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RECENT DEVELOPMENTS IN INSURER'S LIABILITY

JOHN C. TINDEL*

I. INTRODUCTION

Although the writing and interpretation of insurance policies and the delineation of the respective rights and duties of insurers and their insureds have been dealt with for many decades by insurance companies, state regulatory bodies and the courts, the never-ending occurrence of novel and unforeseen fact situations continues to produce new litigation and new problems of interpretation for the courts. Recently several significant decisions dealing with such problems have been handed down by the Missouri courts, which should be noted by Missouri attorneys.

II. LIABILITY INSURANCE

A. *Insured's Duty to Cooperate*

Should plaintiff's counsel in a personal injury case consider it a part of his duties to be sure that the defendant appears at court? Perhaps so if he wants to be sure that he collects his judgment from defendant's liability insurer. The insuring company defended a garnishment action in *Lenhart v. Rich*¹ on the basis of the failure of the insured to appear at the trial. The company had written to him, he had been furnished money for bus fare, and had been called just before the trial, but he did not appear. The court held that the insured had breached his duty to cooperate with the insurer under the provisions of the policy, and therefore the company was absolutely relieved of any liability on the policy and was justified in refusing to defend the personal injury suit.

A somewhat unusual situation was presented to the court in *Farmers Mut. Auto. Ins. Co. v. Drane*,² where the claimant, Terry Gene Drane, was able to solve his problem by virtue of the enactment of a statute introduced with his situation in mind. Terry was injured in 1957 by a

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1. 384 S.W.2d 812 (K.C. Mo. App. 1964).

2. 383 S.W.2d 714 (Mo. 1964).

fall from a farm truck. The insured defendant had two liability policies. MFA wrote an automobile liability policy that included the defendant's truck; Farmers Mutual wrote a farm public and employee liability policy also covering the defendant. Farmers Mutual concluded that defenses under the terms of its policy were available and refused to pay, but defended the personal injury suit under a non-waiver agreement.

While that suit was pending, Section 537.065, RSMo, providing that an injured person and the tort-feasor or his insurer may contract to limit recovery to specified assets or insurance, became law on August 29, 1959. Terry's attorney stated to the appellate court in oral argument that the bill had been introduced because of the situation presented by Terry's injury.³

An agreement under the terms of the statute was entered into between the insured defendant, MFA and the Dranes by which MFA paid \$11,000 and the Dranes, Terry and his parents, agreed not to levy execution against the insured defendant or his truck driver or MFA, but specifically retained the right to bring a garnishment action against Farmers Mutual.

Farmers Mutual then brought the present declaratory judgment suit asking for a declaration of its nonliability due to the agreement entered into by its insured. Three arguments were asserted: (1) that the agreement constituted a complete bar to the claimant's personal injury action; (2) that because the agreement relieved the insured defendant of any legal obligation to pay damages, Farmers Mutual had no liability due to the policy limitation to "sums which the insured shall become legally obligated to pay as damages"; and (3) that by signing the agreement the insured had breached the cooperation clause of the policy.

The first of these contentions was rejected by the court on the basis of the statute itself. The second was rejected on the familiar principle that liability policies are not indemnity policies, and no *actual* payment by the insured is necessary. His legal obligation (and hence, that of Farmers Mutual) was fixed at the time of the casualty. As to the cooperation clause, the court found no breach, but admitted that the agreement would be a damaging admission of liability by the insured if it should be introduced into evidence by Farmers Mutual in the personal injury action to reduce damages awarded to the Dranes. The way to avoid this, the court

3. *Id.* at 718.

stated, is for the payment made with the agreement, \$11,000 in this case, to be considered separately in subsequent proceedings to enforce the insurer's liability as a partial satisfaction of any recovery obtained by the Dranes in the personal injury suit. Thus, if the jury awards the claimant a sum in excess of the payment, say \$15,000, a credit of the amount of payment, \$11,000, would be allowed in subsequent garnishment proceedings against Farmers Mutual, leaving the balance to be paid by the insurer. With this approval by the court, the new statute should provide a convenient and safe method for future claimants to settle with less than all liability insurers covering the same insured on the same accident without waiving or releasing their rights against those insurers who choose not to settle.

B. Insurer's Duties to Defend and to Settle Within Policy Limits

Cases allowing a judgment in excess of policy limits against liability insurers because of a bad faith refusal to settle within policy limits sometimes occur, as do those involving refusal of the company to defend because of an asserted lack of coverage. What happens when these two problems are combined in the same case as they were in *Landie v. Century Indem. Co.*?⁴

The situation was this: The named insured loaned a truck insured by Century to Landie. Landie had an accident with it. Redman, the injured party, made a claim which Century refused to defend, claiming that the truck was not loaned and that Landie was using it without permission. Landie proceeded to defend himself, and before trial communicated to Century an offer to settle within the policy limits. Without making any new investigation, Century refused, solely on the basis of the coverage question. Redman took judgment against Landie for \$22,500 and brought garnishment action against the company for \$15,000, the policy limit. The company asserted the coverage question as a defense to the garnishment and a jury returned a verdict against the company for \$15,000.

At this point it is clear that the company is liable for the policy limits and for the insured's cost of defending the suit. No question of

4. 390 S.W.2d 558 (K.C. Mo. App. 1965). This was a suit by the insured for the amount in excess of the policy limits which the insured had paid to the claimant under the damage suit judgment, this action being subsequent to the claimant's garnishment against Century in which the policy coverage questions were determined against Century.

good or bad faith of the company in refusing to defend on the ground of lack of coverage is involved. A company chooses not to defend at its peril, and after the adverse decision of the question of coverage, is liable for damages awarded against its insured up to the policy limits plus the insured's cost of defending.

It is well settled in Missouri that if the company is defending and refuses to settle within the policy limits in bad faith, it is liable for a judgment rendered against the insured in excess of the policy limits. However, if the company in good faith believes it has a valid defense, it is not liable beyond the policy limits for an honest mistake in refusing to settle within policy limits. What then if the company's refusal to settle is based on a question of *coverage*?

The court in *Landie* was able to find only one reported case precisely in point, *Comunale v. Traders & Gen. Ins. Co.*⁵ The *Comunale* opinion contained a rather sketchy examination of this problem. Nevertheless, the court in *Landie* relied on *Comunale* in holding the insurer liable in the present case beyond the policy limits due to its refusal to settle within policy limits. The court reasoned that if no question of coverage had existed and the insurer had defended the damage suit, it would have had the duty to investigate the merits of the claim and the defenses and to make reasonable settlements within policy limits for the protection of its insured, unless it believed in good faith that the claim was defensible on the merits. Since Century refused to defend on the ground of lack of coverage, it refused to settle *solely on that ground* without investigation of or regard for the merits of the claim.

The issue of coverage having been subsequently decided against Century, its refusal to defend was a breach of its duty for which the insured was entitled to be made whole in damages. The insured would not be made whole here if Century's liability were restricted to the policy limits plus the cost of defense, when Century, had it discharged its duty to defend, would have been liable beyond the policy limits for bad faith refusal to settle within the policy limits. The jury had determined on sufficient evidence that Century's refusal to settle without investigation of the merits of the claim was in bad faith. Consequently, the court held compensatory damages in this case include the full amount of the recovery against the insured and his costs.

5. 50 Cal.2d 654, 328 P.2d 198 (1958). The case is also reported in 68 A.L.R. 2883 (1958) but the annotation is on a different question.

The company was convinced that Landie was not covered when the offer of settlement within the policy limits was made. The company may have believed that the offer was reasonable if they were liable for anything, but their view was that they were not. What to do? The court pointed out that declaratory judgment route was open to the company to determine whether or not Landie was covered. Does this mean that a liability insurer *must* litigate all coverage questions in cases where there is a possibility of a judgment in excess of policy limits? It is likely that at the time the settlement offer was made an offer by the company to litigate the coverage issue would not have been acceptable to the claimant because of the delay involved. The only completely safe procedure for the company would have been the declaratory judgment action as soon as it appeared that there was a possibility of an excess verdict.

III. PROPERTY INSURANCE

A. *Insurer's Liability to Transferee of Insured Property*

What are the rights of a purchaser of property by sale on contract for deed against the insurer of the property under a policy issued in the name of the seller prior to the sale? Although certain teachers of real property law insist that it is fraught with danger, there are still a great many real estate transactions which take the form of a sale on contract for deed. Generally the procedure works satisfactorily, and if it does not, the value of the property is often so low that no reported litigation results. The objection usually voiced to use of contracts for deed is the uncertainty involved due to the lack of principles worked out by the courts.

One small point relating to this problem has now been settled by the decision in *Miller v. National Union Fire Ins. Co.*⁶ *S* sold to *M* on contract for deed. *S*'s insurance with National was retained in *S*'s name, and an additional policy with another company was written with *M* as named insured and *S* appearing on a standard mortgage clause.

After a total loss, the second company paid the face amount of the \$8,000 policy it had written proportionately to *S* and *M* under the mortgage clause. On demand National refused to pay under the \$10,000 policy it had written although the value of the property was in excess of \$18,000. Since *S* refused to sue National for *M*'s benefit, *M* brought the present suit for declaratory judgment against both National and *S*.

6. 386 S.W.2d 668 (K.C. Mo. App. 1964).

National's argument that *M* acquired no interest in the policy because he was not named therein was rejected by the court on the basis of earlier cases. Legal title did not pass from *S*, the named insured, to *M* under this arrangement, so the policy did not require any notice to National of the transaction. In fact *M* had remitted the premiums to *S* who in turn paid them to National. Thus *M* was entitled to sue to get the benefit of the insurance for which *M* paid; otherwise, National would receive a windfall.

National then contended that in any event its liability should be limited to the proportionate amount its policy limit bore to the total insurance coverage of *S*'s mortgagee's interest, or \$4,187.50. The court rejected this argument as improper in a case of total loss where the value of the insured property exceeds the aggregate amount of insurance, as it did here. Thus this insurance arrangement (contract seller as named insured) has court approval. It is worth pointing out that most companies provide a contract clause for this arrangement.

The court affirmed the trial court's judgment, which included the sum of \$1,000 "accrued interest." It appears that the petition prayed for penalties and attorneys' fees, but the opinion does not reveal whether this request was allowed or not. It would appear that this might have been a proper case for allowance of the statutory penalty for vexatious refusal to pay the loss.⁷ Since the \$1,000 allowance for "accrued interest" was ten per cent of the face amount of the policy, the amount of the statutory penalty, it may have represented the penalty.

B. *Insurer's Defense of Cancellation by Insured*

The courts had an opportunity to consider the problem of cancellation by the insured in two cases which presented almost opposite approaches to the problem. In *Vaughn v. Great American Ins. Co.*⁸ the insured brought the policy into the office of the insurer's local agent who had issued it and asked to have it cancelled. The next day the insured property burned. Although the insured argued that there had been no effective cancellation, the court found that he had brought the policy to an end by bringing it in and requesting cancellation, although the insurer had not returned unearned premiums by the time the loss occurred. Once the insured had unequivocally requested cancellation and surrendered the policy to the

7. § 375.420, RSMo 1959.

8. 390 S.W.2d 622 (Spr. Mo. App. 1965).

agent, the insured had done all he had to do, and the insurer was obligated to complete the cancellation. Consequently the policy was effectively cancelled at that point.

The argument made by the insured, that he alone could not procure an effective cancellation because the policy was issued in the names of himself and his wife, was a novel question, evidently never having been ruled on before. The court found that the evidence was sufficient to give the husband apparent authority to cancel as his wife's agent, even though she did not join in the request to cancel.

The doctrine of cancellation by substitution was advanced in *MFA Mut. Ins. Co. v. Southwest Baptist College, Inc.*⁹ The new college administration adopted a new insurance program, cancelling all old policies and obtaining new ones on all college property. A policy with MFA for \$2,000 was found and cancelled, but an MFA policy on old Pike Auditorium in the amount of \$42,500 of which the new administration had no knowledge went unlocated and uncanceled. Pike burned, and the college first learned of this policy when the MFA agent called to ask about having the adjusters visit the property.

The new policies were paid in full for a total of \$55,000. When MFA learned of the situation, the premium paid was tendered and refused. MFA then asked for declaratory judgment. MFA argued that the doctrine of cancellation by substitution should be adopted in Missouri, as found in some other states.

The court refused to decide whether or not the doctrine would be adopted in Missouri, since this case could be decided without reaching that question. The doctrine requires that notice of the replacement be communicated to the insurer, and no such communication was found here. "A mere intention on the part of the insured, not communicated to the insurer, is not sufficient to effect a cancellation by the insured, under this doctrine."¹⁰

Obviously, the college received a windfall. MFA asserted that public policy should intervene to prevent this. The court did not agree, and found that public policy in this area, expressed in the valued policy law, was to the contrary.¹¹

While this was a case of first impression, it offers little guidance on

9. 381 S.W.2d 797 (Mo. 1964).

10. *Id.* at 802.

11. §§ 379.140, .145, RSMo 1959.

the question of cancellation by substitution because of the limitation of the decision. It is still not known whether or not Missouri follows the doctrine of cancellation by substitution. The case does hold that there is no inadvertent cancellation by obtaining new insurance when the existence of a present policy is unknown.

IV. PROBLEMS IN INTERPRETING POLICY PROVISIONS

Several cases involving interpretation of policy provisions and exclusions reached the courts, in spite of the company lawyers' efforts to draft policies so as to avoid litigation. Some presented questions never before considered in this state.

A. *Exclusion of Liability for Intentionally Inflicted Injuries*

One particularly interesting case¹² involved neighbors, Crull and Gleb, who got into a dispute, as neighbors sometimes do. One day Crull was dumping debris in a drainage ditch to change its flow, and Gleb saw him. Gleb then got in his pickup truck and drove down the road toward Crull, who was by then in his car and backing down the road away from Gleb. This effort was not successful and Gleb struck Crull's car head-on, and then hit it head-on three more times within a distance of 150 to 200 feet, hard enough to bend the frame of Crull's car.

Crull, suspecting that the incident was not purely accidental, filed suit against Gleb alleging that the acts mentioned were done by the defendant deliberately and purposely. Gleb's liability insurer took the position that the policy provision excluding injury caused intentionally by the insured relieved the company of any liability.

The possibility of losing the deep pocket of the insurer resulted in plaintiff's filing an amended petition. This petition was in two counts. Count one charged defendant with ordinary negligence, and count two charged that defendant's acts were reckless or wanton. Plaintiff prayed for both actual and punitive damages. The jury returned a verdict for plaintiff for \$1,500 actual and \$2,000 punitive damages. The insurer resisted garnishment on the ground that Gleb's acts were intentional and therefore not covered by the policy.

The court, holding the insurer liable, found a "subtle difference"¹³

12. Crull v. Gleb, 382 S.W.2d 17 (St. L. Mo. App. 1964).

13. *Id.*, at 21.

between intentional acts and wanton and reckless acts. Wanton and reckless acts are those done intentionally without regard for the consequences. There is a conscious intent to do the act, knowing it is wrong, but no conscious intent to inflict or cause the harm that followed.¹⁴ This approach will limit the use of the intentional act exclusion rather strictly, since the company will be forced to show that the insured had a conscious intent *to inflict the harm that followed* from his acts, and the parties in the best position to know, the insured and the claimant, will both be interested in coming within the coverage of the policy.

The company fared better on the question of punitive damages. The court, holding the insurer not liable for the punitive damages recovered by Crull, found that there is a public policy against allowing the sting of punitive damages to be shifted from the wrongdoer to his insurer and that the insurer could not indemnify the insured for this category of damages even if it contracted to do so.

B. *Provision for Uninsured Motorist Coverage*

In two recent cases the courts dealt another blow to the requirement of arbitration of differences between the insured and the company in uninsured motorist coverage provisions. The court in *State ex rel. State Farm Mut. Auto. Ins. Co. v. Craig*¹⁵ held that such arbitration provisions could not require arbitration as a prerequisite to filing suit. The same result was reached in *Hill v. Seaboard Fire & Marine Ins. Co.*¹⁶ It appears that such policy provisions are a dead letter in Missouri in view of these decisions and the Missouri statute providing that no arbitration clause in any contract shall preclude suit on the contract *at any time*.¹⁷

What does the insured who is making a claim under an uninsured motorist provision have to show as to lack of insurance of the other driver in order to collect?

In the *Hill* case the insured showed that the company adjusters had made an effort to find any insurance coverage of the other driver, but the search was unavailing. The company learned that the other driver had been insured but the policy was cancelled before the accident. The insured's husband also inquired and was informed that the policy was

14. *Ibid.*

15. 364 S.W.2d 343 (Spr. Mo. App. 1963).

16. 374 S.W.2d 606 (K.C. Mo. App. 1963).

17. § 435.010, RSMo 1959.

cancelled. The other driver did not testify. The court held that the insured had carried the burden of proof on this point.

In the case of a hit-and-run accident, the policy provision involved in *Basore v. Allstate Ins. Co.*¹⁸ contained a specific coverage, setting out certain steps to be followed by the injured insured. Although he had not strictly complied, the court found that the injured insured and her husband had cooperated fully with the company and that the company had waived strict compliance.

Uninsured motorist coverage still remains a relatively untested field in this state. Evidently the situation has not yet arisen in which the insured sues the uninsured motorist, and then the motorist files a counterclaim. In effect, the company is then on both sides of the case.

C. *Miscellaneous Provisions and Exclusions*

Questions of policy coverage were raised in several cases which may be briefly summarized:

1. If a hospitalization was initially caused by a condition excluded from a hospitalization policy, but during the hospitalization another unrelated condition arose which was covered and both conditions were treated, can the company allocate a portion of the hospital expenses to the excluded condition and pay only the remainder? Answer: no.¹⁹

2. A collision policy covered an automobile lessor and lessee. Lessee had an option to buy the car at any time. By agreement with the lessor, lessee surrendered possession of the car to his aunt, who bought it from lessor and paid for it, but who wrecked it before receiving the certificate of title and before any change had been made in the collision coverage. The lessee-nephew sued the insurer under the existing policy. Must the insurer pay? Answer: no. The court found that the lessee had no insurable interest.²⁰

3. If an insured enters a bar with a gun and threatens people so that the bartender, to protect himself and others, strikes him, and he falls fracturing his skull thereby causing death, has he met an accidental death? Answer: no.²¹

18. 374 S.W.2d 626 (K.C. Mo. App. 1963).

19. *North Kansas City Hosp. v. Wiley*, 385 S.W.2d 218 (K.C. Mo. App. 1964).

20. *Galati v. New Amsterdam Cas. Co.*, 381 S.W.2d 5 (St. L. Mo. App. 1964).

21. *Di Paoli v. Prudential Ins. Co.*, 384 S.W.2d 861 (St. L. Mo. App. 1964).

4. Will a bank's insurance, indemnifying *the bank* against loss of *its* property by robbery, also cover a robbery loss suffered by *a customer* in the bank's parking lot on the theory that the customer is a third-party beneficiary of the policy? Answer: yes.²²

5. Does a homeowner's policy, covering loss by "mysterious disappearance," cover loss of a necklace where there is no evidence of theft? Answer: yes. This case carefully distinguishes types of mysterious disappearance provisions, a provision on which there were no Missouri cases.²³

V. CONCLUSION

It seems that in the more recent cases the courts have not limited their decisions quite so strictly to the particular facts in the case before them as had been their tendency in the past.²⁴ This is a desirable trend, because insurance decisions are carefully studied by those directly concerned with this area of the law; the courts should write with this wider audience, as well as those before the bench, in mind.

22. *Brugione v. Maryland Cas. Co.*, 382 S.W.2d 707 (Mo. 1964).

23. *Hammontree v. Central Mut. Ins. Co.*, 385 S.W.2d 661 (Spr. Mo. App. 1965).

24. See Tindel, *Insurance*, 28 Mo. L. REV. 549, 553 (1963).