ohio v. Green,* 182 S.W.2d 804, 804 (Tex. 1944) ("Whether material or not to the risk, the representations were warranties, and since at least some of them were admittedly untrue, they avoided the policy."); *Goddard v. East Tex. Fire Ins. Co.,* 1 S.W. 906, 907 (Tex. 1886) (observing that, if a given clause was a warranty, "the law exacts a compliance with their terms, according to their true intent and meaning, whether material or not, or whether known to the assured or not, if he had the opportunity; and it was his duty, under the circumstances, to acquaint himself with them").

53. *See* Act of March 27, 1903, 28th Leg., R.S., ch. 69, § 1, 1903 Tex. Gen. Laws 94, 94 (current version at TEX. INS. CODE § 705.004 (requiring the party seeking rescission to show "that the matter or thing misrepresented was material to the risk or actually contributed to the contingency or event upon which said policy became due and payable")).

54. *See, e.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 164(1) (1981) ("If a party's manifestation of assent is induced by either a fraudulent or a material misrepresentation by the other party upon which the recipient is justified in relying, the contract is voidable by the recipient."). According to one com-

mentator, most material misrepresentations are intentionally made. *See* Robert R. Googins, *Fraud and the Incontestable Clause: A Modest Proposal for Change,* 2 Connecticut Ins. L.J. 51, 63 (1996) ("Of course, it would have to be an unusual case for a material misrepresentation of a manifest condition to be other than intentional.").

55. Act of May 22, 2003, 78th Leg., R.S., ch. 1274, § 27, 2003 Tex. Gen. Laws 3611, 4139.

56. *See Fleming Foods of Tex., Inc. v. Rylander,* 6 S.W.3d 278, 284 (Tex. 1999) (holding that "clear, specific language" in a recodified statute that changes prior law must be applied as written, even though the enabling act provided that "no substantive change in the law is intended").

57. *Id.* 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, H.J. of TEX., 77th Leg., R.S. (2001).

58. Act of May 22, 2003, 78th Leg., R.S., ch. 1274, §§ 1-28, 2003 Tex. Gen. Laws 3611, 3611-4139. As part of this recodification, articles 21.16, 21.17, 21.18, 21.19, and 21.35 (among other articles) were repealed effective April 1, 2005. Id. § 26(a)(1), 2003 Tex. Gen. Laws at 4138.

59. According to the Texas Department of Insurance, insurance fraud "is one of the most costly white collar crimes in America, ranking second to tax evasion," and may have an annual total cost in excess of $120 billion. Texas Dept. of Insurance Facts and Frequently Asked Questions, http://www.tdi.state.tx.us./fraud/faq.html (last visited August 19, 2007). Consistent with its focus on insurance fraud, the Texas Legislature recently amended Texas Penal Code section 35.02 to make it a state jail felony to commit application-related fraud after September 1, 2005. TEX. PEN. CODE § 35.02(a-1), (d). The Texas Legislature had criminalized claim-related fraud in 1995. *See id.* § 35.02(a), added by Act of May 25, 1995, 74th Leg., R.S., ch. 621, § 1, 1995 Tex. Gen. Laws 3483, 3483. Similarly, any person who determines or reasonably suspects a fraudulent insurance act (which now includes application-related fraud) has been or is about to be committed must report the information in writing within 30 days to the insurance fraud unit of the Texas Department of Insurance. TEX. INS. CODE § 701.051(a).

60. TEX. INS. CODE §§ 701.001-.154.

61. *Id.* §§ 702.001-.006.

62. *Id.* §§ 703.001-.104.

63. *Id.* §§ 704.001-.054.

64. *Id.* §§ 705.001-.105. Admittedly, "[t]he heading of a title, subtitle, chapter, subchapter, or section does not limit or expand the meaning of a statute." TEX. GOV'T CODE § 311.024. The titles chosen by the Texas Legislature, while not controlling, are nonetheless instructive.

65. TEX. INS. CODE §§ 705.001-.005.

66. *Id.* § 705.051.

67. *Id.* §§ 705.101-.105.

68. *Id.* §§ 705.004(b)-(c). This requirement is generally consistent with the materiality requirement in the now-repealed article 21.16. *See* Insurance Code, 52d Leg., R.S., ch. 491, § 2(b), 1951 Tex. Gen. Laws 868, 1074 (repealed 2003). Under this disjunctive provision, an insurer must prove either the misrepresentation was material to its decision to issue coverage or the undisclosed condition contributed to the insured's death. *See 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); *Fireman's Fund Ins. Co. v. Wilburn Boat Co.*, 300 F.2d 631, 644 (5th Cir.) ("It is obvious that a fact can be material to the risk without contributing to bring about the destruction of the insured's property."), *cert. denied*, 370 U.S. 925 (1962).

69. TEX. INS. CODE § 705.005(b). This requirement is generally consistent with the 90-day notice requirement in the now-repealed article 21.17. *See* Insurance Code, 52d Leg., R.S., ch. 491, § 2(b), 1951 Tex. Gen. Laws 868, 1075 (repealed 2003). Under section 705.005, the insurer must establish the date it discovered the falsity of the insured's representation and that it gave notice to the insured or his beneficiary less than 91 days thereafter of its refusal to be bound by the policy. *See National Union Fire Ins. Co. of Pittsburgh, Pa. v. Hudson Energy Co.*, 780 S.W.2d 417, 425 (Tex. App. – Texarkana 1989, writ granted) (interpreting article 21.17), *aff'd*, 811 S.W.2d 552 (Tex. 1991). The notice must state the insurer refuses to be bound by the policy; an interim notice the insurer is investigating a potential misrepresentation is not enough. *See id.* (finding that the insurer's letter stating it was investigating the claim did not satisfy the notice requirement in article 21.17).

70. TEX. INS. CODE § 705.105. This provision is generally consistent with the second part of the now-repealed article 21.35. *See* Insurance Code, 52d Leg., R.S., ch. 491, § 2(e), 1951 Tex. Gen. Laws 868, 1084-85 (repealed 2003).

71. *Id.* § 705.051. These requirements are generally consistent with the requirements in the now-repealed article 21.18. *See* Insurance Code, 52d Leg., R.S., ch. 491, § 2(b), 1951 Tex. Gen. Laws 868, 1075 (repealed 2003).

72. *See Old Am. County Mut. Fire Ins. Co. v. Sanchez,* 149 S.W.3d 111, 115 (Tex. 2004) (observing that, "because we presume that every word of a statute has been included or excluded for a reason, we will not insert requirements that are not provided by law"); *Cameron v. Terrell & Garrett, Inc.*, 618 S.W.2d 535, 540 (Tex. 1981) (observing that "we believe every word excluded from a statute must also be presumed to have been excluded for a purpose"). An insurer making this argument should, however, nonetheless be prepared to establish the insured's intent if the court (notwithstanding the recodification) elects to impose that requirement as a matter of Texas common law.

73. *See City of Garland v. Dallas Morning News,* 22 S.W.3d 351, 358 (Tex. 2000) ("Courts are not responsible for omissions in legislation, but must take statutes as they find them."); *see also Fort Worth & D.C. Ry. Co. v. Welch,* 183 S.W.2d 730, 736 (Tex. Civ. App. – Amarillo 1944, writ ref'd) (noting that a statutory revision "implies a re-examination and restatement of the law in a corrected or improved form with or without material changes" and that "[i]t will be presumed that… the Legislature proceeded diligently and with full knowledge of the consequences of its act").

74. TEX. INS. CODE § 705.103. These requirements are generally consistent with the attachment requirement in the first part of the now-repealed article 21.35. *See* Insurance Code, 52d Leg., R.S., ch. 491, § 2(e), 1951 Tex. Gen. Laws 868, 1084-85 (repealed 2003).

75. *Id.* § 705.104.

76. *Id.* § 1201.208(a).

77. Act of May 24, 1955, 54th Leg., R.S., ch. 397, § 3(a)(2), 1955 Tex. Gen. Laws 1044, 1046, *repealed by* Act of May 22, 2003, 78th Leg, R.S., ch. 1274, § 26(a)(1), 2003 Tex. Gen. Laws 3611, 4138.

78. TEX. INS. CODE § 1201.208(b)(1).

79. *See Meritor Automotive, 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."); *see also 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 excluded).

80. TEX. INS. CODE §§ 705.003(a), 705.004(a).

81. *Id*. § 705.003(b). This requirement is generally consistent with the fraud requirement in the now-repealed article 21.19. *See* Insurance Code, 52d Leg., R.S., ch. 491, § 2(b), 1951 Tex. Gen. Laws 868, 1075 (repealed 2003).

82. *Id*. § 705.004(b).

83. *Id*. § 1201.272.

84. *Id*. § 1202.051(c)(2).

85. *See* Rob Norton, *Unintended Consequences,* THE CONCISE ENCYCLOPEDIA OF ECONOMICS, http://www.econlib.org/library/Enc/UnintendedConsequences.html (last visited August 19, 2007) ("The law of unintended consequences, often cited but rarely defined, is that actions of people – and especially of government – always have effects that are unanticipated or 'unintended.").

STATE BAR OF TEXAS

ANNUAL MEETING

JUNE 26, 2008
HOUSTON, TEXAS

INSURANCE LAW SECTION

ANATOMY OF AN INSURANCE CASE

3.0 HOURS CLE/1.0 HOURS ETHICS

COURSE DIRECTOR, Karen Keltz **EXECUTIVE DIRECTOR, Donna Passons**

1:30 pm **Section Business Meeting**

CLE PROGRAM

2:00 pm **Introductory Remarks and Moderator**
Brian Martin, Houston

2:05 pm **Anatomy of an Insurance Policy**
Linda Dedman, Dallas

2:35 pm **Getting it Started: Selection of**
(.5 Ethics) **Independent Counsel**
Trevor Hall, Amarillo

3:05 pm **BREAK**

3:25 pm **Where Do We Go From Here:**
The Duty to Defend/Extrinsic Evidence
Michael Huddleston, Dallas
Karen Keltz, Dallas

3:45 pm **Preparing the Insurance Witness**
(.5 Ethics) Meloney Perry, Dallas

4:10 pm **Mechanics of Auto, Liability, Property Insurance**
Bill Chriss, Austin
Janet Colaneri, Arlington

4:40 pm **Who Pays: The Right to Reimbursement**
Robert Perry, Dallas

5:05 pm **What the Supreme Court Had to Say this Year**
Brian Blakeley, San Antonio
Lee Shidlofsky, Austin