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The 1st Party Report
A PROPERTY AND INSURANCE UPDATE
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CONSTRUCTION CORNER: SLANDER OF TITLE?

By David C. King

On all too many occasions, my construction clients have come to me about an inaccurate lien filed against their property. They are seeking a quick and just fix to what is an extremely unfair encumbrance upon their land. They can bond off the lien or bring a potentially lengthy and expensive declaratory judgment suit. The owner can also wait one year until the lien expires. But can't they also make the lien filer liable for damages resulting from such an inaccurate claim? Unfortunately, in all but the most egregious cases, they cannot.

In Georgia, O.C.G.A. § 51-9-11 provides the only clear, legal relief a property owner has once his property has been liened, and that relief is hard to get. "The owner of any estate in lands may bring an action for libelous or slanderous words which falsely or maliciously impugn his title if any damage accrues to him therefrom." This section gives rise to a cause of action commonly known as "slander of title," which is extremely difficult to prove. In order to recover for slander of title, a plaintiff land-owner must not only prove it owns the property and a lien was filed (which are both easily proved), but also prove that other substantive elements are met: (1) the lien claim was known to be false when made; (2) the claim was malicious; and (3) that the owner sustained special damages.

Falsity

At first glance, the requirement that the plaintiff prove the lien was known to be false at the time it was filed appears simple to prove, but it can often be difficult. The plaintiff must prove that the lien is false ***and*** that the claimant was ***aware*** of its falsity at the time it was filed. The lien claimant is not likely to admit that he knew that the lien was false at the time he filed it, so the plaintiff will typically be forced into proving that the lien claimant was aware of circumstances that "should have" alerted him that the lien was false. While not an insurmountable burden, this poses problems in situations where the lien claimant has at least an arguable basis for asserting his lien.

Malice

An owner must also prove that the inaccurate lien was filed with malice, i.e., a "reckless disregard of the law or a person's legal rights" and/or an "intent to injure." This is inherently a subjective inquiry that will require the plaintiff to "get into the head" of the lien claimant and prove the requisite intent before a jury.

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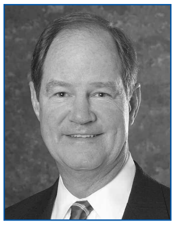
CHANGING THE RULES IN THE MIDDLE OF THE GAME

By Michael H. Schroder



The language of insurance policies in Georgia and in most other states is pre-approved by the State Insurance Commissioner. The insurance commissioner is empowered to require that certain provisions be changed before a policy form is approved for use in the state. For example, the Georgia Insurance Commissioner has recently threatened to require homeowners policies to allow more than the usual one-year contractual suit limitation. However, this would apply only to policies issued or renewed after a certain date.

What if the insurance commissioner or the legislature decides that it wants to change the rules in the middle of the game? That is exactly what happened in Louisiana with the recent Hurricane Katrina and Hurricane Rita claims. Almost one year after Hurricane Katrina, the Louisiana Insurance Commissioner and the state legislature teamed up to require all companies insuring property in Louisiana to extend the contractual suit limitations period contained in their policies to allow an insured two years to file a lawsuit as a result of a Hurricane Katrina or Hurricane Rita claim. Most insurance policies issued in Louisiana legally require an insured to file suit within one year after the date of loss, which is in accord with Louisiana law.

This raises a valid question: Is it legal for a legislature to alter the written terms of a contract retroactively? If the legislature can change one provision of a contract, can it change any other, such as the flood exclusion? There is no question that the Louisiana legislators would have been very popular if they had required homeowners insurers to cover damage caused by hurricane storm surge or flooding after the broken levees in New Orleans. What prevents them from doing so?

The answer is the Contract Clause of the United States Constitution, which provides that "No state shall… pass any… law impairing the Obligation of Contracts." The purpose of the clause, as noted by this country's first Chief Justice, was to prevent legislative interference with contracts, a power that in Colonial times "had been used to such an excess by the state legislatures, as to break in upon the ordinary intercourse of society, and destroy all confidence between man and man." *Ogden v. Saunders*, 25 U.S. 213 (1827).

Aware of this constitutional restraint, the Louisiana Legislature mandated that the State Attorney General immediately file an action to establish the constitutionality of the statute that retroactively changed the contractual suit limitation. That action resulted in a

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Special Damages

A landowner can recover only such special damages as he "actually sustained" and which are "traceable to the slanderous lien." This test has proven difficult, and there are a number of cases that illustrate Georgia courts' skepticism over such special damages.

For example, in *Daniel v. Johnson*, 191 Ga. App. 70, 381 S.E.2d 87 (1989), a plaintiff did not meet the special damages requirement when he provided no basis for the $5,000 of damages alleged. Simply noting the frustration and difficulty the lien caused, without proving a specific monetary injury, did not meet the special damages requirement. Likewise, in *Hicks v. McLain's Building Materials*, 209 Ga. App. 191, 433 S.E.2d 114 (1993), the generalized allegation of the plaintiff that she and her husband had trouble obtaining credit as a result of the lien was insufficient to establish special damages.

Proving special damages can therefore be very difficult. Some actual amount of monetary damage must be specifically linked to the lien, and such damage must be proved plainly, fully, and distinctly. Further, attorneys' fees incurred prosecuting the claim do not qualify as "special damages." Instead, there must be proven financial damage to the owner above and beyond the costs of the suit itself.

With these requirements, it is difficult to prevail on a slander of title case in this state. As another option, an owner can always bring a declaratory judgment action to have a court declare the lien invalid. Those cases, however, can be lengthy and costly, and they will often subject the owner to a counter-suit. An owner might be able to recover his attorneys' fees spent in a declaratory judgment action if he can show that filer's failure to withdraw the lien was "frivolous," but every court has a different definition of just what is "frivolous." Thus, even if an owner prevails on a declaratory judgment action, he will not always recoup his attorney's fees, and in fact, he may only recoup them in the most egregious of circumstances.

Using the Unknown to Your Advantage

What other options does an owner have? He can certainly threaten the filer with a slander of title suit. Even though such suits are difficult to win, the threat of such a suit may be enough to intimidate the filer of an inaccurate lien into releasing that lien. Contractors often do not know the difficulty of proving slander of title, and the unknown outcome of such a suit may motivate the filer to back down. Indeed, at the end of the day, the mere threat of recovery upon a slander of title claim may have more actual impact on the filer than a suit against him on the same subject. Further, the prospect of having to bear attorneys' fees defending a slander of tile claim may also motivate the lien claimant to withdraw the lien.

CHANGING THE RULES... *continued*

decision from the Louisiana Supreme Court last month upholding the constitutionality of the statute. *State of Louisiana v. All Property and Casualty Insurance Carriers*, 2006 La. LEXIS 2214 (La. Sup. Ct., August 25, 2006).

Will the Louisiana Legislature now be emboldened to mandate coverage for floods in homeowners policies? That is unlikely. Our courts have made exceptions to the seemingly exact and unyielding nature of the Contract Clause, ruling that the clause must yield at times to another important interest, such as the police power of the state. As a result, a limited and temporary exercise of the power to change substantive contractual rights retroactively may be approved if made necessary by a great public calamity, such as fire, flood or earthquake, and if the impairment is reasonable under the circumstances. *Home Building and Loan Association v. Blaisdell*, 290 U.S. 398 (1934). The Louisiana Supreme Court held that the contractual suit limitation is not such a substantial right that it cannot be temporarily impaired during the time of a public emergency. Because the hurricanes constituted "the worst natural disaster to ever have occurred in the United States," the Louisiana court found that the legislative extension of the prescriptive period was based upon "a significant and legitimate public purpose." The change was found to be "both appropriate and reasonable in order to protect the rights of the citizens of Louisiana and their general welfare."

In comparison, forcing insurance companies to cover flood damages when their policies clearly exclude such claims would be a substantial impairment of contractual relations that amounts to nothing less than a total destruction of the insurers' contractual expectations. Any such attempt would be struck down by the courts as a violation of the Contract Clause of the United States Constitution. Of course, that will not keep our politicians from trying.

INTERNET FRAUD: A COVERED THEFT?

By Steven J. DeFrank

The Internet, as we all know, has truly become a global commercial hub, providing buyers and sellers worldwide with the ability to transact business electronically, complete with photographs, advertisements, "insurance" for the transaction, and methods of shipping. Of course, the Internet also offers new avenues for fraud and abuse: Many times in these transactions, the buyer and seller do not know each other and simply have to have "faith" that the other party will hold up its end of the bargain.

Therefore, ample opportunities exist for fraud. For example, one type of fraud happens when an insured attempts to sell property on the Internet, but is scammed and never receives money for the sale. In one scam, a perpetrator posing as a prospective buyer will place an offer on the item and begin communications with the insured. Upon agreement to the sale, the perpetrator invites the insured to use an Internet escrow service where money for the transaction can be held while the property is in transport. When the insured opens the e-mail from the perpetrator about the escrow service, a virus is installed on the insured's computer that will lead the insured to a bogus escrow site controlled by the perpetrator. The perpetrator then places false information that the funds have been deposited in the phony escrow account to induce the seller/insured to ship the item. Of course, once the item is shipped and received, the insured attempts to obtain the "escrowed" money, but finds that the escrow service no longer has a website and that e-mails to the "buyer" are no longer deliverable.

We have started to see claims for such losses under homeowners insurance policies, with the insured claiming theft by conversion or theft by inducement and seeking coverage in order to recoup their loss. To make a *prima facie* case of loss by theft under a policy of insurance, the insured must show that the property was (1) taken *at a particular time*, and (2) taken *without the insured's knowledge* or *consent. Canal Insurance Co. v. Savannah Bank & Trust Co.*, 181 Ga. App. 520, 352 S.E.2d 835 (1987). Under these requirements, the insured can make a *prima facie* case for theft if the insured has the shipping bill to show that the theft took place at a particular time and place and he has copies of the virus-laden e-mails or documentation of the bogus escrow websites.

Once the insured makes a *prima facie* case for a covered loss, the burden shifts to the insurer to prove that an exclusion in the policy applies. Policies in the past sometimes contained specific exclusions for property losses resulting from "theft by inducement or trickery" or for losses occurring "off the residence premises," but such exclusions are now more rare. Most policies will not contain any exclusion that would plainly apply, and absent some other ground for non-coverage, coverage would therefore likely apply.

When faced with a claim stemming from a scam such as this, insurers may be tempted to consider an "insurable interest" defense. An insured cannot recover under an insurance policy for a property loss if the insured has no "insurable interest" in the property. Put in the context of an Internet scam, when an insured parts with property pursuant to a fraudulent sale, does the insured retain insurable interest in the property so as to qualify for insurance benefits?

In Georgia, the answer is generally "yes." An insurable interest means "any actual, lawful, and substantial economic interest in the safety or preservation of the subject of the insurance free from loss, destruction, or pecuniary damage or impairment." O.C.G.A. § 33-24-4(a). Under Georgia law, if one maintains the title to property, one maintains an insurable interest in the property. The case of *Thomas v. State*, 62 Ga. App. 725, 9 S.E.2d 854 (1940), is instructive. According to the holding in *Thomas*, if personal property is voluntarily placed in the hands of a person upon the condition that there should be returned to the owner at once its value in money (a cash sale), *neither title nor right of possession passes and becomes complete until this condition is complied with.* Therefore, if the insured agrees to the terms of an Internet sale wherein the insured is promised consideration for the sale of property, but the promised consideration is merely a sham to induce the insured to sell, the insured retains its "insurable interest" in the property and the insurable interest condition to coverage would not limit the insured's recovery.

Recent Case Update:

Yeomans & Associates Agency, Inc. v. Bowen Tree Surgeons, Inc.

By Brian W. Burkhalter

The Georgia Court of Appeals tackled two noteworthy issues in *Yeomans & Associates Agency, Inc. v. Bowen Tree Surgeons, Inc.*, 274 Ga. App. 738, 618 S.E.2d 673 (2005): (1) An agent's relationship to an insurer under the dual agency doctrine, and (2) an insurer's duty to defend an insured against groundless allegations, even though it is undisputed that the company will have no duty to indemnify under the policy at the conclusion of the lawsuit.

The insured, Bowen, and its employee, Black, were sued for Black's alleged negligence in causing a collision. The suit alleged that Black was acting within the scope of his employment at the time of the collision, making Bowen liable under the doctrine of *respondeat superior*. However, the undisputed "true fact" was that Black was driving his own car on personal business outside the scope of his employment when the collision occurred. Bowen provided notice of the lawsuit to its independent insurance agency, Yeomans. Bowen had auto liability insurance and commercial general liability insurance. The agent notified the auto liability carrier of the suit, but did not provide any notice to the commercial general liability carrier, Canal Indemnity Co. Because Canal did not receive notice from Yeomans and therefore did not provide a defense for this lawsuit, and because the auto liability carrier disclaimed coverage, a default judgment was entered against Bowen and Black. Bowen then filed suit against Yeomans and Canal for failing to provide coverage and a defense, seeking the amount of the default judgment, plus attorney's fees and bad faith penalties. After a jury trial, judgment was entered against Yeomans and Canal in the amount of $1,550,000.

With respect to the dual agency doctrine, Canal contended that no agency relationship existed between Canal and Yeomans. The court disagreed, finding that evidence was presented at trial that justified the jury finding an agency relationship, and that Canal received constructive notice of the claim as a consequence of Yeomans having received notice. The court ruled this way despite the fact that Yeomans had <u>no</u> contractual relationship with Canal authorizing Yeomans to accept notice on Canal's behalf. Instead, Yeomans had a contract with Canal's broker, had obtained coverage only through the broker and not through Canal directly, and in the past had sent notices of claims to the broker, not Canal. Because evidence existed that Yeomans had accepted premiums and notices of claims on Canal's behalf in the past, and because no evidence existed that Canal had ever objected to this "custom," a jury question existed as to the extent of Yeomans' authorization to accept notices of claims on Canal's behalf "as a fiduciary and a dual agent."

Yeomans has serious ramifications for insurers who disclaim coverage on the basis of the insured's breach of a notice condition. If there is even the slightest indication that an independent agent has sent notice or premiums to the insurer or the insurer's broker in the past, which were accepted by the insurer without any objection, then the court will likely conclude that a question of fact exists as to whether the agent is a dual agent. In such circumstances, insurers would be better served by providing a defense under a reservation of rights and bringing a declaratory judgment action on the issue of agency. If the jury concludes that an agency relationship exists, then the insurer can pursue a separate action against the agent for its failure to provide the insurer actual notice of the claim.

With respect to the insurer's duty to defend, Canal's policy excluded bodily injury that arose out of the use of an automobile by any "insured." The policy defined "insured" as an employee of the named insured if the employee was acting within the scope of his employment at the time of the collision. It was <u>undisputed</u> that Black was not acting within the scope of his employment with Bowen at the time of the collision and was therefore not an "insured" under the policy. Therefore, the court concluded that the auto exclusion did not apply, and Canal had a duty to defend Bowen because plaintiffs had alleged bodily injury caused by an occurrence in their complaint.

The court so held despite the fact that if the underlying case not gone into default, Bowen would have not been found liable under the doctrine of *respondeat superior*, and, therefore, Canal would have had no duty to indemnify Bowen under the policy. The court emphasized that an insurer's duty to defend is separate from its duty to indemnify, and the insurer must consider whether the alleged claim falls within policy coverages, regardless of whether the insured could actually be held liable to the plaintiffs. Also important to the court's decision was the insurer's duty to conduct a "reasonable investigation" into the insured's contentions to determine whether a duty to defend had been triggered. Even though the four corners of the complaint indicated that the auto exclusion should apply, Canal's duty to defend was triggered when Bowen told Yeomans that Black was not acting within the scope of his employment.

However, an argument exists that the court's decision does not give due consideration to the intent of the insured. Where the alleged injury was caused by the use of the employee's personal automobile outside the scope of his employment, most people would reasonably expect coverage to fall entirely under Black's personal auto liability policy. Regardless, *Yeomans* provides a warning to insurers as to how they should proceed in such claims in the future. An insurer should provide a defense to the insured under a reservation of rights. As pointed out by the court, this would give the insurer the opportunity to prove that the insured was not liable under *respondeat superior*, satisfying its "duty to seek that favorable decision on its insured's behalf." If the court agrees that the driver was not acting within the scope of his employment, then the insured employer will not be held liable, and the insurer will have no duty to indemnify and will have incurred only the cost of defense. If, on the other hand, the jury determines that the driver was acting within the scope of his employment, then the auto exclusion will apply to prevent any duty to indemnify the insured for an adverse verdict. The insurer also should put the driver's personal liability carrier on notice of the claim, because in the event the driver was not acting within the scope of his employment, the personal auto policy typically will provide primary coverage.

Save the Date!

Friday, November 3, 2006, 9:00 a.m. to 2:30 p.m.

You and your co-workers are invited to attend our Annual Swift, Currie, McGhee & Hiers Seminar. This year's seminar is in a new location at Villa Christina, 4000 Summit Boulevard in Atlanta, Georgia. The seminar is free of charge and includes a complimentary lunch. We plan to offer 4 CEUs, including one ethics hour, pending approval from the Georgia Insurance Department.

You can register for this seminar online at our web site, ***http://www.swiftcurrie.com/news/seminars.asp***

Property Attorneys

Michael H. Schroder	*404.888.6126*	*mike.schroder@swiftcurrie.com*
Mark T. Dietrichs	*404.888.6127*	*mark.dietrichs@swiftcurrie.com*
Thomas D. Martin	*404.888.6128*	*tom.martin@swiftcurrie.com*
Frederick O. Ferrand	*404.888.6182*	*fred.ferrand@swiftcurrie.com*
Stephen M. Schatz	*404.888.6133*	*steve.schatz@swiftcurrie.com*
David C. King	*404.888.6132*	*david.king@swiftcurrie.com*
Brian M. Leepson	*404.888.6135*	*brian.leepson@swiftcurrie.com*
Melissa K. Kahren	*404.888.6179*	*melissa.kahren@swiftcurrie.com*
Kelley C. Herrin	*404.888.6177*	*kelley.herrin@swiftcurrie.com*
Steven J. DeFrank	*404.888.6130*	*steven.defrank@swiftcurrie.com*
M. Boyd Jones	*404.888.6131*	*boyd.jones@swiftcurrie.com*
Amanda B. Speed	*404.888.6171*	*amanda.speed@swiftcurrie.com*
Robert M. Sneed, Jr.	*404.888.6174*	*robert.sneed@swiftcurrie.com*
Shannon V. Alexander	*404.888.6136*	*shannon.alexander@swiftcurrie.com*
Brian W. Burkhalter	*404.888.6142*	*brian.burkhalter@swiftcurrie.com*

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