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Client Alert

Insurance Coverage & Recovery Practice Group

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Recent Georgia Coverage Decisions Affecting Policyholders

The Georgia Supreme Court recently issued three pro-policyholder decisions that provide policyholders with clarity about the scope of damages available under certain types of policies, and guidance on how insurers should respond to coverage claims in their "reservation of rights" or denial of coverage letters. The Eleventh Circuit also recently reaffirmed Georgia's adherence to the pro-insurer rule that under Georgia law, an insurer is not required to show that it was prejudiced by a policyholder's failure to comply with the notice provisions of a policy in order to deny coverage for late notice, although the court suggested that policyholders may be able to offer justifications for untimely notice.

While mostly favorable to insureds, these decisions highlight the need for risk managers and in-house counsel to engage experienced coverage counsel to provide assistance during insurance policy negotiations and early on during the insurance claims process.

In *Royal Capital Development LLC v. Maryland Casualty Co.*, --- S.E.2d ---, No. S12Q0209, 2012 WL 1909842 (Ga. May 29, 2012), the Georgia Supreme Court held that property insurance policies may cover both the cost of repairs and diminution in value.

- In *Royal Capital*, a building owner sought coverage for repair costs and post-repair diminution in value after its building was damaged by nearby construction. The insurer acknowledged that repair costs were covered by the policy, but refused to provide coverage for the policyholder's alleged losses attributable to diminution in value.

- The Georgia Supreme Court had previously ruled in *State Farm Mut. Auto. Ins. Co. v. Mabry*, 274 Ga. 498 (2001) that an automobile insurer must pay for any diminution in value of the repaired vehicle in addition to the repair costs, but had not specified whether its decision was limited to automobile insurance policies. Thus, in *Royal Capital*, the Eleventh Circuit certified the question of whether a property insurance policy may similarly cover losses for diminution in value.

- Deciding that question in the affirmative, the Georgia Supreme Court noted that the objective of awarding damages is to place an injured party in the position it would have occupied if the loss had never occurred. Consistent with this general principle, the measure of

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damages in Georgia cases involving damage to real property is generally the difference in value before and after the injury. Georgia damages law also recognizes that if repairing the defects to property alone will not fully compensate the injured party, it may be appropriate to award damages for both the cost of repair and diminution in value.

- The court concluded that these general damages rules apply with equal force in the context of coverage under property insurance policies. It explained that where "[an] insurance policy, drafted by the insurer, promises to pay for the insured's loss; what is lost when physical damage occurs is both utility and value; therefore, the insurer's obligation to pay for the loss includes paying for any lost value."

- In extending its ruling in *Mabry* to the property insurance context, the Georgia Supreme Court has bolstered the ability of businesses and homeowners to be made whole following any type of property loss, including a catastrophic loss to commercial buildings and machinery.

In *Hoover v. Maxum Indemnity Co.*, --- S.E.2d ---, Nos. S11G1681, S11G1683, 2012 WL 2217040 (Ga. June 18, 2012) (reconsideration denied, July 26, 2012), the Georgia Supreme Court clarified the purpose of reservation of rights letters in Georgia and held that insurers that deny their duty to defend and disclaim coverage cannot also reserve their right to assert new coverage defenses later.

- In *Hoover*, an employee sustained a serious brain injury due to an accident at work and sued his employer for negligence. After the employer tendered the claim to its CGL insurer, the insurer disclaimed coverage under the policy and refused to provide a defense, citing the policy's Employer Liability Exclusion. The insurer's denial of coverage letter also purported to reserve the right to assert that "coverage for this matter may be barred or limited to the extent the insured has not complied with the notice provisions under the policy," as well as "the right to disclaim coverage on any other basis that may become apparent as this matter progresses and as [the insurer] obtains additional information."

- After obtaining a $16.4 million negligence judgment against the employer, the employee filed suit against the employer's insurer pursuant to an assignment of claims. In response, the insurer asserted a late notice defense and moved for summary judgment on that basis. The trial court granted that motion, and its decision was affirmed by the Georgia Court of Appeals.

- On appeal, the Georgia Supreme Court reversed, holding that the insurer waived its right to assert a defense based on untimely notice because it did not deny coverage on that basis when it first denied coverage on the Employer Liability Exclusion. In reaching this holding, the court clarified that the purpose of reservation of rights letters authored by insurers under Georgia law is as follows:

> "A reservation of rights does not exist so that an insurer who has *denied coverage* may continue to investigate to come up with additional reasons on which the denial could be based if challenged. Rather, a reservation of rights exists to protect both the insurer and the insured by allowing an insurer who is uncertain of its obligations under the policy to undertake a defense while reserving its rights to ultimately deny coverage following its investigation or to file a declaratory judgment to determine its obligation."

Based on this reasoning, the court concluded that the insurer's denial of coverage letter could not also reserve the right to raise new coverage defenses at some later date. Because the insurer failed to assert late notice in its denial letter, it waived the right to assert a late notice defense.

- In holding that an insurer cannot both deny a claim outright and also attempt to reserve its rights to assert other unspecified coverage defenses in the future, the *Hoover* decision should increase the likelihood that even where coverage defenses may exist, insurers in Georgia will still offer policyholders a defense, subject to a clearly-worded reservation of rights letter that places the policyholder on notice of any potential coverage defenses.

In *American Empire Surplus Lines Ins. Co. v. Hathaway Development Co., Inc.*, 288 Ga. 749 (2011), the Georgia Supreme Court held that a CGL policy may cover unforeseen property damage when it arises from a contractor's faulty work.

- In *Hathaway*, a general contractor sued its plumbing subcontractor for negligent plumbing work at three job sites. The contractor sought to recover the cost of repairs, as well as the costs associated with repairing water and weather damage to surrounding properties.

- After a default judgment was entered against the subcontractor, the general contractor sought payment from the subcontractor's insurer. The subcontractor's insurer denied liability, asserting that Hathaway's claim was not covered under the subcontrator's CGL policy because it did not arise out of an "occurrence," defined by the policy as "an accident, including continuous or repeated exposure to substantially the same, general harmful conditions." The issue before the Georgia Supreme Court was whether the subcontractor's negligent workmanship could be deemed an "accident."

- Because the term "accident" was not defined in the policy, the court looked to commonly accepted definitions of the term, such as "an unexpected happening without intention or design," and held that even though the subcontractor's acts were performed intentionally, the ***result*** of these acts -- in this case substantial damage to surrounding properties -- was unexpected and unintended. The court reasoned that the seminal inquiry in determining whether there has been an "occurrence" is not whether the acts themselves were deliberate, but whether the effect of the acts was the result that the insured intended or expected. Based on this reasoning, the court concluded that the subcontractor's work was an "occurrence" under the policy, and therefore was covered under the policy.

Despite these recent pro-policyholder rulings, in *OneBeacon America Insurance Co. v. Catholic Diocese of Savannah*, No. 11-14557, 2012 WL 1939104 (11th Cir. May 30, 2012), the Eleventh Circuit recently reaffirmed the longstanding rule in Georgia that a failure to strictly comply with notice provisions in insurance policies can defeat coverage, even in the absence of prejudice to the insurer. However, the court left the door open to policyholders that can provide justification for untimely notice.

- In *OneBeacon*, a lawsuit alleging vicarious liability for an employee's actions was filed against the Catholic Diocese of Savannah in April 2006, but the Diocese did not notify its insurer OneBeacon of the suit until January 2008 when it located policies that might provide coverage. OneBeacon eventually agreed to defend its insured subject to a reservation of rights, but after the underlying lawsuit settled in 2009, it filed a declaratory judgment

action against the Diocese in 2010, asserting late notice and various other coverage defenses. The trial court granted OneBeacon's motion for summary judgment because it determined that the Diocese failed to comply with the policy's notice provision.

- On appeal, the Diocese argued that OneBeacon waived its coverage defenses by failing to immediately file a declaratory judgment action after the Diocese contested OneBeacon's coverage positions. The Eleventh Circuit acknowledged that under Georgia law, in some circumstances an insurer may waive coverage defenses if it fails to immediately pursue declaratory relief. But the court also explained that to find waiver, the policyholder must suffer prejudice – such as a default – due to the insurer's delay. Because the Diocese had not been prejudiced in this manner by OneBeacon's delay, the court found that OneBeacon had not waived its right to pursue its coverage defenses.

- Further, in affirming the district court's refusal to excuse the Diocese's late notice, the court noted that a conclusory affidavit from the Diocese's lawyer that failed to provide any details about the reasons for the Diocese's 21-month delay in providing notice was insufficient as a matter of law to create an issue of fact on whether there was any justification for the late notice. However, the court declined to find that a 21-month delay is always unreasonable as a matter of Georgia law, suggesting that policyholders faced with extenuating circumstances – such as an extended hospital stay after an accident – may be able to offer justifications for untimely notice.

- Finally, contrary to the majority rule in most jurisdictions, the court reaffirmed that in Georgia, an insurer is not required to show that it was prejudiced by the late notice in order to deny coverage under Georgia law. Thus, notwithstanding the Diocese's argument that OneBeacon was not prejudiced by the untimely notice, the court affirmed the trial court's grant of summary judgment for OneBeacon.

- *OneBeacon America* underscores the importance of promptly providing notice of claims to insurers. Because untimely notice may serve as an absolute bar to an insurer's defense and coverage obligations in Georgia -- even if the insurer cannot demonstrate that it was prejudiced by the alleged late notice -- it is critical to promptly notify insurers and consult experienced coverage counsel in the event of a claim.

We work closely with our clients and their risk managers to ensure their insurance affords adequate protection, and we have assisted many businesses with collecting from their insurers and maximizing coverage for losses arising from unexpected claims.