

## **Insurance Fraud, Agency, and Opportunism: False Swearing in Insurance Claims**

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## INSURANCE FRAUD, AGENCY, AND OPPORTUNISM: FALSE SWEARING IN INSURANCE CLAIMS

*Jay M. Feinman\**

This paper discusses the law of insurance fraud at the point of claim, what in the United States is known as the “false swearing” doctrine.<sup>1</sup> It situates that doctrine within the broader landscape of both the claims process and of responses to insurance fraud. It suggests the proper contours of the doctrine and the applicable standard of proof and changes in other doctrines that address the particular problem of false swearing and the broader problem of agency and opportunism in insurance claims by both insured and insurer. The false swearing doctrine should require reliance by the insurer and proof by clear and convincing evidence, and the insurer’s conduct in asserting fraud should be evaluated by a reasonableness standard.

### I. THE FALSE SWEARING RULE

In the United States, as in the United Kingdom, false swearing by an insured in a proof of loss or other element of the claim process enables the insurer to avoid paying a claim, even if the false swearing concerned only a portion of the loss.<sup>2</sup> Most insurance policies in the US explicitly include a provision declaring that fraud or other false statements permit the insurer

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<sup>1</sup> There is a related problem of the provision of erroneous information by the insured negligently but not intentionally that is not within the scope of this paper. On the broader issue, see George M. Cohen, *The Negligence-Opportunism Tradeoff in Contract Law*, 20 *Hofstra Law Review* 941 (1992).

<sup>2</sup> Jeffrey W. Stempel & Erik S. Knutsen, *Stempel and Knutsen on Insurance Coverage* § 908[C] at 9-221 (4th ed. 2015); Robert H. Jerry II & Douglas R. Richmond, *Understanding Insurance Law* § 83 (5th ed. 2012); *Versloot Dredging BV and another v. HDI Gerling Industrie Versicherung AG and others*, [2016] UKSC 45, ¶ 1.

to void the policy.<sup>3</sup> The first paragraph of the 1943 New York Standard Fire Policy—the “165 Lines” that became the basis for many standard, legislatively adopted policies—states such a provision:

**Concealment, Fraud**

This entire policy shall be void if, whether before or after a loss, the insured has willfully concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof, or the interest of the insured therein, or in case of any fraud or false swearing by the insured relating thereto.

More modern examples expand on the concept:

**I. Conditions**

**R. Concealment Or Fraud**

We provide coverage to no "insureds" under this policy if, whether before or after a loss, an "insured" has:

1. Intentionally concealed or misrepresented any material fact or circumstance;
  2. Engaged in fraudulent conduct; or
  3. Made false statements;
- relating to this insurance.<sup>4</sup>

Violation of such a provision generally requires that the insured make a false statement regarding a material fact with an intent to deceive the insurer.<sup>5</sup> Some but not all jurisdictions also require that the insurer have relied on the misrepresentation.<sup>6</sup>

This simple statement of the doctrine conceals much complexity, of course. The Appleman treatise notes, for example, that

The rules thus far set forth are generally accepted. A few cases apply them far more stringently than do the great majority of decisions. . . . The great majority of cases, while following the general principles enunciated, take a liberal construction. . . . The delineation line between the tests used by the various courts is

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<sup>3</sup> 13 Couch on Insurance § 197:1.

<sup>4</sup> ISO, Homeowners-3 Special Form, HO 00 03 05 11 (2010).

<sup>5</sup> 13 Couch on Insurance § 197:33.

<sup>6</sup> Id. at § 197:4, 19.

narrow and wavering, but should, perhaps, be at least indicated.<sup>7</sup>

And there is a minority rule that false swearing enables an insurer to avoid coverage only as to the portion of the claim that was misrepresented.<sup>8</sup>

## II. THE BASIS FOR THE RULE

The false swearing doctrine rests on four bases that span legal doctrine, morality, and public policy.

The first rationale for the false swearing rule is doctrinal. Part of the insured's contractual obligation with the insurer is to refrain from misrepresentation in the claim process. The obligation is clear and specific where the insurance policy contains a provision relating to misrepresentation after a loss, as in the 165 Lines. Even if the provision is less specific, it reasonably is interpreted to apply to post-loss conduct as well as to misrepresentations in the course of applying for the insurance.<sup>9</sup> This element of the analysis is an instance of a fundamental principle of insurance law, that the relation between insurer and insured is created and substantially defined by their agreement.<sup>10</sup> Indeed, even if an express provision was not included, the obligation to avoid misrepresentation would attach because of the general obligation of good faith inherent in every contract.

The second rationale provides an economic justification for the false swearing doctrine. Left to its own devices, an insured has an incentive to misrepresent or conceal information from its insurer during the claim process in order to maximize its recovery. This behavior runs a spectrum from the callously deceitful, as the functional equivalent of stealing, to the wrong but less ill-spirited, to make up for an inadequacy of record-keeping or a careless decision to under-insure. As the New Jersey Supreme Court stated the concern, "Such misrepresentations strike at the heart of the insurer's ability to acquire the information necessary to determine its

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<sup>7</sup> Appleman on Insurance Law & Practice Archive § 3587 (2nd ed. 2011).

<sup>8</sup> Stempel & Knutsen, *supra*, at § 908[C] at 9-221,222.

<sup>9</sup> Longobardi v. Chubb Ins. Co. of New Jersey, 582 A.2d 1257, 1261 (N.J. 1990).

<sup>10</sup> See Kenneth S. Abraham, Four Conceptions of Insurance, 161 University of Pennsylvania Law Review 653, 658 (2013).

obligations and to protect itself from false claims.”<sup>11</sup> Insurers, being aware of this possibility, must invest resources to monitor insureds’ behavior and to ferret out their fraud. The false swearing doctrine deters wrongful behavior by insureds and reduces the need for inefficient monitoring behavior by insurers.

The third rationale is moral: *fraus omnia corrumpit* (“fraud corrupts all”). Davey and Richards describe this principle as “a broadly moral purpose consistent with judicial refusal to engage with those who commit fraud.”<sup>12</sup> In the ordinary contract context the principle allows for the avoidance of a contract for fraud.<sup>13</sup> In the insurance fraud context this is the story Baker describes as “the immoral insured”: “The normally decent, law-abiding American . . . , if left to his own devices, has a little larceny in his soul . . . . And really, people can’t see it as anybody’s money. The insurance company and the federal government—people like that—they are fair game where the public is concerned.”<sup>14</sup>

The first three rationales focus on the two-party relation between insurer and insured. The fourth rationale treats the two-party relation as one among many similar relations. Baker colorfully expresses this as the merger of the story of the “immoral insured” with the story of the “depravity of those who threaten the public interest.”<sup>15</sup> Insurance fraud by false swearing cheats not only the individual insurer but the pool of insureds that the insurer embodies. The same logic extends the deterrence and efficiency rationales; false swearing deters behavior and minimizes investigative costs, both of which ultimately are borne by all insureds. The false swearing rule deters insurance fraud that otherwise “results in substantial and unnecessary costs to the general public in the form of increased rates.”<sup>16</sup>

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<sup>11</sup> 582 A.2d at 1261. See also James Davey & Katie Richards, Deterrence, Human Rights and Illegality: The Forfeiture Rule in Insurance Contract Law, *Lloyds Maritime and Commercial Law Quarterly* 2015, 315, 318.

<sup>12</sup> Davey & Richards at 318.

<sup>13</sup> 7 Joseph M. Perillo, *Corbin on Contracts* § 28.21 (rev. ed. 2002).

<sup>14</sup> Tom Baker, “Constructing the Insurance Relationship: Sales Stories, Claims Stories, and Insurance Contract Damages,” *72 Texas Law Review* 1395, 1411 (1994).

<sup>15</sup> *Id.*

<sup>16</sup> *Merin v. Maglaki*, 599 A.2d 1256, 1259 (N.J. 1992), referring to the

### III. AGENCY AND OPPORTUNISM

Much of the four-part rationale for the false swearing rule rests on the recognition of a potential problem in the insurance relation: the problem of agency and opportunism by the insured in filing a claim. In an agency relationship, one party has freedom to act in a way that affects the other party and may have different incentives and access to different information that may shape its performance. That creates monitoring problems in which the party subject to the other's action either needs to incur costs in monitoring the performance or takes the risk of a disadvantageous performance. Opportunism is an extreme form of agency in which the party with freedom to act exploits circumstances for selfish advantage without regard for prior commitment — "self-interest seeking with guile."<sup>17</sup> From this perspective, the risk that an insured will conceal or misrepresent information in the claim process is an agency problem in which the insured may act opportunistically.

#### A. *By the Insured*

The doctrinal rationale for false swearing recognizes that a fraud or concealment term in the policy is designed to check agency and opportunism by the insured and that the insurer's ability to avoid coverage is the necessary remedy. The Supreme Court in *Versloot Dredging* noted "the asymmetrical positions of the parties to an insurance contract, the insurer being vulnerable on account of his dependence on the insured for information both at the formation of the contract and in the processing of claims."<sup>18</sup> Even in the absence of a policy term, the general obligation of

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purpose of the New Jersey Insurance Fraud Prevention Act, NJSA 17:33A-2. See also *Versloot Dredging BV*, ¶ 10 ("Fraudulent insurance claims are a serious problem, the cost of which ultimately falls on the general body of policy-holders in the form of increased premiums."), and ¶ 55 (Lord Hughes: "if claims have to be investigated in detail and routinely verified by insurers, the cost of the systems necessary to do this will fall on policyholders generally through increased premiums, and good claims will be delayed alongside the bad.").

<sup>17</sup> Oliver E. Williamson, *Opportunism and Its Critics*, 14 *Managerial & Decision Econ.* 97 (1993). See Cohen, *The Negligence-Opportunism Tradeoff*, at 953-961.

<sup>18</sup> *Versloot Dredging BV*, ¶ 9.

good faith would prohibit fraud by the insured for the same reason.<sup>19</sup>

The economic rationale for the false swearing rule similarly responds to potential agency and opportunism. The false swearing doctrine deters fraudulent breach by the insured and reduces investigation costs by the insurer, both of which reduce their joint costs.<sup>20</sup>

The fourth rationale extends the economic logic to the pool of insureds. The efficient allocation of the risk of fraud and cost of preventing it in an individual transaction becomes the sum of all such individual transactions in considering the interests of the pool.<sup>21</sup>

#### *B. By the Insurer*

The four-part rationale for the false swearing rule embodies a certain vision of the relationship between insurer and insured, one in which the insured's freedom to act in an opportunistic way in the claim process must be checked by the rule. That vision is at best incomplete and its incompleteness leads astray in formulating and applying the rule.

It is true that insured and insurer are in an agency relationship in the claim process and that opportunism is a risk, but agency and opportunism run in both directions; the insurer as well as the insured possesses agency and has incentives to act opportunistically. When a loss occurs, the insured usually lacks effective means of monitoring the company's performance in handling the claim, and policy terms and the surrounding law that measure the company's performance are vague and difficult to enforce. Moreover, it is in the company's interest to not pay a claim or to pay as

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<sup>19</sup> At least in the American context, the obligation of good faith is not an expression of the insurance law doctrine of *uberimma fides*, with its grand translation of "utmost good faith," See R. A. Hasson, *The Doctrine of Uberimma Fides in Insurance Law—A Critical Evaluation*, 32 *Modern Law Review* 615 (2011), or what Judge Posner described as "injection of moral principles into contract," "some newfangled bit of welfare-state paternalism," or "the sediment of an altruistic strain in contract law." *Market Street Associates v. Frey*, 941 F.2d 588 (7th Cir. 1991). See Jay M. Feinman, *Good Faith and Reasonable Expectations*, 67 *Arkansas Law Review* 525 (2014).

<sup>20</sup> *Mkt. St. Assocs. v. Frey*, 941 F.2d at 595.

<sup>21</sup> The moral rationale may speak more broadly about external norms of morality, but it seems to be at most a minor theme in the case law.

little as possible. The company that denies payment of a claim in whole or part increases its profits. The company that only delays payment of a claim increases its investment income and thereby increases its profits. Market competition, reputational effects, and administrative regulation fail to provide effective checks on opportunistic behavior.<sup>22</sup>

The false swearing doctrine aims to respond to opportunism by the insured. One might consider the problem of opportunism by the insurer to be entirely separate so that it is irrelevant to the false swearing doctrine and should be addressed through entirely separate doctrines and remedies. But in fact the two problems are linked. One potential form of insurer opportunism is the assertion of fraud by the insured as a reason for not paying a claim. The doctrine that enforces and evaluates that reason becomes a tool for opportunism, and the severe consequences of a finding of false swearing raises the stakes considerably. Therefore, with respect to false swearing in the claim process, agency and opportunism are present on both sides.

Each of the rationales for the false swearing doctrine relates to insurer opportunism as well. Opportunism by insurers constitutes an egregious form of breach of the insurance contract, not only its express terms requiring payment of what is owed but also the obligation of good faith. Insurer opportunism imposes inefficient monitoring costs on insureds, costs many insureds cannot bear at all. It violates moral and legal strictures. And insurer fraud imposes costs on members of the pool whose claims are not paid, just as the prevention of that kind of fraud benefits the entire pool by ensuring that the claim process works better for all claimants.

Resolving the challenge of both types of opportunism should involve considering the relative risk and severity of each of them. How likely are insureds to control relevant information and at what expense could insurers discover it? If an insurer asserts fraud, how likely is an insured to contest its determination? How likely are insurers to opportunistically deny claims? How often does that behavior take the form of improper assertions that the insured's claim is fraudulent? As an introduction to the answers to those questions, consider three elements in the US context, at least the first of which appears to have spread throughout the common law

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<sup>22</sup> Jay M. Feinman, *The Regulation of Insurance Claim Practices*, 5 UC Irvine Law Review 1319 (2015).



world.<sup>23</sup>

First, in large sectors of the insurance industry in the US, opportunism has become systematically embedded in the claim process. Through reorganization of the claims process, incentives to employees and managers, and a more aggressive approach to litigation, the companies have embarked on a strategy that increases profits at the expense of claimants. The strategy involves delaying payment of claims, denying valid claims in whole or part, and forcing insureds to pursue coverage litigation and then aggressively defending that litigation—“delay, deny, defend.”<sup>24</sup>

Second, the false swearing doctrine is only a small part of a large-scale, public/private system designed to detect, punish, and deter fraud by insureds in the claim process.<sup>25</sup> The evils of insurance fraud and the consequences for fraudsters are marketed to the public through billboards, television advertisements, and promoted news reports. Sophisticated predictive analytics trigger identification of potentially fraudulent claims.

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<sup>23</sup> See, e.g., Sarah Miles, *The Christchurch Fiasco: The Insurance Aftershock and Its Implications for New Zealand and Beyond* (2012), discussing the insurance response to earthquakes in Christchurch, NZ. (“A second major disaster is currently taking place in Christchurch—the insurance aftershock, in which tens of thousands of people are currently being cynically exploited by the local insurance industry.” *Id.* at 110.)

<sup>24</sup> .” See Jay M. Feinman, *Delay, Deny, Defend: Why Insurance Companies Don’t Pay Claims and What You Can Do About It* (2010). In the most famous and well-documented example, Allstate retained McKinsey & Co. “to redefine the game ... to ... question, improve, and radically alter our whole approach to the business of claims.” “We can and should manage specific components of severity [the average paid on claims] to provide greater financial support to the company.” In short, “We will win the economics game. ... Winning will be a zero sum game.” *Id.* at 10-11. In another well-known example, Unum, the largest seller of disability insurance and long-term care insurance in the United States, was castigated by numerous courts and regulators for unscrupulous tactics and an opportunistic lack of objectivity amounting to bad faith in denying claims. See *Radford Trust v. First Unum Life Ins. Co.*, 321 F. Supp. 2d 226, 247 (D. Mass. 2004); John H. Langbein, *Trust Law as Regulatory Law: The Unum/Provident Scandal and Judicial Review of Benefit Denials under ERISA*, 101 *Northwestern University Law Review* 1315 (2007).

<sup>25</sup> Feinman, *Delay, Deny, Defend*, ch. 10.

Insurance companies contain Special Investigation Units to which claims of fraud are referred for more aggressive investigation. Insurance regulators and prosecutors in most states have established distinct units to seek civil and criminal penalties for fraud, and legislation often requires insurers to report suspected cases of fraud to them. All states now make insurance fraud a crime, with two-thirds of the states treating it as a felony.

Third, the reorganization of the claim process and the increased attention to insurance fraud are connected. No doubt insurance fraud is a problem, but likely not on the scale that is often proclaimed. The most authoritative quantitative study of insurance fraud concluded that the ratio of fraud alleged and reported by insurance companies to actual, provable fraud, was about 25 to 1.<sup>26</sup> To a considerable extent, the campaign against fraud by insureds is part of the redesign of the claim process so that “Proactive fraud detection and handling of suspected claims should reduce fraudulent activity and positively impact claim costs,” as mega-consultant McKinsey & Co. suggested to Allstate in its redesign of the claim process.<sup>27</sup>

Industry advocates of course disagree with my characterization of the claim process and the insurance fraud campaign.<sup>28</sup> For present purposes, the essential point is that the possibility of insurer opportunism in the claim process and its manifestation in excessive claims of fraud is at least significant enough to enter into consideration of false swearing cases. The insurer’s and the pool’s interest in preventing fraudulent claims are legitimate, but so are the insured’s and the pool’s interest in preventing fraudulent claims of fraud.

## V. RESPONSES TO OPPORTUNISM

The false swearing rule focuses on agency and opportunism by the insured. The presence or at least possibility of insurer opportunism requires a more balanced response than the all-or-nothing consequences of the rule.

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<sup>26</sup> Richard A. Derrig, *Insurance Fraud*, 69 *Journal of Risk and Insurance* no. 3, 271 (2002).

<sup>27</sup> Feinman, *Delay, Deny, Defend*, at 173.

<sup>28</sup> “The central thesis of ‘Delay, Deny, Defend’ is unsupported by the facts.” Robert P. Hartwig, President, Insurance Information Institute, 24 March 2011.

An analogous instance of balancing insurer, insured, and pool interests in cases of misrepresentation involves misrepresentation or concealment at the front end of the insurance relationship, in the application process. Information provided by the insured in the process of applying for an insurance policy should play a significant part in the underwriting decision of the insurer—whether to issue the policy, with what terms of coverage, and at what rate. In the classic example of “post-claim underwriting,” however, life insurance companies failed to do proper investigation before issuing the policy; after a claim was filed they would refuse to pay death benefits, asserting that the insured had misrepresented his physical condition or medical history when applying for the policy, which rendered the policy void. These practices caused disproportionate forfeiture because the insured’s beneficiaries lost the benefit of the policy because of a minor error, perhaps knowing or perhaps unintentional, that may or may not have affected the insurer’s underwriting decision. Even worse, companies sometimes required voluminous but vague disclosures on the application for insurance to set up the misrepresentation argument,<sup>29</sup> a clear instance of insurer opportunism. Over time, legislatures and courts recognized this problem and responded in various ways, such as through doctrines of incontestability, waiver, estoppel, and materiality of misrepresentation.<sup>30</sup> Those doctrines attempt to balance the interests of insurer, insured, and pool in checking agency and opportunism on both sides of the insurance relation.

Misrepresentation in the claim process deserves the same type of balanced response. I suggest three types of responses: one about the false swearing doctrine itself, one about the process of litigation of cases, and one collateral to the litigation about the insured’s claim. In each of the first two there is a split among states in the US, and I suggest that one of the two positions is better suited to addressing the presence of opportunism on both sides of the insurance relation.

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<sup>29</sup> E.g., *Connecticut Mut. Life Ins. Co. v. Union Trust Co.*, 112 U.S. 250 (1884); *Baumgart v. Modern Woodmen of Am.*, 55 N.W. 713 (Wis. 1893).

<sup>30</sup> See Thomas C. Cady & Georgia Lee Gates, *Post Claim Underwriting*, 102 *West Virginia Law Review* 809 (2000).

*A. Doctrine*

A doctrinal response that balances the two forms of opportunism, consider the elements of materiality and reliance in the false swearing rule. The basic elements of false swearing permitting an insurer to avoid coverage are a false statement regarding a material fact with an intent to deceive the insurer. Couch on Insurance summarizes the materiality requirement as follows:

The requirement that a misrepresentation be material is satisfied, in the context of an insurer's post-loss investigation, if the false statement concerns a subject relevant and germane to the insurer's investigation as it was then proceeding. Accordingly, false answers are material if they might have affected the attitude and action of insurer, and they are equally material if they may be said to have been calculated either to discourage, mislead, or deflect company's investigation in any area that might seem to the company, at that time, a relevant or productive area to investigate.<sup>31</sup>

The materiality requirement might be thought of as an objective element; a misrepresentation is material if it “concerns a subject relevant and germane to the insurer's investigation” so that it might have deceived the insurer or impeded its investigation of the claim.

The states divide on the related question of whether reliance by the insurer is an element of false swearing. Some jurisdictions hold that materiality is sufficient in itself so reliance is not required; others conclude that the insurer must further prove that it relied on and actually was misled or deceived by the insured's misrepresentations.<sup>32</sup> The latter position is consistent with the law of misrepresentation generally; whether fraud in the inducement is used as a basis for avoidance of a contract<sup>33</sup> or as the basis for a tort cause of action independent of a contract,<sup>34</sup> justifiable reliance is a necessary element.

The more draconian rule that materiality is enough even without reliance is based on the rationales for the false swearing doctrine generally. Courts may emphasize the presence of a concealment or fraud provision in the policy without a specific reliance requirement or the immorality of the

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<sup>31</sup> 13 Couch on Insurance § 197:16 (footnotes omitted).

<sup>32</sup> 13 Couch on Insurance § 197:19.

<sup>33</sup> E. A. Farnsworth, I Farnsworth on Contracts §4.13 (1990).

<sup>34</sup> American Law Institute, Restatement (Second) of Torts §525 (1977).

fraudulent insured.<sup>35</sup> Most important, however, is the need to prevent insured opportunism.

Moreover, if the law out of some misgivings about forfeitures, were to require that the insurer demonstrate that it has been misled to its prejudice by the fraud, the policy provision would be virtually worthless and put a premium on dishonest dealings by the assured. . . . The mendacious assured, surveying the possibilities and contemplating prospective tactics and strategy in the handling of his claim, would sense immediately that vis-a-vis himself and the underwriter, there would be no risk at all in his deceit. If it worked, he would have his money and, at worst, could be compelled to disgorge only by affirmative suit by the insurer if the fraud were discovered in time to be legally or practicably effective. If it didn't work—if, before consummation, fraud was detected—he would suffer no disadvantage whatsoever. *It would be an everything-to-win, nothing-to-lose proposition.*<sup>36</sup>

What this approach fails to recognize, of course, is the possibility of insurer opportunism, in either of two forms. As suggested above, an insurer could use allegations of fraud as part of a broader scheme to deny payment of valid claims. Or it could make use of the non-reliance false swearing rule in a parallel way to post-claim underwriting. If an insurer discovers a misrepresentation during the course of its investigation of a claim, it can use the misrepresentation as a basis for denying the claim even if the misrepresentation played no part in its investigation, just as an insurer in past times could use a misrepresentation on the application even if the misrepresentation they played no role in its underwriting decision.

Accordingly, a false swearing rule that includes a requirement of actual reliance better addresses the twin problems of opportunism by insurer and insured. Oregon law provides an example of the way in which the requirement of reliance works. Oregon originally enacted the fraud and concealment provision of the 165 Lines and in 1985 added a requirement of reliance: "In order to use any representation by or on behalf of the insured

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<sup>35</sup> American Diver's Supply & Mfg. Corp. v. Boltz, 482 F.2d 795, 797 (10th Cir. 1973).

<sup>36</sup> Id. (emphasis in original). See also Longobardi, 582 A.2d at 1262 ("[T]he better rule is one that induces insureds to answer truthfully questions about their losses.")

in defense of a claim under the policy, the insurer must show that the representations are material and that the insurer relied on them."<sup>37</sup> The requirement in the statute "means ordinary reliance, which requires some evidence of a detrimental action or change in position."<sup>38</sup> An insurer losing the opportunity adequately to investigate the cause of a fire and incurring extra investigative expenses<sup>39</sup> or incurring significant expenses associated with being required to conduct a second Examination Under Oath and otherwise incurring time and expense in added investigation of a claim constitute sufficient detrimental reliance;<sup>40</sup> processing the claim independently of the alleged misrepresentations does not.<sup>41</sup>

#### *B. Process*

Some jurisdictions require that the elements of false swearing be proven by clear and convincing evidence; others use only a preponderance of the evidence standard.<sup>42</sup> The former is the standard ordinarily applied in cases involving the tort of fraud, the latter in cases in which fraud is the basis for avoidance of a contract. At a crude doctrinal level, therefore, one way to choose the appropriate burden of proof is to decide whether false swearing is essentially a breach of a term of the contract or a failure of condition under the contract, or whether it is more akin to tortious misrepresentation. One line of authority, for example, distinguishes cases in which the insurer asserts that the insured has attempted to defraud the insurer from those in which the insurer asserts breach of a concealment clause as the basis for voiding the contract.<sup>43</sup> But this makes no sense. The

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<sup>37</sup> Oregon Revised Statutes § 742.208(3).

<sup>38</sup> *Eslamizar v. Am. States Ins. Co.*, 894 P.2d 1195 (Ore. App. 1995). See also Nebraska Revised Statutes § 44-358, applied to misrepresentations in the claim process in *McCullough v. State Farm Fire & Cas. Co.*, 80 F.3d 269 (8th Cir. 1996); *Bryant v. Nationwide Mut. Fire Ins. Co.*, 67 N.C. App. 616, 622, 313 S.E.2d 803, 808 (1984), *aff'd in part, rev'd in part*, 313 N.C. 362, 329 S.E.2d 333 (1985)

<sup>39</sup> *Allstate Ins. Co. v. Breeden*, 410 Fed. Appx. 6, 8 (9th Cir., 2010).

<sup>40</sup> *Leander Land & Livestock, Inc. v. Am. Econ. Ins. Co.*, 2013 WL 5940027, at \*6 (U.S.D.Ct. Ore., Nov. 1, 2013).

<sup>41</sup> *Leavenworth v. State Farm Fire & Cas. Co.*, 297 Fed. Appx. 602 (U.S.D.Ct. Ore., Oct. 22, 2008).

<sup>42</sup> 13 Couch on Insurance § 197:6.

<sup>43</sup> *Hall v. State Farm Fire & Cas. Co.*, 937 F.2d 210, 215 (5th Cir. 1991), citing *McGory v. Allstate Ins. Co.*, 527 So.2d 632 (Miss.1988). See also *McCord v. Gulf*

typical policy provision bars both concealment and fraud and in both cases the gravamen of the insurer's claim and the consequences for the insured are the same.

Therefore, assigning a burden of proof requires more analysis. A canonical exposition of the differences among burdens of proof and the reasons for them is the United States Supreme Court opinion in *Addington v. Texas*.

The function of a standard of proof, as that concept is embodied in the Due Process Clause and in the realm of fact-finding, is to "instruct the factfinder concerning the degree of confidence our society thinks he should have in the correctness of factual conclusions for a particular type of adjudication." The standard serves to allocate the risk of error between the litigants and to indicate the relative importance attached to the ultimate decision.<sup>44</sup>

As the Court further noted, the lower preponderance of evidence standard is appropriate for "the typical civil case involving a monetary dispute between private parties." Because "society has a minimal concern with the outcome of such private suits . . . the litigants thus share the risk of error in roughly equal fashion." In criminal cases "the interests of the defendant are of such magnitude that . . . they have been protected by standards of proof designed to exclude as nearly as possible the likelihood of an erroneous judgment" — that is, proof beyond a reasonable doubt. In between lies the standard of clear and convincing evidence, variously phrased, in which "the interests at stake . . . are deemed to be more substantial than mere loss of money" such as "the risk to the defendant of having his reputation tarnished erroneously" through allegations of fraud or the like. Other uses of the intermediate standard are those in which some public interest is at stake or the effect on the defendant is more severe than a money judgment; in public law these uses include commitment to a mental institution and the termination of parental rights,<sup>45</sup> and in private law, suits on oral contracts to make a will and actions to reform written transactions.<sup>46</sup>

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Guar. Life Ins. Co., 698 So. 2d 89, 92 (Miss. 1997).

<sup>44</sup> 441 U.S. 418, 423-25 (1979) (citation omitted).

<sup>45</sup> 2 Handbook of Federal Evidence § 301:5 (7th ed. 2015).

<sup>46</sup> 2 McCormick on Evidence § 340 at 666-667 (Kenneth S. Broun, general

The use of clear and convincing evidence in a fraud cause of action is well-established.<sup>47</sup> Indeed, the application of the standard is so well established that modern cases seldom specifically explain its logic in fraud cases, but it follows from the general rationale. Allegations of fraud are more serious than allegations of ordinary breach of contract, and “more evidence should be required to establish grave charges than to establish trifling or indifferent ones.”<sup>48</sup>

Under this rationale, false swearing should require proof by clear and convincing evidence. Indeed, false swearing in the insurance context is potentially a more serious matter than some other types of fraud. Insurance is about security and the consequences for the insured in losing the security of the insurance policy are often severe or even catastrophic. Especially where insurer reliance on the misrepresentation is not required, the trier of fact needs to be more certain that the other elements are met before attaching such drastic consequences, and more of the risk of error in fact-finding should be borne by the insurer. Finally, the threat of insurer opportunism in using allegation of fraud as a strategy to avoid paying claims—exploiting false claims of false swearing, as it were—suggests that courts ought to be cautious in enabling an insurer to use a claim of false swearing to entirely void its obligation under the policy and should assign the risk of error in fact-finding to the insurer.

### *C. Other responses*

My argument has been that the best way to understand the false swearing doctrine is to situate it in the broader landscape of insurance claim practices. That perspective argues for a particular approach to elements of the doctrine itself and the process by which it is applied in litigation. But it also suggests that the underlying issue can be addressed by other means as well.

Once again, the first step is to define the underlying issue. The insurer-side perspective is that the issue is the immoral insured. The appropriate response is a draconian false swearing doctrine and an elaborate structure for the investigation and sanctioning of insurance fraud of the kind

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editor; 7th ed. 2013).

<sup>47</sup> 37 American Jurisprudence 2d Fraud and Deceit § 479 (2016).

<sup>48</sup> *Ziegler v. Hustisford Farmers Mut. Ins. Co.*, 298 N.W. 610 (Wis. 1941), citing Jones’ Commentaries on Evidence.



described earlier, wide latitude for an insurer in invoking that structure, and immunity for it from liability for reporting suspected fraud to civil and criminal authorities. In litigation with an insured, an insurer should be subject to liability only for the most grievous errors in challenging a claim as fraudulent, perhaps where it does so intentionally or recklessly alleges fraud that does not exist. Today, in many states, an insurer is protected by such rules in both of these situations.

From the perspective that insurer-side opportunism also is a problem, however, the landscape looks much different and the responses to it should be different as well. The insurance fraud structure is far too elaborate for the scope of the problem and there is little of a parallel structure for investigating and remedying insurer-side fraud in the wrongful delay or denial of claims.<sup>49</sup> One desirable response is to buttress the law of claim practices by requiring an insurer to observe reasonable standards of claim practices and making it civilly liable to an insured where it does not—that is, defining what is usually referred to as “bad faith” to be a negligence standard rather than intent or recklessness.<sup>50</sup> A negligence standard would provide a more effective deterrent for insurer opportunism, including opportunism through improper assertions of fraud by an insured, but still would enable an insurer to deny a claim for false swearing where it is reasonable to do so.

## CONCLUSION

The false swearing rule developed to address the particular problem of agency and opportunism by an insured in the claim process. But that problem is best understood within the insurance claim process in broad perspective, a perspective that recognizes the possibility of agency and opportunism by an insurer as much as—perhaps more than—by an insured. From that perspective, the doctrine needs to be properly defined and applied and supplemented by other doctrines to balance the legitimate interests of insureds and insurers.

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<sup>49</sup> Feinman, *The Regulation of Insurance Claim Practices*, at 1333-40.

<sup>50</sup> See Jay M. Feinman, *The Law of Insurance Claim Practices: Beyond Bad Faith*, 47 *Tort Trial & Insurance Practice Law Journal* 693 (2012).