

## **RECENT SIGNIFICANT INSURANCE LAW DECISIONS**

**By: Walter J. Price, III**

The following decisions involving insurance matters were released by Alabama appellate courts in 2008. Many of these cases involve automobile insurance, particularly uninsured and underinsured motorist coverage. In addition, in *Jones v. Alfa Mutual Insurance Company* the Supreme Court of Alabama considered proof of an “abnormal” claim for bad faith denial of an insurance claim. While rather fact-specific, in *Jones* the Court permitted a claim for bad faith failure to investigate to survive summary judgment while, on the other hand, affirming dismissal of the “normal” claim based upon the existence of an arguable reason for Alfa’s position.

### **Rejection of Uninsured Motorist Insurance Coverage**

*Progressive Specialty Insurance Company v. Gore*, 2008 WL 2554286 (Ala.)

Alabama statutory law requires that any automobile liability insurance policy issued for delivery in the state must include uninsured and underinsured motorist coverage. However, such coverage can be rejected by the named insured. Ala. Code §32-7-23(a). The rejection of uninsured and underinsured motorist coverage must be in writing. Oral rejection is not sufficient. *Insurance Company of North America v. Thomas*, 337 So.2d 365 (Ala. 1976).

Note that each named insured must reject uninsured motorist coverage for the rejection to be effective. Rejection by one named insured is not effective as a rejection by other named insureds under the same policy. *Insurance Company of North America v. Thomas*, 337 So.2d 365 (Ala. 1976).

The requirement that all named insureds provide written rejection, for the rejection to be effective for each, extends to policies covering spouses. Where both spouses are named insureds, rejection by one is ineffective so as to waive coverage for the other. *Nationwide Insurance Company v. Nichols*, 868 So.2d 457 (Ala. Civ. App. 2003). A similar issue arose in *Gore* where Jeanette Gore completed an application for automobile insurance. Her husband, Gerald Gore, was the named insured on the policy. Jeanette Gore signed a rejection form in her own name purporting to reject uninsured motorist coverage. Ms. Gore was not identified as a named insured, though

she, like her husband, was listed on the policy as a “driver”.

Jeanette Gore was injured in an automobile accident involving an uninsured motorist. Progressive filed a declaratory judgment action to determine its obligation, if any, to pay uninsured motorist benefits as a result of the accident. Progressive recognized the above requirement that each named insured reject the coverage. It argued, however, that Jeanette Gore’s actions were as the agent of her husband allowing her to bind him regarding this policy provision.

The Supreme Court of Alabama noted that “a person relying on another to make him or her a named insured may reasonably expect that the coverages obtained will be those mandated by law”. The court did not address the agency issue finding that there was no rejection because the form signed by Ms. Gore was signed in her name as opposed to that of her husband. Again, while not ruling on the agency issue, the Court suggested that it may not allow rejection in such a manner given its statement that:

Our statute makes no provision for waiver by anyone other than the named insured. §32-7-23 (a) flatly declares “*that the named insured shall have the right to reject such coverage*”.

Note that where the appropriate named insured rejects coverage, such rejection can bind non-named insureds. The named insured can reject for all other non-named insureds. *Funderburg v. Black’s Insurance Agency*, 743 So.2d 472 (Ala. Civ. App. 1999). In addition, the named insured can reject uninsured motorist coverage for some, but not all, additional insureds. In *Federated Mutual Insurance Company, Inc. v. Vaughn*, 961 So.2d 816 (Ala. 2000), the Supreme Court of Alabama held that an employer could reject uninsured motorist coverage for insured employees, while accepting it for directors, officers, partners, owners, and their family members.

### **Only Named Insured May Reject Uninsured Motorist Coverage**

*Rimas v. Progressive Insurance Company*, 2008 WL 4173838 (C.A. 11 (Ala.))

The Eleventh Circuit Court of Appeals affirmed summary judgment in favor of Progressive on both breach of contract and bad faith claims. The plaintiff, an insured on a motorcycle policy, maintained that he was entitled to uninsured motorist benefits because he, a listed driver on the policy, never rejected the uninsured motorist



have had a “colorable” claim in any dispute with State Farm as regards the insurer’s pro rata share of her attorney fee and costs.

### **Loss of Consortium in Uninsured/Underinsured Context**

*Jenkins v. State Farm Mutual Automobile Insurance Company*, 2008 WL 4531800 (Ala. Civ. App.)

In *Jenkins*, the Alabama Court of Civil Appeals reversed summary judgment in favor of State Farm on a loss of consortium claim made by the injured insured’s wife. The husband had been involved in an automobile accident. He initially filed suit against the tortfeasor only. He later agreed to settle his claims against the tortfeasor, though only two days before then did he advise State Farm of his intent to seek UIM benefits. Ultimately, the husband added State Farm as a defendant in his case against the tortfeasor though in light of the settlement he then dismissed the legal claims against the tortfeasor.

In the interim, the wife sought UIM benefits for her claim of loss of consortium. State Farm argued that her claim was barred because of the husband’s failure to notify it of his intent to settle which impaired State Farm’s subrogation rights. In addition, State Farm asserted that the wife’s claim was derivative of the husband’s and, therefore, when the husband dismissed his claims with prejudice against the tortfeasor the wife’s claim was extinguished. The trial court granted summary judgment on this basis.

As indicated above, the Court of Civil Appeals reversed. The Court noted that State Farm correctly asserted that the loss of consortium claim was derivative; however, it is considered under Alabama law to be a separate property right of the non-injured spouse. Since the wife did not assert her loss of consortium claim in the same action against the tortfeasor, the settlement and release by the husband did not release the tortfeasor from liability for the wife’s loss of consortium claim. Thus, the wife was entitled to pursue her claim against State Farm.

*Jenkins* refers to the effect of settlement by the insured with the tortfeasor. The procedure applicable to such a settlement was set forth in *Lambert v. State Farm Mutual Automobile Insurance Company*, 576 So.2d 160 (Ala. 1991). The following steps protect the rights of the insured and the underinsured motorist carrier if the insured settles with the tortfeasor:

- (1) The insured, or the insured’s counsel, should give notice to

the underinsured motorist carrier of the claim under the policy for underinsured motorist benefits as soon as it appears that the insured's damages may exceed the tortfeasor's limits of liability coverage.

- (2) If the tortfeasor's liability insurance carrier and the insured enter into negotiations that ultimately lead to a proposed compromise or settlement of the insured's claim against the tortfeasor, and if the settlement would release the tortfeasor from all liability, then the insured, before agreeing to the settlement, should immediately notify the underinsured motorist carrier of the proposed settlement and the terms of any proposed release.
- (3) At the time the insured informs the underinsured motorist carrier of the tortfeasor's intent to settle, the insured should also inform the carrier as to whether the insured will seek underinsured motorist benefits in addition to the benefits payable under the settlement proposal, so that the carrier can determine whether it will refuse to consent to the settlement, will waive its right of subrogation against the tortfeasor, or will deny any obligation to pay underinsured motorist benefits. If the insured gives the underinsured motorist carrier notice of the claim for underinsured motorist benefits, as may be provided for in the policy, the carrier should immediately begin investigating the claim, should conclude such investigation within a reasonable time, and should notify its insured of the action it proposes with regard to the claim for underinsured motorist benefits.
- (4) The insured should not settle with the tortfeasor without first allowing the underinsured motorist carrier a reasonable time within which to investigate the insured's claim and to notify its insured of its proposed action.
- (5) If the underinsured motorist carrier refuses to consent to a settlement by its insured with the tortfeasor, or if the carrier denies the claim of its insured without a good-faith investigation into its merits, or if the carrier does not conduct its investigation in a reasonable time, the carrier would, by any of those actions, waive any right to subrogation against



such, for the insured in a guest passenger scenario to be able to recover uninsured or underinsured motorist benefits, the insured must prove that the tortfeasor was guilty of wanton or willful misconduct.

Here, USAA's insured claimed that the driver was guilty of such conduct when she, while driving, turned and waved to a friend and ultimately lost control of the vehicle when avoiding another when she returned her attention to the road. However, the Court found that these actions did not rise to the level of proof of "knowledge and consciousness" that a likely result of her momentarily waving to her friends would be an automobile accident in which the passenger would be injured. Since plaintiff could only prove inadvertence on the part of the driver she could not recover against the tortfeasor and, as such, the insurer was entitled to summary judgment on the claim for UIM benefits.

### **Acceptance of Post-Accident Premium Payment After Policy Lapse**

*Jackson v. State Farm Fire and Casualty Company*, 2008 WL 162125 (Ala. Civ. App.)

On January 18, 2008, the Alabama Court of Civil Appeals released this decision in which it affirmed summary judgment in favor of State Farm. State Farm's insured was involved in an accident on September 17, 2003. She asserted that she was entitled to uninsured or underinsured motorist insurance benefits from State Farm. State Farm established, however, that the policy had lapsed for non-payment of premiums on September 4, 2003. No coverage was found even though the insured's husband reported the accident to the agent and made payment of the outstanding premium amount on September 19, 2003.

The Court reiterated that under Alabama law an insurer that has knowledge that an insured has suffered a loss during a period of default resulting from failure to pay a premium may respond to late tender of the overdue premium by returning the premium for the defaulting period, applying the premium prospectively from a reinstatement date, or it can retain the premium and cover the loss. Note, however, before applying the premium prospectively, the insurer's intent must be clearly conveyed to the insured before acceptance of the premium amount.

### **Claim for Bad Faith Denial of UM Claim Not Ripe, Dismissed**

*Ex parte Safeway Insurance Company of Alabama, Inc.*, 990 So.2d 344 (Ala. 2008)

On February 29, 2008, the Supreme Court of Alabama released this decision in which it held that a bad faith allegation arising out of an uninsured motorist claim was not ripe and due to be dismissed for lack of subject matter jurisdiction. In particular, the Court noted that “there can be no breach of an uninsured motorist contract and therefore no bad faith, until the insured proves that he is legally entitled to recover”. The Court granted Safeway’s Petition for Writ of Mandamus because Safeway presented evidence indicating that damages were in dispute and, therefore, the claim was not ripe.

*Safeway* is the latest in a number of decisions addressing bad faith claims since that tort was originally recognized in 1981. In order to prove a claim for bad faith, the insured must show denial with “no lawful basis for the refusal coupled with actual knowledge of that fact” or “intentional failure to determine whether or not there was any lawful basis” for the denial. *Chavers v. National Security Fire & Casualty Company*, 405 So.2d 1 (Ala. 1981). Intent can be proved by circumstantial evidence as well as direct evidence, and the recoverable damages include mental anguish and economic loss. The lawful basis upon which the insurer relies in denying the claim must be supported by admissible evidence. Also, advice of counsel prior to denial is not an absolute defense though it is evidence of good faith. In such a situation, counsel must have been provided complete information and base his or her opinions on admissible evidence. Further, *Chavers* indicates that a filing of a declaratory judgment action is also evidence of good faith on the part of the insurer.

Again, in order to prove a claim for bad faith, the insured must show a breach of the insurance contract by a denial which was without a lawful basis. Proof of these elements is made if the insured is entitled to a directed verdict on the claim for coverage under the insurance contract. Thus, generally, in order for the Court to submit a claim for bad faith to the jury, the insured must be entitled to a directed verdict on the contract claim.

An insurer must investigate a claim to determine whether the claim is covered and the amount of benefits owed. The insurer must consider all facts and effects on coverage. Whether an insurance company owes a defense and indemnity is determined primarily by the allegations of the complaint. If the allegations of the injured party’s complaint show an accident or occurrence within the coverage of the policy, then the insurer is obligated to defend, regardless of the ultimate liability of the insured. *Ladner & Co. v. Southern Guaranty Insurance Company*, 347 So.2d 100 (Ala. 1977). The insurer can, however, look beyond the bare allegations of the complaint. Again, however, the facts relied upon must be proved by admissible evidence. *Alfa Mutual*

*Insurance Company v. Jones*, 555 So.2d 77 (Ala. 1989); *Pacific Indemnity Company v. Run-A-Ford Co.*, 276 Ala. 311, 161 So.2d 789 (1964).

An insurer cannot selectively consider only favorable information and discount unfavorable information. *Continental Assurance Company v. Kountz*, 461 So.2d 802 (Ala. 1984). Moreover, an insurer may not deny a claim in hopes that it can later gather information to support the denial. The decision to deny will be based upon the information available to the insurer at the time the decision is made. *National Life Insurance Company v. Dutton*, 419 So.2d 1357 (Ala. 1982). There is, however, no duty to investigate until the claim is submitted. *Huff v. United Insurance Company of America*, 674 So.2d 21 (Ala. 1985); *United Insurance Company of America v. Cope*, 630 So.2d 407 (Ala. 1993).

Long before recognizing a claim for bad faith denial, Alabama courts held that an insurance company could be guilty of bad faith for failure to settle a claim on behalf of the insured. The rationale is that the insurance contract gives the insurer the exclusive right to make a settlement and, thus, the duty on the insurer is heightened because of the possibility of an excess verdict. The elements of a claim for bad faith denial were derived from the prior recognized claim for bad faith refusal to settle. *Waters v. American Casualty Company of Reading, Pa.*, 261 Ala. 252, 73 So.2d 524 (1953).

Of course, *Safeway* involved a claim for uninsured motorist benefits. Historically, bad faith claims in this context have been limited. *Quick v. State Farm Mutual Automobile Insurance Company*, 429 So.2d 1033, 1035 (Ala. 1983) (“There can be no breach of an uninsured motorist contract, and therefore no bad faith, until the insured proves that he is legally entitled to recover.”); *Bowers v. State Farm Mutual Automobile Insurance Company*, 460 So.2d 1288, 1290 (Ala. 1984) (“ . . . where a legitimate dispute exists as to liability, whether under primary coverage or uninsured motorist coverage, a tort action for bad faith refusal to pay a contractual claim will not lie.”). This same rationale applied in *Safeway* where the court when further and specifically held that such claims are not ripe for review.

### **Bad Faith Failure to Investigate**

*Jones v. Alfa Mutual Insurance Company*, 2008 WL 2406132 (Ala.)

*Jones* involved claims of bad faith on the part of Alfa in failing to make payment for damages allegedly resulting from Hurricane Opal. The Alabama Supreme Court affirmed summary judgment except as regards the “abnormal” bad faith claim. As indicated previously, generally in order to recover for bad faith the insured must establish that he or she is entitled to a directed verdict on the contract. However, in

“abnormal” cases the insured may prove bad faith failure to investigate the claim. This may involve the failure to obtain necessary materials [*Aetna Life Insurance Company v. Lavoie*, 470 So.2d 1060 (Ala. 1984)] or the failure to submit the investigative materials to cognitive review [*Continental Assurance Company v. Kountz*, 461 So.2d 802 (Ala. 1984)].

After considering the complicated investigative history in *Jones*, the Court determined that the adequacy of Alfa’s claims investigation presented a jury question as to the “abnormal” bad faith claim. In addressing the insurer’s duty, the Court noted that “an insurance company has a ‘responsibility to marshal all . . . facts’ necessary to make a determination as to coverage ‘before its refusal to pay’”. (citations omitted). *Jones*, is unusual in the sense that even though the Court found that there was a debatable reason for denial a fact issue still remained regarding the “abnormal” bad faith claim. Previously, the Alabama Supreme Court has held that if a legitimate reason for denial existed there could be no claim for bad faith failure to investigate. See *Gulf Atlantic Life Insurance Company v. Barnes*, 405 So.2d 916 (Ala. 1981). Nonetheless, while not changing this rule, the Court permitted the “abnormal” bad faith claim to survive summary judgment.

### **Rejection of Claim Based on Misrepresentation in Application**

*American Heritage Life Insurance Company v. Blackmon*, 2008 WL 4757147 (Ala. Civ. App.)

In *Blackmon*, the Alabama Court of Civil Appeals reversed and rendered a judgment in favor of the insured who sought benefits under a life insurance policy. Specifically, the Court found that the trial court incorrectly determined that the application was ambiguous. The Court further noted that an insurer may, under Alabama law, reject an insurance claim where the insurer would not have issued the policy, or would have not issued it at the premium rate applied for, if it had known the truth of information misrepresented on the application. Further, even an innocent misrepresentation on the application provides a basis for the insurer to void the policy. In order to do so, the insurer need only establish that the misrepresentation in the application was a “material contributing influence that induced the insurer to issue the policy”.

### **Rescission of Policy Based on Misrepresentation of Application**

*MEGA Life and Health Insurance Company v. Pieniozek*, 516 F.3d 985 (11<sup>th</sup> Cir. 2008)

This matter involved a life insurance policy. MEGA attempted to rescind the policy issued to the insured because the insured had misrepresented her income. The District Court granted summary judgment in favor of the insured finding that there was no rational basis for how the insurer's risk varied with the insured's income. The Eleventh Circuit Court of Appeals reversed finding that Alabama law did not require a rational basis, but, instead, it only required that the insurer establish that but for the misrepresentation it would have not issued the policy. The Court found, however, given the lack of documentation presented by MEGA confirming this underwriting policy that a jury question was presented.

The policy also required that to recover the accidental death benefit proof was required to show that the death was directly caused by accidental bodily injury, independent of all other causes, and supported by an autopsy. Here, the coroner reported that the insured died of "closed head trauma" as a result of a motor vehicle accident. His report, however, acknowledged that no autopsy was performed, and he even testified that he was not qualified to perform an autopsy. However, the policy did not define the term "autopsy" and since some definitions of that term only require a post-mortem examination, as opposed to a dissection of the body, the term was found ambiguous and, therefore, was construed against the insurer.

The plaintiff's claims for bad faith were dismissed as the breach of contract issue was "fairly debatable".

### **Prior Litigation Exclusion**

*HR Acquisition I Corporation, f/k/a Capstone Capital Corporation v. Twin City Fire Insurance Company*, 2008 WL 4767256 (C.A. 11 (Ala.))

This appeal involved application of a "prior litigation" exclusion in a company non-securities claim liability policy. The insured was Capstone Capital Corporation, a real estate investment trust. Capstone was a Defendant in a shareholder derivative suit filed against HealthSouth and Capstone, which was owned or controlled by three HealthSouth directors and officers, including Richard Scrusby. Capstone sought coverage for the lawsuit.

Twin City, in addressing coverage, relied in part on a "prior litigation" exclusion

which provided that Twin City would not be liable to make any payment for loss in connection with any claim that was:

Based upon, arising from, or in any way related to any demand, suit, or other proceeding against any Insured which was pending on or existed prior to the applicable Prior Litigation Date specified by endorsement to this Policy, or the same or substantially the same facts, circumstances or allegations which are the subject of or the basis for such demand, suit, or other proceeding.

Capstone had previously been named as a defendant in a false claims *qui tam* suit which also included HealthSouth and Scrushy as defendants. The appellate court found that the circumstances of the prior matter, alleged sale of property by HealthSouth to Capstone which was then leased back at allegedly inflated prices, was “related” to the shareholder derivative suit. Further, even though Capstone had not been served with the *qui tam* action, which was settled by HealthSouth, the Court found that it had “existed” or been “pending” against Capstone so as to invoke the exclusion.

### **Marine Cargo Insurance**

*Great Southern Wood Preserving, Inc. v. American Home Assurance Company, AIG*, 2008 WL 3890170 (C.A. 11 (Ala.)).

Great Southern Wood Preserving, Inc. appealed the summary judgment in favor of American Home Assurance Company. Great Southern had imported raw lumber which would ultimately be chemically treated and re-sold to retail and independent business customers. The lumber at issue was received from two ships at the Port of Gulfport and temporarily stored at a warehouse leased from the Mississippi State Port Authority. While located at the warehouse, the lumber was destroyed by the impact of Hurricane Katrina.

American Home issued a Marine Open Cargo Insurance Policy which contained a “warehouse-to-warehouse” provision which stated as follows:

This insurance attaches from the time the goods leave the warehouse and/or store at the place named in the Declaration and/or Certificate for the commencement of transit and continues during the ordinary course of transit, including customary transshipment, if any, until the goods are

discharged overside from the overseas vessel at the final port. Thereafter the insurance continues whilst the good are in transit and/or awaiting transit until delivered to the final warehouse at the destination named in the policy or until the expiry of fifteen days (or thirty days, if the destination to which the good are insured is outside the limits of the port) whichever shall first occur.

Although Great Southern maintained that the final destination would be one of its treatment facilities, the Eleventh Circuit Court of Appeals agreed with the District Court finding that once Great Southern exercised dominion and control over the cargo it was no longer in transit and coverage ceased.

In addition, the Court rejected Great Southern's argument that the lumber could not be under its control because the United States Department of Agriculture had not yet released the lumber when the hurricane struck. The Court stated that "restrictions imposed by the USDA regulations did not annul the dominion and control exercised by Great Southern over the goods held exclusively in its possession".