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

In this edition of our newsletter, we feature a number of cases from Alabama and its federal courts. Of particular interest are *Har-Mar Collisions, Inc. v. Scottsdale Ins. Co.*, --- So. 3d ----, 2016 WL 3136189 (Ala. June 3, 2016), *Smith v. State Farm Fire & Cas. Co.*, 2016 WL 3144082 (N.D. Ala. June 6, 2016), and *American Safety Indem. Co. v. Fairfield Shopping Ctr., LLC*, 2016 WL 3878496 (N.D. Ala. July 18, 2016). In *Har-Mar*, the Alabama Supreme Court, as a matter of first impression, held that the ñnamed insuredò in an insurance contract may be reformed on the basis of a mutual mistake. In *Smith*, the Northern District of Alabama determined that a third-party contractor may maintain a negligence or wantonness claim against an insurer. Finally, in *American Safety Indemnity Company*, the Northern District of Alabama examined whether material misrepresentations in the application process voided the insurance policy as to the insuredôs and mortgageeôs claims. The court concluded that the insurance policy was voided as to the insuredôs claims, but the policy was not voided as to the mortgageeôs claims.

We hope you find this information useful. If you have any questions or would like to discuss, please do not hesitate to let us know.

Alabama State Law Update

Reformation of an Insurance Contract

Har-Mar Collisions, Inc. v. Scottsdale Ins. Co., --- So. 3d ----, 2016 WL 3136189 (Ala. June 3, 2016).

Facts: Wayne Hartung incorporated his paint-and-body shop as Har-Mar Collisions, Inc., (ñHar-Mar Collisionsò) but operated the business under the name Marshall Paint & Collision. Mr. Hartung sought insurance coverage for Har-Mar through Kris Kahalley, a certified insurance counselor employed by International Assurance, Inc. (ñInternational Assuranceò). Mr. Kahalley completed and submitted an application that listed the prospective insuredôs name as ñMarshall Paint & Collision,ò and listed the named insuredôs mailing address as ñHARMAR Inc dba 2869 Government Boulevard Mobile, AL 36606.ò

As a result of the application, Scottsdale issued a commercial property policy to ñHARMAR, INC. d/b/a MARSHALL PAINT AND COLLISION.ò During the coverage period, a fire destroyed Har-Mar Collision. After a dispute about payments, Har-Mar Collision filed an action against Scottsdale, seeking, among other claims, a declaration that it was the named insured, despite the way the agent had obtained the policy. The trial court held that the Scottsdale policy should be reformed to reflect Har-Mar Collision as the named insured based upon ñmutual mistake,ò and Scottsdale appealed.

Issue: ***Whether the "named insured" in an insurance contract can be reformed on the basis of mutual mistake.***

Holding: Yes. Alabama Code Section 8-1-2 provides that a court may revise a contract if there is a mutual mistake between the parties as long as there will be no prejudice to the rights, acquired in good faith and for value, from third parties. Alabama courts require the moving party to establish the need for reformation through clear and convincing evidence. A ñmutual mistakeò is a ñmutual misunderstanding concerning a basic assumption on which the contract was made.ò *Finley v. Liberty Mut. Ins. Co.*, 456 So. 2d 1065 (Ala. 1984).

Noting that this was a case of first impression in Alabama, the Alabama Supreme Court looked to a case from the Ohio Supreme Court as guidance in holding that reformation was appropriate under these facts. The Court held that neither partyôs belief was ñin accord with the factsò because Harmar Inc., a non-entity, was the named insured and not Har-Mar Collision. Therefore, the Court held that Har-Mar Collisions met the clear and convincing evidence requirement, and affirmed the trial courtôs decision. Moreover, the Court held that Har-Mar Collision had standing to file the action against Scottsdale because the Court affirmed the reformation of the policy.

Alabama Federal Law Update

Bifurcation/Stay Bad-Faith Claims
Georgia-Pacific Consumer Products, LP v. Zurich American Ins. Co., 2016 WL 1695085 (S.D. Ala. Apr. 26, 2016).

Facts: S&S contracted with Georgia-Pacific Consumer Products, LP (ñGPò) to perform work at a paper mill facility and was required to maintain insurance in favor of GP. An employee of S&S was killed while working at GPôs facility, and GP filed this lawsuit against numerous defendants, including two insurers that issued excess/umbrella policies to GP through S&S. GP asserted claims for breach of contract, bad faith, and negligence against the insurers. The insurers filed a motion to bifurcate the bad-faith claims from the breach-of-contract and negligence claims and stay discovery on the bad-faith claims pending the resolution of the other two claims.

Issue: ***Whether the court should bifurcate and stay the bad-faith claims pending the resolution of the other claims.***

Holding: No. Federal courts are given broad discretion to determine whether to bifurcate and stay claims. U.S. District Judge William Steele noted that bifurcating bad-faith claims in other cases has not improved judicial economy. Since judicial economy can only be improved if the defendants win the breach-of-contract claims, two rounds of discovery, dispositive motions, and trials could potentially be required if the insurers

do not prevail on the breach-of-contract claims. The court held that there would be overlap between the discovery of the breach-of-contract and bad-faith claims as well as the bad-faith and negligence claims. Although discovery of the bad-faith claims could be inconvenient or ñeven embarrassing,ò it does not ñamount to meaningful prejudice.ò Therefore, the court denied the motion to bifurcate and stay.

Motion to Dismiss
Long v. Patton Hospitality Management, LLC, 2016 WL 1677565 (S.D. Ala. Apr. 26, 2016).

Facts: After sustaining injuries in a slip and fall, the plaintiff filed this action against the company managing the property (ñthe insuredò) and the insuredôs liability insurer. The insurer moved to dismiss the action.

Issue: ***Whether the liability insurer should be dismissed without prejudice, as the insured's liability has not been determined at this time.***

Holding: Yes. Alabama law does not permit a cause of action against a liability insurer for the alleged actions of an insured when the insuredôs liability has not yet been determined in a final judgment. Therefore, the court dismissed the insurer without prejudice.

Default Judgment in Coverage Action
Axis Ins. Co. v. Appeal Ins. Agency, Inc., 2016 WL 1698095 (N.D Ala. Apr. 28, 2016).

Facts: Chad Sanders and Sanders Cabinetry, LLC (ñSandersò) contracted with Appeal Insurance Agency, Inc. (ñAppealò) to acquire insurance for three rental properties. Six months after insurance was allegedly in place, one of the properties was vandalized and damaged. Sanders sought coverage for this damage and was notified that no policy was in effect for Sandersôproperty. Sanders filed a lawsuit against Appeal and other entities seeking damages for the lack of coverage. After defending Appeal under a reservation of rights, Appealôs professional liability insurer, Axis Insurance Company (ñAxisò), filed this declaratory judgment action in the United States District Court for the Northern District of Alabama, seeking a declaration of no coverage. Appeal was properly served through a registered agent but did not make an appearance in the action. Two months after service, Axis filed for a default judgment and the clerk entered a default. Axis then filed a renewed motion for default judgment.

Issue: ***Whether the insurer's renewed motion for default judgment against its insured should be granted.***

Holding: Yes. The court held that it had subject matter jurisdiction over the matter, as there was diversity between the parties and the amount in controversy exceeded $75,000. Federal Rule of Civil Procedure 55 requires the court to examine whether there is ña legitimate basis for any award it enters.ò *Anheuser Busch, Inc. v. Philpot*, 317 F.3d

1264 (11th Cir. 2007). Since Appeal defaulted, the court may rely on the allegations in the complaint as true. Although the policy requires Axis to provide coverage to Appeal in connection with a ñWrongful Act,ò the complaint states that the allegations in the Sanders complaint against Appeal do not constitute a ñWrongful Actò as described in the policy. Because Appeal did not answer and deny the allegations in Axisôs complaint, the court must consider this statement as admitted by Appeal. Therefore, the court held there is no coverage under the policies and Axis had no duty to defend or indemnify Appeal in the underlying lawsuit.

Amount in Controversy
State Farm Fire and Cas. Co. v. Johnson, 2016 WL 1704322 (M.D. Ala. Apr. 28, 2016).

Facts: Following a fire that damaged the insuredôs home, the insured made a claim to recover damages from its insurer. The insured and insurer disagreed as to the correct amount of damages. Eventually, the insured invoked the policy provision allowing the insured and insurer to select an appraiser and submit each appraisal to an umpire. The insurer disputed the amount the umpire awarded and filed a declaratory judgment action in the United States District Court for the Middle District of Alabama. The insured moved to dismiss for lack of subject matter jurisdiction.

Issue: ***Whether the amount in controversy is satisfied and creates subject matter jurisdiction.***

Holding: No. Because the insured brought a ñfactual attackò on the complaint, the court may hear conflicting evidence in order to determine whether subject matter jurisdiction exists. *See Lawrence v. Dunbar*, 919 F.2d 1525 (11th Cir. 1990) and *Colonial Pipeline Co. v. Collins*, 921 F.2d 1237 (11th Cir. 1991). The court concluded that the actual amount in dispute was less than the $75,000 threshold. Therefore, the action was due to be dismissed.

Residency as Element of Insured Definition in UM/UIM Context
Z.C. v. Progressive Specialty Ins. Co., 2016 WL 2997219 (N.D. Ala. May 25, 2016).

Facts: The named insured is the mother of a minor son who was involved in a single vehicle accident. In order for the son to qualify as an insured under the UIM provisions of the motherôs policy, he had to be ñprimarily residingò with his mother at the time of the accident. The son generally lived at his fatherôs house on school days and lived primarily with his mother when he was not in school. His father testified that his son lived at his house a little more than his motherôs house. The son testified that he could not remember where he lived more. His mother testified that she could not say where he lived more since her son came to her house sometimes on school days. The insurer denied coverage to the son, and the son (through his father as next friend) filed this lawsuit against the insurer in state court. The insurer then removed the action to the

United States District for the Northern District of Alabama. The insurer filed a motion for summary judgment and the son opposed it.

Issue: ***Whether the minor son was "primarily residing" with his mother, the named insured under an automobile policy, in order to qualify for UIM coverage under the policy.***

Holding: No. Under the terms of the policy, an ñinsured personò includes a dependent blood relative ñprimarily residingò in the same household as the named insured. The policy states that ñ[y]our unmarried dependent children temporarily away from home will qualify as primarily residing in the same household as you if they intend to continue to reside in your household.ò The Alabama Supreme Court held that, when a child lives ñfor the most partò with one parent, the child cannot live ñprimarilyò with the other parent as well. *See State Farm Mut. Auto. Ins. Co. v. Harris*, 882 So. 2d 849 (Ala. 2003). The Northern District concluded that Alabama law does not allow a child to have more than one primary residence. Since the testimony from the father indicated that the son lived a greater amount of time with him instead of the mother, the court concluded that the son failed to prove that coverage existed and granted the insurerôs motion for summary judgment.

Negligence/Wantonness
Smith v. State Farm Fire & Cas. Co., 2016 WL 3144082 (N.D. Ala. June 6, 2016).

Facts: The insured submitted a claim to her property insurer to make repairs to her home after it suffered damage. The insurer allegedly agreed to pay for the repairs, and the insurer agreed to the amount the insuredôs contractor estimated it would cost to repair the damage. After the repairs were made, the insurer allegedly refused to pay for the repairs. The insured and the contractor filed a breach-of-contract, bad-faith, negligence, and wantonness action against the insurer. The insurer moved to dismiss the negligence and wantonness claims.

Issue: ***(1) Whether an insured can maintain a negligence or wanton claims handling claim against her insurer.***
(2) Whether a third-party contractor can maintain a negligence or wantonness claim against an insurer.

Holding: (1) No. The insured conceded that Alabama law does not permit an action against an insurer for negligent or wanton handling of insurance claims, and agreed that her negligence and wantonness claims were due to be dismissed.

(2) Yes. The federal court for the Northern District of Alabama held that Alabamaôs rule that an insured cannot sue her insurer for negligent or wanton claim handling did not mean that an insurer can never be sued for negligence

or wantonness. The court held that Alabama law permits negligence and wantonness actions when ña person volunteers to act on behalf of another,ò including when insurance agents and insurance companies volunteer to act. *See Palomar Ins. Corp. v. Guthrie*, 583 So. 2d 1304 (Ala. 1991). In this case, the insured and contractor alleged that the insurer promised to pay the contractor for the repairs it made. Accordingly, the court found that the contractor had sufficiently pleaded a claim recognized under Alabama law against the insurer for the assumption and breach of the duty to pay the contractor. Therefore, the federal court denied the insurerôs motion to dismiss the contractorôs claims.

Material Misrepresentations, Duties of a Mortgageholder, and Expert Testimony
American Safety Indem. Co. v. Fairfield Shopping Ctr., LLC, 2016 WL 3878496 (N.D. Ala. July 18, 2016).

Facts: In September 2006, Fairfield Shopping Center, LLC (ñFairfieldò) bought a shopping center with $3.52 million it borrowed from GE Commercial Property Finance Corporation (ñGEò). Fairfield defaulted on the loan from GE in April 2009 and filed Chapter 11 bankruptcy to avoid foreclosure in May 2009. The last tenant vacated the property in May 2010 and power and water were cut off to the property. In September 2010, American Safety Indemnity Company (ñASIò) issued a commercial property insurance policy on the vacant building. During the application process, Fairfieldôs insurance broker stated that no bankruptcies or liens had been filed against it over the past five years, mortgage and tax payments were up to date, the property had a sprinkler system and alarm, and power and water were turned on. ASI issued a notice of cancellation in December 2010 and became effective in February 2011 after repeated requests to inspect the property were ignored.

During various inspections conducted by GE and after police arrested individuals for stealing copper from HVAC units, it became apparent that the all HVAC units were damaged and the roof was not in good condition. GE filed an insurance claim with ASI, and ASI filed a declaratory judgment action in the United States District Court for the Northern District of Alabama to determine the rights of the parties. ASI moved to exclude testimony of GEôs experts and ASI filed a motion for summary judgment.

Issue: ***(1) Whether the insured's material misrepresentations in the application process voided the insurance policy as to the insured's claims;***
(2) Whether the insured's material misrepresentations in the application process voided the insurance policy <u>as to the mortgagee's claims</u> as a matter of law;
(3) Whether the insurer was entitled to summary judgment on the insured's bad-faith claim.

Holding: (1) Yes. The insurer was entitled to summary judgment based on the insuredôs material misrepresentations. Fairfield represented to the insurer during the application process that it was not involved in bankruptcy and had not defaulted on its mortgage, and that it had power, and an active alarm and fire system. None of this was true. The insurer presented testimony that it would not have issued the policy if it had known this information before issuance. Both California law (where the insurance contract was issued) and Alabama law provide that material misrepresentations made in the application process can void the insurance contract. The court held that, because Fairfield made material misrepresentations upon which the insurer relied in issuing the policy, the policy was void, and the insurer owed no coverage for Fairfieldôs claims.

(2) No. The policy provides that ñ[The insurer] will pay for covered loss of or damage to buildings or structures to each mortgageholder shown in the Declarations. . .. If [the insurer] den[ies] [Fairfieldôs] claim because of [Fairfieldôs] acts or because [Fairfield] ha[s] failed to comply with the terms of this Coverage Part, the mortgageholder will still have the right to receive loss payment. . ..ò The court held that, under Alabama law, the misrepresentations Fairfield made during the application process did not extend to its properly listed mortgageholder, GE, to void coverage for GEôs claims. *See Norwest Mortgage, Inc. v. Nationwide Mut. Fire Ins. Co.*, 718 So. 2d 15 (Ala. 1988). The insurer did not cite any conflicting California law. Moreover, both Alabama and California law provide that ña mortgagorôs actions do not negate a mortgageeôs right to recover under an insurance policy containing a standard mortgage clause.ò

The insurer also argued that GE violated the mortgage clause because it failed to submit a ñsigned, sworn proof of loss within 60 days of receiving notice from [the insurer] of [Fairfieldôs] failure to do soò and failed to notify the insurer ñof any change of ownership, occupancy or substantial change in risk known to the mortgageholder.ò The court disagreed, finding that the insurerôs notice to GE did not clearly explain that Fairfield failed to submit a timely proof of loss. Also, GE did not learn that the property was not secure until two weeks before the policy ended. The policy does not provide a deadline a mortgageholder must abide by to report substantial changes in risk, and the court held that a jury could find the failure to report within two weeks was not unreasonable.

(3) Yes. The insurer provided numerous reasons why it had an arguable or debatable reason to deny coverage to GE. In contrast, GE only argued that the insurer breached the policy terms and so a bad-faith claim should survive summary judgment. The court did not find this argument compelling, and granted summary judgment in favor of the insurer on GEôs bad-faith claim.

"Business Activities" Exclusion – No Duty to Defend and Indemnify

Allstate Indemnity Company v. Berrey, 2016 WL 3906414 (N.D. Ala. July 19, 2016).

Facts: Frederick Berrey, Jr. (ñBerreyò) purchased 470 acres of land in Talladega County, Alabama, developed the property and sold tracts under real estate installment sales contracts to individuals. He created a development within this property called Whispering Pines of Lay Lake. Berrey owns this development individually and through a corporation. Berrey owns all of the roads, drains and ditches on the 470 acres.

Robert Sajnacki (ñSajnackiò) was killed when he was sucked into one of the drains running under a road on the 470 acre property. Sajnackiôs personal representative filed a wrongful death action against Berrey and his corporation in state court. Berreyôs homeownerôs insurer and personal umbrella insurer filed this declaratory judgment action in the United States District Court for the Northern District of Alabama, asking the court to declare that neither insurer had a duty to defend or indemnify Berrey in the underlying lawsuit. Both parties filed summary judgment motions.

Issue: ***(1) Whether the business activities exclusion of the homeowner's policy excluded coverage; therefore, the homeowner's insurer did not owe a duty to defend or indemnify.***

2) Whether the "personal activity" limitation contained in the insuring agreement of the personal umbrella policy and the business activities exclusion contained in the same umbrella policy precluded coverage; therefore, the umbrella insurer did not owe a duty to defend or indemnify.

Holding: (1) Yes. Based on the ñbusiness activitiesò exclusion, the court held that the homeownerôs insurer did not have a duty to defend or indemnify.

The court held that a question of fact existed as to whether the allegations of the underlying complaint met the insuring agreement of the homeownerôs policy. The policy provides coverage to property the insured owns if it is named in the policy or if the property is vacant land, not farmland that is owned by or rented to the insured. The property at issue is not listed in the policy. Although part of the land in question was occupied by an individual who had a real estate installment sales contract, some of the land in question was vacant. Therefore, the court held there was an issue of fact and the insurer could not escape coverage under the terms of the insuring agreement.

However, the court held, as a matter of law, that the ñbusiness activitiesò exclusion precluded both a duty to defend and a duty to indemnify. The homeownerôs policy excluded coverage for ñbodily injury or property damage arising out of the past or present business activities of an insured person.ò ñBusinessò is described as ñany full

or part-time activity of any kind engaged in for economic gain including the use of any part of any premises for such purposesò or ñany property rented or held by for rental by an insured person.ò Although the insured did not expect to gain a profit from the road where Sajnacki was injured, the road provided access to different parcels on the property, and gaining access to the parcels would allow the insured to earn a greater profit than if the road were not present. Therefore, the insured owned the road ñfor economic gain.ò Since Sajnackiôs injury arose out of the insuredôs business activities, the court held that the business exclusion excluded coverage, and the homeownerôs insurer owed neither a duty to defend nor a duty to indemnify.

(2) Yes. The insuring agreement in the umbrella policy only provides coverage if an occurrence arises out of ñpersonal activitiesò of the insured and not ñbusiness activities.ò Moreover, the umbrella policy also contains a ñbusiness activitiesò exclusion similar to that in the homeownerôs policy. Because the court established that the subject injury arose out of business activities, the court also held that umbrella policy does not provide coverage both because the allegations do not meet the insuring agreement and because of the application of the ñbusiness activitiesò exclusion. Therefore, the court held that the umbrella insurer also had no duty to defend or indemnify the insured.