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Rescission Of Medical Malpractice Liability Policy Permitted Barring Innocent Third Party Recovery Even Though Statute Requires That Physicians Have Insurance

December 4, 2015

In DeMarco v. Stoddard, A-104-13, decided December 1, 2015, the New Jersey Supreme Court, in a 5-2 decision, held that an insurer may rescind a policy of medical malpractice liability insurance and have no duty to defend or indemnify its insured, who made material misrepresentations on the application for insurance, for a claim made against the insured by an innocent third party.

The Court's decision overturned the Appellate Division which followed the automobile liability insurance model for innocent third-party claimants whose claims arose prior to rescission.

The plaintiffs filed a malpractice suit against a defendant podiatrist, claiming the podiatrist negligently performed surgery upon the husband plaintiff, causing him injury. The podiatrist sought coverage from his malpractice insurer, the Rhode Island Medical Malpractice Joint Underwriting Association ("RIJUA"). The RIJUA denied coverage to the insured podiatrist because he had misrepresented on his application for insurance that 51% or more of his practice was based in Rhode Island. The plaintiffs then amended their complaint to include the RIJUA and sought declaratory judgment that it was required to defend and indemnify the defendant podiatrist up to the $1 million limit of the policy. The plaintiffs and the RIJUA filed cross-motions for summary judgment, and the motion court granted summary judgment to the plaintiffs. The RIJUA then appealed, and the Appellate Division affirmed the motion court's order, holding that, although rescission of a compulsory medical malpractice liability insurance policy due to misrepresentation of material facts in the application was permitted, a patient whose claim arose prior to rescission should be protected, up to the minimum amount of statutorily required coverage, analogizing to the compulsory automobile insurance model which does not permit rescission of coverage after an insured injures an innocent third party.

The RIJUA then sought leave to appeal which the Supreme Court granted. The Supreme Court overturned the decision of the Appellate Division. The Supreme Court analogized medical malpractice insurance with

legal malpractice insurance and cited to the well-developed body of law that exists regarding rescission of legal malpractice insurance policies. The Court noted that it is well-established that an attorney will not have malpractice coverage to respond to claims from injured third parties if a professional liability policy has been rescinded due to misrepresentations of material fact in the policy application. It concluded that the same reasons that permit rescission of legal malpractice liability policies pertain to medical malpractice liability policies. In both cases, misrepresentation of a material fact in the application undermines the insurer's risk assessment and its ability to decide to provide coverage. To permit reformation to conform to a statutorily mandated minimum amount would suggest that such fraudulent conduct is condoned. Finally, the Supreme Court specifically rejected the Appellate Division's analogy to compulsory automobile insurance, holding that the statutes pertaining to that insurance specifically reject rescission of such policies after an innocent third party is injured. In a dissent, Justice Albin opined that the majority decision is contrary to New Jersey public policy that innocent third parties should be protected where insurance is compulsory.

Should you have any questions, please feel free to contact Vincent E. Reilly, Esq. or Jason A. Pozner, Esq.