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# Misrepresentation in Renewal Application Voids Professional Liability Policy

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*Lawyers for the Profession® Alert*

*Illinois State Bar Association Mutual Insurance Co. v. Law Office of Tuzzolino and Terpinas,* 2015 IL 117096, 2015 WL 728111 (2015)

**Brief Summary**

The Illinois Supreme Court held that an insurer rescind a professional liability policy because it was procured with a false statement of facts, even though another attorney with the firm did not know about the misrepresentation.

**Complete Summary**

This case arose from a partner's statement to the Illinois State Bar Association Mutual Insurance Co. ("ISBA Mutual") on a professional liability insurance renewal form. While renewing the firm's policy in May 2008, the partner ("Partner A") claimed that none of the members of his law firm were aware of any pending claims against its lawyers. That was less than three months after that partner was allegedly confronted by a client, who alleged that partner failed to inform him about a separate suit being dismissed from court.

When the other partner at the firm ("Partner B") received a lien letter from the client's attorney in June 2008, he immediately informed ISBA Mutual, which filed suit about a year later seeking to rescind the firm's policy and arguing that it had no duty to defend against the client's claims.

ISBA Mutual argued that Section 154 of the Illinois Insurance Code allowed for rescission of the policy in its entirety. Section 154 states that a misrepresentation on an insurance policy application "made by the insured or in his behalf" can void the policy if it is "made with actual intent to deceive or materially affects either the acceptance of the risk or the hazard assumed by the company."

Partner B disagreed and argued that it was against public policy and the common law "innocent insured doctrine" to hold him accountable for Partner A's alleged lie, of which he had no knowledge.

The Illinois Supreme Court noted that Illinois cases that have used the "innocent insured doctrine" have often been arson or vandalism cases "where an innocent insured seeks recovery under a policy that includes an exclusion for intentional acts." The court noted that the appellate court cited the 1979

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case of *Economy Fire & Casualty Co. v. Warren*, 71 Ill.App.3d 625, 390 N.E.2d 361 (1st Dist. 1979), in which a husband's share of a settlement was sustained even after his wife claimed to have set the fire that damaged their home. The Illinois Supreme Court agreed with ISBA Mutual, however, in noting that case was different because it involved rescission of a settlement agreement, not the rescission of an insurance policy falling under Section 154 of the Insurance Code.

The court then stated that this case was more similar to *Home Insurance Co. v. Dunn*, 963 F.2d 1023 (7thCir. 1992), where the court ruled that it did not matter when other attorneys were unaware of a colleague's misrepresentations on a malpractice policy application. "[T]he falsehood on the application is fatal," the 7th Circuit held, because it caused the insurer to issue a policy to all the attorneys "that otherwise would not have been forthcoming."

The Illinois Supreme Court went on to explain the difference between policy exclusions — triggers that void a policy after it has been issued — and rescission, an act that establishes that the policy or contract was void from the outset. "In the case of a misrepresentation that materially affects the acceptance of the risk, the issue is the effect of that misrepresentation on the validity of the policy as a whole. A misrepresentation on the policy application goes to the formation of the contract,"

The court stated: "The innocent insured doctrine, on the other hand, has a narrower focus, typically dealing with the situations where an insured's wrongdoing triggers a policy exclusion, and the question is whether the insurer has a duty to defend the innocent insured under a policy that is still in effect."

The court also held that the appellate court was wrong to partially sever the policy in order to apply the innocent insured doctrine because although the clause creates a separate agreement with each insured party, each agreement is made of the "particulars and statements contained in the application."

The dissenting justice noted that the innocent insured doctrine aims to protect people who could not have reasonably known that a co-insured's wrongdoing would hurt them. The dissent indicated that the court's ruling will cause trouble for midsize and large law firms. "Under the majority's view, a material misrepresentation on an insurance application could cause rescission of the policy as to each and every attorney, despite their reasonable expectations of continued professional liability insurance coverage," the dissenting justice wrote. He also stated that "as the size of the affected firm increases, so does the potential harm to the public."

**Significance of Opinion**

This decision is significant because the Illinois Supreme Court ruled against coverage given the materiality of the insured's misstatement on the renewal application. This opinion underscores the importance of any claims or circumstances which may reasonably give rise to a claim to an insurer during the application or renewal process.

For more information, please contact Terrence P. McAvoy.

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