Spring 2016 Issue

RECENT DEVELOPMENTS IN ALABAMA AND THE ELEVENTH CIRCUIT
Selected Insurance Cases and Other Matters of Interest

In this edition, we have included several cases we hope you find interesting. Included is a case from the Alabama Supreme Court reversing and rendering a trial courtôs grant of summary judgment in the insuredôs favor and finding that a mysterious disappearance exclusion applied to preclude coverage for the unexplained disappearance of a sailboat in *St. Paul Fire and Marine Ins. Co. v. Britt*, --- So. 3d ---, 2016 WL 360654 (Ala. Jan. 29, 2016).

Also, from the Eleventh Circuit Court of Appeals, a case in which the Eleventh Circuit reversed a trial courtôs grant of summary judgment in favor of the insurer on bad faith claims finding that there was an issue of fact as to whether the insurer knew, or should have known, that it was relying on unreliable expert reports given the inconsistencies and missing information contained in the reports in *Atlantic Specialty Ins. Co. v. Mr. Charlie Adventures, LLC*, --- Fed. Appx. ---, 2016 WL 767263 (11th Cir. Feb. 29, 2016).

In a case from the United States District Court for the Southern District of Alabama, the matter involved an insurerôs duty to defend an insured homebuilder for faulty workmanship and resultant damage in *Employers Mut. Cas. Co. v. Kenny Hayes Custom Homes, LLC*, 2016 WL 527075 (S.D. Ala. Feb. 9, 2016).

Finally, we have also included a summary of a lengthy opinion from the United States District Court for the Northern District of Alabama addressing claims of bad faith failure to investigate and settle and legal malpractice arising from an excess verdict against an insured in *Leo, in his Capacity as Trustee for the Bankruptcy Estate of Ashley Murphree v. Alfa Mut. Ins. Co.*, 2016 WL 1180108 (N.D. Ala. Mar. 28, 2016).

Alabama State Law Update

Common Fund Doctrine
Ex parte State Farm Mut. Auto. Ins. Co., --- So. 3d ----, 2016 WL 360665 (Ala. Jan. 29, 2016).

Facts: James Pritchard (ñPritchardò) brought an action against Boderick McCants (ñMcCantsò), State Farm Mutual Automobile Insurance Company (ñState Farmò) and others to recover damages for his injuries caused in an automobile accident. McCantsô insurer, GEICO, offered to settle with Pritchard for its policy limits of $50,000. State Farm, Pritchardôs UIM insurer, ñbought outò GEICO, advanced the $50,000 to Pritchard, and opted out of the litigation. After the jury returned a $400,000 verdict in favor of Pritchard, he asked the trial court to require State Farm to contribute $20,000 toward his attorneyôs fees under the common fund doctrine. The trial court granted the motion and the Alabama Civil Court of Appeals affirmed the order. The Alabama Supreme Court granted certiorari.

Issue: ***Whether a UIM insurer that agrees to a Lambert advance is required to contribute to the insured's attorney's fees based on the common fund doctrine.***

Holding: No. The common fund doctrine provides that, when an insured recovers damages against a tortfeasor, the insuredôs UIM insurer is obligated to pay for a proportionate share of the expenses the insured incurred to receive the damages award. As described in *Lambert v. State Farm Mutual Automobile Insurance Co.*, 576 So. 2d 160 (Ala. 1991), ñ[i]f the [UIM] insurer wants to protect its subrogation rights, it must, within a reasonable time, in any event before the tort-feasor is released by the carrierôs insured, advance to its insured an amount equal to the tort-feasorôs settlement offer.ò However, a *Lambert* advance does not create a UIM insurerôs right to subrogation proceeds within a UIM insurerôs policy limits. Therefore, a *Lambert* advance is not a subrogation right, and the common fund doctrine does not apply. The UIM insurer is not required to contribute to attorneyôs fees.

Mysterious-Disappearance Exclusion
St. Paul Fire and Marine Ins. Co. v. Britt, --- So. 3d ---, 2016 WL 360654 (Ala. Jan. 29, 2016).

Facts: Michael Britt (ñMichaelò) lived on his sailboat and purchased an all-risk policy from St. Paul. He told his family he was sailing from West Palm Beach to Jacksonville, Florida to store the boat and rent a car so he could attend an orientation for his new job in Oklahoma City. During his trip to Jacksonville, the U.S. Coast Guard detained him for a routine inspection and he placed a call to a creditor regarding the sailboat. No one else had contact with him and he did not make it to Jacksonville. The weather was not poor during that time. After searching for him for a lengthy period of time, the cause of his disappearance remained unknown. The conservator filed a claim for the sailboat with St. Paul and, after an investigation, St. Paul declined coverage. Two years after making a claim with St. Paul, the conservator filed a breach-of-contract, bad-faith, and fraud action against St. Paul. The trial court granted St. Paulôs motion to dismiss the fraud claim. The trial court also granted the conservatorôs motion for summary judgment on the breach-of-contract claim and declared the bad-faith claim moot. St. Paul appealed.

Issue: ***(1) Whether the mysterious-disappearance exclusion precluded coverage.***
(2) Whether the 30-day provision applied and made coverage illusory.

Holding: (1) Yes. The policy did not include a definition of ñmysterious disappearance,ò and the Alabama Supreme Court concluded the common meaning was ñif the insured property cannot be found and the circumstances surrounding the disappearance are so óunknown, puzzling, or baffling[,] . . . as to make the disappearance inexplicable, a person of ordinary intelligence would not find the circumstances would determine that disappearance to be ómysterious.ò Although many speculated as to the reason for his disappearance, there was no evidence to prove the cause of his disappearance.

Because the term was not ambiguous, and the facts of the case fell within the definition of ñmysterious disappearance,ò the exclusion applied.

(2) No. The conservator argued that a 30-day provision in the policy provided coverage when the covered property has been missing for more than 30 days. Therefore, the conservator argued that the policy language contradicted the mysterious disappearance exclusion and the policy coverage was illusory. The Court disagreed because not all disappearances are mysterious. If the sailboat sank and Michael survived to explain what happened, or if the sailboat was stolen and there was evidence to indicate theft, the boatôs disappearance would not be mysterious. Because these two policy provisions did not ñcompletely contradictò each other, the conservatorôs argument failed. The Court reversed the summary judgment in favor of the conservator and instructed the trial court to enter summary judgment in favor of St. Paul on the breach-of-contract and bad-faith claims.

Apparent Authority of Agent

Southern Cleaning Service, Inc. v. Essex Ins. Co., --- So. 3d ----, 2016 WL 687048 (Ala. Feb 19, 2016).

Facts: Winn Dixie grocery store subcontracted with Southern Cleaning Service, Inc. (ñSouthern Cleaningò) and provided janitorial services to the grocery. Southern Cleaning was required by contract to add the grocery as an additional insured under its liability policy. Southern Cleaning contacted Alabama Auto Insurance Center (ñAlabama Autoò), an independent insurance agency, to obtain insurance. Alabama Auto, in turn, contacted a general managing agency, Genesee General Agency, Inc. (ñGeneseeò), to procure the insurance. Genesee located a policy with Essex Insurance Company (ñEssexò), which Southern Cleaning accepted.

A customer of the grocery store slipped on a wet floor and suffered injuries. Within days of the fall, the grocery notified Southern Cleaning and retail agent Alabama Auto, and asked Alabama Auto to notify general managing agent Genesee. However, Essex did not learn of the incident until fifteen months later.

The Essex policy required an insured to provide notice of an occurrence ñas soon as practicable.ò After an investigation, Essex denied the claim on the basis of late notice. In coverage litigation, Essex filed a summary judgment motion, arguing that it did not owe coverage because of late notice, and the trial court agreed. The named insured, Southern Cleaning, and the additional insured, Winn-Dixie appealed to the Alabama Supreme Court.

Issue: ***Whether an insured's retail agent had "apparent authority" such that notice to the agent was notice to the insurer.***

Holding: Yes. The contract between Genesee (the managing general agent) and Alabama Auto (the retail agent) provides that Alabama Auto is not an agent or employee of any insurance company represented by Genesee and that Alabama Auto is the agent of insureds. The Court accepted that Alabama Auto was not the agent-in-fact of the insurer; however, the Court noted that there are certain situations where an agent becomes ñcloakedò in apparent authority from the insurer to accept notice of claims on behalf of the insurer. *See Protective Life. Ins. Co. v. Atkins*, 389 So. 2d 117 (Ala. 1980) (holding that a contract that limits an agency relationship ñdoes not affect third persons relying upon the agentôs apparent authority without notice of [the agentôs] limitationsò).

The Court noted that all communications regarding the policy went through Alabama Auto; Alabama Auto was listed as the agent in the policy; Alabama Autoôs contact information was the only contact information provided in the policy; and nothing indicated that the insured could not file a claim with Alabama Auto. Accordingly, the Court concluded that a genuine issue of material fact existed as to whether Alabama Auto had apparent authority to accept notice of the claim. The Court reversed the summary judgment in favor of the insurer and remanded the case to trial court for trial.

Alabama Federal Law Update

Duty to Defend
Employers Mut. Cas. Co. v. Kenny Hayes Custom Homes, LLC, 2016 WL 527075 (S.D. Ala. Feb. 9, 2016).

Facts: Homeowners filed a negligence action in state court against the insured, a builder, for lack of supervision that caused additional construction costs and defects in construction, including water intrusion. The insuredôs CGL insurer filed a declaratory judgment action in the United States District Court for the Southern District of Alabama seeking a determination that it did not owe the insured a duty to defend in the underlying action. The insurer moved for summary judgment and the insured opposed the motion.

Issue: ***Whether the insurer owed a duty to defend the insured.***

Holding: Yes. The insurer argued that it did not owe a duty to defend because the water damage was not caused by an occurrence since faulty workmanship is not an ñoccurrence.ò The court disagreed, finding that the plaintiffs claimed the interior walls were damaged not by faulty workmanship, but by water intrusion. The court determined that the water intrusion could be deemed an ñoccurrenceò under the terms of the policy.

The insurer also argued that it had no duty to defend because there was no ñproperty damage.ò However, the court found that the plaintiffsôallegation that the color of the walls inside the house had changed because of the water intrusion was an allegation of ñproperty damageò sufficient to trigger the duty to defend.

The insurer also argued that the plaintiffsôclaim for mental anguish damages was not ñbodily injury.ò The policy defined ñbodily injuryò in part as ñsickness or disease sustained by a person.ò The court noted that Alabama courts include mental anguish in the definition of ñsickness.ò *See Morrison Assur. Co. v. North American Reinsurance Co.*, 588 F. Supp. 1324 (N.D. Ala. 1984) *aff'd sub nom. Morrison Assur. Co. v. North American Reinsurance Co.*, 760 F.2d 279 (11th Cir. 1985). Therefore, the court found that the plaintiffsô claim for mental anguish damages alleged ñbodily injuryò for which the insurer owed a duty to defend.

Bad Faith - Basing Denial on Expert Opinions

Atlantic Specialty Ins. Co. v. Mr. Charlie Adventures, LLC, --- Fed. Appx. ---, 2016 WL 767263 (11th Cir. Feb. 29, 2016).

Facts: A fire destroyed the insuredôs 40-foot yacht. The insured filed a claim with her property insurer, Atlantic Specialty. As part of its investigation, Atlantic Specialty hired two experts ï a marine surveyor and a fire cause-and-origin investigator. Both experts concluded that the fire was caused by marine life in or on the engine and that the engine suffered maintenance issues that contributed to the loss. Both of these causes are excluded from coverage; therefore, based on the expert reports, Atlantic Specialty denied the claim.

Atlantic Specialty then filed a declaratory judgment action in the United States District Court for the Southern District of Alabama seeking a declaration that it did not owe coverage. The insured filed a counterclaim alleging breach of contract and bad faith. Both parties filed summary judgment motions. The district court granted the insuredôs motion for summary judgment on the breach-of-contract claim and the insuredôs motion for summary judgment on the insurerôs declaratory judgment claim. However, the district court granted the insurerôs motion for summary judgment on the bad-faith claim. The insured appealed to the Eleventh Circuit.

Issue: ***Whether Atlantic Specialty's reliance on inadmissible expert opinions is sufficient to survive a motion for summary judgment on bad faith.***

Holding: No. Prior to granting summary judgment in favor of the insurer on the bad-faith claim, the district court held that the opinions of the experts upon which the insurer had relied to make its coverage determination were inadmissible under Federal Rule of Civil Procedure 702. The district court reconciled the two rulings by finding that Atlantic Specialty did not know or have reason to know of the unreliability of the

opinions.

On appeal, the Eleventh Circuit disagreed and reversed the summary judgment in favor of the insurer and remanded the bad-faith claim for trial. The Eleventh Circuit held that an issue of fact existed regarding whether the insurer should have known its expertsô reports were unreliable, given the inconsistencies between the reports and missing information.

Bad-Faith Failure to Pay Additional Losses
Harless v. Cincinnati Ins. Co., 2015 WL 10521807 (N.D. Ala. Nov. 5, 2015) (opinion adopted in *Harless v. Cincinnati Ins. Co.*, 2016 WL 1085878 (N.D. Ala. Mar. 21, 2016)).

Facts: The insureds had a rental policy with Cincinnati Insurance Company (ñCincinnatiò). Following two fires at the rental property, the insureds submitted claims for contents damage to Cincinnati. Although evidence of arson existed, Cincinnati made a number of payments to the insureds without first receiving documentation of the contents. While Cincinnati was in the process of reviewing financial information the insureds provided, the insureds filed in state court a breach-of-contract, bad-faith, and negligence/wantonness/reckless action against the insurer for failure to pay the full market value of their lost property. Cincinnati successfully removed the case to the United States District Court for the Northern District of Alabama and eventually filed a motion for partial summary judgment on the insuredsô bad-faith and negligence/wanton/reckless claims.

Issue: ***Whether the insurer was entitled to summary judgment on the bad-faith and negligent/wanton/reckless claims.***

Holding: Yes. The district court found that Alabama law does not recognize a cause of action for negligent or wanton claim handling against an insurer. Also, regarding the bad-faith claim, the court found that the insurer had paid the insureds the actual cash value of the contents. Moreover, the insureds failed to provide proof of the additional claimed loss of the contents for many months; admitted that they made a claim for items they did not own; and admitted that they inflated the value of some other items. Accordingly, the court held that the insurer had an arguable basis for its decision not to pay additional benefits.

Bad Faith Failure to Settle
Leo, in his Capacity as Trustee for the Bankruptcy Estate of Ashley Murphree v. Alfa Mut. Ins. Co., 2016 WL 1180108 (N.D. Ala. Mar. 28, 2016).

Facts: Ashley Murphree (ñMurphreeò) and Willow Cameron (ñCameronò) were involved in an automobile accident in which Cameron was injured. Murphree had an automobile insurance policy with Alfa, and Cameronôs medical expenses exceeded the Alfa

$100,000 policy limit. Cameron filed suit against Murphree asserting claims of negligence and wantonness. Alfa accepted coverage and defended the case on behalf of Murphree.

Throughout the litigation, Cameronôs counsel made policy-limits settlement demands and advised Murphreeôs counsel that Cameron would seek collection of an excess verdict if the case did not settle. Murphreeôs counsel advised Alfa of the demand and that an excess verdict was possible, but also advised that liability was uncertain. Murphreeôs counsel advised Alfa that the case was dangerous but did not recommend that Alfa settle the case.

Murphreeôs counsel also advised Murphree of the risks in the case, that an excess verdict was possible, and the defenses to the claims against her. Murphreeôs counsel also discussed her options in the event of a excess verdict, including that Murphree could file bankruptcy to discharge the excess judgment. Murphreeôs counsel did not recommend to Murphree that she ask Alfa to settle the case; instead, she left the decision up to Murphree who, according to Murphreeôs counsel, insisted that the case be tried.

After a trial, the jury returned a $260,000 verdict against Murphree. Murphree, having not been advised of any potential claim against Alfa, filed bankruptcy and asked Alfa to pay for the bankruptcy filing. Alfa agreed to pay for the bankruptcy in exchange for Murphreeôs execution of a ñCovenant Not to Sueò drafted by Murphreeôs counsel.

Later, the bankruptcy trustee filed the current litigation seeking to set aside the Covenant Not to Sue as a fraudulent transfer under the bankruptcy code and asserting claims for negligent/wanton failure to settle, bad faith failure to investigate and settle, suppression and conspiracy against Alfa. The bankruptcy trustee also asserted a legal malpractice claim against Murphreeôs retained defense counsel.

The defendants filed summary judgment motions.

Issue:

(1) Whether Murphree's failure to demand that Alfa settle the case and her agreement to proceed to trial precluded her claims of negligent, wanton, or bad faith failure to settle.

(2) Whether Alfa's reliance on the recommendations of Murphree's retained defense counsel is an absolute defense to claims for negligent, wanton, or bad faith failure to settle.

(3) Whether the insured's claim for negligent/wanton/bad-faith failure to investigate and settle the underlying action should survive summary judgment.

(4) Whether Murphree's counsel was entitled to full summary judgment on the legal malpractice claim.

Holding: (1) No. Citing Alabama Supreme Court decisions, the district court specifically rejected Alfaôs argument and applied the ñtotality of the circumstancesò test for determining whether the insurer could be held liable for the excess verdict.

(2) No. The district court held that Alfaôs reliance on Murphreeôs counselôs advice was just one of the circumstances to be considered under a ñtotality of the circumstancesò test and could not be, in and of itself, dispositive of the insuredôs claims.

(3) No/Yes. The district court found that the plaintiff failed to establish the standard of care for a negligent failure to investigate claim. The court found that the facts established that ALFA conducted enough investigation to determine that an excess verdict was possible but also that liability was in question. The court determined that plaintiff had failed to present evidence establishing that such a result was likely or expert testimony establishing the standard of care or that ALFA breached. As a result, the court granted summary judgment, but only to the extent that plaintiff made claims for negligent or wanton failure to investigate, allowing the negligent/bad faith failure to settle claims to survive.

(4) No. The district court denied defense counselôs summary judgment regarding the trusteeôs allegations that counsel breached the standard of care by failing to advise Alfa to settle the case. The court found that, because the insured provided expert testimony that Murphreeôs counsel should have advised Alfa to settle the case, a fact issue existed precluding summary judgment. However, the court granted defense counselôs summary judgment regarding her trial preparation and to the extent that the trustee alleged that she violated a duty to advise Murphree to demand settlement. The court also granted defense counselôs summary judgment for any claimed liability arising out of the drafting of the Covenant Not to Sue. Finally, the court granted defense counselôs summary judgment regarding the trusteeôs claims that defense counsel did not adequately convey the risks involved in trying the case, the possibility of an adverse judgment, and Murphreeôs right to seek advice from outside counsel.

Bad Faith Discovery
Graham & Co., LLC v. Liberty Mut. Fire Ins. Co., 2016 WL 1319697 (N.D. Ala. Apr. 5, 2016).

Facts: Liberty Mutual Fire Insurance Company (ñLiberty Mutualò) issued a policy to the insureds that included property coverage. One of the insuredsô buildings suffered property damage, and the insureds submitted a claim to Liberty Mutual. Liberty Mutual denied the claim because the building (along with eight others) was not listed on the policy. The insureds contended that the policyôs errors and omissions clause (ñE&O clauseò) created coverage for the property, but Liberty Mutual disagreed. The insureds then sued for breach of contract and bad faith. During the course of the

litigation, Liberty Mutual objected to certain discovery requests from the insureds, and the insureds moved to compel responses and production of the requests.

Issue:

(1) Whether the insurer can be compelled to produce information related to prior bad faith lawsuits.

(2) Whether the insurer can be compelled to produce reserve information.

(3) Whether the insurer can be compelled to produce a list of other claims handled by the adjuster at issue.

(4) Whether the insurer can be compelled to produce discovery related to performance goals and evaluations of the insurer's claims department.

(5) Whether the insurer can be compelled to produce the personnel files of the employees involved in the claim;

(6) Whether the insurer can be compelled to produce discovery regarding quality assurance and claim dispute resolution.

Holding: (1) Yes (with limitations). The district court held that the requests were overbroad and unduly burdensome as written; however, it compelled Liberty Mutual to respond to the requests within the following limitations: actual lawsuits (not just claims) involving similar type claims against the actual insuring entity and its affiliated entities handling underwriting, in Alabama for the past four years.

(2) No. The district court adopted the ñmajorityò view in first-party claims that reserve information is outside the scope of discovery because the information is not relevant to what the insurer thought of the merits of the claim.

(3) Yes. The district court allowed discovery of a list of other claims on which the adjuster at issue worked, but only within the narrowed scope identified by the court (*see* section (1) above).

(4) Yes. The district court found that employee incentives, to the extent that they exist, would be deemed relevant. However, Liberty Mutual was only required to produce this information regarding the specific individuals involved in the claim or to the claims department as a whole that would, in effect, be applicable to the individuals involved.

(5) No. The strong presumption against production of personnel files precluded discovery of those files in the case.

(6) Yes. The district court held that Liberty Mutual was required to produce the guidelines applicable to the individuals involved in the claim within the narrowed time frame.

Amount in Controversy (Removal)

Nationwide Prop. and Cas. Ins. Co. v. Dubose, 2016 WL 1448855 (S.D. Ala. Apr. 12, 2016).

Facts: Kimberly Dubose (ñDuboseò) was injured in a single car accident while her friend was driving Duboseôs car. Duboseôs father maintained a policy with Nationwide Property and Casualty Insurance Company (ñNationwideò) for her vehicle, although he signed a document refusing uninsured/underinsured motorist coverage. Nationwide denied coverage and filed a declaratory judgment action in the United States District Court for the Southern District of Alabama against Duboseôs father individually and in his capacity as Duboseôs parent and next of friend. Duboseôs father moved to dismiss the action for lack of subject matter jurisdiction, claiming Nationwide had not show the requisite amount in controversy, claiming the available policy limit was $75,000, but did not exceed $75,000.

Issue: ***Whether an insured's settlement demand letter seeking $500,000 establishes that the amount in controversy exceeds $75,000.***

Holding: No. Nationwide argued that it met the amount-in-controversy requirement because the insured sent a settlement demand in the amount of $500,000 to both the liability carrier for the driver and Nationwide. The court found that the demand was to both carriers and included the following qualification: ñ$500,000 or all of the available policy limits, whichever is the least.ò Therefore, the settlement letter was insufficient to establish that the amount of the claim solely against Nationwide exceeded the jurisdictional minimum.

Removal

James v. McDaniel, 2016 WL 1573457 (S.D. Ala. Apr. 19, 2016).

Facts: The plaintiff filed a wrongful death action against Allstate Insurance Company (ñAllstateò) and Curtis McDaniel (ñMcDanielò) in state court. Allstate filed an answer, and several weeks later, McDaniel filed a notice of removal to the United States District Court for the Southern District of Alabama. The plaintiff moved to remand the case and argued that Allstate did not provide written consent to remove the case and Allstate did not timely oppose the motion to remand.

Issue: ***(1) Whether Allstate, as a co-defendant, was required to provide written consent to validate the notice of removal.***

(2) Whether the fact that Allstate's opposition to the motion to remand was not filed on time requires the case to be remanded.

Holding: (1) No. Allstate did not sign the notice of removal, but the notice stated that McDanielôs counsel corresponded with Allstateôs counsel and Allstate provided its consent to removal. The Eleventh Circuit labels the requirement that all defendants agree to join a notice of removal to make a removal effective as the ñunanimity rule.ò

See Bailey v. Janssen Pharmaceutica, Inc., 536 F.3d 1202 (11th Cir. 2008). In *Stone v. Bank of New York Mellon N.A.*, 609 Fed. Appôx. 979 (11th Cir. 2015), the Eleventh Circuit held that a technical defect, such as failure to sign the notice, could be cured if the party who fails to sign the notice opposes the motion to remand. Because Allstate opposed the motion to remand, the defect is cured.

(2) No. Relying on the holding in *Stone*, the district court held that ñAllstateôs ultimate acquiescence to removal was a curable ótechnical defect.ôò Therefore, the district court denied the motion to remand.