Survey of Recent Developments in Insurance Law

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I. INTRODUCTION

The past year was a busy one in the area of insurance law. Over the course of the survey period[1] there were more than twenty-five published opinions rendered by the state appellate courts, the federal district courts, and the Seventh Circuit Court of Appeals. Of the more than twenty-five cases, several contained interesting new law. This Article will focus upon the cases which are most likely to impact upon practitioners who represent insurance companies, insureds, and claimants.[2]

The Indiana Court of Appeals decided the most noteworthy case to be discussed in this Article, *Demoss Rexall Drugs v. Dobson*,[3] just a few days after the survey period ended. *Demoss* does not specifically address insurance law *per se*, but its impact upon insurance practice is so profound that it cannot be omitted from an insurance law article. In *DeMoss*, the Indiana Court of Appeals expanded the opportunity for a plaintiff to discover the statements and other materials developed by an insurance company in the course of a liability investigation into a plaintiff's claim against the company's insured.[4]

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1. Approximately August 1, 1988 to July 1, 1989.

2. As usual, there were a number of interesting cases that discussed or reaffirmed existing insurance law. *See* United States Fire Ins. Co. v. Charter Fin. Group, 851 F.2d 957 (7th Cir. 1988) (discussing whether an excess insurance carrier has a duty to drop down when the underlying policy is inadequate or non-existent); Ellington v. Metropolitan Life Ins. Co., 696 F. Supp. 1237 (S.D. Ind. 1988) (discussing the issue of ERISA preemption of state substantive insurance law); Town & Country Mut. Ins. Co. v. Sharp, 538 N.E.2d 6 (Ind. Ct. App. 1989) (describing a "first aid" clause contained in an automobile policy); Bush v. Washington Natl. Ins. Co., 534 N.E.2d 1139 (Ind. Ct. App. 1989) (reaffirming the rule that an insurer may void a policy for the insured's material misrepresentation even though the fact misrepresented did not relate to the event or loss that gave rise to the pending claim); High v. United Farm Bureau Mut. Ins. Co., 533 N.E.2d 1275 (Ind. Ct. App. 1989) (reaffirming the rule that insurance companies may include language in their policies to preclude "stacking" of uninsured motorist coverages); Hancock v. Kentucky Central Life Ins. Co., 527 N.E.2d 720 (Ind. Ct. App. 1988) (reaffirming the rule that a divorce does not automatically remove an ex-spouse as beneficiary on a life insurance policy).

3. 540 N.E.2d 655 (Ind. Ct. App. 1989).

4. *Id.* at 658.

Other cases reported in this Article will deal with: (1) the efforts of automobile accident victims to recover from a tortfeasor's homeowner insurance coverage; (2) the meaning of "intentional" as used in exclusionary clauses of liability insurance policies; and (3) other miscellaneous issues. The Article will also contain a brief review of insurance related legislation enacted by the 1989 Indiana General Assembly.

II. Discovery of the Insurance Claims File

The decision of the Indiana Court of Appeals in *Demoss Rexall Drugs v. Dobson*[5] has sent shock waves through the insurance litigation system. In *DeMoss*, the court adopted the broad concept that liability insurance claim investigation files are discoverable for the portion of time that the insurer's investigation was being performed in the ordinary course of business rather than in anticipation of litigation.[6] For reasons that will be discussed below, the precedent established by *DeMoss* will increase the expense of insurance claims handling, will increase the cost of liability litigation, and will involve the trial court in discovery to a greater degree than was originally anticipated by the trial rules.

A brief examination of earlier precedent demonstrates the significant effect of *DeMoss*. Since 1985, the guidelines concerning the discoverability of an insurance claim file had been established by *CIGNA-INA/Aetna v. Hagerman-Shambaugh*.[7] In *CIGNA*, the insured brought a breach of contract suit against CIGNA-INA/Aetna after CIGNA refused to honor the insured's first party[8] claim for flood damage of a water pollution control plant the insured was constructing.[9] During discovery, the insured requested that CIGNA produce its claim file.[10] CIGNA objected to production on the basis that the file was protected by the work product privilege because it was prepared in anticipation of litigation.[11] The trial court ordered the file produced.[12]

In upholding the trial court, the Indiana Court of Appeals cited a line of first party cases from other states in which the courts had held that an insurer does not automatically "anticipate litigation" when in-

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5. 540 N.E.2d 655 (Ind. Ct. App. 1989).
6. *Id.* at 658-59.
7. 473 N.E.2d 1033 (Ind. Ct. App. 1985).
8. A "first party" case is one in which the insured is suing his own insurer for breach of contract for failing to pay the insured under the terms of the policy.
9. 473 N.E.2d at 1034.
10. *Id.*
11. *Id.*
12. *Id.* at 1035.

vestigating and evaluating a claim made by its own policyholder.[13] The court held that CIGNA's claim file was discoverable up until the point that litigation between the insurer and insured was imminent.[14]

The reasoning of the court in *CIGNA* was sound in the context of a first party lawsuit. Common sense dictates that in the vast majority of cases an insurer does not automatically anticipate litigation with its insured when a first party claim is submitted for evaluation and payment. Further, in *CIGNA* the insurer's file was particularly relevant because the insurer's good faith was an issue in a punitive damage claim filed by the insured.[15] Thus, in a first party case, an insurer should not be allowed to hide its claim file by painting the "anticipation of litigation" protection with a broad stroke.[16]

Therefore, in light of the earlier precedent which allowed discovery of the claim file of the insurer only in first party cases the court of appeals made a quantum leap in *DeMoss* by applying the reasoning of *CIGNA* to third party claims.[17] In *DeMoss*, Farm Bureau Insurance Company provided a policy of liability insurance to DeMoss Rexall Drugs. In August of 1987, the plaintiff, Barbara Dobson, had a prescription filled at the pharmacy. After experiencing physical problems, the plaintiff discovered that the pharmacist had given her the wrong medication, and she reported the error to DeMoss. DeMoss in turn reported the claim to Farm Bureau.[18]

The Farm Bureau adjuster assigned to investigate the claim recognized immediately that Mrs. Dobson and her husband would be hard to please because the adjuster had an earlier claim with Mrs. Dobson, and he was also aware that Mr. Dobson had a bodily injury claim pending against his employer.[19] Without much delay, the adjuster went out and took recorded statements from four employees of the pharmacy.[20] In the subsequent litigation the Dobsons requested the four statements, and the trial court ordered their production.[21]

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13. *Id.* (citing State Farm Fire and Cas. Co. v. Perrigan, 102 F.R.D. 235 (D. Va. 1984); Carver v. Allstate Ins. Co., 94 F.R.D. 131 (S.D. Ga. 1982); Fine v. Bellefonte Underwriters Ins. Co., 91 F.R.D. 420 (S.D.N.Y. 1980); APL Corp. v. Aetna Cas. & Sur. Co., 91 F.R.D. 10 (D. Md. 1980)).

14. 473 N.E.2d at 1035.

15. *Id.* at 1036-37.

16. The anticipation of litigation protection is found in IND. R. TR. P. 26(B)(3).

17. A third party claim is one in which an insurer provides a liability defense to its insured for a claim being presented by a third party, usually an injured plaintiff.

18. DeMoss Rexell Drugs v. Dobson, 540 N.E.2d 655, 656 (Ind. Ct. App. 1989).

19. *Id.*

20. *Id.*

21. *Id.*

On appeal DeMoss challenged the production of the statements on the basis that the statements were protected work product prepared in anticipation of litigation under T.R. 26(B)(3).[22] DeMoss also argued that the court should treat statements between an insurer and its insured as a privileged communication under T.R. 26(b)(1).[23]

The court made short work of the privilege argument. It noted that no such privilege had yet been adopted in Indiana, and that an evidentiary privilege of that nature was the prerogative of the legislature.[24]

On the issue of whether the file was protected because it was prepared in anticipation of litigation the court sided with the trial court and ordered the statements produced.[25] The court adopted the precedent of *CIGNA-INA/Aetna*[26] completely, stating:

> [T]he work product doctrine demands more than just a recognition that a claim will eventually lead to litigation; it requires evidence supporting the conclusion that the insurer is actively working based upon the premise that the claim will lead to litigation and has obtained the statements at issue in furtherance of that purpose.[27]

Even though the court acknowledged that insurance claims adjusters sometimes can recognize that a claim is going to lead to a lawsuit merely because of the nature of the claim and the people involved, that was not enough to meet the anticipation of litigation standard.[28]

A thorough criticism of *DeMoss* could alone be the subject of an article, but this author will not take that opportunity here. However, suffice to say that the *DeMoss* opinion flies in the face of reality and will wreak havoc in tort and insurance litigation. In the long run, no one will benefit from the *DeMoss* decision. A few examples of anticipated problems may be illustrative.

One immediate effect of the case will be the added burden imposed upon trial courts. When the Indiana trial rules were drafted, they were intended to be self-executing with minimal supervision from the trial court.[29] In fact, in order to reduce the burden of discovery pleadings

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22. *Id.* (citing IND. R. TR. P. 26(b)(3)).

23. 540 N.E.2d at 656-57 (citing IND. R. TR. P. 26(b)(1)).

24. 540 N.E.2d at 657 (citing Scroggins v. Uniden Corp. of Am., 506 N.E.2d 83, 86 (Ind. Ct. App.), *trans. denied* (1987)).

25. 540 N.E.2d at 658.

26. 473 N.E.2d 1033 (Ind. Ct. App. 1985).

27. *DeMoss*, 540 N.E.2d at 659.

28. *Id.* at 658-59.

29. W. HARVEY, 2 IND. R. OF PROC. ANN. 493 (1987) (quoting Chustak v. Northern Ind. Pub. Serv. Co., 259 Ind. 390, 395, 288 N.E.2d 149, 153 (1972); Front v. Lane, 443 N.E.2d 95, 98 (Ind. Ct. App. 1982); Chrysler Corp. v. Reeves, 404 N.E.2d 1147, 1151 (Ind. Ct. App. 1980)).

on the trial court, the Indiana Supreme Court changed the rules in 1987 so that discovery pleadings are no longer filed with the court unless a dispute arises.[30] A review of the cases involving production of insurance files reveals that an *in camera* inspection of the file is always necessary to allow the trial judge to address relevance and to pinpoint the date at which the company began to anticipate litigation.[31] As recently as 1976, *in camera* inspections were considered rare.[32] Now such inspections will occur in every lawsuit in which an insurer defends someone. Who will bear the attendant costs, as well as the additional delay in litigation?

Aside from the additional burden that *DeMoss* will impose upon insurance-related litigation, the most alarming result is that the relationship between insurers and insureds is sure to be undermined. Under the standard liability insurance policy, insureds have an obligation to cooperate with the insurer in defending claims.[33] Once insureds and their personal attorneys learn that statements taken prior to litigation may be discoverable, the willingness of an insured and his employees or families to give statements may diminish. In fact, in instances in which the insured is facing a punitive damage claim or a similar uninsured exposure, the insured's counsel may be obligated to advise a client not to cooperate. Although insurance claims representatives are by and large very professional and well-trained, they may not appreciate the harm that could be caused to an insured if an inartfully taken statement is produced to the opposition.

Another potential detriment of *DeMoss* is that insurers may now be inclined to limit the nature and amount of pre-litigation investigation rather than risk having their mental impressions, reserves, and the fruits of their labor end up in the plaintiff's hands. The only other alternative will be for insurers to spend the money to employ counsel at a much earlier stage so that counsel can direct investigation and make sure that it is well-documented that the investigation is being done in anticipation of litigation. Unfortunately, the earlier intervention of counsel will add expense, and may result in more litigation.

In view of the anticipated problems and detriments created by the *DeMoss* decision, this author encourages the Indiana Supreme Court to overturn the decision through case law or rule-making. Alternatively,

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30. *See* IND. R. TR. P. 5(D)(2).

31. *See, e.g.*, DeMoss Rexall Drugs v. Dobson, 540 N.E.2d 655 (Ind. Ct. App. 1989); CIGNA-INA/Aetna v. Hagerman-Shambaugh, 473 N.E.2d 1033 (Ind. Ct. App. 1985) and cases cited therein; Newton v. Yates, 170 Ind. App. 486, 353 N.E.2d 485 (1976).

32. Newton v. Yates, 170 Ind. App. 486, 494, 353 N.E.2d 485, 490 (1976).

33. *See, e.g.*, Annotation, *Liability Insurer's Waiver of Right, or Estoppel, to Set Up Breach of Co-operation Clause*, 30 A.L.R. 4th 620, 625 (1984).

the Indiana General Assembly should address the question of whether to create the insured-insurer communication privilege advanced by the pharmacy in *DeMoss*.[34]

III. Availability of Homeowner Liability Coverage for Automobile Accidents

On two occasions during the survey period, auto accident victims tried to reach the tortfeasor's homeowner's liability coverage for additional compensation.[35] In each case, the result was the same: no coverage.

In *Standard Mutual Insurance Co. v. Bailey*,[36] decided by the Seventh Circuit Court of Appeals, Christopher Cook was struck by a car while riding his bike. Following the accident Christopher and his parents sued Robert Jones, the driver of the car, and Elodie Bailey, the owner of the car. The suit against Bailey was based upon a theory of negligent entrustment.[37]

At the time of the accident, Bailey was covered by a Standard Mutual homeowner's policy that provided the following personal liability coverage: "If a claim is made or a suit is brought against any insured for damages because of bodily injury or property damage, we will . . . pay up to our limit of liability for the damages for which the insured is legally liable."[38] The policy also contained an exclusion which stated that there would be no personal liability coverage for bodily injury "arising out of the ownership, maintenance, use, loading or unloading of: . . . a motor vehicle owned or operated by, or rented or loaned to any insured. . . ."[39]

Standard Mutual filed a declaratory judgment action against Bailey and the Cooks to determine whether coverage should apply.[40] The trial court granted summary judgment for Standard Mutual.[41]

On appeal the Seventh Circuit Court of Appeals recognized that this was a case of first impression in Indiana. The Cooks argued that the exclusionary language relating to the operation and use of an automobile should not control because Bailey's liability arose solely from her initial

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34. *DeMoss*, 540 N.E.2d at 656-57.

35. Standard Mut. Ins. Co. v. Bailey, 868 F.2d 893 (7th Cir. 1989); Sharp v. Indiana Union Mut. Ins. Co., 526 N.E.2d 237 (Ind. Ct. App. 1988).

36. 868 F.2d 893 (7th Cir. 1989).

37. *Id.* at 894.

38. *Id.* at 895.

39. *Id.*

40. *Id.*

41. *Id.*

entrustment of the vehicle.[42] The court disagreed, and held that operation and use of a motor vehicle are "inextricably intertwined" with negligent entrustment.[43] Thus, the Cook boy's injury did arise out of the operation and use of a motor vehicle and the exclusion applied. The court noted that its ruling was in accord with twenty-eight of the thirty-two jurisdictions which have considered the issue.[44]

In *Sharp v. Indiana Union Mutual Insurance Co.*,[45] the Indiana Court of Appeals had the opportunity to address a very similar question. In *Sharp*, the insured, Richard Leinenbach, was covered by a homeowner's policy with personal liability coverage and an automobile exclusion virtually identical to the one in the *Standard Mutual* case.[46] During a two day period in November of 1984, Leinenbach went on a drinking binge at his home. While in a state of extreme intoxication,[47] Leinenbach got into his automobile and subsequently had a head-on collision with Mr. Sharp.[48]

In an attempt to invoke coverage, the Sharps argued that Leinenbach's use of the car was only a concurrent cause of Sharp's injuries.[49] They argued that Leinenbach's act of drinking to excess was a separate and independent act of negligence for which the homeowner coverage should apply.[50] In support of their position, the Sharps relied upon several out of state cases which stood for the proposition "that where two separate, independent acts of negligence combine to cause injury and one of those acts is excluded from coverage under an insurance policy, the policy will still cover the damage incurred if the other act of negligence is not excluded under the policy."[51]

The court of appeals made short shrift of the Sharps' argument. The court pointed out that it was not even necessary to decide whether it is negligent for a person to become intoxicated in his own home. Without the element of driving the automobile there would be no injury or accident.[52] Thus, the auto exclusion controlled.

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42. *Id.* at 897.
43. *Id.* at 898.
44. *Id.* (citing Cooter v. State Farm Fire & Cas. Co., 344 So. 2d 496 (Ala. 1977)). The reader may wish to review n.6 on page 898 of the opinion for a complete list of the jurisdictions in accord.
45. 526 N.E.2d 237 (Ind. Ct. App. 1988).
46. *Id.* at 239.
47. Leinenbach's blood alcohol content was 0.301. *Id.* at 238.
48. 526 N.E.2d at 238.
49. *Id.* at 240.
50. *Id.*
51. *Id.* (citing Waseca Mut. Ins. Co. v. Naska, 331 N.W.3d 917 (Minn. 1983); Lauver v. Boling, 71 Wis. 2d 408, 238 N.W.2d 514 (1976); Mutual Auto Ins. Co. v. Partridge, 10 Cal. 3d 94, 514 P.2d 123 (1973)).
52. 526 N.E.2d at 240.

The rulings in *Standard Mutual* and *Sharp* are both sound and supportable. In the factual context of these cases, the automobile exclusion in each of the policies was clear and unambiguous. Furthermore, the use of the automobile in causing the injury could not reasonably be separated from the negligence. Now that Indiana has precedent in this area, it should reduce, if not end, further litigation on the subject.

IV. Exclusions for Intentional Acts

For years liability insurance policies have contained provisions that have excluded an insured from liability coverage if the injury-producing acts of the insured were intentional.[53] During the survey period, the Indiana Court of Appeals handed down two fascinating cases on the subject of intentional acts.[54] In each instance, the court made new law in Indiana.

A. "Expected" Defined

In *Indiana Farmers Mutual Insurance Co. v. Graham*,[55] the court of appeals was called upon to interpret the meaning of the word "expected" as used in a standard liability exclusion. Although the word "intended" had been defined before,[56] the word "expected" had never been defined in this state.[57]

In 1984, Jeffrey and Jean Graham learned that their herd of hogs had contracted an infectious disease that had particular impact upon breeding herds. After the disease was discovered the herd was quarantined. Thereafter, under State Board of Health regulations, the herd could not be sold unless the hogs were vaccinated and tagged, and certain forms filed with the State.[58]

So that the premises could be disinfected, the Grahams arranged to sell the hogs through a broker. The Grahams informed the broker of the disease and the quarantine, but at the broker's request, they did not tag the hogs. Furthermore, the Grahams did not follow the other regulations.[59] The broker in turn sold the hogs to Mark and Debra

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53. *See, e.g.*, Home Ins. Co. v. Neilsen, 165 Ind. App. 455, 332 N.E.2d 240 (1975).

54. Indiana Farmers Mut. Ins. Co. v. Graham, 537 N.E.2d 510 (Ind. Ct. App. 1989) and West Am. Ins. Co. v. McGhee, 530 N.E.2d 110 (Ind. Ct. App. 1988), *trans. denied* (1989).

55. 537 N.E.2d 510 (Ind. Ct. App. 1989).

56. *See* Home Ins. Co. v. Neilsen, 165 Ind. App. 445, 332 N.E.2d 240 (1975).

57. *Indiana Farmers*, 537 N.E.2d at 512.

58. *Id.* at 510.

59. *Id.*

Good. In doing so, he failed to advise them of the disease. Not surprisingly, the Goods mixed the hogs with their own herd, and ultimately lost their existing herd to the disease.[60]

The Goods filed suit against the Grahams, and the Grahams turned to Indiana Farmers for coverage under a comprehensive farm liability policy. Indiana Farmers responded to the claim by filing a declaratory judgment action against the Grahams. Indiana Farmers contended that it did not have to defend the Grahams for "property damage which is either expected or intended from the standpoint of the Insured."[61] Each party moved for summary judgment. The trial court granted the Grahams' motion and denied Indiana Farmers' motion.[62]

On appeal, the Indiana Court of Appeals stated at the outset that the policy language "expected or intended" was ambiguous.[63] On this point, the court noted that in the 1975 case of *Home Insurance Co. v. Neilsen*,[64] the parties argued no fewer than three possible definitions of "caused intentionally" before the court finally defined it as "an intentional act of the insured which was intended to cause injury."[65] The *Neilsen* court held that the type of intent could be proven "either by showing an actual intent to injure or by showing the nature and character of the act to be such that intent to cause harm to the other party must be inferred as a matter of law."[66]

The court opined that the insurance industry must have wanted the terms "expected" and "intended" to have separate meanings, and the term "intended" would simply require a greater degree of proof and a higher degree of probability than the term "expected."[67] Because no other Indiana court had ever been called upon to define "expected" as used in the exclusion, the court drew on other jurisdictions and defined "expected" as follows: "Expected injury or damage means that the insured acted although he was consciously aware that the harm caused by his actions was practically certain to occur."[68]

Using the definitions of "intended" and "expected" the court found that the Grahams did neither; they were simply negligent.[69] The trial court ruling in favor of the Grahams was affirmed.[70]

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60. *Id.* at 510-11.
61. *Id.* (quoting policy language from the Farmer's policy exclusion).
62. 537 N.E.2d at 510-11.
63. *Id.*
64. 165 Ind. App. 445, 332 N.E.2d 240 (1975).
65. *Indiana Farmers*, 537 N.E.2d at 511 (citing Home Ins. Co. v. Neilsen, 165 Ind. App. 445, 451, 332 N.E.2d 240, 244 (1975)).
66. 537 N.E.2d at 511.
67. *Id.*
68. *Id.* (citing Bay State Ins. Co. v. Wilson, 96 Ill. 2d 487, 494, 451 N.E.2d 880, 882 (1983)).
69. 537 N.E.2d at 512.
70. *Id.*

A ruling of this nature is helpful and appreciated by practitioners. Although the definition of "expected" adopted by the court is broad enough that every case will be fact-sensitive, the court nevertheless has given a guideline to follow. These cases are usually fact-sensitive anyway, so it is preferable to have a definition even if the definition requires a factual interpretation in each case.

B. Insanity Defense to the Intentional Act Exclusion

The case of *West American Insurance Co. v. McGhee*,[71] is one that is sure to increase the intensity of litigation in cases involving the intentional acts exclusion. Even so, it is a well-reasoned and necessary new wrinkle in the body of Indiana law with respect to the intentional act exclusion.

The case arises from a sad and brutal incident in which Mr. Philmore Hankerson bludgeoned to death a woman who lived in his home, and also shot and killed her teenage daughter with a point-blank shotgun blast. A short time later he committed suicide.[72] Following this incident the deceased woman's estate brought a wrongful death lawsuit against Hankerson's estate.[73]

Hankerson's estate sought a liability defense from West American under a homeowner's policy that was in force at the time of the incident. West American then filed a declaratory judgment action in which it contended that it owed no defense to Hankerson's estate because Hankerson had violated the policy provision which excluded coverage for "bodily injury . . . which is expected or intended by the insured. . . ."[74] The trial court, without stating its rationale, held that the estate was entitled to a defense.[75]

On appeal, the court of appeals applied the intent standard[76] of *Home Insurance Co. v. Neilsen*[77] and recognized immediately that the nature and character of Mr. Hankerson's conduct was such that his intent to cause harm could be inferred as a matter of law.[78] However, the court also acknowledged the appellees' argument that Indiana should

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70. *Id.*
71. 530 N.E.2d 110 (Ind. Ct. App. 1988), *trans. denied* (1989).
72. *Id.* at 111.
73. *Id.*
74. *Id.* (quoting policy language).
75. 530 N.E.2d at 111.
76. *See supra* notes 83-84 and accompanying text.
77. 165 Ind. App. 445, 332 N.E.2d 240 (1975).
78. *West American*, 530 N.E.2d at 111-12 (citing Home Ins. Co. v. Neilsen, 165 Ind. App. 445, 332 N.E.2d 240 (1975)).

adopt an insanity defense to the intentional act exclusion.[79] After noting that a majority of other jurisdictions had adopted the insanity defense, the court also adopted it.[80] The court indicated that the purpose of the intentional act exclusion was to prevent persons from benefiting from acts intentionally caused and to deter intentional misbehavior.[81] With such a purpose in mind, the court reasoned that it did not make sense to apply the intentional acts exclusion to persons who lacked the mental capacity to be concerned about the existence of insurance.[82]

In spite of the court's favorable ruling on the insanity defense, the estate did not prevail on the issue of coverage. The court found there was a presumption that a person is sane until proven otherwise.[83] Hankerson's estate bore the burden of proving by a preponderance of the evidence that Hankerson was insane.[84] Further, the court stated that "[p]roof of legal insanity, in this context, requires some evidence tending to prove that the actor was unable to conform his behavior to societal norms."[85] In this instance, the only evidence of insanity was the heinous nature of the acts. That was not enough to satisfy the court that Hankerson was insane.[86]

It is hard to quarrel with the reasoning of the court in *West American*. It will be interesting as time passes to see how the defense will develop in Indiana. Although it is a defense that is seldom successful in the criminal setting because it means that a bad actor may be set free, no one knows what factfinders will do with it in the civil context where a successful defense means a victim may receive compensation.

V. Miscellaneous Cases

A. Right to Demand Appraisal

A common provision in physical damage insurance policies is what is known as the appraisal clause. When invoked, an appraisal clause is a speedy means of alternative dispute resolution that enables parties to each select a disinterested appraiser. The two appraisers then select a

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79. 530 N.E.2d at 112.

80. *Id.* (citing Annotation, *Liability Insurance: Intoxication or Other Mental Incapacity Avoiding Application of Clause in Liability Policy Specifically Exempting Coverage of Injury or Damage Caused Intentionally by or At Direction of Insured*, 33 A.L.R. 4th 983 (1984)).

81. 530 N.E.2d at 112.

82. *Id.*

83. *Id.* (citing Rush v. Mcgee, 36 Ind. 69 (1871)).

84. 530 N.E.2d at 112.

85. *Id.* (citing Globe Am. Cas. Co. v. Lyons, 131 Ariz. 337, 641 P.2d 251 (1981)).

86. 530 N.E.2d at 112.

third person known as an umpire. Once the panel is selected the appraisers try to resolve the dispute, and if they are unsuccessful, the umpire will then render the deciding vote.

In *Monroe Guaranty Insurance Co. v. Backstage, Inc.*,[87] the Indiana Court of Appeals decided for the first time in Indiana the question of when a person may demand an appraisal if the policy is silent on the amount of time allowed.[88] The answer was short and sweet. The right to demand appraisal may be waived unless it is made "within a reasonable time under the circumstances of the case. . . ."[89] Waiver occurs when good faith negotiations have ended *and* prejudice has occurred because of the parties' delay in demanding the appraisal.[90]

In this particular case, the court of appeals permitted Monroe Guaranty to demand appraisal even though the insured had already filed suit.[91] In doing so, the court noted that good faith negotiations had ended more than seven months before appraisal had been demanded.[92] Nevertheless, the court found that no evidence of prejudice to the insured had been presented, and Monroe Guaranty had made a substantial advance payment.[93] Furthermore, the court noted that appraisal was an appropriate method for resolving the parties' differences in this case.[94]

The rule enunciated by the court will be helpful to practitioners. However, attorneys should probably be a little more diligent in demanding appraisal than Monroe Guaranty was in this case. It is difficult to imagine that courts are going to be very tolerant of appraisal demands being routinely made after suit has been filed. Attorneys would be well-advised to demand appraisal (if they choose to do so) just as soon as they sense any breakdown in negotiations. Particularly from the vantage point of the insurer, experience has shown that delay in acting upon policy rights rarely works to the insurer's benefit.

B. Statute of Limitations for Insurance Agent's Failure to Procure Coverage

Under Indiana law an insurance agent may be liable to his insurance customer if he fails to procure coverage, fails to procure coverage in

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87. 537 N.E.2d 528 (Ind. Ct. App. 1989).

88. *Id.* at 529.

89. *Id.* (citing Hanby v. Maryland Cas. Co., 265 A.2d 28, 30 (Del. Super. Ct. 1970)).

90. 537 N.E.2d at 529 (citing School Dist. No. 1 v. Globe & Republic Ins. Co., 146 Mont. 208, 404 P.2d 889; Annotation, *Time Within Which Demand for Appraisal of Property Loss Must Be Made, Under Insurance Policy Providing for Such Appraisal*, 14 A.L.R. 3d 674 (1967)).

91. 537 N.E.2d at 529.

92. *Id.*

93. *Id.*

94. *Id.*

the right amount, or procures coverage that is inappropriate for the needs of the customer.[95] The cause of action by the customer may be brought on a theory of negligence or on a theory of breach of an implied contractual duty to use reasonable care in procuring coverage.[96] Until recently, the question of whether a tort or contract statute of limitations applied to such an action was left open to dispute.

In *Butler v. Williams*,[97] the Indiana Court of Appeals answered two questions: (1) which statute of limitations applied, and (2) when does the statute begin to run.[98] On the first question the court imposed the two-year statute of limitations, reasoning that Indiana has adhered to the rule "that the nature or substance of the cause of action determines the applicability of the statute of limitations."[99] With respect to the errors or omissions of insurance agents the court felt that the nature or substance of the claim is for negligent failure to procure the correct insurance. Thus, the two-year statute was appropriate.[100]

On the second question of when the statute begins to run, the court held that it begins to run when the damage occurs.[101] The court specifically rejected the idea that the cause of action would accrue when the extent of the damage was ascertainable.[102] Further, the court implied that it would also look to evidence of when the insured knew or should have known the damage had occurred for purposes of deciding the issue of when the statute commences running.[103]

The determination of the court that a two year statute of limitations should apply appears to be sound. However, the holding of the court as to when the statute begins to run will cause problems. Under current liberal notice pleading and relation back rules, it is not always easy for an insured to determine every basis for a suit against him. Furthermore, the absence or inadequacy of coverage is not always known until litigation is old and developed because insurance companies are increasingly providing defenses under a reservation of rights. If the courts apply a "knew

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95. *See, e.g.*, Stockberger v. Meridian Mut. Ins. Co., 182 Ind. App. 556, 395 N.E.2d 1272 (1979); Automobile Underwriters v. Hitch, 169 Ind. App. 453, 349 N.E.2d 271 (1976).

96. Carrier Agency v. Top Quality Bldg. Products, Inc., 519 N.E.2d 739 (Ind. Ct. App.), *trans. denied* (1988).

97. 527 N.E.2d 231 (Ind. Ct. App. 1988).

98. *Id.* at 233-34.

99. *Id.* at 233 (citing Whitehouse v. Quinn, 477 N.E.2d 270, 273 (Ind. 1985); Shideler v. Dwyer, 275 Ind. 270, 276, 417 N.E.2d 281, 285 (1981)).

100. 527 N.E.2d at 233-34.

101. *Id.* at 234 (citing Shideler v. Dwyer, 275 Ind. 270, 282, 417 N.E.2d 281, 289 (1981); Monsanto Co. v. Miller, 455 N.E.2d 392, 394 (Ind. Ct. App. 1983)).

102. 527 N.E.2d at 234.

103. *Id.*

or should have known'' standard with respect to the insured's knowledge of damage, then insureds will be fine. If not, insureds and their attorneys will have to be prepared to file suit against their agent the moment it appears that coverage trouble is arising.

VI. Statutory Amendments

The statutory amendments or additions made in the past year are noteworthy only because they display evidence of growing concern for consumers in the Indiana General Assembly. Many of the changes appeared to be in direct response to news stories of the last year.

As an example, in Indiana Code section 27-1-20-21 the legislature expanded the types and amounts of underwriting information that must be reported each year by insurers who provide coverage in such areas as dram shop liability, recreational facility liability, lawyers professional liability, product liability, premises liability, and day care center liability.[104] Without question these reporting requirements were the result of the so-called ''liability crisis'' wherein insurers were refusing to write coverage in these high risk areas because of allegedly poor underwriting loss ratios.

As additional evidence of growing consumerism, the legislature also passed more rigorous financial reporting procedures for domestic insurance companies;[105] rigorous standards for the marketing and sale of medicare supplement insurance;[106] a definition of and cancellation requirements for farmers' drought insurance;[107] and more stringent guidelines for the marketing, pricing, and underwriting of worker's compensation insurance.[108]

One other interesting statutory change occurred in the area of arson prevention.[109] The statute allows certain civil authorities to order an insurer to withhold payment of insurance proceeds for limited periods of time while investigations are pending. It will be curious to see what problems will be caused by such a statute.

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104. Ind. Code Ann. § 27-1-20-21 (West Supp. 1989).
105. *Id.* § 27-1-3-9 (1989).
106. *Id.* §§ 27-8-13-1 to -19 (1989).
107. *Id.* §§ 27-7-11-1 to -2 (1989).
108. *Id.* §§ 27-7-2-1.1 to -1.2 (1989).
109. *Id.* § 27-2-13-5 (1989).