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that Carolin and the Benz principals had invoked the safeguards of the Chapter 11 bankruptcy proceeding for impermissible purposes, because they effectively had protected themselves against the risks of any loss that might have occurred if reorganization efforts were unsuccessful. The Fourth Circuit affirmed the district court's dismissal of Carolin's Chapter 11 bankruptcy petition for lack of good faith in filing and remanded the case to the district court with instructions to remand the case to the bankruptcy court to determine whether to impose sanctions on Carolin.

The dissenting opinion of Judge Widener concluded that the Bankruptcy Code does not require a good faith requirement in filing a Chapter 11 petition because of the absence of such language in the text of section 1112(b). The dissent argued that the predecessor to the Bankruptcy Code, the Bankruptcy Act, contained a good faith filing requirement, but no similar requirement is found in the modern Code. The dissent believed that the majority failed to give adequate consideration to congressional intent in making this significant change in bankruptcy procedure.

The Fourth Circuit's adoption of the stringent two-prong test for determining when a bankruptcy court may dismiss a Chapter 11 petition for lack of good faith in filing is the better approach for evaluating these kinds of dismissals. Unlike the less demanding test of the Eleventh Circuit, which requires only a showing of either objective futility or subjective bad faith, the Fourth Circuit's test more adequately protects the various and conflicting interests of the debtor and creditor involved in bankruptcy proceedings. The objective futility inquiry insures that the Chapter 11 petition bears some relation to the statutory objective of rehabilitating the financially troubled debtor, while the subjective bad faith inquiry insures that the debtor intends to use the bankruptcy petition to reorganize an existing enterprise.

INSURANCE

Two frequent issues arising out of insurance disputes are accord and satisfaction and material misrepresentation. Accord and satisfaction occurs when the insurer and insured agree to settle the dispute by the payment of an amount less than the insured claims the insurer owes and more than the amount the insurer claims it owes. The Supreme Court, when considering the issue of accord and satisfaction, has required that the parties reach a meeting of the minds regarding the compromise agreement before payment will constitute satisfaction of the entire debt.[181] Courts considering claims

181. *See* Fire Ins. Assoc., Ltd. v. Wickham, 141 U.S. 564 (1891) (holding that where parties to dispute intend by agreement to make settlement of amount in dispute, claim is satisfied, but if one party does not intend settlement of entire claim, claim is not satisfied); Baird v. United States, 96 U.S. 430 (1877) (stating relevant question is whether payment was in fact made in satisfaction of claim); United States v. Bostwick, 94 U.S. 53 (1876) (explaining that payment by debtor of part of amount owed is not satisfaction of whole debt unless made upon new consideration).

of material misrepresentations have held that misrepresentations which would have resulted in a denial of the policy or in higher premiums are material and, thus, justify the insurer's rescission of the policy.[182] When a court grants a motion for a directed verdict on these issues, the court of appeals reviews the motion *de novo*.

In *Parker v. Prudential Insurance Co.*, 900 F.2d 772 (4th Cir. 1990), the United States Court of Appeals for the Fourth Circuit considered whether the district court erred in granting the defendant's motion for a directed verdict for accord and satisfaction, and whether the district court properly denied the defendant's motion for a directed verdict for material misrepresentation. In *Parker* the plaintiff's decedent (Parker) purchased a one hundred thousand dollar life insurance policy from the defendant, Prudential Insurance Company (Prudential). Parker responded negatively to a Prudential agent's questions asking whether he or his spouse had ever smoked cigarettes or used illegal drugs. At the conclusion of the agent's background questioning, Parker read and signed the insurance application form.

Approximately four months after obtaining the policy in question, Parker died in a head-on automobile accident. The plaintiff (Mrs. Parker) filed a claim with Prudential as the primary beneficiary under the life insurance policy. Prudential then conducted an investigation of Parker's medical history and discovered that Parker, contrary to his representations to the Prudential agent, had been a cigarette smoker at the time of his death and had used cocaine and heroine in the past. Prudential denied Mrs. Parker's claim based on this information, stating that Parker's negative answers regarding smoking and drug use constituted material misrepresentations. Prudential informed Mrs. Parker that Prudential's only liability was to refund the premium of approximately seventy-seven dollars that Parker had paid. After consulting an attorney, Mrs. Parker requested the premium refund, and upon receipt she deposited the refund check. Mrs. Parker then filed an action in Maryland state court to recover the one hundred thousand dollar policy benefit. Prudential removed the case to federal court based on diversity of citizenship.

At the conclusion of the plaintiff's case at trial, Prudential moved for a directed verdict on the grounds of accord and satisfaction, or alternatively, rescission of the contract for material misrepresentation. Prudential argued that Mrs. Parker's acceptance of the premium refund check constituted an accord and satisfaction. Mrs. Parker argued that she believed she could pursue her claim against Prudential even after depositing the refund check.

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182. *See* Skinner v. Aetna Life & Casualty, 804 F.2d 148 (D.C. Cir. 1986) (holding that insured's misrepresentations materially affected insurer's acceptance of insurance contract, justifying rescission and summary judgment for insurer); Dukes v. South Carolina Ins. Co., 770 F.2d 545 (5th Cir. 1985) (holding that insured's representations were necessarily material because insured would not have issued policy if insured had told truth, and affirming summary judgment for insurer rescinding coverage); Blair v. Inter-Ocean Ins. Co., 589 F.2d 730 (D.C. Cir. 1978) (holding that misrepresentations materially affected hazard assumed by insurer, and justified insurer's abrogation of insurance contract).

Asserting the attorney-client privilege, Mrs. Parker's attorney did not testify as to his advice to Mrs. Parker. The United States District Court for the District of Maryland granted Prudential's motion for a directed verdict based on accord and satisfaction, but rejected material misrepresentation as a basis for the directed verdict.

Mrs. Parker appealed the district court's ruling, arguing that the lower court used Mrs. Parker's attorney's failure to testify to draw an inference that the attorney advised Mrs. Parker that accepting the check would constitute accord and satisfaction. This inference, according to Mrs. Parker, impermissibly intruded on the attorney-client privilege. Prudential cross-appealed, arguing that the district court erred in denying material misrepresentation as a basis for the directed verdict.

The Fourth Circuit first considered Mrs. Parker's allegation that the trial court impermissibly intruded on the attorney-client privilege in making a negative inference about the substance of Mrs. Parker's attorney's advice to her. The *Parker* court agreed with Mrs. Parker's argument, stating that the district court's inference intruded on Mrs. Parker's right to effective counsel. The court relied on *State v. Pratt*, 284 Md. 516, 398 A.2d 421 (1979), and *Helferstay v. Creamer*, 58 Md. App. 263, 473 A.2d 47 (1984), to hold that courts should encourage individuals to consult with an attorney without the fear of the attorney's compelled disclosure. Because the district court did not allow Mrs. Parker's attorney to testify about the substance of his advice to Mrs. Parker, the Fourth Circuit concluded the district court should not have drawn the inference that the attorney advised Mrs. Parker that acceptance of the refund check would constitute accord and satisfaction.

Next, the *Parker* court briefly stated the standard of review in assessing a motion for a directed verdict. Mrs. Parker argued that the district court erroneously considered all evidence in favor of the defendant in ruling on the directed verdict. Mrs. Parker also argued that the district court placed the burden of proving accord and satisfaction on her, rather than on Prudential. The Fourth Circuit again agreed with Mrs. Parker's arguments, but stated that the record indicated that the district judge was either temporarily confused or misspoke. The court said that the district court's assertions were not crucial on appeal, however, because a motion for a directed verdict raises a question of law, which the court of appeals reviews *de novo*.

Having stated the applicable burden of proof and standard of review, the Fourth Circuit went on to review Prudential's motion for a directed verdict based on the grounds of accord and satisfaction. Prudential argued that by depositing the premium refund check, Mrs. Parker waived her right to pursue any additional claim against Prudential. The Fourth Circuit relied on *Rust Engineering Co. v. Lawrence Pumps, Inc.*, 401 F. Supp. 328 (D. Mass. 1975), to hold that accord and satisfaction is an affirmative defense that requires the defendant to prove three elements to succeed. First, a bona fide dispute must exist between the parties as to the existence or extent of liability. Second, subsequent to the arising of that dispute, the parties must enter into a settlement agreement. In this agreement, one party must

agree to pay a sum greater than the amount that party claims to owe, while the other party must agree to accept a lesser sum than that party claims is due. The parties must enter into the agreement for the purpose of settling the dispute. The third and final requirement is that the parties must perform according to the agreement. In *Parker* the plaintiff conceded that the defendant proved the first and third elements of the *Rust Engineering* test, but argued that a material question of fact existed as to whether the parties had entered into a compromise agreement.

Prudential contended that its letter to Mrs. Parker, acknowledging only a duty to refund the premium price, together with Mrs. Parker's acceptance of the refund, constituted an agreement between the parties within the meaning of the *Rust Engineering* test. Prudential conceded that the letter did not condition payment expressly on Mrs. Parker's waiver of any other claims. However, Prudential argued that under the circumstances, Mrs. Parker knew or should have known that Prudential intended the check to settle any and all possible claims.

The *Parker* court rejected Prudential's argument, holding that a reasonable jury could find that Prudential failed to meet its burden of proving the existence of a settlement agreement. The court found that Prudential's letter to Mrs. Parker did not condition payment of the premium refund on a waiver of Mrs. Parker's claim to the policy benefits. According to the court, a jury reasonably could believe Mrs. Parker's testimony that she believed acceptance of the refund check would not affect her right to any additional claims against Prudential. Therefore, the Fourth Circuit found that the district court erred in basing the motion for a directed verdict on Prudential's claim of accord and satisfaction.

The Fourth Circuit next addressed whether the district court properly denied the defendant's motion based on the grounds of material misrepresentation. Prudential claimed that Parker's failure to disclose his history of smoking and drug use amounted to a material misrepresentation that justified rescission of the policy. The *Parker* court considered whether a jury could reasonably find for Mrs. Parker based on the evidence in the record. The record indicated that Parker was smoking one half a package of cigarettes per day at the time he applied for the life insurance policy. Additionally, Mrs. Parker admitted that the decedent had used cocaine and heroin three years prior to obtaining the insurance policy.

Mrs. Parker argued that, although her husband had smoked cigarettes and used drugs, the insurance application form was ambiguous and, therefore, the court should construe the policy in favor of the insured. The relevant portion of the insurance form asked if any "person to be covered" by the policy had used drugs. Mrs. Parker argued that "person to be covered" could mean either the insured or the insured's spouse. Rejecting this argument, the Fourth Circuit held that the policy application was unambiguous. The application made clear that the important issue was the health of the insured whose death triggers coverage, not the health of the beneficiary of the policy. Further, even if Mrs. Parker had proved the ambiguity of the question on the application, Parker's negative response to the question clearly was a misrepresentation.

Finally, the *Parker* court addressed the issue of materiality of the misrepresentation. Under Maryland law, the insurer may deny recovery if the misrepresentation is such that the insurer would not have issued the policy, or if the insurer would have required a higher premium had it known the truth. Prudential contended that had it known of the decedent's history of smoking and drug use, it most likely would not have issued the policy, or would have required a substantially higher premium. Testimony at trial revealed that the Prudential agent listed Parker as a nonsmoker to give him a lower premium. The Fourth Circuit held that this admission alone constituted an adequate basis for summary judgment for material misrepresentation.

The *Parker* court concluded that, while Prudential was not entitled to a motion for a directed verdict based on accord and satisfaction, the district court should have granted the motion on material misrepresentation. The Fourth Circuit held that a reasonable jury could find that Prudential failed to prove the existence of a compromise agreement. Therefore, the plaintiff would be entitled to a jury trial on this issue. However, the court found that Parker materially misrepresented his history of smoking and drug use in an attempt to obtain a lower insurance premium. This misrepresentation justified Prudential's rescission of the policy, and, therefore, entitled Prudential to a directed verdict. Accordingly, the Fourth Circuit affirmed the district court's holding, albeit on different grounds.

This decision put the Fourth Circuit in agreement with other circuits. Those circuits considering the issue of accord and satisfaction have held that payment of a claim constitutes accord and satisfaction only when the accepting party has sufficient knowledge that the payment is made in full satisfaction of the claim.[183] Also, the circuits considering misrepresentation are in agreement that if an insured makes a material misrepresentation on the insurance application, the insurer may rescind the insurance contract

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183. *See* Rang v. Hartford Variable Annuity Life Ins. Co., 908 F.2d 380 (8th Cir. 1990) (holding check's restrictive endorsement stating that it represented full payment of claim constituted accord and satisfaction); Gulf Life Ins. Co. v. Folsom, 907 F.2d 1115 (11th Cir. 1990) (holding that execution of new agreement compromising amount in dispute from previous agreement supplants previous agreement, and payment under new agreement satisfies debt between parties, as long as parties know that agreement represents satisfaction); Rhone v. State Auto Mutual Ins. Co., 858 F.2d 1507 (11th Cir. 1988) (holding that party's endorsement of check stating that it represented payment in full constituted accord and satisfaction); Lowrance v. Hacker, 866 F.2d 950 (7th Cir. 1989) (stating that accord and satisfaction requires explicit understanding of both parties that payment is in satisfaction of entire claim); Hall v. Time Ins. Co., 854 F.2d 440 (11th Cir. 1988) (explaining that parties must intend to reach an accord and satisfaction agreement); Hines v. Blue Cross & Blue Shield of Virginia, 788 F.2d 1016 (4th Cir. 1986) (same); Allegheny Airlines, Inc. v. Forth Corp., 663 F.2d 751 (7th Cir. 1981) (same); Brown v. Presbyterian Ministers Fund, 484 F.2d 998 (3d. Cir. 1973) (same); Markel Service, Inc. v. Nat'l Farm Lines, 426 F.2d 1123 (10th Cir. 1970) (same). *But see* Geeslin v. Knight Brothers, Inc., 554 F.2d 865 (8th Cir. 1977) (holding that retention and use of check by party constitutes accord and satisfaction even if party notifies paying party that check represents only partial payment of debt).