PLUNKETT COONEY

Supreme Court Holds Innocent Third-Party Rule Does Not Survive, Insurers may Rescind Fraudulent Policies

July 20, 2018

Mary Massaron
(313) 983-4801
mmassaron@plunkettcooney.com

Rapid Report - Appellate Law Practice Group

Since its 2012 decision in *Titan Ins Co v Hyten*, 491 Mich 547 (2012), the Michigan appellate courts have struggled to resolve questions involving the interplay between Michigan's common law defenses to coverage and the statutory provisions establishing recovery under the Michigan No-Fault Act.

In a decision issued late in the Michigan Supreme Court's term in *Bazzi v Sentinel Insurance Company*, __ Mich __ (2018)(Docket No. 154442), the Supreme Court has squarely held that an insurer may rescind a policy obtained by fraud even if an innocent third party seeks mandatory PIP benefits.

In reaching this decision, the Supreme Court announced several clear principles. First, "the plain language of the no-fault act does not preclude or otherwise limit an insurer's ability to rescind a policy on the basis of fraud." As a result, Sentinel is entitled to raise the defense of rescission and seek rescission of the no-fault insurance policy.

Second, the Supreme Court explicitly rejected the idea that a public policy rationale compelled the adoption of the so-called innocent-third-party rule. The court pointed to its earlier holding in *Titan* that "an insurer is not precluded from availing itself of traditional legal and equitable remedies to avoid liability under an insurance policy on the ground of fraud in the application for insurance, even when the fraud was easily ascertainable and the claimant is a third party." *Titan*, 491 Mich at 571.

The *Bazzi* majority explained that the same rationale it had adopted in *Titan* applied here and quoted with approval its statement that "there is simply no basis in the law to support the proposition that public policy requires a private business in these circumstances to maintain a source of funds for the benefit of a third party with whom it has no contractual relationship." *Titan*, 491 Mich at 568-569 quoted with approval in *Bazzi*, slip op at 10.

© 2026 Plunkett Cooney, PC

Third, the Supreme Court rejected the contention that a "there is a controlling distinction between mandatory coverage, i.e., statutorily mandated PIP benefits, and optional coverage." The court expressly pointed out that "[w]hether statutory benefits or optional benefits are at issue, each is predicated on the existence of a valid contract between the insured and insurer." It explained that its "reasoning in *Titan* was not dependent on whether the coverage at issue was mandatory or optional." Instead, according to the *Bazzi* court, "common-law defenses are available when there are contractual insurance policies but limited when a statute prohibits the defense."

But much as insurers and litigants have waited for clarification from the Supreme Court, *Bazzi* raises as many questions as it answers. Rather than simply affirming the Michigan Court of Appeals decision, the majority has remanded to the trial court to "determine whether rescission is available as an equitable remedy as between Sentinel and plaintiff."

The plaintiff's bar will undoubtedly insist that the equities favor the so-called innocent third party, even if, as the dissent recognizes, "[t]he Act created a system in which all insurers share the cost of eligible claims from innocent third parties in proportion to the insurer's market share." *Bazzi*, Hon. Judge Bridget Mary McCormack, dissenting, slip op, p 13. In that circumstance, third-party claimants would be eligible for PIP benefits under the Michigan Assigned Claims Plan, which is the statutory provision intended to address the situation – and, therefore, a strong argument can be made that the equities favor the defrauded insurer.

The dissenting opinion, authored by Justice McCormack, who was joined by Justice David F. Viviano, disagreed with the majority on the basis that innocent third parties "are always eligible claimants" and insisting that the majority's approach will result in "costly litigation to determine in every case who will be the payor and who will be the reimbursor. …" *Id* at p 3. The dissent would "hold that Sentinel may not independently seek to rescind the PIP coverage mandated by the no-fault act but that Sentinel may seek to avoid or reduce its obligations relative to the assigned claims insurer, Citizens Insurance Company, by raising defenses permitted by the Act."

Given the many cases held in abeyance for the *Bazzi* decision, and the issues it has left open, the Michigan appellate courts are likely to remain busy until they can resolve the issues that *Bazzi* left open.

Plunkett Cooney appellate attorney Mary Massaron argued the case before the Supreme Court on behalf of Sentinel Insurance Company. To view Ms. Massaron's oral argument before the court, click here. Writing for the majority, Justice Kurtis T. Wilder's decision was joined by an unusual alliance comprised of Justices Stephen J. Markman, Brian K. Zahra, Richard Bernstein and Elizabeth T. Clement.

© 2026 Plunkett Cooney, PC