

Court Finds Triable Issue of Fact as to Rescission of Health Insurance, but Upholds Dismissal of Bad Faith and Punitive Damage Claims

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Following the Hailey and Nieto decisions, issues exist whether a Health Care Service Plan completed sufficient medical underwriting prior to rescission

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In [Nazaretyan v. California Physicians' Service](#), ___ Cal. Rptr. 3d ___, 2010 WL 1038685 (2010), the California Court of Appeal reversed the trial court's grant of summary judgment in favor of California Physicians' Service dba Blue Shield of California ("Blue Shield"), a health care service plan, following its rescission of Gevork Nazaretyan and Narine Ghazaryan's (the "Plaintiffs") health care coverage. In a fact-driven decision, the Court of Appeal held that Blue Shield failed to establish, as matter of law, that its investigation prior to issuing Plaintiffs' coverage was sufficient to demonstrate that it completed medical underwriting, as required under [Health & Safety Code § 1389.3](#), to rescind for non-willful, material misrepresentations in the application for coverage.

The Court of Appeal also concluded that, as a matter of law, it could not hold that the Plaintiffs, who are husband and wife, willfully misrepresented material information in their application to Blue Shield. However, the Court of Appeal affirmed summary adjudication in Blue Shield's favor on the Plaintiffs' bad faith and punitive damage claims.

In August 2004, the Plaintiffs applied for health care coverage with Blue Shield with the assistance of their long-time insurance broker Ahman Yusop. On September 10, 2004, Blue Shield sent Yusop a form requesting information that was missing from the initial application. On September 21, 2004, the missing-information form was returned to Blue Shield with the questions answered, and on October 12, 2004, the Plaintiffs resubmitted their application to Blue Shield. Based on the information in the applications, Blue Shield approved coverage at its most favorable rate on November 1, 2004.

On May 17, 2005, Ghazaryan gave birth prematurely to twin girls, which were conceived as a result of in vitro fertilization ("IVF"). On or about November 11, 2005, the Plaintiffs' case was referred to Blue Shield's eligibility review unit ("ERU"), which was responsible for investigating potential material misrepresentations or nondisclosure of medical history by Blue Shield subscribers. In the course of its investigation, the ERU obtained medical records revealing that Ghazaryan had begun IVF treatments in 2004 and also had undergone a "D & C procedure" for spontaneous abortions in October 2002 and October 2004. The records also showed that on October 12, 2004, Ghazaryan was seen for an infertility evaluation and was scheduled for the various steps of the IVF procedure. During discovery, Blue Shield also learned that in 2002, the Plaintiffs had undergone fertility treatment including IVF, and that their second round of IVF treatment began on August 17, 2004, before they first applied to Blue Shield.

There were several places on the application to Blue Shield where the Plaintiffs should have disclosed their previous and ongoing infertility treatments, but they failed to do so. Had the Plaintiffs disclosed that they were being treated for infertility, Blue Shield would not have issued coverage to them. On March 24, 2006, Blue Shield sent the Plaintiffs a letter advising them that their coverage had been rescinded, effective November 1, 2004. The Plaintiffs filed suit against Blue Shield in July 2006, and on October 29, 2005, the trial court entered judgment in favor of Blue Shield following its motion for summary judgment. The Plaintiffs appealed.

The Court of Appeal first acknowledged the leading decisions of [*Hailey v. California Physicians' Service*](#), 158 Cal. App. 4th 452 (2007), and [*Nieto v. Blue Shield of California Life & Health Ins. Co.*](#), 181 Cal. App. 4th 60 (2010), which also dealt with rescission of a member's coverage by a health care service plan. (See summary of Nieto [here](#).)

The Court noted that, as discussed in *Hailey*, a health care service plan is entitled to rescind a plan contract on the basis of material misrepresentations in the application if either of the following two conditions is satisfied: (1) The plan completed medical underwriting before issuing the plan contract; or (2) the subscribers willfully made material misrepresentations in their application. According to the *Hailey* court, to complete medical underwriting the plan must "make reasonable efforts to ensure a potential subscriber's application is accurate and complete."

Thus, the Court of Appeal in *Nazaretyan* first examined whether Blue Shield provided sufficient facts to demonstrate as a matter of law that it had completed medical underwriting. It determined that Blue Shield had not, for purposes of summary judgment, provided sufficient facts in that regard with respect to the Plaintiffs' coverage.

In reaching this conclusion, the Court of Appeal specifically noted that Blue Shield did not identify what efforts it undertook, beyond making sure that no required fields in the application were left blank and checking its own systems, to otherwise confirm that the Plaintiffs' application was accurate and complete.

The Court next examined whether the Plaintiffs willfully misrepresented information in their application to Blue Shield. According to the Plaintiffs, their broker filled out the applications, and they merely signed the applications without reading them. Their broker, Yusop, testified that, apart from the signatures, all of the handwriting on the applications was his. The Plaintiffs further asserted that because of both their limited education and English language skills (both were immigrants) and Yusop's expertise, they trusted and relied on him to ask them for any necessary information and to record the information accurately on the application (as well as to copy certain information from a previous application in his files). Because the Court of Appeal had to accept these facts as true in ascertaining whether summary judgment was appropriate (and specifically noted that it did not hold the Plaintiffs' version of the facts as true), it found that as a matter of law it could not conclude that the Plaintiffs willfully misrepresented information in their application.

In addition, the Court of Appeal rejected Blue Shield's argument that the rescission did not constitute unlawful postclaims underwriting because it was not "due to" any underwriting failure on the part of Blue Shield, as required by [Health & Safety Code § 1389.3](#). Blue Shield contended

that the Plaintiffs introduced no evidence that “had any further inquiry of some sort been made [by Blue Shield,] it would have revealed the concealed information.” The Court of Appeal rejected this argument, concluding that Blue Shield failed to carry its initial burden on the argument for purposes of summary judgment; thus, the burden never shifted to the Plaintiffs to introduce evidence of their own.

Finally, the Court of Appeal affirmed the grant of summary adjudication on the Plaintiffs’ bad faith and punitive damage claims against Blue Shield. In so doing, the Court specifically distinguished *Hailey*, where the appellate court reversed summary adjudication on bad faith and punitive damages, noting that unlike *Hailey*, there was no evidence of any delay on Blue Shield’s part in investigating and rescinding the agreement.