Case Law Developments

By James W. Bryan

As a regular feature of the newsletter, a summary of recent case law developments on insurance coverage is in order. What follows are published cases from state and federal courts in North Carolina in 2013.

CGL Policy - Duty to Defend and Trigger of Coverage. Erie Ins. Exch. v. Builders Mut. Ins. Co., 742 S.E.2d 803 (N.C.App. 2013). This case highlights how the injury-in-fact trigger rule is applied in property damage claims. A general contractor was hired to build a single family residence and completed construction on the home. A certificate of occupancy was issued on September 21, 2007. At the time of completion, the general contractor was insured by plaintiff Erie Insurance under a general liability policy. On December 7, 2009, the altered slope and retaining wall above the residence collapsed, damaging the house and the homeowners' personal property. At the time of the collapse, the general contractor was insured by defendant Builders Mutual. The homeowners brought an action against the general contractor on June 23, 2010. Erie Insurance agreed to defend the general contractor in the action. However, Builders Mutual denied having a duty to defend in the underlying action. Subsequently, plaintiff brought this action seeking a declaratory judgment addressing the rights and obligations of plaintiff and defendant regarding the claims in the underlying action.

The issue was whether defendant Builders Mutual (subsequent insurer) had a duty to defend the insured in the homeowner's claim when defendant was the carrier at risk at the time that the damage occurred, but plaintiff (initial insurer) was on the risk when the defective construction was completed. The North Carolina Court of Appeals held that defendant Builders Mutual did have a duty to defend the insured in the underlying action because the property damage related to a single occurrence that happened while defendant was the carrier at risk. Where the date of the *injury-in-fact* can be known with certainty, the insurance policy or policies on the risk on that date are triggered. The builder and its subcontractors negligently altered the slope and constructed an inadequate retaining wall, and this faulty construction ultimately caused the slope collapse that resulted in the property damage to the Hardisons' property. All property damage alleged in the underlying action relates to the single occurrence of the slope collapse that occurred during defendant's policy period. Thus, since plaintiff Erie Insurance paid $170,000 on behalf of the builder in the settlement of the underlying action, defendant was liable to plaintiff for the amount of the settlement. However, defendant was not liable to plaintiff for defense costs because the complaint did not state an amount as plaintiff's defense costs and plaintiff did not include any supporting allegations addressing the defense costs.

Business Auto Policy – UIM, Arbitration, Extra-Contractual Liability, and Affirmative Defenses. Guessford v. Pennsylvania Nat'l Mut. Cas. Ins. Co., 918 F.Supp.2d 453 (M.D.N.C. 2013). This case is a textbook example of the difficulty predicting the outcome of summary judgment motions in bad faith/coverage actions. Penn National issued an automobile liability policy to Waggoner Manufacturing, the employer of plaintiff Mr. Guessford, with UIM limits of $1,000,000. In July 2007, tortfeasor Ms. Coriher negligently drove her car, causing a collision with Guessford's motor vehicle and personal injuries to Guessford. Guessford received workers' comp benefits from his employer's workers' comp carrier. Coriher's insurer Nationwide tendered its policy limits of $100,000 to Guessford. Guessford did not discover the policy issued by Penn National until March 2009. Penn National declined to advance Nationwide's tender and instead waived its subrogation rights against Coriher. Guessford demanded arbitration under the UIM policy and also filed suit against Ms. Coriher to toll the statute of limitations. By November 2009, Penn National was aware that Guessford's accident-related medical expenses totaled $590,620, and by September 2010, Penn National was aware that the amount had increased to $727,753. On January 12, 2011, days before the arbitration, Penn National offered $525,000 to settle. The arbitration panel awarded $2.5 mil., and Penn National tendered payment of $900,000 conditioned upon a release. Guessford sued Penn National for breach of contract and extra-contractual liability.

One issue before the Court was whether Penn National breached the policy by not investigating Guessford's claim and not making any reasonable settlement offer despite having sufficient information to formulate a reasonable offer, thereby forcing Guessford to demand arbitration. The District Court held that Guessford failed to allege sufficient facts showing a breach of the policy. There is no provision in the UIM policy requiring Penn National to make a settlement offer to its insured prior to arbitration. The policy specifies that in the event of a dispute regarding value, Guessford may choose to institute arbitration proceedings, or else Penn National's liability will be determined "only in an action against [Penn National]." After ongoing correspondence with Penn National failed to produce a settlement offer, Guessford chose to initiate arbitration, the very procedure provided under the contract in the event of a disagreement over the value of a claim. Penn National complied with these same procedures and upon the issuance of the arbitration decision, the insurer promptly sent Guessford a check for $900,000, the full liability limits under the policy.

Another issue was whether Penn National's motion for summary judgment on the unfair and deceptive trade practice claim, bad faith claim and punitive damages should be denied due to genuine issues of material fact. The District Court found that yes, Guessford pled sufficient facts to plausibly state a UDTPA claim, bad faith refusal to settle claim and grounds for punitive damages. *First*, evidence was presented that Penn National misrepresented pertinent insurance policy provisions and the law governing those provisions when the insurer informed Guessford that a voluntary mediation could be set only "if the Worker's Compensation carrier was in agreement and in

a position to resolve their lien." The policy had no such requirement. *Second*, evidence was presented that Penn National failed to provide a reasonable explanation of the basis for a compromise settlement offer when the insurer provided no information to explain its lone settlement offer of $525,000 prior to arbitration. *Third*, evidence was presented that the insurer attempted to settle Guessford's claim for less than the amount which a reasonable person would have believed he was entitled by offering $525,000, despite having timely information that Guessford's medical expenses exceeded the amount being offered by Penn National. The court also found evidence sufficient for five other unfair claim settlement practices by Penn National: failure to respond to multiple communications and requests for settlement offers, failure to adopt and implement reasonable standards for the investigation of claims, failure to conduct a reasonable investigation of Guessford's claims, failure to attempt in good faith to effectuate a prompt settlement, and forcing Guessford to initiate arbitration and litigation proceedings by failing to make a settlement offer despite having sufficient information.

The District Court ruled on a number of affirmative defenses pled by Penn National. With respect to the UDTPA and bad faith claims, the District Court held (a) that Penn National may not assert "arbitration and award" as a defense because neither claim is subject to arbitration; (b) that Penn National may not assert "unclean hands" as a defense because these claims do not seek an equitable remedy; (c) that Penn National may assert "failure to mitigate damages" as a defense in an effort to reduce any potential damage award; (d) that Penn National may assert "reliance on the advice of counsel" as a defense to the bad faith claim to show that it acted in good faith and for the jury to assess the reasonableness of Penn National's conduct in regard to punitive damages; and (e) that Penn National may not assert "reliance on the advice of counsel" as a defense to the UDTPA claim because good faith is not a defense to a claim for unfair or deceptive trade practices.

Personal Auto Policy – Release. N.C. Farm Bureau Mut. Ins. Co. v. Smith, 743 S.E.2d 647 (N.C.App. 2013). This case illustrates the need to know who are the tortfeasor's insurers before settling the claim. The Savage family sustained injuries in an automobile collision that was caused by the tortfeasor driver of the other vehicle. The Savages entered into settlement agreements with the tortfeasor and his auto insurance provider, Allstate. The agreements provided a sum of money to the Savages in exchange for a covenant not to execute any judgment against the tortfeasor relating to that accident. Plaintiff Farm Bureau, insurer of the tortfeasor's father, brought a declaratory judgment action to establish that it was not be liable in connection with the accident. The trial court granted Farm Bureau's motion for summary judgment and the Savages appealed from that order. The issue was, did the trial court err in determining that the Savage's settlement agreements with the tortfeasor and his insurer Allstate preclude Farm Bureau's liability on any claim brought by the Savages relating to that accident. The Court of Appeals found no error and held that plaintiff Farm Bureau could not be held liable to the Savages. The settlement agreements shielded the tortfeasor from additional liability relating to the accident. The Court stated that an insurance carrier's liability is "derivative in nature" and, therefore, if the Savages had forfeited the right to collect damages from the tortfeasor insured, they also forfeited the right to collect damages from Farm Bureau, as an insurer of the tortfeasor. When an insurer's obligation under a policy is to pay "all sums which [the] insured shall become *legally obligated to pay* " and when the insured under that policy is given a release by the injured parties of the nature set forth in the Covenants, i.e., where the parties covenant that no judgment shall be executed against the insured, the insurer's "obligations under the policy [are] extinguished by the execution of the [covenant]." The Court found no meaningful distinction between the phrase "legally obligated to pay" found in the policy at issue in other case law and the phrase "legally responsible" found in the policy at issue in the case *sub judice*.

Personal Auto Policy - Reasonable Belief Exclusion. Integon Nat'l Ins. Co. v. Villafranco, 745 S.E.2d 922 (N.C.App. 2013). This case focuses on when the exception to the reasonable belief exclusion applies to save coverage. Plaintiff Integon issued an auto insurance policy to defendant insured Ms. Villafranco to cover her 1998 Buick automobile. Ms. Villafranco's fourteen-year-old son Ramses Vargas was driving the covered vehicle when he lost control and overturned the vehicle, injuring four passengers in the vehicle. Integon brought the declaratory judgment action seeking a declaration that it was not liable for the defense or indemnification of Vargas and Villafranco for the claims arising from the accident. The trial court granted summary judgment in favor of the passengers, finding that the policy did provide coverage for their personal injury claims arising from the action. Integon appealed arguing that coverage was barred by an exclusion to coverage for an insured "using a vehicle without a reasonable belief that insured is entitled to do so," despite the exclusion then stating that the exclusion "does not apply to a family member" of the insured vehicle owner. The trial court ruled against Integon on all issues. On appeal, the issue was whether the trial court erred in finding that the personal injury claims arising from the accident were covered because the fourteen-year-old driver Vargas was an insured under the policy and the "reasonable belief" exclusion did not apply. The Court of Appeals found no error and held that the fourteen-year-old son of Ms. Villafranco was an "insured" under the policy and that the "reasonable belief" exclusion did not apply. The son lived in the household with Villafranco, was a family member and fit the definition of an insured. The court found the policy contained a clear and unambiguous exception to the "reasonable belief" exclusion for family members of the insured vehicle owner. By including the family member exception to the reasonable belief exclusion, Integon explicitly extended coverage to family members using the covered vehicle even when they do not have a reasonable belief that they were entitled to use the covered motor vehicle. Therefore, the policy covered the personal injury claims arising from the accident.

Personal Auto Policy – UIM and Material Misrepresentation. James v. Integon Nat'l Ins. Co., 744 S.E.2d 491 (N.C.App. 2013). This case presents a basic issue about the material misrepresentation defense pled by an insurer – does it require proof of *scienter.* Plaintiff was injured in an automobile accident while driving a vehicle, owned by his fiancé and insured by defendant Integon. The policy included $50,000 in Underinsured Motorist ("UIM") coverage. Plaintiff filed a UIM claim with defendant, under his fiancé's policy, after the liability coverage on the vehicle of the tortfeasor was exhausted. Defen-

dant denied plaintiff's claim because his fiancé had allegedly made a material misrepresentation in her policy application, which barred plaintiff from coverage under her policy. The Plaintiff lived in the household at the time of the application but was not listed on the application as a driver. Plaintiff brought an action seeking a declaration that he was covered by the policy. The trial court granted Plaintiff's motion for summary judgment because defendant had not provided evidence of scienter to establish the affirmative defense of fraud. Defendant appealed arguing that it was not raising the affirmative defense of fraud but was raising the affirmative defense of material misrepresentation, which did not require proof of *scienter.*

On appeal, the issue was whether material misrepresentation, which does not include a scienter element, is a valid affirmative defense to liability for UIM coverage in excess of the statutory minimum. The Court of Appeals held that a material misrepresentation on a policy application was a valid affirmative defense to UIM liability in excess of the statutory minimum. Pursuant to N.C. Gen. Stat. 20-279.21(f)(1), insurance required by the Financial Responsibility Act "shall become absolute whenever injury or damage covered by said motor vehicle liability policy occurs," and "no statement made by the insured ... and no violation of said policy shall defeat or void said policy." However, pursuant to paragraph (g) of the same UIM statute, N.C. Gen. Stat. 20-279.21(g), automobile liability coverage in excess of the statutorily required minimum is not subject to the Financial Responsibility Act. Thus, the Court held that the defense of material misrepresentation is an acceptable affirmative defense to such coverage. The court reversed the trial court's order granting summary judgment for plaintiff, and found issues of fact existed for trial as to whether a material misrepresentation had been made on the insurance application.

Personal Auto Policy – UIM and Stacking. Lunsford v. Mills, 747 S.E.2d 390 (N.C.App. 2013). This case emphasizes the liberal interpretation of the Financial Responsibility Act when it comes to UIM coverage and stacking. Two motor vehicle accidents occurred on Interstate 40 in McDowell County on September 18, 2009. The first accident occurred when defendant Mills, employee of defendant Crowder, crashed his tractor trailer in a single-vehicle accident. Plaintiff Lunsford, a volunteer firefighter, was carrying Mills away from the wreckage when the second accident occurred. Defendant Buchanan lost control of his vehicle because of the stopped traffic and ran into Lunsford, injuring him severely. Mills and Crowder had a $1.0 mil. liability policy with U.S. Fire, Buchanan had a $50,000 liability policy with Allstate, and Lunsford had UIM coverage under two policies with Farm Bureau—a $300,000 business auto policy and a $100,000 personal auto policy. Lunsford sued Mills, Crowder and Buchanan. As UIM insurer, Farm Bureau filed an answer as an unnamed defendant. Allstate tendered its $50,000 policy limit to settle. Lunsford notified Farm Bureau of the tender and demanded Farm Bureau to tender payment for the UIM claim. Farm Bureau declined. Lunsford later settled his claim against Mills and Crowder for $850,000 with the U.S. Fire policy. Farm Bureau sought a judicial declaration that Lunsford was not entitled to UIM coverage from Farm Bureau because the aggregate amount of his settlements—$900,000.00—exceeded the aggregate amount of the UIM coverage—$400,000.00. The trial court held that the policy limits under Lunsford's Farm Bureau policies stack and that he was entitled to judgment against Farm Bureau in the amount of $350,000.00, which represented his aggregate UIM coverage *minus* the $50,000.00 that he had received pursuant to his settlement with Buchanan.

The issue on appeal was whether the trial court erred in entering summary judgment in favor of Lunsford in the amount of $350,000. The Court of Appeals found no error. Farm Bureau was obligated to provide UIM coverage to Lunsford once Allstate had tendered its policy limits to Lunsford on behalf of Buchanan, and Farm Bureau was not entitled to withhold coverage until Lunsford had recovered (or attempted to recover) under the liability policies insuring the tractor trailer driven by Mills. Under the Financial Responsibility Act, N.C. Gen. Sta. 20-279.21(b)(4) provides that: "Underinsured motorist coverage is deemed to apply when, by reason of payment of judgment or settlement, all liability bonds or insurance policies providing coverage for bodily injury caused by the ownership, maintenance, or use of *the underinsured highway vehicle* have been exhausted." The court concluded that UIM coverage is triggered the moment that an insured has recovered under all policies applicable to "a"—meaning one—"underinsured highway vehicle" involved in a motor vehicle accident resulting in injury to the insured. The court saw no reason why insureds such as Plaintiff should be kept hanging in limbo as they are forced to sue any and all possible persons before they could recover UIM benefits just because other potential tortfeasors also happen to be covered under automobile policies. Had Farm Bureau tendered its policy limits in response to notice of Allstate's tender, Farm Bureau would have had the opportunity to seek an offset through reimbursement or exercise of subrogation rights.

Public Officials Liability Policy - Waiver of Sovereign Immunity Through Purchase of Insurance. White v. Cochran et al, 748 S.E.2d 334 (N.C.App. 2013). This case is a good example of how an action against a public official may fare against the sovereign immunity defense—when there is insurance coverage. On October 9, 2009, the Sheriff of Swain County was sued by a detention officer Ms. White for retaliatory termination and wrongful discharge. The suit was after the N.C. Dept. of Labor had denied the officer's claim for wrongful termination after seeking workers compensation benefits. She was terminated in March 2009. The Dept. of Labor notified the Sheriff of the complaint on June 5, 2009. The Sheriff pled in his answer the defense of governmental immunity. Public officials employed by Swain County were covered by a claims-made policy issued by Argonaut for July 1, 2008 to July 1, 2009, and coverage was also provided by an occurrence-based policy by the N.C. Assn of County Commissioners Risk Management Pools for July 1, 2009 to July 1, 2010. The trial court denied the Sheriff's motion for summary judgment in part because the Sheriff had waived sovereign immunity through the purchase of liability insurance.

On appeal, the issue was whether the trial court erred in denying the Sheriff's motion for summary judgment on the ground that the Sheriff had waived sovereign immunity through the purchase of liability insurance. The Court of Appeals found no error and noted that waiver of a sheriff's official immunity may be shown by the existence of his official bond as well as by his county's purchase of liability insurance. Under the Argonaut policy, a claim arising

from a "wrongful act" has been asserted in a timely manner "if a claim for 'damages' is first made in writing against any insured during the policy period or any Extended Reporting Period," with "[a] claim by a person or organization seeking 'damages' deemed to have been made when written notice of such claim is received by any insured or by [Argonaut], whichever comes first." The court held that because the Sheriff and other county officials had received written notice of both the existence and nature of Ms. White's claim before the end of June 2009, the Sheriff received notice of the claim in a form consistent with that required by the applicable policy language before the Argonaut policy expired. Nothing in the policy language indicates that the required notice must take the form of the initiation of a civil action as contended by the Sheriff. The Sheriff also argued the applicability of the policy provision excluding "[Equal Employment Opportunity Commission] hearings or similar proceedings conducted by state agencies or commissioners" under the Argonaut policy. But the Sheriff did not offer any support for the contention that Ms. White's retaliatory discharge claim is either an EEOC claim or a similar state proceeding.

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