IN THE SUPREME COURT OF THE STATE OF NEVADA

DIAMOND SERVICES UNLIMITED, INC., A NEVADA CORPORATION,
Appellant,
vs.
LLOYDS OF LONDON, AN UNKNOWN ENTITY AND CERTAIN UNDERWRITERS AT LLOYDS OF LONDON, SUBSCRIBING TO AUTHORITY REFERENCE NUMBER CG 77578 AND CERTIFICATE NUMBER 0237,
Respondents.

No. 41591

FILED

SEP 0 9 2005

JANETTE M. BLOOM
CLERK OF SUPREME COURT
BY J. Richards
CHIEF DEPUTY CLERK

ORDER OF AFFIRMANCE AND REMAND

This is an appeal from a district court judgment entered on a jury verdict in favor of respondents in a breach of contract action, and an order denying a new trial motion. Eighth Judicial District Court, Clark County; Michael A. Cherry, Judge.

FACTS AND PROCEDURAL HISTORY

Following a theft of merchandise, appellant Diamond Services Unlimited, Inc. (Diamond Services), filed an insurance claim for $722,470 with its insurer, respondent Lloyds of London (Lloyds). After conducting an investigation, Lloyds prospectively cancelled the policy, denied the claim,[1] and returned a pro-rata portion of the unearned premium. Diamond Services filed suit to enforce the policy.

[1]Lloyds states on appeal that it declined coverage on the claim based on three grounds: (1) Diamond Services' failure to disclose the truth in Questions 1J, 4, and 12 of the "proposals" set forth in the insurance application; (2) Diamond Services breached the "books and records" clause

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At trial, Lloyds contended that Kalin Manchev, the owner of Diamond Services, provided three false answers on the initial application for insurance and failed to correct these statements on the subsequent year's application, thus permitting Lloyds to decline the insurance claim. More particularly, in its answer, Lloyds asserted that these misrepresentations supported two affirmative defenses: (1) cancellation and declination under the terms of the policy; and (2) rescission. Notably, the only instruction given to the jury that set forth the elements of Lloyds' affirmative defenses tracked NRS 687B.110.

Diamond Services presented alternate theories at trial. The first theory was that NRS 687B.110 did not support rescission because any misrepresentations on the application were immaterial and therefore had no effect on the premium or risk assumed by Lloyds. Diamond Services further asserted that Manchev did not knowingly provide false answers to ambiguous questions on the application, i.e., that his responses were true and accurate based upon his reasonable interpretation of the questions, and that the jury was required to construe any ambiguity in the application against the insurer. In addition, Diamond Services maintained that Lloyds waived its right to rescind the policy under NRS 687B.110 because Lloyds prospectively cancelled the policy after learning of the alleged grounds for rescission, returning only a portion of the total premium. As discussed below, Diamond Services claims that the cancellation effectively confirmed coverage for the theft.

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of the policy; and (3) Diamond Services' account of the alleged robbery lacked credibility. However, we note that this declination/cancellation letter was not included in the record on appeal.

After a six-day trial, and two days of deliberations, the jury found in favor of Lloyds. Diamond Services subsequently moved for a new trial under NRCP 59(a)(5), which the district court denied. Diamond Services now appeals from the judgment in favor of Lloyds, and from the order denying its motion for a new trial.[2]

DISCUSSION

Jury Instruction 21B:

Jury Instruction 21B provides:

> An application for insurance is part of an insurance policy. The language of an insurance policy is to be construed most strongly against the insurance company. The insurer is bound to use such language as to make the questions in the application clear to the ordinary mind. Where there is any doubt, or any ambiguity about the meaning of a policy of insurance or some part of it, the resulting uncertainty will be resolved by a construction in favor of the insured.

Diamond Services argues that Lloyds effectively nullified Instruction 21B by making the following statement during closing argument:

> And, again, I think that in connection with the so-called ambiguity issues, I think it's clear there's been no expert testimony offered on that point. That is something that does require expert testimony by plaintiffs. They haven't met their burden of proof on that issue.

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[2]We reject Lloyds' assertions that this appeal is precluded because Diamond Services failed to move for judgment notwithstanding the verdict. In addition to its appeal from the judgment entered below, Diamond Services appeals from the district court's denial of its NRCP 59(a)(5) motion for a new trial. NRAP 3A(b)(20) expressly permits such an appeal.

Diamond Services argues that the portion of Lloyds' closing argument referenced above was a misstatement of the law because there is no requirement that an ambiguity in an insurance contract be established by expert testimony.[3] While this is true,[4] substantial evidence in the record suggests that at least one of the three application questions pertinent to this appeal was not ambiguous, and that Kalin Manchev misrepresented material facts in his answer thereto.[5]

Jury Instruction 21C and NRS 687B.110

Diamond Services claims that the district court erred in denying its NRCP 59 motion for a new trial. Unlike the federal rule, the Nevada rule lists specific grounds for granting such relief.[6] NRCP 59(a)(5)

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[3]Diamond Services failed to lodge a contemporaneous objection to counsel's argument that it now contends nullifies Instruction 21B. While failure to object and to litigate the issue via post-trial motion may constitute a waiver of any claim concerning misconduct of counsel, the failure to contemporaneously object does not constitute a waiver of an argument that the jury manifestly disregarded the trial court's instructions to the jury. Thus, Diamond Services' claim that the jury manifestly disregarded instruction 21B is properly cognizable in this appeal. See NRAP 3A(a).

[4]See National Union Fire Ins. v. Reno's Exec. Air, 100 Nev. 360, 364, 682 P.2d 1380, 1382 (1984).

[5]See Powers v. United Servs. Auto Ass'n, 114 Nev. 690, 698, 962 P.2d 596, 601 (1998) (where the materiality of representations "must be shown by matters outside the terms of the contract, it is a question of fact") (citations and quotations omitted); see also Ringle v. Bruton, 120 Nev. 82, 91, 86 P.3d 1032, 1038 (2004) (a jury's determination of factual questions will not be disturbed on appeal if supported by substantial evidence).

[6]These grounds are retained under the 2004 amendment. See Drafter's Note to the 2004 Amendment to NRCP 59.

provides that the "(m)anifest disregard by the jury of the instructions of the court" is grounds for a new trial. A district court is obligated to grant a new trial if the jury could not have reached their verdict had they properly applied the court's instructions.[7] This court must review the evidence in a light most favorable to the respondent.[8] "The refusal of the trial court to set aside a verdict entered contrary to its instructions is an error of law and not within the mere discretion of the trial court."[9]

Diamond Services argues that the jury manifestly disregarded Jury Instruction 21C, which provides:

> Rescission of an insurance policy and cancellation of an insurance policy are different procedures. Rescission is based upon a claim that no valid insurance policy ever existed. The insurance company must return the entire premium to the insured. Cancellation affirms the existence of a valid insurance policy. The insurance company retains the earned premium covering the period of insurance until the time of cancellation and returns the unearned premium for the period of the policy after cancellation. If an insurance company has reason to believe that there is a basis for rescission and instead of rescinding, the insurance company cancels the policy, this action affirms the existence of a valid insurance policy and waives the right to rescind on the basis known

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[7]See Taylor v. Silva, 96 Nev. 738, 740, 615 P.2d 970, 971 (1980) (citing Groomes v. Fox, 96 Nev. 457, 611 P.2d 208 (1980); Price v. Sinnott, 85 Nev. 600, 460 P.2d 837 (1969); Eikelberger v. Tolotti, 94 Nev. 58, 574 P.2d 277 (1978); Shere v. Davis, 95 Nev. 491, 596 P.2d 499 (1979)).

[8]See Van Duzer v. Shoshone Coca-Cola, 103 Nev. 383, 385, 741 P.2d 811, 813 (1987).

[9]Price, 85 Nev. at 606, 460 P.2d at 840-41.

> to the insurance company at the time of cancellation.

Diamond Services cites Couch on Insurance[10] and Appelman, Insurance Law and Practice[11] for the proposition that by canceling the policy, with knowledge of the potential grounds for rescission, and retaining a portion of total premium paid, Lloyds waived the right to seek rescission. While these statements correctly articulate general principles of insurance law, the instruction based upon them does not compel reversal. First, under certain circumstances the remedies of cancellation and rescission are not antagonistic as instruction 21C suggests. Certainly, a tender of the entire premium in this instance would have been futile because the insured could not have accepted total return of the consideration and preserved its claim of coverage. Second, NRS 687B.110 refines the interplay between the insurer and the insured in these instances, providing for rejection of a claim based upon fraud in the inducement:

> All statements and descriptions in any application for an insurance policy or annuity contract, by or in behalf of the insured or annuitant, shall be deemed representations and not warranties. Misrepresentations, omissions, concealment of facts and incorrect statements shall not prevent a recovery under the policy or contract unless either:
>
> 1. Fraudulent; or
>
> 2. Material either to the acceptance of the risk, or to the hazard assumed by the insurer; or

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[10]2 Couch on Insurance 3d § 31:110 (1997).

[11]12 Appelman, Insurance Law and Practice § 7124 (1981).

> 3. The insurer in good faith would either not have issued the policy or contract, or would not have issued it at the same premium rate, or would not have issued a policy or contract in as large an amount, or would not have provided coverage with respect to the hazard resulting in the loss, if the true facts had been made known to the insurer as required either by the application for the policy or contract or otherwise.[12]

Under this provision, an insurer may deny or "decline" a claim based upon fraud in the inducement of the coverage. While Diamond Services correctly notes that NRS 687B.110 preserves the insurer's common law rights of rescission,[13] Lloyds could assert those rights in response to Diamond Services' complaint below under NRCP 8(c). Nothing in the statute requires contemporaneous tender of the premium as a condition to enforceable claim denial, particularly where the insurer either affirmatively sues in declaratory relief to determine non-coverage, or seeks to allow a judicial determination of its rescission rights in response to a suit by the insured to enforce the policy. Going further, nothing in the statute prohibits prospective cancellation based upon fraud in the inducement while the insurer litigates its rights of rescission.[14]

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[12]NRS 687B.110.

[13]See Randono v. CUNA Mutual Ins. Group, 106 Nev. 371, 374-75 793 P.2d 1324, 1326 (1990) (addressing NRS 687B.110 and indicating that it provides a mechanism for statutory rescission). Although the insurer in Randono returned the entire premium paid, with interest, after its investigation revealed the insured's material misrepresentation, the statute does not necessarily implicate the general rule requiring tender back of the consideration.

[14]We note that NRS 687B.320(c) permits midterm cancellation of an insurance contract upon "[d]iscovery of fraud or material

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Thus, while we have previously indicated that an action to rescind an insurance policy under NRS 687B.110 may be subject to the defense of waiver,[15] we conclude that the factors present in this case make this particular waiver defense inapplicable.[16]

CONCLUSION

We conclude that Lloyds did not waive its right to seek rescission by canceling the policy and only returning a pro-rata portion of the premium. Further, we conclude that substantial evidence supports the jury verdict. However, having successfully defended suit based on NRS 687B.110, Lloyds must now restore Diamond Services to the position

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misrepresentation in the obtaining of the policy or in the presentation of a claim."

[15]See Schneider v. Continental Assurance Co., 110 Nev. 1270, 1273, 885 P.2d 572, 574 (1994) (stating "CNA points to no language in NRS 687B.110 which would preclude insured persons from raising estoppel against insurers"); Violin v. Fireman's Fund Ins. Co, 81 Nev. 456, 458, 406 P.2d 287, 288 (1965) (recognizing waiver and estoppel are valid defenses to the common law right of rescission). We note that, unlike the situation in Violin, the insurer in this case is not chargeable with prior knowledge of the misrepresentation and could rightfully rely on the representations made in the insurance proposals. See id. at 462, 406 P.2d at 290.

[16]See, e.g., Pittsburgh Plate Glass Co. v. Hotel Corporation, 150 S.E. 877, 878 (N.C. 1929) (stating that "in an action to recover on the contract it is not necessarily a waiver of the right of avoidance for a surety company, while defending said action, to retain the premium paid on the policy until its alleged fraudulent procurement can be determined"); Woody v. Continental Life Ins. Co., 141 S.E. 880, 882 (W.Va. 1928) (stating that "it is a general rule that a return of the premiums is not essential to the avoidance of a policy, nor is its retention a waiver, where the insured was guilty of fraud in obtaining the policy").

it occupied prior to entering into the contract. Thus, Lloyds must return the entire premiums paid, with interest.[17] Accordingly, we

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[17]In this, we note the following exchange between the court and the parties below with respect to instruction 21C:

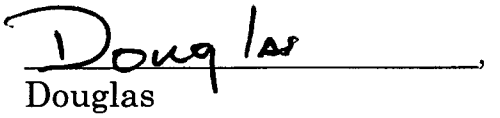
> Mr. Tarkian [counsel for Lloyds]: Because first it was cancelled. It was cancelled. When we moved for rescission, the rescission never actually took place. That's where the key is. The rescission takes place now.
>
> The Court: So, in other words if you – if you win, you owe them money still?
>
> Mr. Tarkian: If we are – if we're successful in the rescission argument, then the paid premiums up to the cancellation, that gets given back to the plaintiff. That is correct. The reason why it hasn't done – the reason why it hasn't been done so yet is right now you only have cancellation. Now we're moving in – moving in as part of our affirmative defense to rescind the policy.

Interestingly, at the oral argument of this appeal, counsel for Lloyds renounced its intention to refund the premium in the event this court affirms the judgment below. Because the primary defense to Diamond Services' claim was based upon Lloyds' rights of rescission under NRS 687B.110, this statement arguably renounces its rescission rights. However, given Lloyds' position on this issue at trial, we will not reverse based upon counsel's speculative statements before this court.

Based on the foregoing, we conclude that Lloyds must return to Diamond Services the entire premium paid, plus interest, on both policies. In this, we note that the misrepresentations relied upon as grounds for rescission were actually contained in the first proposal (submitted in 1998) and the claimed loss occurred during the effective dates of the 1999 policy. However, testimony at trial established that representations on a previous year's proposal carry over into subsequent years.

ORDER the judgment of the district court AFFIRMED and remand this matter for proceedings consistent with this order.[18]


_____, J.
Maupin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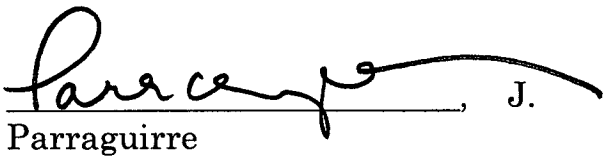
Douglas


_____, J.
Parraguirre

cc: Hon. Michael A. Cherry, District Judge
Bourgault & Harding
Carroll, Burdick & McDonough
Lee & Russell
Clark County Clerk

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[18]Lloyds also litigated the proposition that Diamond Services violated a condition subsequent under the policy by failure to comply with the "books and records" clause in the insurance agreement. Because we affirm the judgment below based upon NRS 687B.110, we need not reach the appellate issues raised in connection with the books and records provisions in the policy.