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A ROAD MAP FOR MOTOR VEHICLE INSURERS AND OWNERS

Court of Appeals Calls for Special Panel to Decide Whether Innocent Third Party Rule Survives in PIP Claims

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SECRET WARDLE NOTES

Bazzi remains the law in Michigan at this time. The conflict procedure invoked by the panel in *Southeast Michigan Surgical Hospital, LLC v Allstate Ins Co*, ___ Mich App ___; ___ NW2d ___ (2016) requires the chief judge of the Michigan Court of Appeals to poll all Court of Appeals judges as to whether the issue in question is outcome determinative and whether it merits convening a special panel to resolve the conflict that would exist had the panel in *Southeast Michigan Surgical Hospital, LLC* not been compelled to follow existing authority. If the poll indicates that a special panel should be convened, then a panel of seven judges, not including any that decided either *Bazzi* or *Southeast Michigan Surgical Hospital, LLC*, will be randomly selected. Their decision of the “innocent third party” issue will be binding on all panels of the Michigan Court of Appeals unless reversed or modified by the Michigan Supreme Court.

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In *Bazzi v Sentinel Ins Co*, ___ Mich App ___; ___ NW2d ___ (2016), a panel of the Michigan Court of Appeals recently held, in a case involving a claim for PIP benefits, that the innocent third party rule precluding the rescission of a contract for fraud as against an innocent third party did not survive the Supreme Court’s decision in *Titan v Hyten*, 491 Mich 547; 817 NW2d 562 (2012). A different panel has now issued a published opinion disagreeing with the *Bazzi* decision and calling for a special conflict panel to take up the issue.

The case is *Southeast Michigan Surgical Hospital, LLC v Allstate Ins Co*, ___ Mich App ___; ___ NW2d ___ (2016). The Court of Appeals again, as in *Bazzi*, faced the question of whether an insurer that discovered fraud by its insured in the procurement of insurance after the occurrence of an accident could rescind the policy as against an innocent third party injured in the accident. The panel followed *Bazzi*, as it was required to do, but expressly stated that it did so only because compelled by court rule, declared a conflict, and called for the convening of a special conflict panel to resolve the issue.

Before reaching the innocent third party issue, the Court of Appeals considered and rejected two alternate grounds for affirming the trial court's denial of the insurer's motion for summary disposition. First, Plaintiffs argued that the claim of fraud in the inducement was waived because it was never validly asserted as an affirmative defense. The Court rejected this argument because, even though the insurer, Allstate, did not validly assert fraud in the inducement, a belated amendment of affirmative defenses would not prejudice the Plaintiffs. This was because Plaintiffs, at the time of filing the complaint in this matter, were already time-barred from asserting a claim against any other insurer or against the assigned claims facility. Thus, "whether or not Allstate's delay in asserting the claim could be considered good practice, it did not have a practically prejudicial effect."

The Court rejected Plaintiffs' claim of equitable estoppel for the same reason. Plaintiffs could not establish the element of prejudice because they were already time-barred from asserting a claim against the assigned claims facility before the complaint was filed in the case before the Court.

Turning to the innocent third party issue, the Court noted that the insurer in *Hyten* "challenged only its responsibility for the liability coverage in excess of the statutory minimum, acknowledging its responsibility for the statutory minimum liability coverage." The panel then characterized the Court's holding in *Hyten*, *supra*, as "holding that when an insurance contract providing coverage in excess of the statutory minimum is procured via fraudulent misrepresentation, the insurer may invoke the traditional remedy to rescind the excess coverage 'notwithstanding that the fraud was easily ascertainable and the claimant is a third party.'" The panel went on to observe that the Court in *Hyten* did not address an insurer's responsibility for PIP benefits under Michigan's statutory "no-fault" scheme. While compelled to follow *Bazzi*, the panel distinguished *Hyten* as only involving the avoidance of *contractual* insurance entitlements in excess of the statutory minimum, whereas the alleged innocent third party's insurance entitlement in the case before the Court was "statutorily mandated, not contractual."

The panel approvingly quoted the unpublished decision of *State Farm Mut Auto Ins Co v Michigan Muni Risk Mgmt Auth*, unpublished per curiam decision of the Michigan Court of Appeals, issued February 19, 2015 (Docket Nos. 319709 & 319710), which held that "the holding of *Titan*, that an insurance carrier may seek reformation to avoid liability for *contractual* amounts in excess of statutory minimums, does not compel a finding that *Titan* overruled the many binding decisions of this Court applying the 'innocent third-party rule' in the context of PIP benefits and an injured third party who is statutorily entitled to such benefits."

The Court concluded that "were we not bound by *Bazzi*, we would find that the innocent third party doctrine is still viable in the context of an innocent third party's claim for PIP benefits under Michigan's no-fault insurance act." Furthermore, the panel agreed with and adopted in full Judge Beckering's dissenting opinion in *Bazzi*. Judge Beckering had reasoned that since "*Titan* did not address benefits that were required by statute," she was "disinclined to extend *Titan* and its reasoning to the innocent third party rule as that rule applies to statutorily mandated PIP benefits."

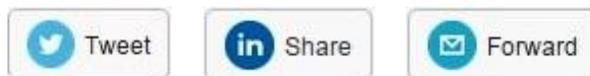
The panel concluded by calling for the convening of a special conflict panel pursuant to MCR 7.215(J)(2).

Judge Sawyer concurred that the alternate grounds asserted for reversal did not warrant reversal, and with the majority's conclusion that the result was controlled by *Bazzi*. However, Judge Sawyer agreed with the majority in *Bazzi* and therefore dissented from the majority's call to convene a special conflict panel.

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