FOR MORE INFORMATION

MCDOWELL KNIGHT
ROEDDER & SLEDGE, L.L.C.
Mobile, Alabama
www.mcdowellknight.com

J. Blair Newman, Jr.
bnewman@mcdowellknight.com

Ransome R. Hare
rhare@mcdowellknight.com

Alabama

REGULATORY LIMITS ON CLAIMS HANDLING

Timing for Responses and Determinations

In the life, accident, and health insurance context, Alabama Insurance Regulation Chapter 482-1-124-.04 sets forth the relevant time requirements for handling claims. Some of the highlights of the regulation are as follows:

- After receiving notification of a claim, an insurer has 15 days to provide the insured with applicable forms, instruction, and reasonable assistance so that they can comply with the insurer's regulations for filing a claim.
- Claims processing must begin within 15 days from receipt of proof of loss.
- For life insurance claims, insurer must affirm or deny liability or inform claimant that claim is being processed within the time set forth in the policy, but no longer than 60 days from receipt of proof of loss.
- Undisputed claims shall be paid "within a reasonable time."
- If a claim is partially disputed, those undisputed portions shall be paid within 60 days of the determination that such claims are undisputed.
- Notification of a continued investigation shall be provided to the insurer every 45 days.
- A reply shall be made within 20 days of any written communications from insured.
- Written notice of a claim denial shall be sent to claimant within 15 days of the decision to deny the claim and the reasons for such denial shall be included in the notice.

Ala. Admin. Code § 482-1-124-.04.

In addition to the above-mentioned requirements, the reimbursement of health claims is governed by Alabama Code § 27-1-17. Both in-state and out-of-state insurers are subject to these provisions to the extent they receive, process, adjudicate, pay, or deny claims for healthcare services submitted for persons residing in Alabama or who receive such services in Alabama. Ala. Code § 27-1-17(a) (1975). The Code requires insurers to pay for services rendered by Alabama healthcare providers within 45 calendar days from receipt of a "clean written claim" or 30 calendar days upon receipt of a "clean electronic claim." *Id.* If the claim is denied or pending, the insurer must, within 45 calendar days for written claims and 30 calendar days for electronic claims, notify the healthcare provider or certificate holder of the reasons for denying or pending the claim, and what, if any, additional information is required to further process the claim. *Id.* The failure to comply with these time restraints can result in the payment of interest on the claim (at the rate of 1.5 percent per month prorated daily) to the healthcare provider. Ala. Code § 27-1-17(c) (1975). Once the necessary

information is received on the claim, the insurer must pay, deny, or otherwise adjudicate the claim within 21 calendar days from receipt of the information. Ala. Code § 27-1-17(a) (1975).

In the property and casualty context, Alabama Insurance Regulation Chapter 482-1-125 sets forth the relevant time requirements for handling claims. Some of the highlights of this regulation are as follows:

- Every insurer shall acknowledge receipt of a first party claim within 15 days.
- Claim forms and instructions shall be provided to a claimant within 15 days after the insurer receives first notice of a claim.
- The insurer shall reply within 15 days to any written communication from an insured which requests a response.
- After receiving a properly executed proof of loss, an insurer shall within 30 days (or other time as specified in the policy) advise the claimant of the status of the acceptance or denial of a claim by the insurer.
- If an insurer needs more time to investigate before making a decision, the claimant shall be so notified within 30 days (or other time as specified in the policy) after submission of proofs of loss, including the reason(s) why more time is needed.
- Every 45 days thereafter until a determination is made, the insurer must notify the claimant of the reason(s) why additional time is needed to investigate.
- If a written denial is requested, the insurer must mail a written denial within a reasonable time.
- Payment must be tendered by the insurer within 30 days (or other time as is stated in the policy) after acceptance of liability, reaching an agreement on the amount of the claim, and receipt of all documents necessary to consummate the settlement.

Ala. Ins. Reg. 482-1-125-.06, .07.

In addition to the above regulatory requirements, Alabama's common law recognizes that an unreasonable delay in the decision-making on a submitted claim may constitute a constructive denial for purposes of a breach of contract or bad faith action brought by the insured. *Congress Life Ins. Co. v. Barstow*, 799 So. 2d 931, 938 (Ala. 2001). The Southern District of Alabama has reaffirmed that an insurer's unreasonable delay in making a claim determination may constitute a constructive denial for purposes of a breach of contract or bad faith action. *Oliver v. M/V Barbary Coast*, 901 F. Supp. 2d 1340, 1348 (S.D. Ala. 2012). The court clarified that, "a plaintiff may establish a constructive denial by showing a passage of time so great the delay alone creates a denial or, a sufficient delay in payment coupled with some wrongful intent by the insurance company." *Id.*

Standards for Determination and Settlements

The Alabama Department of Insurance has enacted "minimum standards" for the investigation and disposition of life, accident, and health claims arising under policies or certificates of insurance issued pursuant to State law (some of which are listed above). Ala. Admin. Code § 482-1-124-.02; Ala. Admin. Code § 482-1-124-.04. Compliance with Section 503 of the Employee Retirement Income Security Act of 1974 ("ERISA"), and any regulations issued thereunder, constitute compliance with these regulations. Ala. Admin. Code § 482-1-124-.02(2).

In the property and casualty context, Alabama Insurance Regulation Chapter 482-1-125 also requires that denials include a reference to the policy provision, exclusion, or condition relied upon in denying the claim. Ala. Ins. Reg.

482-1-125-.07.

Special regulations also apply to automobile policies and fire policies on residential structures in Alabama. Ala. Ins. Reg. 482-1-125-.08, -.09. The automobile policy regulation provides that an insurer issuing an automobile policy providing for adjustment of losses on an actual cash value or replacement basis can apply one of the following methods: 1) offer a replacement automobile that is at least comparable; or 2) elect a cash settlement based upon actual cost, less any applicable deductible. Ala. Ins. Reg. 482-1-125-.08. The fire policy regulation provides that an insurer issuing a fire policy providing for adjustment of losses on an actual cash value basis can determine this cash value as the replacement cost of the property less depreciation. Ala. Ins. Reg. 482-1-125-.09. The insurer shall provide, upon request of the insured, a copy of all claim file worksheets detailing any and all deductions for depreciation. *Id.*

In most other areas, Alabama has left the policing of insurers and their claim handling practices to the common law currently embodied in the tort of bad faith first recognized in *Chavers v. National Security Fire & Casualty Co.*, 405 So. 2d 1 (Ala. 1981).

PRINCIPLES OF CONTRACT INTERPRETATION

Any ambiguities in an insurance contract must be construed liberally in favor of the insured. *Johnson v. Allstate*, 505 So. 2d 362, 365 (Ala. 1987). A corollary to this rule is that exceptions to coverage must be interpreted as narrowly as possible in order to provide maximum coverage to the insured. *Id.* However, courts are not at liberty to rewrite policies to provide coverage not intended by the parties. *Id.* (citing *Newman v. St. Paul Fire & Marine Ins. Co.*, 456 So. 2d 40, 41 (Ala. 1984)). In the absence of statutory provisions to the contrary, insurance companies have the right to limit their liability and write policies with narrow coverage. *Id.* (citing *United States Fid. & Guar. Co. v. Bonitz Insulation Co. of Ala.*, 424 So. 2d 669, 573 (Ala. 1982)). If there is no ambiguity, courts must enforce insurance contracts as written and cannot defeat express provisions in a policy, including exclusions from coverage, by making a new contract for the parties. *Id.* (citing *Turner v. United States Fid. & Guar. Co.*, 440 So. 2d 1026, 1028 (Ala. 1983)).

If an insurance policy is clear and unambiguous in its terms, then there is no question of interpretation and construction. *Am. & Foreign Ins. Co. v. Tee Jays Mfg. Co.*, 699 So. 2d 1226, 1228 (Ala. 1997). If an insurance policy is unclear and ambiguous in its terms, but not void for uncertainty, then it must be interpreted and construed under well-settled rules of construction applicable to all contracts. *Id.* It is the province of the court, not the jury, after duly considering the whole of the policy, to determine if it is uncertain or ambiguous in its terms. *Id.* The fact that parties interpret the insurance policy differently does not make the insurance policy ambiguous. *Tate v. Allstate Ins. Co.*, 692 So. 2d 822, 824 (Ala. 1997). While ambiguities or uncertainties in an insurance policy should be resolved against the insurer, ambiguities are not to be inserted by strained or twisted reasoning. *Kelley v. Royal Globe Ins. Co.*, 349 So. 2d 561, 563 (Ala. 1977). Where the parties disagree on whether the language in an insurance contract is ambiguous, a court should construe language according to the meaning that a person of ordinary intelligence would reasonably give it. *Western World Ins. Co. v. City of Tuscumbia*, 612 So. 2d 1159, 1161 (Ala. 1992). The issue of whether a contract is ambiguous or unambiguous is a question of law for the court to decide. *Phillips v. National Sec. Fire & Cas. Co.*, 59 So. 3d 711, 714 (Ala. 2010).

Where an insurance policy defines certain words or phrases, a court must defer to the definition provided by the policy, provided such definition is one that a person of ordinary intelligence would assign the word or phrase. *See St. Paul Fire & Marine Ins. Co. v. Edge Mem'l Hosp.*, 584 So. 2d 1316, 1322 (Ala. 1991). An undefined word or phrase in an insurance policy does not create an inherent ambiguity. To the contrary, where questions arise as to the meaning of an undefined word or phrase, the court should simply give the undefined word or phrase the same meaning that a person of ordinary intelligence would give it. *Id.*; *see also Carpet Installation & Supplies of*

Glenco v. Alfa Mut. Ins. Co., 628 So. 2d 560, 562-63 (Ala. 1993). The terms of an insurance policy should be given a rational and practical construction. *Green v. Merrill*, 308 So. 2d 702, 704 (Ala. 1975). A court must consider the policy as a whole and not consider the language in question in isolation. *Phillips*, 59 So. 3d at 714 (quoting *Nationwide Ins. Co. v. Rhodes*, 870 So. 2d 695, 697 (Ala. 2003)); *but see Owners Insurance Co. v. Keeble*, 584 F. Supp. 3d 1076, 1088 (M.D. Ala. 2022) (citing *Rhodes* but holding that "words of refinement" in a policy must be afforded due weight).

CONTRACT INTERPRETATION

Common Issues

1. Faulty Workmanship as an "Occurrence"

Pursuant to Alabama law, "faulty workmanship itself is not an occurrence." *FCCI Ins. Co. v. Capstone Process Systems, LLC*, 49 F. Supp. 3d 995, 998 (N.D. Ala. 2014) (quoting *Town & Country Property, LLC v. Amerisure Ins. Co.*, 111 So. 3d 699, 705 (Ala. 2011)). However, under a CGL policy in Alabama, "faulty workmanship may lead to an occurrence if it subjects personal property or other parts of the structure to 'continuous or repeated exposure' to some other 'general harmful condition' . . . and, as a result of that exposure, personal property or other parts of the structure are damaged." *Id*. As such whether faulty workmanship equates to an occurrence depends on the "nature of the damage" resulting from the faulty workmanship. *Id*.

In *FCCI*, the court held that neither the insured's faulty work – rubber installation – nor the resulting loss of use to its customer's machine was an "occurrence" under the insured's CGL policy. *Id*. at 1000. In rejecting the insured's argument, the court reasoned that "[i]n this case, the only harmful condition was the failure of the rubber installed by [the insured], which necessitated that the [machine] be taken offline and thus resulted in a loss of use." *Id*. In other words, "the faulty workmanship did not lead to any additional harmful condition; rather, the rubber failure was the only condition that led to the [machine] being taken offline." *Id*. As such, the court held that the faulty workmanship, by itself, was not an occurrence, and therefore the alleged "loss of use" was not covered under the policy. *Id*.

See also Shane Traylor Cabinetmaker, L.L.C. v. American Res. Ins. Co., Inc., 126 So. 3d 163, 167-68 (Ala. 2013) (holding that faulty woodwork was not an "accident" or "occurrence" where there were no allegations of additional damage to the properties as a result of the workmanship beyond the cost to repair and replace, and no damage resulting from continuous or repeated exposure to some *other* general harmful condition (i.e., a condition other than the contractor's allegedly defective work)) (emphasis in original) (internal quotations omitted); *U.S. Fid. & Guar. Co. v. Warwick Dev. Co.*, 446 So. 2d 1021 (Ala.1984) (insurance policy did not provide coverage for alleged faulty workmanship and noncomplying materials in the construction of plaintiff's residence when the alleged damage was confined to the residence itself because there was no occurrence).

But cf. Moss v. Champion Ins. Co., 442 So. 2d 26 (Ala. 1983) (finding an occurrence for CGL policy purposes where a contractor's poor work on a roof resulted in not just a poorly made roof, but also damage to the plaintiff's attic, interior ceilings, and some furnishings caused by rain); *U.S. Fid. & Guar. Co. v. Bonitz Insulation Co. of Ala.,* 424 So. 2d 569 (Ala. 1982) (holding that negligence in installing a roof did not prevent there from being an occurrence when it rained and leaked through the roof).

2. Does Your State Have an Anti-Indemnity Statute?

Yes, effective July 1, 2021, Alabama enacted a new statute, Ala. Code § 41-9A-3, which prohibits

certain indemnity provisions in "design professional" contracts and establishes a single standard of care for design professionals in Alabama (the "Statute"). For the purposes of the Statute, "design professional" is defined as "a person or entity who is licensed or authorized in this state to practice architecture, landscape architecture, surveying, engineering, interior design, or geology." Ala. Code § 41-9A-3(a).

> The Statute renders void and unenforceable any "design professional" contract provision which:
>
> (1) Requires the design professional to indemnify or hold harmless a contracting party, an indemnitee, or a third party against liability for damage other than liability for damage to the extent caused by, or in proportion to the extent the design professional participates in resolution of a claim based on, an act of negligence, recklessness, intentional tort, intellectual property infringement, or failure to pay a subconsultant or supplier that is committed by the design professional or the design professional's agent, consultant under contract, or other entity for which the design professional is legally liable.
>
> (2) Requires the design professional to defend a contracting party, an indemnitee, or a third party against a claim arising out of the rendering of or failure to render professional services by the design professional or its agents that is not otherwise covered by the design professional's policy of professional liability insurance.
>
> (3) Requires the design professional to list a party or any other person or entity as an additional insured on the design professional's policy of professional liability insurance.
>
> (4) Subjects the design professional to a standard of care different than that provided under subsection (d).

Id. § 41-9A-3(b). However, nothing in Section 41-9A-3(b) voids a provision in a design professional contract to the extent that it includes any or all of the following:

> (1) A requirement that the design professional list an additional insured on the design professional's general liability insurance policy, automobile liability insurance policy, or both, and provide coverage and any defense provided by those policies.
>
> (2) A provision for the reimbursement of a contracting party's or an indemnitee's reasonable attorney fees, damages, losses, injuries, or other litigation costs in proportion to the design professional's liability, or in proportion to the extent the design professional participates in resolution of a claim also made against the contracting party or indemnitee.
>
> (3) A provision or requirement not otherwise in conflict with subsection (b).

Id. § 41-9A-3(c). Such contracts shall require the design professional to perform the services "with the professional skill and care ordinarily provided by a competent design professional practicing under the same or similar circumstances and professional licenses as expeditiously as is prudent considering the ordinary professional skill and care of a competent design professional." *Id*. § 41-9A-3(d)(1). If any contractual standard of care in a design professional contract differs from that set forth above, the standard of care provided by the Statute shall govern. *Id*. § 41-9A-3(d)(2). However, parties may include and enforce conditions that "relate to the scope, fees, and schedule of a project that is subject to the contract, so long as the conditions are subject to the requirements of subsection (d)." *Id*. § 41-9A-3(e).

CHOICE OF LAW

Alabama law follows the traditional conflict-of-law principles of *lex loci contractus* and *lex loci delicti.* *Lifestar Response of Ala., Inc. v. Admiral Ins. Co.*, 17 So. 3d 200, 213 (Ala. 2009) (citing *Liberty Mut. Ins. Co. v. Wheelwright Trucking Co., Inc.*, 851 So. 2d 466 (Ala. 2002)). Under the principles of *lex loci contractus*, a contract is governed by the law of the jurisdiction within which the contract is made. *Id.* (citing *Cherry, Bekaert & Holland v. Brown*, 582 So. 2d 502 (Ala. 1991)). The substantive rights of the parties under the contract, including the issue of damages, are controlled by the law of the state where the contract is executed. *Shelter Mut. Ins. Co. v. Barton*, 822 So. 2d 1149, 1158 (Ala. 2001). Alabama has long recognized the right of parties to an agreement to choose the law of a particular state to govern the agreement (provided the other state's law is not contrary to Alabama policy). *Cherry, Bekaert & Holland v. Brown*, 582 So. 2d 502 (Ala. 1991). Under the principle of *lex loci delicti*, an Alabama court will determine the substantive rights of an injured party according to the law of the state where the injury occurred. *Lifestar Response of Ala., Inc.*, 17 So. 3d at 213 (citing *Fitts v. Minnesota Mining & Mfg. Co.*, 581 So. 2d 819 (Ala. 1991)).

DUTIES IMPOSED BY STATE LAW

Duty to Defend

1. Standard for Determining Duty to Defend

If the complaint against the insured alleges a covered accident or occurrence, then the insurer owes the insured a duty to defend even though the evidence may eventually prove that the gravamen of the complaint was not a covered accident or occurrence. Tanner v. State Farm Fire & Cas. Co., 874 So. 2d 1058, 1065 (Ala. 2003); but cf. Frankenmuth Mut. Ins. Co. v. Taylor Burton Co., Inc., No.: 2:22-cv-00224-RDP, 2022 WL 3588038, at *5 (M.D. Ala. Aug. 22, 2022) (holding that Tanner should not be read as requiring a complaint as a prerequisite for a duty to defend). If the complaint against the insured does not allege on its face a covered accident or occurrence, but the evidence proves one, then the insurer likewise owes the duty to defend. Id.; see also Penn. Nat'l Mut. Cas. Ins. Co. v. Roberts Bros., Inc., 550 F. Supp. 2d 1295, 1304 (S.D. Ala. 2008) (stating that a district court is not constrained to the allegations of the underlying complaint and may look to additional facts if they are proven by admissible evidence); Gunnin v. State Farm and Cas. Co., 508 F. Supp. 2d 998, 1002 (M.D. Ala. 2007) (same). The insurer owes a duty to defend unless (a) the complaint against the insured alleges neither a covered accident or occurrence or (b) the evidence in litigation against the insured fails to prove a covered accident or occurrence. Roberts Bros., 550 F. Supp. 2d at 1304 (citing Tanner v. State Farm Fire & Cas. Co., 874 So. 2d 1058, 1065 (Ala. 2003)). If there "is any uncertainty as to whether the complaint alleges facts that would invoke the duty to defend, the insurer must investigate the facts surrounding the incident that gave rise to the complaint in order to determine whether" it has such a duty. Blackburn v. Fid. & Deposit Co. of Maryland, 667 So. 2d 661, 668 (Ala. 1995). When a complaint alleges both acts covered under the policy and acts not covered, the insurer is under a duty to at least defend the allegations covered by the policy. Id. at 670.

When an insurer elects not to defend, it does so at its peril. Insurers should be mindful that if a plaintiff changes its theory of liability from that contained in the original complaint and asserts a claim against the insured that is covered by the policy, it is very possible that the insurer will have to step in and defend the insured and/or pay the judgment. Ladner & Co., Inc. v. Southern Guar. Ins. Co., 347 So. 2d 100, 104 (Ala. 1977).

2. Issues with Reserving Rights

Generally, an insurer is obligated to indemnify an insured if it undertakes to defend the insured without first reserving the right to deny coverage. *Shelby Steel Fabricators, Inc. v. United States Fid. & Guar. Ins. Co.*, 569 So. 2d 309, 311 (Ala. 1990). This general rule is limited as an insurer may avoid operation of the rule by giving notice that the assumption of the defense is not a waiver of its right to deny coverage. *Id.*

Where the insurer assumes the defense of an insured under a reservation of rights, the insurer does so under an enhanced obligation of good faith toward its insured. *L & S Roofing Supply Co. v. St. Paul Fire & Marine Ins. Co.*, 521 So. 2d 1298, 1303-04 (Ala. 1987). The enhanced duty of good faith has implications both for the insurer and for defense counsel retained by the insurer. First, the insurer's conduct must meet four specific criteria: 1) a thorough investigation of the accident and the claimed injuries and damages; 2) the retention of competent defense counsel of the insured, with the understanding that the insured is defense counsel's only client; 3) fully informing the insured of the reservation-of-rights defense, of the progress of the suit, of developments relevant to the insured's coverage, and of all settlement offers made by the insurer; and 4) refraining from any action demonstrating greater concern for the insurer's monetary interest than for the insured's financial risk. *Id.* at 1303. Similarly, defense counsel must understand that he/she only represents the insured, and owes a duty of full and ongoing disclosure to the insured, including disclosure of potential conflicts of interest, information relevant to the lawsuit's defense, and all offers of settlement as they are presented. *Id.*

Where an insurer fails to meet the obligations imposed by the enhanced duty of good faith, the insurer may be obligated to indemnify the insured for any liability in the underlying action. *See Shelby Steel Fabricators*, 569 So. 2d 309 at 312. An insurer's breach of the enhanced duty of good faith may also give the insured the right to retain counsel of its choice at the expense of the insurer. *State Farm Fire & Cas. Co v. Myrick*, No. 2:06-cv-359-WKW, 2008 WL 2020447, at *3 (M.D. Ala. May 9, 2008).

Under Alabama law, a separate contractual cause of action for the breach of the enhanced obligation of good faith exists independently of the duty to indemnify. *Id.* at *4.

State Privacy Laws; Insurance Regulatory Issues; Arbitration/Mediation

Alabama recognizes that an insurance company's list of policyholders is confidential, proprietary information to which a litigant has no right except through court-ordered discovery. *Ex parte Nat'l Sec. Ins. Co.*, 773 So. 2d 461, 464 (Ala. 2000). Alabama does allow the discovery of the identity of other insureds in a proper case. *See Ex parte John Alden Life Ins. Co.*, 999 So. 2d 476, 484-86 (Ala. 2008) (finding that although the identity of an insurer's policyholders is confidential and proprietary information, the identity of other insureds is discoverable in actions alleging fraud provided that the discovery request is narrowly tailored to the fraud allegation). In some instances, restrictions have been placed upon the manner in which counsel may contact these other customers. *See id.* at 487 (restricting the method by which counsel could contact customers); *Ex parte Henry*, 770 So. 2d 76, 81-82 (Ala. 2000) (same).

Alabama has promulgated regulations largely mirroring the protections of the federal Gramm-Leach-Bliley Act. *See* Ala. Ins. Reg. 482-1-122; Ala. Ins. Reg. 482-1-126. These regulations protect against the unauthorized

disclosure of non-public personal information and personally identifiable financial information, as well as require initial and periodic privacy notices to an insurer's customers.

1. Criminal Sanctions

Under Alabama law, criminal eavesdropping, a class A misdemeanor, is a criminal offense when a person "intentionally uses any device to eavesdrop, whether or not he is present at the time." ALA. CODE § 13A-11-31 (1975).

Section 27-3A-2 outlines the purposes of the insurance statute which includes, in pertinent part, that "utilization review agents maintain the confidentiality of medical records in accordance with applicable laws." ALA. CODE § 27-3A-2(5) (1975). Section 34-26-2 governs confidentiality relations between licensed psychologists, licensed psychiatrists, or licensed psychological technicians and their clients. ALA. CODE § 34-26-2 (1975). But see Marks v. Tenbrunsel, 910 So. 2d 1255, 1259-60 (Ala. 2005) (holding that the privilege granted by § 34-26-2 is impliedly repealed by the immunity provision of the child-abuse reporting statutes, found at § 26-14-9).

Section 34-24-504 governs the confidentiality of patient medical records as follows:

> Any licensee licensed under the provision of this article shall comply with all laws, rules, and regulations governing the maintenance of patient medical records, including patient confidentially requirements, regardless of the state where the medical records of any patient within this state are maintained.

ALA. CODE § 34-24-504 (1975).

Under section 22-11A-2, the disclosure of information relating to reportable diseases is required. ALA. CODE § 22-11A-2 (1975). The Alabama Supreme Court has stated that the statutory requirement that a physician disclose information regarding his or her HIV and AIDS patients, including names and addresses, was not an unconstitutional invasion of privacy because the State has a legitimate interest in the prevention of spreading HIV and AIDS, which was supported by the fact that the disclosure was limited to representatives of the state having responsibility for the health of the community. Middlebrooks v. State Bd. Of Health, 710 So. 2d 891, 893 (Ala. 1998).

Section 22-11A-69 governs confidentiality related to records, proceedings, deliberations, and documents in the investigation and review of any infected health care worker. ALA. CODE § 22-11A-69 (1975). Section 22-11A-22 renders medical records of persons infected with sexually transmitted diseases as confidential and imposes a penalty for their unauthorized release. ALA. CODE § 22-11A-22 (1975). Section 22-21-30 addresses the disclosure of information as follows:

> Information received by the State Board of Health through on site inspections by the State Licensing Agency is subject to public disclosure and may be disclosed upon written request. Information received through means other than inspection will be treated as confidential and shall not be directed publicly except in a proceeding involving the question of licensure or revocation of license.

ALA. CODE § 22-21-30 (1975).

2. The Standards for Compensatory and Punitive Damages

"An award of damages for mental anguish generally is not allowed in breach-of-contract actions in Alabama." Bowers v. Wal-Mart Stores, Inc., 827 So. 2d 63, 68-69 (Ala. 2001); Barko Hydraulics, LLC v. Shepherd, 167 So. 3d 304, 312 (Ala. 2014). While some exceptions to this rule have evolved through precedent, an express exception has not been recognized for the breach of an insurance contract; thus, mental anguish damages are generally not recoverable. See also Bashir's Inc. v. Sharif, No. 2:09–CV–536–RDP, 2012 WL 3637582, *4, n.3 (N.D. Ala. April 22, 2012) ("Recovery for mental anguish damages is permitted for breach of contract only in a narrow range of cases involving contracts which create especially sensitive duties . . ."). But see Independent Fire Ins. Co. v. Lunsford, 621 So. 2d 977, 979 (Ala. 1993) (permitting mental anguish damages when the insurance involved a mobile home) and Pate v. Rollison Logging Equip., Inc., 628 So. 2d 337, 345 (Ala. 1993) (reversing summary judgment for insurers on breach of contract and mental anguish claims in light of recent Lunsford holding and the "special nature of credit disability insurance"). Generally, the only exception to rule arising in the insurance context has been limited to cases involving home insurance. See Ruiz de Molina v. Merritt & Furman Ins. Agency, Inc., 207 F.3d 1351, 1360-61 (11th Cir. 2000).

A plaintiff may, however, recover punitive damages for the bad faith failure to pay a claim under an insurance contract. See, e.g., Nationwide Mut. Ins. Co. v. Clay, 525 So. 2d 1339, 1344 (Ala. 1987) (affirming award of 1.25 million in punitive damages when disability insurer failed to pay $46,000 in benefits and holding that "punitive damages need not necessarily bear any particular relationship to compensatory damages."). See also Intercontinental Life Ins. Co. v Lindblom, 598 So. 2d 886 (Ala. 1992). In order to sustain a claim for punitive damages, a plaintiff must prove at least "nominal damage and that the acts complained of were committed with malice, willfulness, or wanton and reckless disregard of the rights of others." Gulf Atl. Life Ins. Co. v. Barnes, 405 So. 2d 916, 925 (Ala. 1981). See also ALA. CODE § 6-11-20 (1975) (providing definitions of "malice" and "wantonness" for punitive damages purposes).

Punitive damages are also capped by statute. See ALA. CODE § 6-11-21 (1975). In cases not involving physical injury or wrongful death, punitive damages are generally limited to three times the compensatory damages or $500,000, whichever is greater. ALA. CODE § 6-11-21(a). In civil actions for physical injury, punitive damages are limited to three times the compensatory damages or $1,500,000, whichever is greater. ALA. CODE § 6-11-21(d). Of course, punitive damages must be proportionate to the compensatory award, consistent with the standards set forth by the U.S. Supreme Court.

Compensatory damages cannot be apportioned in cases of multiple defendants and an indivisible injury, as contribution is not permitted among joint tortfeasors. See, e.g., Tatum v. Schering Corp., 523 So. 2d 1042, 1048 (Ala. 1988) (J. Houston dissenting). The plaintiff may collect from any or all of the tortfeasors. Id. at 1048-49. Alabama courts have also applied the rule of non-apportionment of punitive damages, under which damages are fixed regardless of the culpability of individual tortfeasors. See, e.g., CP & B Enter., Inc. v. Mellert, 762 So. 2d 356, 361 (Ala. 2000) (citing Robbins v. Forsburg, 257 So. 2d 353, 355 (1971)). C.f. Reserve Nat. Ins. Co. v. Crowell, 614 So. 2d 1005, 1009-10 (Ala. 1993) (noting the punitive damages cap does not represent apportionment of damages among joint tort-feasors but holding that the punitive damages cap can apply to one tort-feasor and not the other where one tort-feasor's conduct excepts it from the statutory cap). However, a valid indemnification agreement will be upheld, despite the general rule that indemnification, like contribution, is not available. Humana Med. Corp. v. Bagby Elevator Co., 653 So. 2d 972, 974 (Ala. 1995). See also Holcim, Inc. v. Ohio Cas. Ins. Co., 38 So. 3d 722, 726 (Ala. 2009) (discussing contribution and indemnity agreements).

3. Insurance Regulations to Watch

Alabama's Insurance Code is contained at § 21-1-1, et seq. Alabama's Insurance Regulations are available online. Two regulations that warrant careful attention are Chapters 482-1-131, entitled "Life Insurance Disclosure Regulation," and 482-1-132, entitled "Advertisements of Life Insurance and Annuities Regulation," each of which address a broad range of group and individual life insurance. The regulations address vocabulary, form, content, disclosure, and penalty provisions.

In addition, Chapter 482-1-097-.04, entitled "NAIC Accounting Practices and Procedures and Insurer Reporting Requirements," requires that all financial reports to the Department of Insurance be submitted on the NAIC forms and be prepared in accordance with NAIC practices and procedures except when in conflict with other Alabama laws or regulations.

4. State Arbitration and Mediation Procedures

The Alabama Arbitration Act gives an arbitrator's award the effect of a jury verdict, including the right to appeal. ALA. CODE § 6-6-12 (1975); ALA. CODE §§ 6-6-14-15 (1975). Although rarely cited in recent decisions, these arbitration provisions remain a valid pre-dispute tool for inclusion in contracts. For a comparison of the Alabama Arbitration Act and the Federal Arbitration Act, see Lanier v. Old Republic Ins. Co., 936 F. Supp. 839 (M.D. Ala. 1996).

The Alabama Civil Court Mediation Rules provide for strictly voluntary mediation by agreement of the parties or by the court sua sponte. No record of the proceedings is made (Rule 12), parties can terminate the proceedings at any time by withdrawal (Rule 13), and they bear the costs equally (Rule 15). The "mandatory" pre-trial mediation provisions of Alabama Code § 6-6-20 make mediation mandatory, either by agreement, upon motion of the parties, or by the court sua sponte. ALA. CODE § 6-6-20(b) (1975). Parties can be subjected to sanctions for failure to mediate if ordered. ALA. CODE § 6-6-20(c). Mediation rules and practices can vary by local circuit.

5. State Administrative Entity Rule-Making Authority

Title 27 of the Code of Alabama governs insurance. Section 27-2-17 empowers the Commissioner of the Department of Insurance to make rules and regulations. ALA. CODE § 27-2-17(a) (1975). Moreover, Section 27-2-19 allows the Commissioner to bring suit to enforce the provisions of Title 27. ALA. CODE § 27-2-19 (1975). If the Commissioner determines that a provision of Title 27 has been violated which may result in a criminal prosecution, the Commissioner is directed to provide this information to the Attorney General to institute such action. Id.

Section 27-2-33 outlines the Commissioner's authority as follows:

The Commissioner of Insurance is empowered to place an insurance company under supervision, after a hearing thereon, by appropriate order, for the following reasons:

- When an insurance company has been notified under the provisions of Section 27-27-41 of impairment or deficiency of assets and given 60 days to make good the impairment;
- A determination by the commissioner that an insurer is impaired or insolvent;
- A determination by the commissioner that an insurer's condition is such as to render the continuation of its business hazardous to its policyholders following an examination of

the operations and financial condition of an insurer by the commissioner;

- Any of the grounds for rehabilitation or liquidation of domestic insurers set forth in Sections 27-32-6 and 27-32-7.

ALA. CODE § 27-2-33 (1975).

EXTRACONTRACTUAL CLAIMS AGAINST INSURERS: ELEMENTS AND REMEDIES

Bad Faith Claim Handling/Bad Faith Failure to Settle Within Limits

3. First Party

Coverage of the underlying claim is a prerequisite to a claim for bad faith. State Farm Fire & Cas. Co. v. Slade, 747 So. 2d 293, 317-318 (Ala. 1999). An insured "who cannot prove [that it is] entitled to benefits under an insurance policy cannot recover on a bad-faith claim." Congress Life Ins. Co. v. Barstow, 799 So. 2d 931, 937 (Ala. 2001).

Alabama allows insurers "a broad range of freedom to thoroughly evaluate claims and to decline payment in non-meritorious cases." Attorneys Ins. Mut. of Ala., Inc. v. Smith, Blocker & Lowther, P.C., 703 So. 2d 866, 871 (Ala. 1996). Bad faith is limited to those instances where the insurer, "without debatable excuse, either fails to process a claim or, on processing, fails to pay a claim for benefits as provided by the policy." Waldon v. Cotton States Mut. Ins. Co., 481 So. 2d 340, 341 (Ala. 1985).

"The plaintiff asserting a bad-faith claim bears a heavy burden." Shelter Mut. Ins. Co. v. Barton, 822 So. 2d 1149, 1154 (Ala. 2001); see also LeFevre v. Westberry, 590 So. 2d 154, 158-59 (Ala. 1991). An insurer is not liable in bad faith "simply because it has exercised poor judgment or has been negligent"; rather, bad faith "must be supported by evidence showing that the insurer had no reasonably arguable ground for disputing the insured's claim or that it acted with an intent to injure." Aplin v. Am. Sec. Ins., Co., 568 So. 2d 757, 760 (Ala. 1990).

The tort of bad faith in Alabama originated in Chavers v. National Security Fire & Casualty Co., 405 So. 2d 1 (Ala. 1981). Shortly after Chavers was decided, the Alabama Supreme Court summarized the elements of a bad faith refusal case as: 1) "an insurance contract between the parties and a breach thereof by the defendant;" 2) "an intentional refusal to pay the insured's claim;" 3) "the absence of any reasonably legitimate or arguable reason for that refusal;" 4) "the insurer's actual knowledge of the absence of any legitimate or arguable reason;" and 5) "if the intentional failure to determine the existence of a lawful basis is relied upon, the plaintiff must prove the insurer's intentional failure to determine whether there is a legitimate or arguable reason to refuse to pay the claim." Nat'l Sec. Fire & Cas. Co. v. Bowen, 417 So. 2d 179, 183 (Ala. 1982).

Bad faith cases diverged into two categories: normal or ordinary bad faith cases, and the unusual or extraordinary bad faith cases. Slade, 747 So. 2d at 306. The plaintiff must prove the first four elements for a "normal" case; the fifth element only applies to the "abnormal" bad-faith case. State Farm & Cas. Co. v. Brechbill, 144 So. 3d 248, 257–58 (Ala. 2013). The Alabama Supreme Court has made it clear that the "normal" and "abnormal" types refer solely to the methods of

establishing a bad-faith refusal to pay an insurance claim, not to two separate torts. Id.

In either type of case, the plaintiff must prove that the claim was covered under the contract of insurance in order to maintain a claim for bad faith. Slade, 747 So. 2d at 317-18. In order to prevail on a "normal" bad faith refusal to pay claim, a plaintiff "must be entitled to a directed verdict on the underlying contract claim." Hilley v. Allstate Ins. Co., 562 So. 2d 184, 190 (Ala. 1990). In other words, "the underlying contract claim must be so strong that the plaintiff would be entitled to a pre-verdict judgment as a matter of law." Barton, 822 So. 2d at 1155. If evidence produced by either the insured or the insurer "creates a fact issue with regard to the contract claim, the bad faith claim must fail." Kizziah v. Golden Rule Ins. Co., 536 So. 2d 943, 946 (Ala. 1988).

In the "abnormal" case, a plaintiff must show: "(1) that the insurer failed to properly investigate the claim or to subject the results of the investigation to a cognitive evaluation and review; and (2) that the insurer breached the contract for insurance coverage with the insured when it refused to pay the insured's claim." Barstow, 799 So. 2d at 936-37 (quoting Slade, 747 So. 2d at 318). In recent years, the Alabama Supreme Court has reduced the burden on the insured in the "abnormal" case. Instead of requiring proof of an insurer's intentional failure to investigate the claim to determine its validity, courts merely require proof that the insurer recklessly failed to conduct an adequate investigation of the facts and to submit those facts to a thorough review. See Employees' Benefit Ass'n v. Grissett, 732 So. 2d 968, 976 (Ala. 1998). Direct proof of such reckless bad faith is unnecessary; instead, bad faith can be inferred from evidence that the insurer showed reckless indifference to facts submitted in the claim investigation. Id. Still, the insured "must prove that a proper investigation would have revealed that the insured's loss was covered under the terms of the contract." Slade, 747 So. 2d at 318.

In Singleton v. State Farm Fire & Cas. Co., the Alabama Supreme Court once again articulated the distinction between "normal" and "abnormal" bad faith cases. 928 So. 2d 280, 283 (Ala. 2005). In "normal" bad faith cases, the insured must show the absence of any reasonably legitimate or arguable reason for denial of a claim; in "abnormal" cases, by contrast, bad faith can consist of: 1) "intentional or reckless failure to investigate a claim"; 2) "intentional or reckless failure to properly subject a claim to a cognitive evaluation or review"; 3) "the manufacture of a debatable reason to deny a claim"; or 4) "reliance on an ambiguous portion of a policy as a lawful basis for denying a claim." Id.; see also White v. State Farm Fire & Cas. Co., 953 So. 2d 340, 347-49 (Ala. 2006). However, the Alabama Supreme Court subsequently clarified that "[t]he existence of an insurer's lawful basis for denying a claim is a sufficient condition for defeating a claim that relies upon the fifth element of the insurer's intentional or reckless failure to investigate." Brechbill, 144 So.3d at 258 (emphasis in original); see also Walker v. Life Ins. Co. of North America, 59 F.4th 1176, 1187 (11th. Cir. 2023) ("More recent precedent . . . suggests that where a 'normal' bad-faith claims fails under the directed verdict standard so does an 'abnormal' bad-faith claim.") (citing White and Breechbill).

4. Third-Party

Alabama does not recognize a right of an underlying third-party to assert a claim for bad faith in the handling of a third-party insurance claim. *Stewart v. State Farm Ins. Co.*, 454 So. 2d 513, 514 (Ala. 1984) (affirming lower court's judgment that the third-party beneficiary of an insurance contract cannot maintain a direct action against the tortfeasor's insurer). "[T]he tort of bad faith

refusal to pay is that refusal to pay valid claims made by the insured of his insurance carrier." *Id.* Once a third-party obtains a judgment against the insured, however, the third-party stands in the shoes of the insured and may bring an action against the insurer as a judgment creditor under Alabama's direct action statute. *See* Ala. Code § 27-23-2 (1975).

Fraud

Alabama Code § 6-5-101 (1975) states that "[m]isrepresentations of a material fact made willfully to deceive, or recklessly without knowledge, and acted on by the opposite party, if made by mistake and innocently and acted upon the opposite party, constitute legal fraud." Ala. Code § 6-5-101 (1975). Generally speaking, the four elements of fraud are 1) a misrepresentation of a material fact; 2) made willfully to deceive or recklessly without knowledge; 3) which was reasonably relied on by the plaintiff under the circumstances; and 4) which caused damage to the plaintiff as a proximate consequence. *See, e.g., State Farm Fire & Cas. Co. v. Slade*, 747 So. 2d 293, 323 (Ala. 1999). A fraud action accrues when a plaintiff has detrimentally relied on the fraud, *i.e.*, when legally cognizable damage occurs. *Ex parte Haynes Downard Andra & Jones, LLP*, 924 So. 2d 687, 694 (Ala. 2005). However, the statute of limitations for a fraud action does not begin to run until the discovery of the facts constituting fraud are discovered or should have been discovered through the exercise of reasonable diligence. *Geans v. McCaig*, 512 So. 2d 1308, 1309 (Ala. 1987). A fraud action is viable only if the plaintiff's damage is a proximate result of his reasonable reliance upon the defendant's misrepresentation. *Bosarge Offshore, LLC v. Compass Bank*, 943 So. 2d 782, 786 (Ala. 2006). Rule 9(b) of the Alabama Rules of Civil Procedure requires that "[i]n all averments of fraud or mistake, the circumstances constituting fraud or mistake shall be stated with particularity." Ala. R. Civ. P. 9(b).

Suppression is fraud by silence or breach of a defendant's duty to disclose. An actionable claim of fraudulent suppression requires proof that: "(1) that the defendant had a duty to disclose the existing material fact; (2) that the defendant suppressed that existing material fact; (3) that the defendant had actual knowledge of the fact; (4) that the defendant's suppression of the fact induced the plaintiff to act or refrain from acting; and (5) that the plaintiff suffered actual damage as a proximate result." *Ex parte Hugine*, 256 So. 3d 30, 56 (Ala. 2017) (internal quotations omitted); *see also State Farm Fire & Cas. Co. v. Owen*, 729 So. 2d 834, 837 (Ala. 1998). The Alabama Supreme Court's decision in Owen discusses in detail the duty to disclose. *Id.*

Intentional or Negligent Infliction of Emotional Distress

In order to maintain a claim for the tort of intentional infliction of emotional distress, a plaintiff in Alabama must demonstrate that 1) the defendant either intended to inflict emotional distress or knew or should have known that emotional distress was likely to result from its conduct; 2) the defendant's conduct was extreme and outrageous; and 3) the defendant's conduct caused emotional distress so severe that no reasonable person could be expected to endure it. *See, e.g., Stabler v. City of Mobile*, 844 So. 2d 555, 560 (Ala. 2002) (quoting *Callens v. Jefferson County Nursing Home*, 769 So. 2d 273, 281 (Ala. 2000)). The conduct must go "beyond all possible bounds of decency" and "be regarded as atrocious and utterly intolerable in a civilized society." *Anderson v. Gentry*, 577 So. 2d 1261, 1264 (Ala. 1991) (quoting *Am. Road Serv. Co. v. Inmon*, 394 So. 2d 361 (Ala. 1980)) (internal quotation marks omitted).

Alabama does not recognize a tort for negligent infliction of emotional distress. *Taylor v. Alabama*, 95 F. Supp. 2d 1297, 1318 (M.D. Ala. 2000), *Gideon v. Norfolk S. Corp.*, 633 So. 2d 453, 453-54 (Ala. 1994). However, a physical injury is no longer a prerequisite to the recovery of damages for emotional distress in a negligence action. *Woodley v. City of Jemison*, 770 So. 2d 1093, 1097 (Ala. Civ. App. 1999) (citing *Flagstar Enterprises, Inc. v. Davis*, 709 So. 2d 1132 (Ala. 1997)). Rather than establish a new cause of action, the Alabama Supreme Court has

"adhered to the principle that negligently causing emotional distress is part and parcel of the traditional tort of negligence." *Id.* (quoting *AALAR, Ltd., Inc. v. Francis*, 716 So. 2d 1141 (Ala. 1998)).

State Consumer Protection Laws, Rules and Regulations

Alabama Code § 8-19-1 *et seq.* generally governs unlawful trade practices in Alabama. Ala. Code § 8-19-1 *et. seq.* (1975) ("Deceptive Trade Practices Act"). However, "[a]ny person or activity which is subject to the provisions of the Alabama Insurance Code, Title 27" is exempt from the Deceptive Trade Practices Act. Ala. Code § 8-19-7(3) (1975).

Title 27, Chapter 12 of the Alabama Code governs trade practices in the insurance context. Section 27-12-1 describes the purpose of trade practice laws:

- The purpose of this chapter is to regulate trade practices in the business of insurance in accordance with the intent of congress as expressed in the Insurance Regulation Act by defining, or providing for the determination of, all such practices in this state which constitute unfair methods of competition or unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined.

Ala. Code § 27-12-1(a) (1975). Section 27-12-2 generally prohibits unfair competition, etc., as follows:

- No person shall engage in this state in any trade practice which is defined in this chapter as, or determined pursuant to this chapter to be, an unfair method of competition or an unfair or deceptive act or practice in the business of insurance.

Ala. Code § 27-12-2 (1975). Section 27-12-11 provides as follows:

- No person shall make or permit any unfair discrimination between individuals of the same class and equal expectation of life in the rates charged for any contract of life insurance or of life annuity, or in the dividends or other benefits payable thereon or in any other of the terms and conditions of such contract.
- No person shall make or permit any unfair discrimination between amount of premium, policy fees or rates charged for any policy or contract of disability insurance, or in the benefits payable thereunder, or in any of the terms or conditions of such contract or in any other manner whatever.

Ala. Code § 27-12-11 (1975). Section 27-12-21 addresses the Commissioner of Insurance's authority relating to unfair trade practices, in pertinent part, as follows:

- Whenever the commissioner has reason to believe that any person engaged in the business of insurance is engaging in this state in any method of competition, or in any act or practice in the conduct of such business which is not defined in this trade practices law, that such method of competition is unfair or that such act or practice is unfair or deceptive and that a proceeding by him in respect thereto would be to the interest of the public, he may issue and serve such person a statement of the charges in that respect and a notice of a hearing thereon to be held at a time and place fixed in the notice, which shall not be less than 10 days after the date of the service thereof . . . .

Ala. Code § 27-12-21(a) (1975). In certain instances, the Commissioner's findings can be appealed to the circuit court within 30 days. Ala. Code § 27-12-22 (1975).

DISCOVERY ISSUES IN ACTIONS AGAINST INSURERS

Discoverability of Claims Files Generally

In the ordinary case filed against an insured, materials in the insurer's claim file that were prepared in anticipation of litigation or that otherwise constitute work product are generally not discoverable. *Ex parte State Farm Mut. Auto Ins. Co.*, 386 So. 2d 1133, 1135-37 (Ala. 1980); *see also Ex parte Flowers*, 991 So. 2d 218, 221-22 (Ala. 2008); *Ex parte Nationwide Mut. Fire Ins. Co.*, 898 So. 2d 720, 723 (Ala. 2004). Once the issue is raised, the burden is on the insurer to establish the privilege or protection. *Flowers*, 991 So. 2d at 221. The insurer must show that from the nature of the case, it reasonably concluded that its insured would be sued. *State Farm*, 386 So. 2d at 1136. In making its determination, courts will "analyze the facts of each case while using phrases like whether litigation was the 'primary motivating factor' in generating a document, or whether the document, or whether the document was created 'because of' actual or expected litigation." *Lewis v. Ameriprise Ins. Co.*, No. 16-00111-B, 2017 WL 890101, at *3 (S.D. Ala. Mar. 6, 2017). Alabama does, however, allow discovery of available insurance coverage and its limits. Ala. R. Civ. P. 26(b)(3); *Ex parte Badham*, 730 So. 2d 135, 137 (Ala. 1999).

Because of the "heavy burden" imposed on a plaintiff in a fraud or bad faith action, and "because the defendant in a fraud or bad faith action is usually the sole possessor of the information needed to meet the burden of proof, wider latitude is given to a fraud plaintiff or a bad faith plaintiff during the discovery process." *Ex parte O'Neal*, 713 So. 2d 956, 959 (Ala. 1998).

Discoverability of Reserves

Few Alabama courts have considered the discoverability of an insurer's reserve information. "The discoverability of reserve information depends on the particular facts of the case and the purpose for which it is sought." *Multi-Marketing, Inc. v. Travelers Indem. Co. of America*, No. 7:08-CV-00268-LSC, Doc. 47 at 2 (N.D. Ala., order entered Jan. 15, 2009) (order granting insured's motion to compel reserve information to the extent it was not otherwise privileged). "As a general matter, if reserve information is sought for the purpose of establishing the value of a claim, then it is not discoverable. … However, when reserve information goes to a party's subjective state of mind, as in a bad faith claim for instance, it generally is discoverable." *Id.* In that case, the court granted discovery of the reserve information as it found that the plaintiff might be able to show that the insurer "acted in bad faith by offering a settlement that was substantially lower than its estimation of the potential value of the claim." *Id.* at 3. Therefore, "as with most discovery matters, the court will look to the justifications given supporting the request for this information as well as whether the discovery of reserves is likely to lead to admissible evidence." *Id.*; *but see Graham & Co. v. Liberty Mut. Fire Ins. Co.*, No. 2:14-cv-02148, 2016 WL 1319697, at *6 (N.D. Ala., Apr. 5, 2016) (denying motion to compel reserve information because such information "is outside the scope of discovery because the information is not relevant as to what an insurer thought of the merits of a claim").

Discoverability of Existence of Reinsurance and Communications with Reinsurers

This specific topic has not been addressed by Alabama courts. However, Rule 26(b)(2) of the Alabama Rules of Civil Procedure provides:

> A party may obtain discovery of the existence of and contents of any insurance agreement under which any person carrying on an insurance business may be liable to satisfy part or all of a judgment which may be entered in the action or to indemnify or reimbursement for payments made to satisfy the judgment.

Ala. R. Civ. P. 26(b)(3); *Badham*, 730 So. 2d at 136. Under this provision, Alabama courts will allow discovery of available insurance coverage and its limits. *Badham*, 730 So. 2d at 136-37. In a first-party bad faith action for

failure-to-defend, this information may likely be discoverable given the broad latitude of discovery afforded in such cases. *O'neal*, 713 So. 2d at 959.

Attorney/Client Communications

The mere fact that an insured settles an underlying lawsuit against it and then sues an insurer for bad faith will not operate as a blanket waiver of the attorney-client privilege in the underlying litigation, even where attorney's fees are claimed as an item of damages. *See Ex parte State Farm Fire & Cas. Co.*, 794 So. 2d 368, 376 (Ala. 2001). Nor will an opinion letter from counsel to an insurer be automatically discoverable, rather, as it is work product, the party seeking to discover such item must show that it had a substantial need for it and could not obtain its equivalent by other means without undue hardship. *Ex parte Great Am. Surplus Lines, Ins. Co.*, 540 So. 2d 1357, 1361 (Ala. 1989).

DEFENSES IN ACTIONS AGAINST INSURERS

Misrepresentations/Omissions: During Underwriting or During Claim

An insurer is statutorily entitled under Alabama Code § 27-14-7 to rescind an insurance policy due to "misrepresentations, omissions, concealment of facts and incorrect statements" in an application which is either (1) fraudulent, (2) material either to the acceptance of the risk or to the hazard assumed, or if (3) the insurer in good faith would either have not issued the policy, or would have issued the policy with different coverage or at a different rate if the true facts were known. See, e.g., Alfa Life Ins. Corp. v. Lewis, 910 So. 2d 757, 761 (Ala. 2005). Section 27-14-7 applies to renewal policies as well as original policies. Ex parte Quality Cas. Ins. Co., 962 So. 2d 242, 246 (Ala. 2006). It is essential that an insurer relying upon this section must demonstrate that it was following established underwriting standards, rather than a subjective decision it made after the claim was filed. Loyal Am. Life Ins. Co. v. Mattiace, 679 So. 2d 229, 234 (Ala. 1996).

Alabama Code § 27-14-7 requires no particular mental state or intent and the insurer may rescind the policy even if the insured lacked any intent to deceive. Caribbean I Owners' Ass'n, Inc. v. Great Am. Ins. Co., 600 F. Supp. 2d 1228, 1240 (S.D. Ala. 2009). See also Duren v. Nw. Nat'l Life Ins. Co., 581 So. 2d 810, 813 (Ala. 1991). However, if the policy language allows voidance only for an intentional misrepresentation, then the policy language controls, and the insurer loses the protection of the statute. Nationwide Mut. Fire Ins. Co. v. Guster Law Firm, LLC, 944 F. Supp. 2d 1116, 1126-27 (N.D. Ala. 2013). In addition, acceptance of premiums after the insurer learns of grounds for forfeiture or rescission may preclude such forfeiture or rescission. Henson v. Celtic Life Ins. Co., 621 So. 2d 1268, 1277 (Ala. 1993). Furthermore, this code section requires that for life insurance and annuity contracts, a recission on the part of the insurer be accompanied by a payment into court of all premiums paid on the policy or contract. ALA. CODE. 27-14-7(b) (1975). Finally, the Alabama Supreme Court has found that contesting a policy on the basis of misrepresentations in an insurance application is an affirmative defense. This means the defense can be waived if not properly pleaded. Patterson v. Liberty Nat. Life Ins. Co., 903 So. 2d 769, 779 (Ala. 2004).

Failure to Comply with Conditions

A condition requiring reasonable notice of claims will be enforceable. *See Pharr v. Cont'l Cas. Co.,* 429 So. 2d 1018, 1019 (Ala. 1983). To determine the reasonableness of a delay in giving notice to an insurer, the court traditionally considers the length of, and reasons for, the delay. *Id.*; *see also Frankenmuth Mut. Ins. Co. v. Brown's*

Clearing, Inc., 579 F. Supp. 3d 1324, 1336 (M.D. Ala. 2022) (collecting cases and holding that late notice may be unreasonable or reasonable "as a matter of law" depending on the circumstances of the case). The question of whether there was prejudice as a result of the delay is immaterial to this determination, where, as in this case, the giving of reasonably timely notice is made a condition precedent to any action against the insurer. *Pharr*, 429 So. 2d at 1020; *see also Nationwide Mut. Fire Ins. Co. v. Estate of Files*, 10 So. 3d 533, 535 (Ala. 2008).

Further, a condition requiring an insured's cooperation is also enforceable. "[A]n insurer's obligation to pay or to evaluate the validity of an insured's claim does not arise until the insured has complied with the terms of the contract with respect to submitting claims." *Nationwide Ins. Co. v. Nilsen*, 745 So. 2d 264, 266-67 (Ala. 1998).

Challenging Stipulated Judgments: Consent and/or No-Action Clause

When an insurer who could defend under a reservation of rights instead denies coverage and absolutely refuses to defend an action against an insured when it could do so under a reservation of rights, the legal consequence of such refusal is that it waives the provisions of the policy against a settlement by the insured and becomes bound to pay the amount of any settlement made in good faith, plus expenses and attorneys' fees. *See Liberty Mut. Ins. Co. v. Wheelwright Trucking Co., Inc.*, 851 So. 2d 466, 475–76 (citing *Stone Building Co. v. Star Elec. Contractors, Inc.*, 796 So. 2d 1076, 1091-92 (Ala. 2000)).

Preexisting Illness or Disease Clauses

Alabama uses the term "preexisting sickness" as well as "preexisting illness or disease." The courts addressing a question of whether a condition is covered by the policy at issue must first examine the language of the policy itself, which is crucial in determining what is to be considered a preexisting illness or disease. In order to preclude coverage for a preexisting illness, the insurer must demonstrate that the illness fits within the definition in the policy at issue and that the insurer did not waive the exclusion for such illness. *Peek v. Reserve Nat'l Ins. Co.*, 585 So. 2d 1303, 1306-07 (Ala. 1991) (examining definition; trial court erred in granting summary judgment because insurer did not provide sufficient evidence that condition predated contract and was thus excluded).

It is also worth noting that Alabama has held that when the plaintiff alleges fraud by the insurer concerning coverage, presumably including for preexisting illnesses, the mere payment of unnecessary premiums, even when no claim has been filed or denied, constitutes sufficient injury to sustain a cause of action against the insurer. *Boswell v. Liberty Nat. Life Ins. Co.*, 643 So. 2d 580, 582 (Ala. 1994). However, such a claim is not ripe if based on a speculative injury. *Allstate Life Ins. Co. v. Parker*, 951 So. 2d 682, 688-89 (Ala. 2006). The Alabama Supreme Court has characterized the requisite injury as an insured "paying for something that did not exist and would never exist." *Donoghue v. Am. Nat. Ins. Co.*, 838 So. 2d 1032, 1038 (Ala. 2002) (reversing dismissal where insured claimed he was told life insurance plan would have separate retirement fund that in reality did not exist).

Statutes of Limitations and Repose

While there is only a two-year statute of limitations under Alabama law for causes of action based upon tort theories, contract actions carry a six-year statute of limitation. Ala. Code § 6-2-34 (1975); Ala. Code § 6-2-38 (1975). Causes of action for fraud do not accrue until the discovery by the plaintiff of the facts constituting the fraud. Ala. Code § 6-2-3 (1975). For cases addressing the application of Alabama's twenty-year statute of repose in the context of insurance cases, see *Am. Gen. Life and Accident Ins.* Co. v. Underwood, 886 So. 2d 807 (Ala. 2004), and *Ex parte Liberty Nat'l Life Ins. Co.*, 825 So. 2d 758 (Ala. 2002). Alabama's rule of repose is not subject to a discovery rule. *Id.*

TRIGGER AND ALLOCATION ISSUES FOR LONG-TAIL CLAIMS

Trigger of Coverage

Triggers are discussed extensively in *Attorneys Mut. Ins. of Alabama v. Smith, Blocker & Lowther, P.C.,* 703 So. 2d 866 (Ala. 1996). In a claims-made policy, a carrier agrees to assume liability for any errors, including those made before the inception of the policy, as long as the claim is made during the policy period. *Id.* at 869. An occurrence policy provides coverage for any acts or omissions that arise during the policy period, even though the claim is made after the policy has expired. *Id.* While the event that triggers coverage under a claims-made policy is transmission of notice of the claim, an occurrence policy can be triggered in several ways. *Id*.

As a general rule, "the time of an occurrence of an accident within the meaning of an indemnity policy is not the time the wrongful act is committed, but is instead the time the complaining party was actually damaged." *Wheelwright Trucking Co.*, 851 So. 2d at 481.

A condition can persist for such a length of time that it no longer constitutes an occurrence. *See United States Fidelity and Guar. Co. v. Bonitz Insulation,* 424 So. 2d 569, 573 (Ala. 1982) (policy issued to roofing contractor after roof had already leaked for four years did not cover damage from leaks).

Allocation Among Insurers

Allocation among insurers at the same coverage level will be on a pro rata basis based upon the proportion of the limits of each insurer to the total available insurance at that level. *Nationwide Mut. Ins. Co. v. Hall*, 643 So. 2d 551, 561 (Ala. 1994).

CONTRIBUTION ACTIONS

Claim in Equity vs. Statutory

Alabama courts have recognized that in the absence of an "other insurance" clause, and where the "insurer has paid the entire amount of a loss, that insurer may seek contribution from other insurers liable for the same risk, even though the policy of the insurer seeking pro rata contribution contains no provision for apportionment of liability." Hall, 643 So. 2d at 561 (emphasis in original) (citing 2 Warren Freedman, Richards on Insurance § 175, at 637 (5th ed. 1952)). The court in Hall noted that the "right to contribution is based on the principle that the paying insurer paid a debt owed by another, concurrently liable insurer." Id. at 561-62. The right to contribution under Alabama law is purely equitable in nature.

Elements

In order to succeed on a claim for contribution under Alabama law, it is not enough to merely show that an insured is covered by two policies. Penn. Nat. Mut. Cas. Ins. Co. v. Progressive Direct Ins. Co., No. 6:14-CV-0038, 2015 WL 5719178, at *9 (N.D. Ala., Sep. 30, 2015). Rather, "the two policies must insure against the same risk, but they must also provide coverage for the same insurable interest." Employers' Mut. Cas. Ins. Co. v. Hughes,

780 F. Supp. 2d 1204, 1208 (N.D. Ala. 2011). Stated differently, the insurers must both "have primary insurance coverage of the same insurable interest, subject matter, and risk." Progressive, 2015 WL at * 9 (emphasis in original); Hall, 643 So. 2d at 561-62 ("[When] an insurer insures two or more parties for the same insurable interest, subject matter, and risk and when it pays the limits of its policy to one of its insureds with notice of an adverse claim by another, the insurer does so at its own risk and may be liable to another insurer of its insured for a pro rata contribution, notwithstanding the limits of its policy.") (citing Gray v. Holyoke Mut. Fire Ins. Co., 302 So.2d 104 (Ala. 1974)).

"When prorating liability in accordance with the policy limits of two or more insurance policies covering the same insurable interest, subject matter, and risk, an insurer generally should not be compelled to contribute more than the limits fixed in its policy." Hall, 643 So. 2d at 562 (citing 16 Mark S. Rhodes, Couch Cyclopedia of Insurance Law, § 62:15, at 447 (1983)). Further, "contribution," as distinguished from "subrogration" under Alabama law, "is not available between an excess insurer and a primary insurer." Progressive, 2015 WL at * 9 (citing Hall, 643 So. 2d at 561).

DUTY TO SETTLE

Alabama recognizes tort actions for bad faith and negligence arising out of an insurer's wrongful failure to settle a claim against its insured. *Waters v. Am. Cas. Co. of Reading, Pa.*, 73 So. 2d 524, 529-30 (Ala. 1954). When an opportunity to settle within policy limits is presented, the law imposes a duty on the insurer to use ordinary care to ascertain the facts on which its performance depends (if it has not already). *Id.* at 529. The cause of action arising out of a failure to settle a third-party claim made against the insured does not accrue unless and until the claimant obtains a final judgment in excess of the policy limits. *Evans v. Mut. Assur., Inc.*, 727 So. 2d 66, 67 (Ala. 1999).

To succeed on a claim alleging negligent failure to settle, a plaintiff must establish that, considering all the circumstances, the insurer, in deciding not to settle the claim, failed to exercise reasonable or ordinary care, *i.e.*, such care as a reasonably prudent insurer would have exercised under the same or similar circumstances. *Mut. Assur., Inc. v. Schulte*, 970 So. 2d 292, 296 (Ala. 2007). To succeed on a claim alleging bad-faith failure to settle, a plaintiff must establish that the insurer had no "lawful basis" for failing to do so, *i.e.*, no "legitimate or arguable reason for failing to pay the claim." *Id.*; *but see Thomas v. Auto-Owners Ins. Co.*, 479 F. Supp. 3d 1218, 1232-34 (dismissing language creating the "arguable reason" standard as dicta).

The fact that a verdict comes back in excess of policy limits is not, standing alone, evidence of negligence. *State Farm Mut. Auto. Ins. Co. v. Hollis*, 554 So. 2d 387, 390 (Ala. 1989). To hold otherwise would require insurers to be prophets. *Id*. Further, it is well-settled that a claim for bad faith failure to settle does not exist where the insured is subject to no personal loss from a final judgment. *Penn. Nat'l Mut. Cas. Ins. Co. v. Ipsco Steel (Alabama), Inc.*, No. 07-0524-WS-M, 2008 WL 192972, at *3 (S.D. Ala., Jan. 21, 2008) (citing *Federal Ins. Co. v. Travelers Cas. And Sur. Co.*, 843 So. 2d 140, 144 (Ala. 2002)).

LH&D BENEFICIARY ISSUES

In general, the designation of the beneficiary of an insurance policy is governed by the provisions of the policy itself. *See, e.g. Gibson v. Henderson*, 459 So. 2d 845, 847 (Ala. 1984) (citing *Williams v. Williams,* 438 So. 2d 735 (Ala. 1983)); *but see Baxley v. Jackson Nat. Life Ins. Co.*, No. 2:20-cv-265-CLM, 2021 WL 4990061, *2 (N.D. Ala. Oct. 26, 2021 (noting that pursuant to Alabama Supreme Court precedent, "an insured may change his beneficiary without abiding by the specified requirements of his policy, which require that the change be noted

thereon, if the insurer waives the requirement . . . .") (quoting *Murphy v. Gibson*, 465 So. 2d 373, 376 (Ala. 1985)). When a beneficiary may be changed at the will of the insured or owner, the beneficiary is said to have a "mere expectancy and no vested right or interest therein." *Flowers v. Flowers*, 224 So. 2d 590, 597 (Ala. 1969), *superseded by statute*, Ala. Code § 30-4-17 (1975), *as recognized in Aderholt v. McDonald*, 226 So. 3d 648, 650-52 (Ala. 2016). Alabama law suggests that the converse is also true in that an irrevocable beneficiary of an insurance policy has a vested interest in the proceeds. *See, e.g.*, *Woodham v. Woodham*, 387 So. 2d 150, 151 (Ala. 1980).

Change of Beneficiary

Changes to an insurance beneficiary are also governed by the provisions of the policy. Midland Nat. Life Ins. Co. v. Turner, No. 06-0429, 2007 WL 2254419, *4 (S.D. Ala. Aug. 2, 2007) (citing Ziegler v. Cardona, 830 F. Supp. 1395, 1398 (M.D. Ala. 1993)). Strict compliance with the terms of the policy for changing the beneficiary is generally required, absent proof of "excusing circumstances." Gibson, 459 So. 2d at 848 (citing 5 Couch on Insurance 2d § 28:76 (1960)). For example, if a policy requires that "the insured actually file the forms before the change is effective," and the forms are not filed by the insured or someone acting at his or her direction, the terms of effectuating a change of beneficiary have not been met. Id. at 849 (internal citations omitted).

Nevertheless, strict compliance with the policy's requirements for changing the beneficiary may be waived by the insurer. Ziegler, 830 F. Supp. at 1398 (citing Whitman v. Whitman, 142 So. 2d 413 (1932)). Alabama courts have held that "where an insurance company interpleads life insurance proceeds, it is held to have waived its requirements under the policy relative to a change of beneficiary." Id.; Midland, 2007 WL 2254419 at *4.

Effect of Divorce on Beneficiary Designation

A recent Alabama supreme court opinion held that Alabama Code § 30-4-17, a statute adopted from the Uniform Probate Code, was the controlling statute on this issue. Blalock v. Sutphin, 275 So. 3d 519, 523-24 (Ala. 2018). That statute provides that "the divorce or annulment of a marriage" revokes any revocable "disposition or appointment of property made by a divorced individual to his or her former spouse in a governing instrument . . . ." ALA. CODE § 30-4-17 (1975). Interpreting that statute, the court held that "it created a prospective default rule, i.e., that a divorce effectively revokes any revocable beneficiary designation in favor of the former spouse, absent further action by the policyholder." Id. at 525.

The above statute and holding seemingly supersedes prior Alabama cases holding that divorce itself has no legal effect on the designation of insurance beneficiaries. See Walden v. Walden, 686 So. 2d 345, 346 (Ala. Civ. App. 1996); Flowers v. Flowers, 284 Ala. 230 (Ala. 1969). Those prior cases held that despite a divorce, "where the insured fails to exercise his right to change the beneficiary, and absent a clause in the policy that conditions the rights of a beneficiary-spouse on the continuance of the marriage, the right of the beneficiary to receive proceeds pursuant to the policy is not affected by a divorce." Id. (citing Flowers, 224 So. 2d at 590). However, the two analyses can be distinguished based on whether the governing instrument was revocable or irrevocable.

Additionally, a divorce decree or judgment requiring the maintenance of an insurance policy for the benefit of the ex-spouse or a child will be upheld. In such an event, the ex-spouse or child is considered to have a "vested equitable interest" in the insurance proceeds and the insured will have "no power to name anyone else as beneficiary." McKinnis v. McKinnis, 564 So. 2d 451, 452-53 (Ala. Civ. App. 1990); See also Hanner v. Metro Bank and Protective Life Ins. Co., 952 So. 2d 1056, 1063-64 (Ala. 2006) (overruled on other grounds).

Additional complications can arise, for example, when an insured purchases a replacement policy for the one in existence at the time of the divorce judgment, when children reach the age of majority, or if the insured re-marries an ex-spouse. See, e.g., Ray v. Ohio Nat. Life Ins. Co., 537 So. 2d 915 (Ala. 1989) (Insured's remarriage to

former wife terminated interest that previously named beneficiaries had in life policy under agreement which was incorporated into divorce judgment), but see Rivera v. Sanchez, 297 So. 3d 1242, 1247 (Ala. Civ. App. 2019) (holding that mere cohabitation of previously divorced parents is not sufficient to establish a basis for applying of the principles set forth in Ray); Whitten v. Whitten, 592 So. 2d 183 (Ala. 1991); Frawley v. U.S. Steel Min. Co., 496 So. 2d 731 (Ala. 1986).

INTERPLEADER ACTIONS

Availability of Fee Recovery

Alabama federal courts generally permit "[t]he award of costs and attorneys' fees in an interpleader action." *Prudential Ins. Co. of Am. v. Boyd*, 781 F.2d 1494, 1497 (11th Cir. 1986). "The usual practice is to tax the costs and fees against the interpleader fund." *Id.* at 1498. The decision to award fees "is discretionary" and there is "no right" to "recover and costs and attorney's fees." *Life Investors Ins. Co. America v. Childs*, 209 F. Supp. 2d 1255, 1256 (M.D. Ala. 2002). The Eleventh Circuit has enumerated three reasons justifying the award of attorneys' fees and costs in interpleader actions: (1) an "interpleader action often yields a cost-efficient resolution;" (2) "the stakeholder in the asset often comes by the asset innocently;" and (3) "fees for the stakeholder typically are quite minor and therefore do not greatly diminish the value of the asset." *In re Mandalay Shores Co-op. Hous. Ass'n, Inc.*, 21 F.3d 380, 383 (11th Cir. 1994). However, Alabama federal courts hold that fee recovery is not warranted "when a stakeholder's interpleader claim arises out of the normal course of business." *Id.*; *Childs*, 209 F. Supp. at 1256. Moreover, "[t]his standard typically is applied to insurance companies. *Mandalay*, 21 F.3d at 383.

In Alabama state courts, fee recovery is governed by Alabama Rule of Civil Procedure 22. Under Rule 22(c), "the court may allow to one or more of the parties a reasonable sum or sums for counsel fees and disbursements payable out of said fund or property." Ala. R. Civ. P. 22(c). However, no such allowance shall be made unless it is claimed in the complaint or answer. *Id.* As with the federal rule, the decision to impose fees "is at the discretion of the trial court." *Youngblood v. Bailey*, 459 So. 2d 855, 861 (Ala. 1984). Any attorney's fee allowed by the trial court must be charged against the fund and not against one of the claimants. *Union Springs Tel. Co. v. Renfroe*, 620 So. 2d 649, 651 (Ala. 1993). For example, in *Renfroe*, the Alabama Supreme Court denied a company's claim to attorney's fee because there was "no money or tangible property" from which a fee could be awarded. *Id.*

Differences in State vs. Federal

Federal interpleader actions proceed under 28 U.S.C. §§ 2361, 1335, and 1397 or Federal Rule of Civil Procedure 22. Interpleader actions filed in Alabama state court proceed under Alabama Rule of Civil Procedure 22. Federal Rule of Civil Procedure 67 and Alabama Rule of Civil Procedure 67 govern the deposit of interplead funds into court.

Statutory interpleader, under 28 U.S.C. § 1335, provides an independent basis for federal court jurisdiction. The statute requires minimal diversity of citizenship to be present among the claimants. Id. Additionally, the amount in controversy must equal or exceed $500 and the stakeholder must deposit with the court the amount in controversy or post a bond at the time of filing the complaint. Id. Under 28 U.S.C. § 1397, venue for statutory interpleader is proper in any district where a claimant resides. Furthermore, 28 U.S.C. § 2361 provides for nationwide service of process and grants federal courts the authority to discharge the stakeholder from liability and enjoin the claimants from further litigation. Conversely, in interpleader actions under Federal Rule of Civil

Procedure 22, there must be an independent basis of federal jurisdiction such as diversity or federal question. Progressive Specialty Ins. Co. v. Hanson, No. 2:12-cv-734, 2012 WL 5966638, *1 (M.D. Ala. Nov. 28, 2012) (citing Perkins State Bank v. Connolly, 632 F. 2d 1306, 1310 n. 3 (5th Cir. 1980)).

Interpleader actions (Federal Rule of Civil Procedure 22 and Alabama Rule of Civil Procedure 22) proceed similarly as "[t]he Alabama Rule is patterned after [Federal] Rule 22." Poss v. Franklin Fed. Sav. & Loan Ass'n of Russellville, Ala., 455 So. 2d 9, 11 (Ala. 1984). There are two noteworthy differences between Federal Rule 22 and Alabama Rule 22. First, Alabama Rule 22(b) expressly provides for the stakeholder's release from liability following deposit or delivery. Ala. R. Civ. P. 22(b). The Federal Rule 22 does not contain a similar provision. Fed. R. Civ. P. 22. However, the same is accomplished by case law in federal interpleader actions. Ohio Nat. Life Assur. Corp. v. Langkau ex rel. Estate of Langkau, 353 F. App'x 244, 248 (11th Cir. 2009). Likewise, Alabama Rule of Civil Procedure 22(c), which provides for attorneys' fees, has no counterpart in the federal rules. Again, federal case law provides for an award of fees and costs. See, e.g., Prudential, 781 F.2d at 1497; Childs, 209 F. Supp. at 1256; Mandalay, 21 F.3d at 382-83.

[1] Alabama Department of Insurance, Administrative Code, Chapter 482, *available at* http://alabamaadministrativecode.state.al.us/docs/ins/index.html (last visited May 12, 2021); Alabama Department of Insurance website, "laws, bulletins, regulations" link, *available at* http://www.aldoi.gov/Legal/ (last visited May 12, 2021).

[1] Civil Court Mediation Rules, Alabama Center for Dispute Resolution website, *available at* https://www.alabamaadr.org/web/CourtADR/Court_Civil.php (last visited May 12, 2021).