

BAD FAITH BLOG

Court Finds Insurer's Denial of Coverage Was Without Just Cause or Excuse - Insurer Awarded Over \$2.5 Million

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SUMMARY: Missouri Court of Appeals, applying Kansas law, found the "care, custody, control" exclusion in CGL policy ambiguous and therefore, found coverage for a third-party property damage claim. Also, the Appeals Court affirmed the statutory award of attorney's fees to insured because the insurer's denial of claim based on the ambiguous exclusion was without just cause or excuse.

Dodson International Parts, Inc. v. National Union Fire Insurance Company of Pittsburg, Pennsylvania

Dodson, the insured, is in the aircraft salvage business. National Union, the insurer, issued a CGL aviation liability policy to Dodson. The declarations page indicated the only coverage purchased by Dodson was for "Products/Completed Operations" with an aggregate limit of \$5 million.

Dodson was hired by Ameristar Jet Charter ("Ameristar") to recover an aircraft that made an emergency landing near the Kansas City airport. Dodson retrieved the aircraft and transported it to a hangar at the airport.

Later, Dodson was advised that there was damage to the aircraft unrelated to the aircraft's emergency landing. Ameristar claimed Dodson caused the damage while disassembling and transporting the aircraft. Dodson claimed the damage occurred after the aircraft was delivered to the hangar.

Dodson was sued by Ameristar for the damage to the aircraft and submitted a claim to National Union. The claims manager reviewed the lawsuit and obtained a statement from the President of Dodson. The President agreed that Ameristar was "trying to claim" that the damage to the aircraft occurred while it was in Dodson's care, custody and control. After taking a recorded statement, the claims manager conducted no further investigation and recommended the claim's denial.

National Union primarily relied on the care, custody and control exclusion contained in the CGL policy which excluded coverage for property damage to “personal property in the care, custody, or control of the Insured.” National Union refused to defend Dodson even after Dodson requested National Union reconsider its denial of coverage.

At trial, the jury returned a verdict in favor of Ameristar on Ameristar’s claim against Dodson for negligence in its handling of the aircraft. The jury apportioned 70 percent of the fault to Dodson and 30 percent of the fault to Ameristar. On appeal, the case was reversed and remanded for new trial on the issue of damages; however, Dodson and Ameristar reached a settlement agreement in the amount of \$1,300,000 before the case was retried.

While the judgment was on appeal, Dodson once again requested that National Union reconsider its denial of coverage. Dodson argued the damage to the aircraft did not occur when the aircraft was within Dodson’s care, custody, or control, but instead occurred after the aircraft had been delivered to the hangar. In response to Dodson’s renewed request for coverage, National Union sought a coverage opinion from coverage counsel. Coverage counsel concluded he was comfortable with the denial of the claim, though he reminded National Union the burden was on the insurer to prove that an exclusionary clause applied. Coverage counsel advised against National Union filing a declaratory judgment action to determine coverage. Coverage counsel explained that his “general rule of thumb relative to declaratory judgment actions is, unless you are confident you will get summary judgment, don’t file it.” This suggested that coverage counsel was telling National Union that it was not likely to prevail on a motion for summary judgment on the coverage issue. Coverage counsel sent a letter on behalf of National Union to Dodson which again denied coverage based upon the care, custody or control exclusion.

Dodson eventually filed a declaratory judgment action against National Union seeking a determination that the policy provided coverage and sought attorneys’ fees for National Union’s denial of coverage without just cause or excuse pursuant to Kansas Statute §40-256. Cross motions for summary judgment were filed on the issue of coverage and (ominously consistent with coverage counsel’s prediction) the Circuit Court held that the care, custody or control exclusion in the policy was ambiguous, requiring it be interpreted in favor of Dodson.

The declaratory judgment action proceeded to a bench trial and the trial court concluded that National Union denied coverage without just cause or excuse under §40-256. The judgment awarded Dodson damages in the amount of \$2,528,679.92, plus post judgment interest. The damage award included the \$1,300,000 settlement of the lawsuit, Dodson’s incurred defense costs of \$475,60720, interest on those costs and \$615,000 in attorneys’ fees pursuant to §40-256.

National Union appealed; however, the Appellate Court affirmed the trial court's judgment. The Appellate Court found the care, custody, or control exclusion to be ambiguous and thus found coverage in favor of Dodson. However, National Union also argued that the trial court erred in awarding attorneys' fees to Dodson because National Union's denial of coverage was not without just cause or excuse. National Union claimed that, at the time of denial of coverage, a good faith legal controversy existed on the issue of coverage in that: 1) the lawsuit specifically alleged that Dodson negligently damaged the aircraft during Dodson's disassembly, loading or transport of the aircraft; 2) the policy contained the care, custody, or control exclusion; and 3) National Union confirmed Dodson's activity in loading and transporting the aircraft during its investigation before the denial of claim.

The Appellate Court found that National Union relied exclusively on the allegations in Ameristar's lawsuit that Dodson negligently damaged the aircraft while transporting the aircraft to reach its initial decision to deny coverage. Even though National Union interviewed Dodson's President before denying coverage, it sought no information from him about the means of disassembling, loading or transporting the aircraft, or any information from him about when or how the claimed damage to the aircraft occurred. The Appellate Court noted this "self-serving reliance on Ameristar's allegation to deny coverage with no independent investigation into the factual basis for the allegations was inappropriate." Under Kansas law, the lawsuit pleadings are merely a starting point for the duty to defend analysis and further investigation may be appropriate.

The Appellate Court also pointed out that Dodson again approached National Union seeking coverage while the lawsuit was on appeal. National Union was on specific notice at this point, based on the evidence at trial, that Dodson claimed the damage to the aircraft occurred after the aircraft left its care, custody or control. Also, the Court found it curious that coverage counsel confirmed his belief that the care, custody, or control exclusion applied however counseled against National Union filing a declaratory judgment action to determine coverage. Coverage counsel also pointed out in his opinion letter that the Kansas Supreme Court concluded that "the care, custody and control clause frequently found in liability insurance policies is of a generally ambiguous character and must be applied to the facts of each individual case with common sense and practicality." *Buchanan v. Employer's Mutual Liability Insurance Company*, 443 P.2d 681, 682-83 (1968). National Union's decision, while the underlying case was on appeal, to restate its denial of coverage thus ignored the presence of any factual dispute about when the damage to the aircraft occurred, notwithstanding coverage counsel's opinion letter advising that the application of the care, custody or control exclusion is "fact driven." Therefore, the Appellate Court found the trial court did not abuse its discretion in awarding Dodson its attorneys' fees under the Kansas statute.

Insurers must be advised that in Kansas, as well as many other states, denial of coverage should not necessarily start and end based upon the allegations in the lawsuit's pleadings. Insurers must know the legal standard which is likely to be applied to their coverage decision. The duty to defend is broad and if further investigation is necessary to determine whether there may be coverage, this investigation should be done early and promptly upon notice. Moreover, insurers should use caution in denying claims based solely on an exclusion, especially when the application of it is unsettled or factually based. Finally, reliance on coverage counsel in the denial of a claim is not necessarily certain to avoid statutory penalties; especially, when the insurer refused a renewed demand to defend in the face of a coverage opinion which can be read to support the insured's coverage position.