

Changes (Maybe) to South Carolina Life Insurance Rescission Procedure

D. Larry Kristinik, III, Nelson Mullins Riley & Scarborough LLP

Changes may be on the horizon in South Carolina for the procedure for life insurers seeking to rescind policies based on material misrepresentations in the application. The South Carolina Legislature is considering adding a provision to the Insurance Code providing that rescission can occur only if either (a) there is a mutual rescission agreement executed by all parties, or (b) the insurer initiates a court proceeding for rescission. This is consistent with the pronouncement by the South Carolina Department of Insurance in Bulletin No. 2019-02 that unilateral rescissions are impermissible under South Carolina law.

But the proposed legislation goes further. In its current form, if a life insurer wishes to rescind without initiating a court proceeding, it can send a letter to the policyholder or beneficiary via certified mail providing the basis for rescission, but the letter must also include a disclosure of rights, including the right to proceed in court and to seek the advice of an attorney. A premium refund check would need to accompany the letter, and language must be included making it clear that negotiating the check is signifying agreement to rescind the policy and that no death benefit will be payable. There has been some debate in the Legislature about the level of detail that will be required regarding the perceived misrepresentations in the application and the basis for deciding that they were false.

The proposed legislation is reflected in House Bill H.4220 and Senate Bill S.744. The latest news on this legislation is that the House Labor, Commerce and Industry Committee advanced the bill out of committee to the full House for consideration, but many House members requested debate, causing the bill to be put on the contested calendar. This will stall the bill, and, with it already being March, it is unlikely the bill can be passed in both chambers of the Legislature before they adjourn for the year. Because this is the second year of a two-year session, the process for this legislation would have to start over from the beginning when the Legislature reconvenes in 2023. Insurers should continue to monitor these bills, in the event the Legislature is able to push it through before the end of this term in May of 2022.

Even without the enactment of the proposed statute, life insurers in South Carolina already must avoid unilateral rescissions. It would be impermissible in the eyes of the Department of Insurance for an insurer to send a rescission letter with a refund check, then take no further action. There must be some acknowledgement by the policyholder or beneficiary that they agree with the decision to rescind and, for beneficiaries, that they will accept the premium refund in lieu of the death benefit. In practice, this means insurers need to follow up and ask beneficiaries to sign and return a copy of the letter or a separate mutual rescission agreement. Sometimes, a letter from a South Carolina attorney can prompt a response. Ultimately, the silence of a policyholder or beneficiary will require the filing of a declaratory judgment action for rescission, and oftentimes mere service of the complaint helps policyholders and beneficiaries understand the gravity of the situation, leading to a response to the insurer's request for mutual rescission.