



IN THE COURT OF CHANCERY OF THE STATE OF DELAWARE

IN AND FOR SUSSEX COUNTY

FIRST STATE STAFFING PLUS, INC.     )  
and FAYE PASSWATERS,                 )  
  )  
  )     Plaintiffs,                     )  
  )  
  )     v.                                 )     Civil Action No. 2100-S  
  )  
MONTGOMERY MUTUAL                     )  
INSURANCE COMPANY and                 )  
THE INSURANCE MARKET, INC.,         )  
  )  
  )     Defendants.                     )

**MEMORANDUM OPINION**

Submitted: May 13, 2005  
Decided: September 6, 2005

Herbert G. Feuerhake, Esquire, THE LAW OFFICE OF H.G. FEUERHAKE,  
Wilmington, Delaware, *Attorneys for Plaintiffs*

Raymond W. Cobb, Esquire, RAYMOND W. COBB, LLC, Wilmington, Delaware,  
*Attorneys for Defendant Montgomery Mutual Insurance Company*

David E. Brand, Esquire, PRICKETT, JONES & ELLIOTT, P.A., Wilmington,  
Delaware, *Attorneys for Defendant The Insurance Market, Inc.*

**PARSONS, Vice Chancellor.**

Before the Court is plaintiff First State Staffing Plus Inc.'s ("First State") action for specific performance of a canceled workers' compensation insurance contract.<sup>1</sup> First State procured the insurance through its insurance agent and former defendant, The Insurance Market, Inc. ("TIM"). Defendant Montgomery Mutual Insurance Company ("Montgomery Mutual") was the insurance provider. After nearly eight months of coverage, the insurance contract was canceled for nonpayment of premiums. First State claims that the cancellation was improper because First State complied with the mandates of the cancellation notice and because it made an oral agreement with TIM to make partial payments to avoid cancellation.

On December 15, 2004, First State settled its claims against TIM, leaving Montgomery Mutual as the sole remaining defendant. This matter was tried on December 20, 2004, briefed and then argued on May 13, 2005. For the reasons stated in this Memorandum Opinion, I conclude that Montgomery Mutual properly canceled the insurance, there was no oral agreement between First State and TIM to modify the terms of the policy and First State failed to prove its related claims against Montgomery Mutual for negligence and fraud based on the acts of its agent TIM.

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<sup>1</sup> Faye Passwaters, First State's principal, was originally a plaintiff but withdrew her personal claims before trial.

## I. BACKGROUND<sup>2</sup>

First State was a Delaware corporation that operated as a medical staffing agency from when it was founded in May 1998 to when it ceased doing business in May 2003. Faye Passwaters, a Licensed Practical Nurse, founded First State, and was its sole stockholder and president. First State employed approximately 100 nurses and certified nursing assistants and an office staff of seven. During its years of operation, First State's yearly revenues were between \$2,000,000 and \$3,000,000. First State placed its nurses with a diverse group of customers including nursing homes, hospitals, poultry plants, schools and prisons. Many of those customers required First State to obtain and show proof of its workers' compensation insurance.<sup>3</sup>

On March 1, 2004, First State was declared "inoperative and void" by the State of Delaware for failure to pay taxes.<sup>4</sup> First State represented at trial an argument that it intended to pay its back taxes and regain its corporate status, but to date the Court has received no indication that First State has been reinstated as a valid corporation.

TIM is a licensed insurance agency offering coverage from a number of insurance providers, including Montgomery Mutual. TIM offered Montgomery Mutual's insurance

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<sup>2</sup> The only witness to appear at trial was Faye Passwaters. The testimony of TIM employees David Noel and Stephen Hartstein was submitted by deposition. Citations to the trial transcript are in the form "Tr. at \_\_\_", and unless otherwise indicated refer to Passwaters' testimony.

<sup>3</sup> The State of Delaware also required First State to have workers' compensation insurance. 19 *Del. C.* § 2372 (every employer must carry compensation liability insurance).

<sup>4</sup> *Aff. of Harriet Smith Windsor, Secretary of State of Delaware*, ¶ 2 (Apr. 27, 2005).

products on an “agency billed” basis, meaning that once TIM had sold a Montgomery Mutual policy, customers paid their premiums directly to TIM and contacted TIM for all customer service needs. In fact, all customer contact was handled by TIM. TIM paid Montgomery Mutual for the insurance premiums and separately billed the customer. That is what occurred in the case of First State. Thus, if a customer failed to pay its premiums, TIM bore the risk.<sup>5</sup>

Passwaters was the First State employee that dealt with obtaining and maintaining insurance. In July 1999, Passwaters discussed First State’s insurance needs with David Noel, a TIM sales agent. Passwaters was familiar with Noel because he had acted as First State’s insurance agent in the past while at another insurance agency. Over the course of the next few months, the two discussed First State’s need for four types of insurance: workers’ compensation, business owner’s, general liability and auto.

Passwaters decided to use TIM for all of First State’s insurance needs and obtained workers’ compensation insurance and business owner’s insurance effective October 9, 1999. Both policies were provided by Montgomery Mutual and had estimated annual premiums of \$33,672 and \$300, respectively.<sup>6</sup> Montgomery Mutual provided the insurance and billed TIM for the premium payments in ten monthly installments,

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<sup>5</sup> See Hartstein Dep. at 20. In fact, Noel explained that “the agency rule is, if a client owes the agency money and we can’t collect it, [the salesperson is] responsible for it.” Noel Dep. at 112.

<sup>6</sup> Noel Dep. Ex. 16.

including a deposit. TIM, in turn, billed First State.<sup>7</sup> Around this time, First State also obtained general liability and auto insurance through TIM, although the general liability was billed directly by the insurance provider.

The circumstances under which First State became insured with Montgomery Mutual are somewhat unclear. An insurance binder is a document given to an insured to confirm coverage before receipt of the actual contract from the insurance company.<sup>8</sup> Passwaters testified that First State never received a Montgomery Mutual insurance binder and that, instead, Noel delivered a Harleysville binder.<sup>9</sup> Noel believes that he did deliver a Montgomery Mutual binder but was not able to recall specifically.<sup>10</sup> First State did not produce an insurance binder in this litigation.

Passwaters also claims that Noel did not give her a quote for the workers' compensation policy before or at the time the insurance became effective. In fact, Passwaters testified that she did not know the total cost of the workers' compensation insurance for many months. Noel, on the other hand, testified that he is able to calculate the price of workers' compensation policies on the spot by using a series of schedules provided by the insurer and remembers providing Passwaters with a quote on October 9, 1999.<sup>11</sup> I find Noel's version of the events more credible. Passwaters was an

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<sup>7</sup> *Id.*

<sup>8</sup> Noel Dep. at 249.

<sup>9</sup> Harleysville was First State's previous insurer.

<sup>10</sup> Noel Dep. at 249.

<sup>11</sup> Noel Dep. at 84, 243–46, 257.

experienced businessperson. It is simply too implausible to believe that she entered into a contract on behalf of First State worth over \$30,000 without knowing the price—a price that Noel was able to calculate on the spot. Furthermore, Passwaters knew the approximate cost of workers' compensation insurance, because she already had received a quote for similar insurance from Montgomery Mutual through a different insurance broker, and the total cost was roughly in-line with her previous coverage from Harleysville.<sup>12</sup>

After the workers' compensation policy became effective, First State did not receive a bill for a number of months. It had been Passwaters' experience with insurance that a 20–25% down payment was necessary, but when she inquired of Noel about the need for a down payment, he told her only that a bill would be forthcoming. Passwaters asserts that Noel never told her what the payment terms would be, but Noel is confident that she knew the premium would be billed monthly.<sup>13</sup>

On January 24, 2000, Noel delivered to First State an invoice requesting payment for October, November, December, January and February. Passwaters recalls the invoice showing a balance owed of over \$20,000.<sup>14</sup> Noel testified that on January 24 he also delivered to Passwaters a copy of the workers' compensation policy and a summary sheet

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<sup>12</sup> Tr. at 74–76.

<sup>13</sup> Noel Dep. at 286–87.

<sup>14</sup> Tr. at 21.

showing the total cost.<sup>15</sup> Although neither party placed a copy of the policy in evidence, TIM did produce the summary sheet. Passwaters denies ever receiving the policy or the summary sheet.

On this issue I find Noel's testimony more credible. Throughout Passwaters' testimony, she repeatedly denied receiving letters, faxes or invoices from TIM. These included monthly invoices,<sup>16</sup> a June 26, 2004 fax,<sup>17</sup> the policy and the summary sheet. In addition, First State did not produce documents that Passwaters acknowledged receiving such as the Harleysville binder or January 24 invoice. On the whole, I found Passwaters, and First State more generally, to be unorganized. I also found Passwaters' memory lacking at times. Therefore, I find that Noel did in fact deliver the policy and summary sheet to Passwaters on or about January 24.

Passwaters testified she was "really upset" by the large bill, because it was too large an amount for her to pay all at once and because she felt she should have been paying it monthly. Noel recalls Passwaters being unhappy that the policy had begun accruing payments long before she received the first bill.<sup>18</sup> First State did not immediately make a payment after receiving the January invoice. Over the next few months Passwaters had numerous conversations with Noel regarding the balance due.

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<sup>15</sup> Plaintiff's Ex. ("PX") 1.

<sup>16</sup> Tr. at 28 (denying receipt of any invoices other than the January 24 invoice).

<sup>17</sup> Tr. at 111 (denying seeing the June 26 fax but acknowledging that someone else in the office might have received it).

<sup>18</sup> Noel Dep. at 257.

She explained to him that First State could not pay the bill all at once and sought to arrange a payment plan. Although Passwaters was aware that the policy continued to accrue additional premiums, First State did not make any payments for nearly four more months.<sup>19</sup>

It was TIM's practice to send computer generated invoices monthly, but it normally did not keep a record of those invoices. The March 8 invoice showed a balance due of \$20,384 owed on the workers' compensation and business owner's policies combined.<sup>20</sup> In April, First State's large unpaid balance came to the attention of the management of TIM, which already had paid Montgomery Mutual for the policies' premiums. Having not received any payment from First State, TIM faced a potential loss of over \$20,000. TIM decided to cancel both policies unless the past due premiums were paid, and on April 12, 2000, asked Montgomery Mutual to send a cancellation notice. On April 26 Montgomery Mutual sent cancellation notices to Passwaters at First State for the workers' compensation and business owner's policies. The notice for the workers' compensation policy read:

CANCELLATION FOR NON-PAYMENT OF PREMIUM:  
Your policy will be cancelled on 05/30/00 at the standard time specified in the policy because the premium has not been received when due. If you are entitled to a refund, it will follow. If payment is received on or before the effective date of cancellation the policy will be continued in force without a

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<sup>19</sup> Tr. at 83-84.

<sup>20</sup> Noel Dep. Ex. 2.

lapse in coverage. Please contact or send payment to your agent.<sup>21</sup>

On or about May 4, 2000, Passwaters sent Noel a letter complaining about her large balance due and the fact that she had not received a quote or a binder at the time the policy became effective.

You tell me that the binder covered me but, I feel I should not have to pay for the time I did not even have a quote. How did I know if I wanted it until I received the quote. . . . We also did not receive a statement or bill until we owed over \$20,000! I do not feel responsible to pay this until the date I knew we had coverage for sure. . . . I would appreciate you talking with whoever can make a decision on this and get me a rebate or a start date of Mar. 2000 because that is about when we actually got a policy. . . . We really do not have \$\$25-30,000.00 to pay out for back workman's comp.<sup>22</sup>

Thereafter, Passwaters and Noel continued to discuss First State's balance owed and ability to make payments. By mid-May, First State owed over \$25,000. Noel testified that during these conversations "she [Passwaters] knew that, without a doubt, that unless the account was brought current, that coverage was not going to continue past the May 30th date . . . ." <sup>23</sup> On May 19 Passwaters and Noel settled on "a figure that I could pay, and \$5,000 was the figure, and he [Noel] picked up a check that day."<sup>24</sup> In connection with that payment, Passwaters also told Noel that she would make another

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<sup>21</sup> PX 2; Noel Dep. Ex. 9. The only difference between the two notices is that the cancellation dates for the business owner's and workers' compensation policies were May 9 and 30, 2000, respectively.

<sup>22</sup> Defendant's Ex. ("DX") 2.

<sup>23</sup> Noel Dep. at 29; *see also id.* at 32.

<sup>24</sup> Tr. at 31.

\$5,000 payment within 30 days. First State did in fact make additional \$5,000 payments in June and July.

TIM first applied approximately \$150 of the \$5,000 May 19 payment to First State's business owner's coverage, because the payment was sufficient to reinstate the policy.<sup>25</sup> On July 21, Montgomery Mutual sent a letter directly to First State that "rescind[ed] the recent Notice of Cancellation effective 05/09/00."<sup>26</sup>

The effect of First State's May payment is a central issue in the parties' dispute. Neither witness had a clear recollection of discussing specifically whether the May payment would affect the impending cancellation of the workers' compensation policy. When asked whether he specifically told Passwaters that the May payment would not affect the impending cancellation, Noel testified "I believe I would have said that to her, yes."<sup>27</sup> On the other hand, Passwaters' testimony provided little support for First State's contrary position. She did not recall, for example, Noel assuring her that the policy would not be canceled at the end of May as a result of the payment.

In fact, the parties may not have bothered to discuss the effect of the May payment because they both assumed that they had an understanding regarding the impending cancellation. Their purported understandings, however, differ markedly. Passwaters testified that she expected the May payment to keep the insurance in force because "he

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<sup>25</sup> The business owner's policy had been canceled on May 9.

<sup>26</sup> Noel Dep. Ex. 18.

<sup>27</sup> Noel Dep. at 31.

knew I needed it and that I needed to keep this in force and that I thought when he took this payment that it would do that. He didn't say it wouldn't or, you know, that it was canceled . . . ."<sup>28</sup> Thus, Passwaters' belief that the payment would avoid cancellation seems to have had more to do with her interpretation of the cancellation notice than anything Noel said to her. Passwaters generally interpreted the cancellation notice to refer only to one overdue payment and not the total overdue balance. Therefore, she believed the notice required only *a* payment, as opposed to *full* payment of the premium then due.<sup>29</sup>

For his part, Noel believed Passwaters understood that the policy was set to cancel absent payment of the full premium due and remembers conveying that fact to her on more than one occasion:

I definitely recall conversations, unless the full premium is paid on the work comp—again, the \$23,000 and change, \$20,000 plus—coverage will cancel on 5/30. And that was in stone. There was no, there was no question that that was the only thing that could happen on that policy.<sup>30</sup>

First State's workers' compensation policy was canceled by Montgomery Mutual on May 30, 2000 in accordance with the cancellation notice. Passwaters denies receiving any notification at that time from either TIM or Montgomery Mutual that the cancellation had actually taken place. Noel, however, testified that he discussed the canceled

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<sup>28</sup> Tr. at 33.

<sup>29</sup> Tr. at 90–93 (“I just thought it was for a premium. I didn't know how much the premium would be. I wasn't even thinking [about the amount in the January invoice].”).

<sup>30</sup> Noel Dep. at 272.

insurance and “the status of the account” during numerous calls with Passwaters after May 30.<sup>31</sup>

In June 2000, taking into account the insurance’s cancellation and the May payment, First State’s balance stood at a little over \$16,000. On June 26, Noel faxed Passwaters a copy of the cancellation notice for First State’s workers’ compensation insurance along with cancellation notices for other agency billed policies obtained through TIM. The fax cover sheet read: “Please see the attached cancellation notices on each policy. I can reinstate w/ payment & past due amounts. Give me a call this morning to discuss. Thanks, David.”<sup>32</sup> Passwaters denied ever seeing the June 26 fax, but acknowledged that it could have been received by one of First State’s other four office employees.<sup>33</sup> Two days later, on June 28, First State made a \$5,000 payment to TIM.<sup>34</sup>

Sometime after May 30, Stephen Hartstein, one of TIM’s principals, became aware of the situation with First State. He was very concerned that First State, which owed TIM over \$16,000, had “no insurance in force so there was no collateral.”<sup>35</sup> Hartstein told Noel that TIM could not afford to lose that kind of money and that he must

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<sup>31</sup> *Id.* at 32.

<sup>32</sup> DX 1. One of the cancellation notices included with the June 26 fax was for the business owner’s policy that already had been reinstated.

<sup>33</sup> Tr. at 111.

<sup>34</sup> Noel Dep. Ex. 16.

<sup>35</sup> Hartstein Dep. at 15.

either collect it or TIM would have to file suit.<sup>36</sup> Soon thereafter, TIM devised a plan to help safeguard the company's interest: it would reinstate First State's insurance if Passwaters agreed to sign a personal note guaranteeing the premium payments.

At some point in June, Noel faxed Passwaters a copy of a personal note. Passwaters did not want to sign the note and instead called Noel. Noel doesn't remember the specific language used in that conversation, but testified that "I'm very, very, confident that I told her that without the personal note being signed, that we could not have the policy reinstated."<sup>37</sup> Noel further testified that following May 30 he had a number of conversations with Passwaters regarding what could be done to effect reinstatement.<sup>38</sup>

During a phone call in late June, possibly the one discussed above related to the personal note, Noel explained to Passwaters that the issue was out of his hands and transferred the call to Hartstein to discuss it further. The witnesses' recollections of this conversation differ. According to Passwaters, they discussed the personal note. She explained to Hartstein that First State needed the insurance and she was somebody that paid her bills. She also stated, however, that the personal note was unnecessary and would be a bad business decision for her. According to Passwaters, Hartstein told her

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<sup>36</sup> *Id.* at 20.

<sup>37</sup> Noel Dep. at 36–37.

<sup>38</sup> *Id.* at 277–78.

that “as long as you pay the payments, everything will be okay.”<sup>39</sup> Passwaters testified that she understood that the insurance was still in force and that by saying “everything will be okay” Hartstein meant the insurance would not be canceled.

Hartstein denied ever speaking to Passwaters about the personal note and did not recall telling her that if she continued to pay there would not be a problem. Hartstein recalls their conversation focused on establishing a plan to pay First State’s debt to TIM in order to avoid litigation. Therefore, Hartstein explained, if he did tell her that everything would be okay if she continued to pay, he would have been referring to the parties staying out of court, rather than continuing the insurance in force. Soon thereafter, Hartstein told Noel he could pick up another \$5,000 payment from First State and Noel picked up the June 28 payment.

On June 28, 2000, Noel sent First State a letter enclosing a payment schedule. It showed a balance due of \$23,972, and scheduled payments for July, August and September 15, in the amounts of \$7990, \$7990 and \$7992, respectively.<sup>40</sup> The proposed schedule of payments included a line for Passwaters to sign personally. The letter explained that “the powers at be are pushing the issue quite hard” and asked Passwaters

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<sup>39</sup> Tr. at 39.

<sup>40</sup> PX 4. The balance of \$23,972 reflected on the payment schedule is interesting, but was not addressed in any detail at trial. The document does not state whether the balance owed only included the worker’s compensation policy or also included auto insurance or professional liability. The amount, however, is exactly \$10,000 (the amount First State had paid in two installments during May and June) less than the total cost for a full year of insurance under the workers’ compensation and business owner’s policies combined. *See* Noel Dep. Ex. 16.

to sign and return the schedule as soon as possible. Noel testified that TIM's owners wanted Passwaters to sign the schedule as an assurance that she would pay the past due premiums, but that signing the schedule was not related to reinstatement as the personal note was.<sup>41</sup> In my opinion, however, whether the proposed schedule of payments related solely to past due premiums or also included possible reinstatement is immaterial. The reason is that Passwaters never signed the schedule.<sup>42</sup>

On July 12, TIM received a credit for \$12,157 from Montgomery Mutual for premiums paid for the canceled insurance.<sup>43</sup> According to TIM's account management software, an invoice was sent to First State on July 14. That invoice showed a remaining balance of \$11,815, which for the first time took into account the early cancellation of the workers' compensation policy.<sup>44</sup>

On or about July 17, First State made another \$5,000 payment and on August 21 TIM sent First State an invoice showing the updated remaining balance of \$6,815. At some point, most likely in October, First State had paid off its entire balance.<sup>45</sup>

In or about early September 2000, Passwaters called Noel to discuss renewing First State's various insurance policies and to make a claim for an accident that had

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<sup>41</sup> Noel Dep. at 100.

<sup>42</sup> *Id.*

<sup>43</sup> Noel Dep. Ex. 16.

<sup>44</sup> Noel Dep. Ex. 17.

<sup>45</sup> Noel Dep. at 50, 282.

happened in June.<sup>46</sup> It was at that time that Noel reminded her that the workers' compensation policy had been canceled since May 30.<sup>47</sup> According to Passwaters, she went "ballistic" because she had no idea it had been canceled and asked Noel, "what have I been paying on if it canceled [?]"<sup>48</sup> During that phone call Noel gave Passwaters a quote for a new term of workers' compensation insurance to begin within 24 hours.<sup>49</sup> A little over a month later, Passwaters did obtain new workers' compensation insurance through TIM.<sup>50</sup>

On December 15, 2004, a few days before trial, First State settled its claims against TIM.<sup>51</sup> The parties reportedly entered into a tortfeasor release.<sup>52</sup> Neither the settlement agreement nor the release, however, was introduced into the record.

## II. THE PARTIES' CONTENTIONS

First State seeks specific performance by Montgomery Mutual of the workers' compensation policy on several grounds. First, it argues that Montgomery Mutual

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<sup>46</sup> First State claims to have two ex-employees whose injuries would have been covered by the workers' compensation policy had it been in effect through its full term: Elizabeth Baggett allegedly suffered a back injury and Lisa Passwaters (no relation to Faye Passwaters) allegedly suffered a wrist injury. Tr. at 45.

<sup>47</sup> Noel Dep. at 47.

<sup>48</sup> Tr. at 46.

<sup>49</sup> Noel Dep. at 50.

<sup>50</sup> *Id.*

<sup>51</sup> Pre-trial Order at 1.

<sup>52</sup> Tr. at 15–16.

breached either: (i) the cancellation notice by canceling the insurance after First State fully complied with its terms, or (ii) an oral agreement reached between First State and Montgomery Mutual's agent, TIM. Second, First State argues that Montgomery Mutual is liable as a joint tortfeasor for the negligence of its agent TIM in allowing the policy to be canceled. Third, First State contends that Montgomery Mutual is liable for TIM's actions that fraudulently induced First State to make payments on the policy even after its cancellation.

Montgomery Mutual denies all of First State's claims. In addition, Montgomery Mutual argues that First State's status as a void corporation deprives it of standing to pursue this suit. Montgomery Mutual also contends that First State's settlement with Montgomery Mutual's agent TIM relieves it of all liability stemming from TIM's actions.

### **III. ANALYSIS**

#### **A. First State's Corporate Status**

First State became inoperative and void on March 1, 2004 after it failed to pay its state taxes. Montgomery Mutual contends that as a void corporation First State has no standing to pursue this action. First State disagrees arguing that even a void corporation has the power to close its affairs.

Montgomery Mutual relies on *Transpolymer Industries, Inc. v. Chapel Main Corp.*,<sup>53</sup> for the proposition that First State's inoperative and void status deprives it of standing. In *Transpolymer*, the Supreme Court held, in a very brief, unpublished opinion,

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<sup>53</sup> 582 A.2d 936 (table), 1990 WL 168276, at \*1 (Del. Sept. 18, 1990).

that a void corporation attempting to appear *pro se* did not have standing to pursue an appeal. It is well established that a corporation cannot appear *pro se*.<sup>54</sup> Thus, the brief reference in *Transpolymer* to a void corporation lacking standing could be considered dicta. In any event, I conclude that, in the circumstances of this case, *Transpolymer* does not require a departure from the traditional rule that “a dissolved Delaware corporation has the power to close its affairs but not to carry on the business for which it was established.”<sup>55</sup>

Based on the evidence presented, I find that First State’s action against Montgomery Mutual falls within the ambit of winding up its corporate affairs. The company seeks specific performance of an expired insurance policy in order to satisfy outstanding obligations to injured former employees. Thus, First State’s questionable corporate status does not preclude it from pursuing this suit.

### **B. Montgomery Mutual’s Breach of Contract**

First State contends that it performed under the insurance contract, the cancellation notice and an oral modification of the cancellation notice and that therefore Montgomery Mutual’s cancellation of the insurance was a breach of those agreements. Montgomery Mutual argues that it was justified in canceling the policy because First State breached the terms of the contract by failing to pay premiums for nearly eight months and did not

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<sup>54</sup> See, e.g., *Weber v. Kirchner*, 2003 WL 23190392, at \*1 (Del. Ch. Dec. 31, 2003) (citing *Transpolymer*, 1990 WL 168276, at \*1).

<sup>55</sup> *Gamble v. Penn Valley Crude Oil Corp.*, 104 A.2d 257, 260 (Del. 1954).

comply with the cancellation notice. Montgomery Mutual denies the parties reached an oral agreement regarding payment terms or cancellation.

This case presents a rather unique situation in that neither party introduced a full copy of the insurance contract into the record. First State contends that it never received a copy of the policy, a charge Montgomery Mutual denies, and instead asserts that the contract between the parties was established by a course of dealing.<sup>56</sup> In any event, First State's allegations of breach by Montgomery Mutual do not concern improper cancellation under the original contract. Instead, Plaintiff contends: (i) that Montgomery Mutual breached an oral agreement its agent, TIM, entered into with First State; and (ii) that First State complied with the terms of the cancellation notice and that Montgomery Mutual therefore had no right to cancel the policy.

First State failed to establish that the parties ever reached an oral agreement regarding cancellation. First State has portrayed the situation as a "he said, she said" situation, pitting Noel's and Passwaters' recollections against each other.<sup>57</sup> First State's characterization of the record, however, overstates the divide between Noel's and Passwaters' testimony. Noel vehemently denied reaching an oral agreement not to

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<sup>56</sup> In discovery, a type of term sheet for the workers' compensation insurance was produced, suggesting that a written contract does in fact exist. I need not decide whether there was a written contract, however, because the evidence shows, and First State does not seriously dispute, that the parties agreed that Montgomery Mutual, through TIM, would provide workers' compensation insurance, among other things, to First State in or around October 1999 in exchange for a premium from First State of approximately \$30,000.

<sup>57</sup> *See, e.g.*, Pl.'s Opening Br. ("POB") at 1; Pl.'s Answering Br. ("PAB") at 6.

cancel. Passwaters did not provide a convincing countervailing recollection: she never testified that she explicitly discussed and agreed with Noel on a plan to avoid cancellation by making a payment or series of payments in the initial amount of \$5,000.

Delaware law places a “high evidentiary burden” on parties alleging oral modifications of contracts.<sup>58</sup> Such alterations must be proven with “specificity and directness.”<sup>59</sup> In addition, any amendment to a contract, whether written or oral, requires mutual assent and consideration.<sup>60</sup>

The record contains little support for the assertion that the communications between, and conduct of, the parties relating to the cancellation notice had the effect of amending the agreement between Montgomery Mutual and First State. Passwaters called Noel after receiving the notice. She explained to him how important it was that First State have the workers’ compensation insurance in place and Noel agreed to pick up a \$5,000 check that day. But Passwaters admits that Noel never agreed to stop the cancellation of the insurance: “He didn’t say it wouldn’t or, you know, that it was canceled or, you know. [The cancellation notice] says here that it wouldn’t cancel if I paid it.”<sup>61</sup> In other words, Passwaters relied on her interpretation of the cancellation notice—that a payment, as opposed to *full* payment, would suffice to avoid cancellation—to form her belief that the insurance would continue in force beyond

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<sup>58</sup> *Continental Ins. Co. v. Rutledge & Co.*, 750 A.2d 1219, 1230 (Del. Ch. 2000).

<sup>59</sup> *Reeder v. Sanford Sch., Inc.*, 397 A.2d 139, 141 (Del. 1979).

<sup>60</sup> *DeCecchis v. Evers*, 174 A.2d 463, 464 (Del. 1961).

<sup>61</sup> Tr. at 33.

May 30. She did not confirm her reading of the cancellation notice with Noel or obtain any assurance from him that the May payment would avoid cancellation.

In sum, there are no facts to suggest that the parties reached any sort of oral agreement to modify the plain terms of the cancellation notice. I therefore look to the language of the cancellation notice to determine whether it supports the conclusion that the parties amended their underlying agreement. First State argues that it complied with the notice of cancellation because it both contacted and sent payment to its agent, TIM. I disagree.

The language of the cancellation notice is brief and direct. It states:

Your policy will be cancelled on 05/30/00 at the standard time specified in the policy because the premium has not been received when due. If you are entitled to a refund, it will follow. If payment is received on or before the effective date of cancellation the policy will be continued in force without a lapse in coverage. Please contact or send payment to your agent.

Passwaters interpreted the notice to demand a payment, but not necessarily full payment. With the benefit of hindsight, perhaps the notice could have been clearer. Nonetheless, I find the cancellation notice to explain unambiguously that cancellation is imminent due to nonpayment of premium and that cancellation can be avoided by payment of the past due premium. It did not, as First State suggests, offer to continue coverage if First State either called its agent or sent a partial payment. The evidence shows that First State did not send full payment of the premium then due. Instead, by May 30, 2000, it had paid only \$5,000 of the then outstanding balance of over \$23,000.

Thus, the cancellation notice itself provides no basis for First State's argument that the parties agreed that a partial payment of the past due premium would avoid cancellation.

Furthermore, even if the parties' conduct in connection with the cancellation notice implied mutual assent to such an agreement, as First State contends, the agreement would fail for lack of consideration, or specificity and directness. A promise to fulfill a pre-existing duty, such as a promise to pay a debt owed, cannot support a binding contract.<sup>62</sup> First State has not identified any consideration it offered in exchange for TIM's agreement not to cancel.

With respect to the terms of the purported oral agreement, First State has only suggested a vague agreement not to cancel in exchange for an immediate \$5,000 payment and another payment within 30 days.<sup>63</sup> If the policy had not been canceled it would have continued to accrue premium through at least July. Assuming First State made the two promised payments, it still would have owed a balance of well over \$10,000. In other words, the purported agreement did not include a plan to bring First State current and did not specify what was to transpire after the two payments. Moreover, if First State and TIM had agreed that the payments would avoid cancellation, then TIM would not have insisted on a personal note signed by Passwaters as a condition precedent to reinstating First State's policy.<sup>64</sup>

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<sup>62</sup> See *Continental Ins. Co.*, 750 A.2d at 1232.

<sup>63</sup> Tr. at 33.

<sup>64</sup> Noel Dep. at 278.

Therefore, First State has failed to prove any of the elements of an oral modification to a contract, including mutual assent, consideration, and specificity and directness.

### **C. Montgomery Mutual’s Vicarious Liability**

First State argues that Montgomery Mutual is vicariously liable for the acts or omissions of TIM. First State contends that TIM acted as Montgomery Mutual’s agent with actual and apparent authority. Montgomery Mutual does not seriously dispute that TIM acted as its agent in the administration of the policy, but does argue that First State’s settlement with TIM released Montgomery Mutual from all claims derived from actions taken by TIM.

“[I]f an agent commits a tort for which the principal is liable, both are tortfeasors.”<sup>65</sup> In Delaware, common law regarding joint tortfeasor liability has been modified by the Uniform Contribution Among Tort-feasors Law (the “UCATL”). It applies to persons “jointly or severally liable in tort for the same injury to the person or property.”<sup>66</sup> Section 6304(a) of the UCATL provides: “A release by the injured person of one joint tort-feasor, whether before or after judgment, does not discharge the other tort-feasor unless the release so provides . . . .”<sup>67</sup>

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<sup>65</sup> *Clark v. Brooks*, 377 A.2d 365, 370–71 (Del. Super. 1977) (quoting Restatement (Second) of Agency § 359B (1958)).

<sup>66</sup> 10 *Del. C.* § 6301.

<sup>67</sup> 10 *Del. C.* § 6304(a).

In *Blackshear v. Clark*, the Delaware Supreme Court applied § 6304(a) to allow a plaintiff to proceed against her doctor for medical malpractice after settling with the doctor's principal, the hospital.<sup>68</sup> In applying § 6304(a) to the situation where a master is released but not the servant, the Court specifically refrained from expressing an opinion on whether the statute would also apply where the servant is released but not the master.<sup>69</sup>

Where the sole basis of liability of a principal is the negligence of an agent, the principal cannot be held liable unless the agent is shown to be liable.<sup>70</sup> For that reason, some courts have held that a release given to the agent without reserving rights against the principal discharges the latter.<sup>71</sup> This situation is logically distinct from that addressed in *Blackshear v. Clark*—where the plaintiff released the principal—because the agent's liability is not dependent on negligence of the principal.<sup>72</sup> It remains undetermined under Delaware law, however, whether a plaintiff may pursue claims against a principal whose only basis of liability derives from the alleged negligence of an agent that has been released from liability.

Montgomery Mutual argues that First State's settlement with its agent, TIM, released it as a principal. First State contends that the TIM settlement does not affect its

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<sup>68</sup> 391 A.2d 747, 748 (Del. 1978).

<sup>69</sup> *See id.*

<sup>70</sup> *See Clark*, 377 A.2d at 371; Restatement (Second) of Agency § 217A cmt. b (1958).

<sup>71</sup> *See* Restatement (Second) of Agency § 217A cmt. a (1958).

<sup>72</sup> *See Clark*, 377 A.2d at 371.

claims against Montgomery Mutual because the claims against TIM were distinct from those asserted against Montgomery Mutual. In essence, First State contends that it only settled its claim against TIM for breach of contract to “procure and maintain” insurance and that it did not release TIM from liability for negligence or fraud. I find this contention dubious because First State stipulated to the dismissal of its claims against TIM, but am unable to test First State’s argument because neither party introduced the settlement into evidence. Under these circumstances, I do not have a sufficient basis to determine what claims against TIM were actually released or what rights, if any, First State reserved against Montgomery Mutual. Because the purported release is an affirmative defense of Montgomery Mutual, it bears the burden of proof on that issue. Based on the record presented, I conclude that Montgomery Mutual has failed to prove its release defense, and that it therefore still may be liable for the acts of TIM.

#### **D. TIM’s Negligence**

First State argues that TIM negligently allowed the workers’ compensation policy to be canceled. First State asserts two primary grounds for this position: (i) that First State entered into an oral agreement with TIM to avoid cancellation after issuance of the cancellation notice and TIM failed to communicate that fact to Montgomery Mutual; and (ii) that TIM failed to either explain the effect of the cancellation notice or timely inform First State of the actual cancellation.

First State contends that TIM negligently canceled the insurance after reaching an oral agreement with Passwaters to avoid cancellation by making two \$5,000 payments. Under the purported agreement, First State promised to immediately make a \$5,000

payment and to make an additional payment within 30 days and TIM was to prevent cancellation of the insurance.<sup>73</sup> First State contends that it performed its obligations under the oral agreement and that TIM was negligent in not informing Montgomery Mutual of the agreement and in failing to stop the cancellation of the insurance.

As discussed above, First State failed to prove the existence of an oral agreement between it and TIM not to cancel the workers' compensation insurance. The parties failed to reach a meeting of the minds regarding cancellation. Moreover, First State never paid consideration for the purported oral modification and the purported agreement fails for lack of specificity and directness. Thus, First State's first argument concerning TIM's negligence necessarily fails because there was no oral agreement for TIM to negligently breach.

First State's second argument of negligence concerns TIM's alleged failure to explain the cancellation to First State or to inform First State of the actual cancellation. To prove negligence, a plaintiff must show that: (1) the defendant owed the plaintiff a duty of care, (2) the defendant breached that duty, and (3) the defendant's breach was the proximate cause of the plaintiff's injury.<sup>74</sup> "As a general rule the standard of care applicable to a professional can only be established through expert testimony."<sup>75</sup> Delaware case law, however, is silent as to whether insurance intermediaries are

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<sup>73</sup> Tr. at 33.

<sup>74</sup> *New Haverford P'ship v. Stroot*, 772 A.2d 792, 798 (Del. 2001).

<sup>75</sup> *Weaver v. Lukoff*, 511 A.2d 1044 (table), 1986 WL 17121, at \*1 (Del. July 1, 1986).

“professionals” for malpractice purposes and other States are divided on this issue.<sup>76</sup> In addition, expert testimony is unnecessary when a layperson exercising common sense can reasonably discern the proper standard of care.<sup>77</sup>

Montgomery Mutual argues that First State has failed to meet its burden by not presenting expert testimony to establish the applicable standard of care. First State contends that the negligence alleged in this case involves common sense concepts for which expert testimony is unnecessary. To wit, the negligence alleged concerns failure to avoid cancellation or reinstate an insurance policy after timely payment. To the extent First State has articulated a duty owed by TIM to First State at all, it is the duty of a reasonable person under the circumstances.<sup>78</sup> Assuming without deciding that this is the correct standard, I conclude that First State has failed to carry its burden of proving a breach of that duty.

First State contends that it was unaware of the impending cancellation of the insurance because the cancellation notice was unclear. First State alleges that the notice failed to convey the amount due and that it only contained “the advice to ‘Please contact or send payment to your agent.’”<sup>79</sup> Passwaters explained that her confusion was exacerbated by the fact that she did not have any contract or premiums to go by and thus

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<sup>76</sup> See *Wal-Mart Stores, Inc. v. AIG Life Ins. Co.*, 872 A.2d 611, 630 n.89 (Del. Ch. 2005).

<sup>77</sup> See *Weaver*, 1986 WL 17121, at \*1; *Larrimore v. Homeopathic Hosp. Assoc.*, 181 A.2d 573, 577 (Del. 1962).

<sup>78</sup> See POB at 9.

<sup>79</sup> POB at 4.

was not aware how much First State owed. Thus, First State argues that TIM was negligent in failing to inform First State as to the status of the policy and the effect of the cancellation notice.

First State's negligence claim relies on the alleged ambiguity of the cancellation notice. First State contends that Passwaters believed the May 19 payment complied with the cancellation notice's mandate and would keep the policy in force. Further, First State complains that Noel accepted the May 19 payment "without objecting to her expressed understanding that it would keep the relevant policy in force."<sup>80</sup>

As discussed above, the cancellation notice's terms are clear. It states that the policy was due for cancellation a little more than one month after issuance of the notice for failure to "pay premium when due." The notice then advised that the policy will remain in force "[i]f payment is received on or before the effective date of cancellation." Finally, the notice directs First State to "contact or send payment to [its] agent."

I conclude that in these circumstances First State must be charged with at least constructive notice that the cancellation notice required full payment of the past due premium to avoid cancellation. In light of the unambiguous cancellation notice and an unpaid balance of over \$20,000, Passwaters' belief that a \$5,000 payment would keep the insurance in force was unreasonable. Thus, TIM did not breach a duty to First State by failing to explain the terms of the impending cancellation.

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<sup>80</sup> *Id.* at 5.

In sum, First State's claim against Montgomery Mutual for negligence by TIM in canceling the insurance fails because First State has not carried its burden to show that TIM breached a duty owed it.

#### **E. TIM's Fraud**

First State also contends that TIM fraudulently induced First State to make a series of payments by failing to inform Passwaters that the policy had been canceled. The conduct cited by First State includes Noel's actions and inactions and Hartstein's assertion that "there wouldn't be a problem" if she made her payments. First State contends that TIM committed fraud by (i) representing false statements as true, (ii) actively concealing facts, and (iii) remaining silent in the face of a duty to speak. Montgomery Mutual argues that Passwaters has admitted that her understanding of the effect of the May 19 payment arose from her interpretation of the cancellation notice and not from anything Noel said to her. In addition, TIM communicated the canceled status of the insurance in writing to First State in the June 26 fax and Noel repeatedly discussed the possibility of reinstatement during discussions regarding signing of the personal note.

The elements of a common law fraud claim are: (1) a false representation, concealment of a material fact, or silence in the face of a duty to speak; (2) the defendant's knowledge or belief that the representation was false, or was made with reckless indifference to the truth; (3) an intent to induce the plaintiff to act or to refrain from acting; (4) the plaintiff's action or inaction taken in justifiable reliance upon the representation; and (5) damage to the plaintiff as a result of such reliance.

The gravamen of First State’s fraud claim is that TIM, and Noel particularly, was worried about not being able to recover the over \$20,000 it was owed by First State. That fear, so the argument goes, led TIM to mislead Passwaters and First State regarding the status of the insurance after it had been canceled, in an effort to encourage prompt payment. First State argues that it “provided payments to TIM acting upon a reasonable understanding that the policy in question had not been cancelled . . . an understanding that TIM could have clarified orally or in writing but did not.”<sup>81</sup> First State specifically cites the June 28 letter enclosing the payment schedule as one “which *could have* contained references to cancellation and/or reinstatement but *did not* . . . .”<sup>82</sup>

That argument, however, is substantially undermined by a fax from TIM to First State sent only two days earlier. On the cover page of the June 26 fax, Noel explained that “I can reinstate w/ payment of past due amounts” and attached the cancellation notice. The import of the offer to reinstate is unmistakable. Whether or not Passwaters ever saw this fax—she denies that she did but admitted that others in her office might have seen it<sup>83</sup>—it belies First State’s claim that TIM intentionally misled it in order to induce further payments. The June 26 fax not only undermines Passwaters’ credibility and First State’s position that TIM intentionally misled it, but also supports Noel’s statements that he repeatedly discussed the possibility of reinstatement with Passwaters.

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<sup>81</sup> POB at 12–13.

<sup>82</sup> *Id.* at 13 (emphasis in original).

<sup>83</sup> Tr. at 111.

Importantly, First State has cited only one conversation where it contends TIM actively misled First State. That conversation included Hartstein's statement that if First State continued to pay "there wouldn't be a problem." When reviewed in context, however, that statement is ambiguous at best. Passwaters interpreted it to mean that continued payments would keep the policy in force. But as with other instances, Passwaters does not remember Hartstein using the term cancellation. Moreover, Passwaters remembers the conversation revolving around TIM's insistence that she sign the personal note. Hartstein denies discussing the personal note with Passwaters; instead, he asserts that they discussed First State's payment of the owed amounts and avoiding ending up in court. According to Hartstein, his reference to avoiding a "problem" related to avoiding the involvement of a collections agency or a lawsuit, not cancellation. Left with only Hartstein's ambiguous statement that "there won't be a problem," First State has simply failed to carry its burden to prove that Hartstein intentionally misled First State.

Furthermore, First State also has failed to prove its claim for fraudulent inducement in that it has failed to prove any harm. TIM could not fraudulently induce First State to pay past due premiums on services rendered—premiums that First State admits it owed and was obligated to pay. Implicit in First State's fraud claim is the contrary suggestion that, if it had known it could not avoid cancellation by making the partial payments it did in May, June and July 2000, it would not have made those payments. Yet, First State's own actions disprove that suggestion. For example, even after First State knew the workers' compensation policy had been canceled as of May 30,

2000, it paid off the remaining balance of the past due premium on that policy and obtained a new workers' compensation insurance policy through TIM. I find it reasonable to infer that First State recognized that it probably could not have obtained a new policy through TIM without paying any amount still outstanding on the Montgomery Mutual policy.

In sum, First State has failed to prove that Montgomery Mutual's agent committed any form of fraud. It has not proven that it was injured by any statements or silence of TIM, that TIM concealed from or misled First State as to any material facts, or that TIM intended to induce First State to act or not act by doing so. Since First State has not proven that TIM committed fraud, Montgomery Mutual cannot be liable for fraud.

#### **IV. CONCLUSION**

For the reasons stated herein, the Court finds in favor of Defendant Montgomery Mutual and against Plaintiff First State. An order will be entered consistent with this Memorandum Opinion.