

# ALFA INTERNATIONAL

THE GLOBAL LEGAL NETWORK



**Thomas W. Brown**  
Cosgrave Vergeer Kester LLP  
Portland, Oregon  
(503) 219-3806  
tbrown@cosgravelaw.com



**Robert L. Hebb**  
Co-Chair, Property &  
Casualty Subgroup  
Semmes, Bowen & Semmes  
Baltimore, Maryland  
(410) 576-4862  
RHebb@semmes.com



**James N. Hurley**  
Fowler White Burnett, P.A.  
Miami, Florida  
(305) 789-9218  
jnh@fowler-white.com



**James H. Johansen**  
Co-Chair, Property &  
Casualty Subgroup  
Butt Thornton & Baehr, PC  
Albuquerque, New Mexico  
(505) 884-0777  
jhjohansen@btblaw.com



**Lisa F. Mickley**  
Hall & Evans, LLC  
Denver, Colorado 80202  
(303) 628-3325  
MickleyL@HallEvans.com

## Client Update

Property and Casualty Sub-Group  
of Insurance Practice Group

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*Edited by James N. Hurley  
Fowler White Burnett, P.A.  
Miami, Florida  
jnh@fowler-white.com*

## Welcome message from the Chairmen

Welcome to the first edition of a Client Update prepared by the Property and Casualty Subgroup of the Insurance Practice Group of ALFA International. ALFA International is a network of independent law firms, with 85 U.S. based firms and 60 non-U.S. based firms. These firms regularly represent many of the insurance carriers in the United States and worldwide on many different coverage issues and claims. This update was designed to keep our clients abreast of recent developments in the case law or jury verdicts in many of the jurisdictions where ALFA lawyers practice.

The Property and Casualty Subgroup plans to periodically publish these updates, and we hope you find this update useful and interesting. If you do not wish to receive future updates, please let us know and we will take you off the mailing list.

### **James H. Johansen**

*Butt Thornton & Baehr, PC  
Albuquerque, New Mexico  
jhjohansen@btblaw.com*

### **Robert L. Hebb**

*Semmes, Bowen & Semmes  
Baltimore, Maryland  
RHebb@semmes.com*

## Florida Supreme Court holds that no independent cause of action exists against an insurer for breach of implied warranty of good faith and fair dealing

In *QBE Insurance v. Chalfonte Condominium Apartment Assoc., Inc.* 2012 Fla. LEXIS 1063, the Florida Supreme Court rejected the argument that a cause of action existed for breach of the implied warranty of good faith and fair dealing by an insured against the insurer. The Court also held that there was no private cause of action for an insurer's failure to comply with F.S. § 627.701(4)(a) which regulates placement, content and font size for hurricane deductibles in a policy. Finally, the Court held that a policy provision requiring payment upon entry of a final judgment was not a waiver of the right to post a superdededeas bond.

QBE provided property damage coverage to Chalfonte which owned property damaged by Hurricane Wilma in 2005. Dissatisfied with the handling of the claim, Chalfonte filed suit against QBE in United States District Court for the Southern District of Florida for declaratory judgment, breach of contract—failure to provide coverage), breach of contract—breach of the implied warranty of good faith and fair dealing, and violation of Fla. Stat. § 627.701(4)(a). After trial, judgment was entered against QBE for \$8,140,099.98 which included monetary damages for the alleged breach of implied warranty of good faith and fair dealing. QBE appealed to the 11th Circuit which

certified the following questions to the Florida Supreme Court:

1. Does Florida law recognize a claim for breach of the implied warranty of good faith and fair dealing by an insured against its insurer based on the insurer's failure to investigate and assess the insured's claim within a reasonable period of time?
2. If Florida law recognizes a claim for breach of the implied warranty of good faith and fair dealing based on an insurer's failure to investigate and assess its insured's claim within a reasonable period of time, is the good faith and fair dealing claim subject to the same bifurcation requirement applicable to a bad faith claim under Fla. Stat. § 624.155?
3. May an insured bring a claim against an insurer for failure to comply with the language and type-size requirements established by Fla. Stat. § 627.701(4)(a)?
4. Does an insurer's failure to comply with the language and type-size requirements established by Fla. Stat. § 627.701(4)(a) render a noncompliant hurricane deductible provision in an insurance policy void and unenforceable?
5. Does language in an insurance policy mandating payment of benefits upon "entry of a final judgment" require an insurer to pay its insured upon entry of judgment at the trial level?

The Court answered Questions 1, 3, 4 and 5 in the negative and refused to address Question 2 holding that it was not necessary. In holding that there was no separate cause of action for breach of an implied warranty of good faith

and fair dealing, the Court noted that no first party action for bad faith existed in Florida prior to the passage of F.S. §624.155(1)(b)1. While Florida contract law does recognize such an implied warranty, that is based upon the “reasonable expectations” doctrine which the Court previously declined to adopt in the context of contracts for insurance. As such, no warranty of good faith exists beyond the statutory bad faith action created by F.S. §624.155(1)(b)1. Under Florida law, bad faith actions may not be brought until contractual issues are determined.

Fla. Stat. § 627.701(4)(a) states that “Any policy that contains a separate hurricane deductible must on its face include in boldfaced type no smaller than 18 points the following statement: “THIS POLICY CONTAINS A SEPARATE DEDUCTIBLE FOR HURRICANE LOSSES, WHICH MAY RESULT IN HIGH OUT-OF-POCKET EXPENSES TO YOU.”” The QBE policy’s hurricane deductible failed to comply with the statutorily prescribed language. The Court held that QBE’s non-compliance with the statutory requirements did not give rise to a private cause of action and could not be a basis to void the wind storm deductible.

Finally, the Court rejected Chalfonte’s arguments that the policy language permits immediate execution on its judgment notwithstanding the posting of a supersedeas bond. The Court held that the contractual language requiring payment on the entry of a final judgment does not act as a waiver of the right to post an appropriate bond under Florida Rule of Appellate Procedure 9.310(b).

*Submitted by:*  
*James N. Hurley*  
*Fowler White Burnett, P.A.*  
*Miami, Florida*  
*jnh@fowler-white.com*

## **\$12 million verdict against Progressive in New Mexico**

A jury in the 2nd judicial district court of the state of New Mexico rendered a startling verdict of \$12,000,000 against Progressive Insurance Company. The Progressive policy had lapsed 90 minutes before a Progressive insured was involved in a fatal accident which also severely injured another person. Progressive defended the two cases and paid policy limits of \$100,000 each for both claims. Progressive also filed a declaratory judgment action seeking a declaration that the policy had lapsed and did not provide coverage, and later sought reimbursement of the \$200,000 paid in the settlements. The insured filed a counterclaim for bad faith, claiming that several computer errors on Progressive’s part contributed to the non-payment of the premium on a timely basis.

Although New Mexico law is fairly clear that a policy lapses when the premiums are not paid on a timely basis, and the evidence put forth by the insured was questionable, the jury determined that it was bad faith for Progressive to not give the insured a “grace period” after the premiums were not timely paid. The jury also seemed offended by the fact that Progressive paid the settlements and then sought to recover from the insured. The case

was tried earlier which resulted in a jury verdict in favor of Progressive, but was reversed by the New Mexico Court of Appeals, who ruled there was a question of fact as to whether the policy had actually lapsed.

Progressive did all the right things in this case. It defended the insured, paid policy limits on demand, and simply sought reimbursement of the monies paid in settlement. The insured had very little in compensatory damages, and thus the verdict was almost entirely punitive in nature. This verdict sends a sobering message to carriers that juries can and will render large punitive damage verdicts even in the absence of any egregious facts.

*Submitted by:*  
*James H. Johansen*  
*Butt Thornton & Baehr, PC*  
*Albuquerque, New Mexico*  
*jhjohansen@btblaw.com*

## **Insurers score a victory with decision that Maryland’s actual prejudice requirement did not apply to a claims-made and reported policy**

In *Minnesota Lawyers Mutual Insurance Co. v. Baylor & Jackson, PLLC*, Civ. No.: JKB-10-2701 (D. Md. April 3, 2012) Judge Bredar of the United States District Court for the District of Maryland held that Minnesota Lawyers Mutual Insurance Co. (“MLM”) was not required to show actual prejudice in declining insurance coverage for the alleged legal malpractice of Baylor & Jackson, PLLC (“Baylor &

Jackson”), holding that Maryland’s notice prejudice statute did not apply to the claims-made and reported insurance policy at issue.

The dispute arose out of the alleged legal malpractice of Baylor & Jackson, which occurred in 2006. Specifically, in representing a client, Baylor & Jackson failed to support an opposition to a motion for summary judgment with any sworn testimony or affidavits. The Judge granted judgment against Baylor & Jackson’s clients and issued an opinion in which he explained that one of the main reasons for his ruling was Baylor & Jackson’s failure to support the opposition with sworn testimony. Through separate appellate counsel, Baylor & Jackson’s clients appealed the decision to the Maryland Court of Special Appeals which affirmed the summary judgment. Baylor & Jackson did not report the unfavorable trial court ruling to MLM until after the Maryland Court of Special Appeals affirmed the trial Court, which was approximately three (3) years after the malpractice. Shortly thereafter, Baylor & Jackson’s clients filed a malpractice claim against Baylor & Jackson. Baylor & Jackson maintained a claims-made and reported insurance policy with MLM, which it renewed on a yearly basis. Pursuant to the policy, a claim is deemed made when the insured should reasonably expect that a malpractice claim could be forthcoming and the insured reports the claim to MLM. MLM declined coverage for the malpractice claim under its 2006 policy because Baylor & Jackson failed to notify MLM

of the malpractice in the same policy period in which it should have reasonably expected that a malpractice claim should have been forthcoming.

This declaratory judgment action revolved around whether Maryland’s notice prejudice statute applied to the insurance policy at issue and whether MLM was required to show actual prejudice when it declined coverage. MD. CODE ANN., INS. § 19-110 requires that insurers show actual prejudice when declining coverage on the grounds that its insured breached the policy by failing to give timely notice. The issue was whether Baylor & Jackson breached the policy by failing to give timely notice, or whether the failure to provide notice was really the non-occurrence of a condition precedent. If a condition precedent does not occur, then no obligation arises under the contract and, thus, there cannot be a breach. Without a breach, Section 19-110 does not apply.

While Maryland case law has seemingly long-held that Section 19-110 does not apply to claims-made and reported insurance policies, this area of law was recently complicated by the Maryland Court of Appeals decision of *Sherwood Brands, Inc. v. Great Am. Ins. Co.*, 13 A.3d 1268 (Md. 2011). In *Sherwood Brands*, the Court of Appeals held that Section 19-110 converted the notice provision in the policy, which was labeled as a “condition precedent,” to a covenant. Since the condition precedent was converted to a covenant, the failure to provide notice was a breach of the policy and Section 19-110 applied.

In this case, however, Judge Bedar distinguished between insurance policies that have a separate notice provision and insurance policies that define a claim as being made when it is reported to the insurer. Judge Bedar held that the former was converted to a covenant, but the latter is a condition precedent. Since the 2006 Policy expired without Baylor & Jackson providing notice to MLM, the condition precedent never occurred and MLM was not required to cover the malpractice claim. As such, Judge Bedar granted summary judgment in favor of MLM.

*Submitted by:*

*Robert L. Hebb, Semmes, Bowen & Semmes, Principal*

*Paul N. Farquharson, Semmes, Bowen & Semmes, Principal*

*Gregory L. Arbogast, Semmes, Bowen & Semmes, Associate*

*Baltimore, Maryland  
RHebb@semmes.com*

## **Oregon’s unique approach to punitive damages awards**

Article VII (Amended), section 3, of the Oregon Constitution provides, in part:

“[N]o fact tried by a jury shall be otherwise re-examined in any court of this state, unless the court can affirmatively say there is no evidence to support the verdict.”

That constitutional provision severely restricts the authority of Oregon courts to review the amount that the jury awards in punitive damages. Thus, unless there is no evidence in the record

to support the jury's factual finding that punitive damages should be awarded, a court is barred under the Oregon Constitution from reviewing a jury's award of punitive damages. *Oberg v. Honda Motor Co.*, 320 Or 544, 549, 888 P2d 8 (1995), cert den, 517 US 1219, 116 S Ct 1847, 134 L Ed 2d 948 (1996) (citing *Van Lom v. Schneiderman*, 187 Or 89, 110–13, 210 P2d 461 (1949)); see also *Lakin v. Senco Products, Inc.*, 329 Or 62, 76, 987 P2d 463 (1999) (observing that Article VII (Amended), section 3, “eliminated Oregon trial courts’ power to grant new trials for excessive verdicts”). Nonetheless, the Supremacy Clause of the United States Constitution binds Oregon courts to review jury awards of punitive damages to ensure compliance with a defendant’s rights under the Due Process Clause. *Oberg*, 320 Or at 549. Accordingly, Oregon courts’ review of a jury’s award of punitive damages is limited to two considerations: whether any evidence supports the jury’s finding that punitive damages should be awarded; and whether the amount of punitive damages is excessive in light of the Due Process Clause.

Based on that constitutional framework, review of a punitive damages award in Oregon involves three stages. *Goddard v. Farmers Ins. Co.*, 344 Or 232, 261–62, 179 P3d 645 (2008). First, the court determines whether there is any factual predicate for the punitive damages award. *Id.* at 261. Second, the court examines, as a matter of law, whether the award of punitive damages comports with due process when the pertinent

facts are evaluated in light of the guideposts set out in *Gore*: (1) the degree of reprehensibility of the defendant’s misconduct; (2) the disparity between the actual or potential harm suffered by the plaintiff and the punitive damages award; and (3) the difference between the punitive damages awarded by the jury and the civil penalties authorized or imposed in comparable cases. *Goddard*, 344 Or at 261. Third, if the court determines that the award of punitive damages exceeds the constitutional limitations, the court applies those same guideposts to determine the “highest lawful amount” that a rational jury could award consistently with the Due Process Clause. *Goddard*, 344 Or at 261–62.

Application of the review standards adopted by Oregon courts since *Oberg* has led to one predictable result: a jury’s decision whether to award punitive damages is very, very difficult (if not impossible) to change on appeal. However, application of the review standards to a jury’s determination of how much to award has yielded much less predictable results. See *Goddard*, 344 Or at 259–61 (providing exhaustive discussion of *Gore* and *Campbell*, and concluding that punitive damage awards generally should be limited to single-digit ratios, and in cases of purely economic injury, to a 4:1 ratio.); *Hamlin v. Hampton Lumber Mills, Inc.*, 349 Or 526, 541–44, 246 P3d 1121 (2011) (concluding that 22:1 ratio was not constitutionally excessive punitive damages award in light of small compensatory damage

award, degree of reprehensibility of defendant’s conduct, and amount of punitive damages actually awarded); see also *Wieber v. FedEx Ground Package System, Inc.*, 231 Or App 469, 2494–97, 20 P3d 68 (2009) (discussing ratios approved in prior economic loss cases and reasons for approval); *Groth v. Hyundai Precision and Ind. Co. Ltd.*, 209 Or App 781, 789–94, 149 P3d 333 (2006) (discussing ratios approved in prior non-economic loss cases and reasons for approval). Thus, while Oregon appellate courts follow, as they must, the Due Process principles expressed by the United States Supreme Court that limit the amount of punitive damages awards, Article VII (Amended), section 3 of the Oregon Constitution has led, and will continue to lead, Oregon courts to narrowly apply those principles—and, indeed, look for independent state grounds to avoid applying them at all—to either avoid disturbing punitive damages awards by Oregon juries or to limit them to the least degree possible consistent with federal due process.

*Submitted by:*

*Thomas W. Brown*

*Cosgrave Vergeer Kester LLP*

*Portland, Oregon*

*tbrown@cosgravelaw.com*

## Get ready for Colorado’s new pilot rules

If you have coverage litigation in Colorado in 2012-2013, be prepared to be impacted by the Colorado Civil Access Pilot Project (CAPP). Intended to streamline cases and change the litigation

culture, this sea change raises the stakes for litigants. Though limited to commercial cases filed in just four counties, coverage litigation will likely be one of the most impacted areas of litigation.

CAPP increases the burdens on the parties, limits the discretion of the courts and mandates sanctions for even inadvertent failure to comply. The increased burden—and potential pitfalls—is immediate. The scope and the timing of initial disclosures are changed. Parties must serve initial disclosures 21 days after service of the case, making the disclosure due at the same time as the answer. Carriers served with a coverage suit in Colorado in the next two years should be prepared to immediately send the claims file, underwriting materials and other potentially relevant information to counsel as soon as they receive notice of a new case. The parties cannot negotiate a different timeline and the courts have very limited discretion to grant one. Moreover, CAPP imposes mandatory sanctions for failure to satisfy the disclosure requirements.

Discovery will be governed on the basis of proportionality. The parties are required to confer and provide a report to the court specifying the issues to be litigated. The court will then issue case management orders structuring the discovery on a case by case basis. This order will also set the deadlines and trial date. Once set, the court has very limited discretion to modify these deadlines; motions for extension are “strongly disfavored” and must be denied absent “extraordinary circumstances.”

There are a few silver linings. Because the parties are required to identify the issues early in the case and provide the court with a proportionality assessment for purposes of setting discovery limitations, plaintiffs’ attempts for broad bad faith discovery may be limited. At the very least, carriers will have an opportunity to head it off early and rely on the proportionality directive as an argument against such broad discovery. Another benefit is the requirement that complaints must set forth the claim with more specificity than is currently required. This should not only better define the issues early in the case, but minimize the chances that the case will grow over time. Finally, if successful, CAPP should reduce litigation costs as fewer discovery disputes should arise; that, at least, is the hope.

*Submitted by:  
Lisa F. Mickley  
Hall & Evans, LLC  
Denver, Colorado  
MickleyL@HallEvans.com*