

Honesty is the Best Policy

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Many professionals know their liability insurance policies are written on a “claims-made” basis, meaning the policies provide coverage for claims made within the policy period and not when the event occurs. Due to the nature of these policies, those seeking coverage are required to report all known pending or potential claims when submitting applications for new policies or renewing existing ones. A recent ruling from the United States District Court for the Western District of Missouri highlights the importance of honest reporting of all pending and potential claims. See [*N. Am. Capacity Ins. Co. v. KM Teh Realty 5, LLC*](#).

In November 2019, a class of individuals (the “Fuentes Class”) filed a lawsuit against the former owner of an apartment complex, KM TEH Realty 8, LLC (“KM 8”), alleging the complex was uninhabitable. The following month, KM 8 signed and submitted an application for insurance with North American Capacity Insurance Company (“Capacity Ins. Co.”) but failed to disclose the pending litigation. Unaware of the litigation and in full reliance on KM 8’s application, Capacity Ins. Co. issued a policy (“2019 Policy”) to KM 8 and other related entities.

In September 2020 the Fuentes Class obtained a \$62,682,672.30 judgment against KM 8 and proceeded to initiate a second class-action to collect the judgment. In December 2020, KM 8 and the other related entities attempted to renew and replace the 2019 Policy with three separate policies, submitting new applications for all three. Again, KM 8 and the other entities failed to disclose the pending litigation.

In a declaratory action brought by Capacity Ins. Co., the court found KM 8’s and the other entities’ failure to disclose the known pending litigation—despite the applications expressly requiring the disclosure of such litigation—amounted to material misrepresentations as a matter of law. The court therefore granted Capacity Ins. Co.’s motion for summary judgment to rescind the four policies. Notably, the court specifically found irrelevant the fact that some of the subsequent owners were not the entities who submitted the false applications.

While the actions of KM 8 and the other related entities were egregious, the lessons learned from their mistakes are worth the attention of all professionals seeking to apply or renew their liability policies. In short, insurance applications are not just formalities. They require an honest assessment of all pending and potential claims—even those that may seem unimportant or meritless. The failure to disclose can allow an insurance carrier to rescind the insurance policy. And the would-be insured could be exposed to significant liability.