The Punitive Damage Exclusion and Motor Carriers Insurance in Alabama

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By F. Lane Finch, Jr. (©)

Under Alabama law, the standard insurance policy language stating the insurer will pay "all sums which the insured shall be legally obligated to pay as a result of bodily injury" requires the insurer to pay punitive damage awards. Since 1935, coverage for "bodily injury" has included coverage for punitive damages, lost wages, and medical bills, in addition to coverage for pain and suffering and mental anguish. See, *Employer's Ins. Co. of Alabama v. Brock*, 172 So. 671 (Ala. 1937); see also, *American Fidelity & Cas. Co. v. Werfel*, 164 So. 383 (Ala. 1935).

To avoid this significant exposure, many -- but certainly not all -- insurance companies have specific punitive damage exclusions in the policy itself (sometimes in the definitional section) or exclude coverage for punitive damages by use of endorsements. Here are some examples:

> We do not provide BI Coverage for punitive or exemplary damages. However, this exclusion does not apply to punitive or exemplary damages which are awarded in a wrongful death action. (Quoted from USAA Auto policy.)
>
> The Company will pay all sums which the Insured or his legal representative shall be legally entitled to recover as damages except punitive damages (other than death) from the owner or operator of an uninsured automobile because of bodily injury .... (Quoted from UM provision in ALFA Auto policy.)
>
> LIABILITY INSURANCE is changed by adding the following exclusion: This insurance does not apply to punitive and/or exemplary damages except in cases of wrongful death. (Quoted from endorsement to Occidental Fire and Casualty Company of North Carolina Business Auto policy.)

Of course, an insurer has the right to limit coverage when writing policies. Exclusions can be contained within the terms of the policy or in an endorsement. By use of exclusions and other limitations (which do not violate any statutes or offend public policy[1]), an insurer has the power to write policies as narrowly as it desires. If the insured wants broader coverage, it has the right to purchase it from another insurer. When attached to a policy, endorsements limit, modify, or exempt coverage, and where an endorsement is not ambiguous or against public policy, it is given precedence over the terms of the policy to which it is attached. *Commercial Std. Ins. Co. v. General Trucking Co.*, 423 So.2d 168 (Ala. 1982).

The courts interpret exclusions as narrowly as possible in order to provide maximum coverage. But where the intention of the parties is clear and unambiguous, it must be enforced as written. See, e.g., *Wakefield v. State Farm Mut. Auto. Ins. Co.*, 572 So.2d 1220 (Ala. 1990) and *State Farm Mut. Auto. Ins. Co. v. Lewis*, 514 So.2d 863 (Ala. 1987).

A recent Eleventh Circuit case upheld a punitive damage exclusion. *Ross Neely Systems, Inc. v. Occidental Fire & Casualty Company of North Carolina*, 196 F.3d 1347 (11th Cir. 1999). The Eleventh Circuit noted an unambiguous endorsement supplants conflicting general terms and, while exclusions are to be construed narrowly, the Court must not favor an insured contrary to the policy's clear meaning. 196 F.3d at 1350, citations omitted. "[A]n unambiguous contract must be enforced as written." 196 F.3d at 1350, citation omitted. An exclusion stating "This insurance does not apply to punitive and/or exemplary damage except in cases of wrongful death" clearly and unambiguously excludes punitive damages. 196 F.3d at 1350.

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[1]/ In *Ross Neely Systems, Inc. v. Occidental Fire & Casualty Company of North Carolina*, 196 F.3d 1347 (11th Cir. 1999), the plaintiff claimed an endorsement excluding punitive damages was against public policy. The Eleventh Circuit declined to adopt that argument.

Such a punitive damage exclusion is not barred by Alabama public policy. "Although no Alabama cases have reached the issue, other courts have approved similar exclusions. The Alabama agency responsible for regulating insurance specifically allows insurers to file for approval of policies containing punitive damages exclusions." 196 F.3d at 1350, citations omitted. The Alabama Department of Insurance's Rate Bulletin No. 245 (Dec.1991-Feb.1992) specifically approved the exclusion of punitive and/or exemplary damage except in the case of wrongful death. Additionally, the particular exclusion at issue in the *Ross Neely* case was submitted to the Alabama Department of Insurance and deemed approved by it. 196 F.3d at 1350.

Despite the foregoing, the issue of punitive damage coverage in the case of a trucking accident caused remains somewhat unsettled. That is because insurance for motor carriers in Alabama typically includes two Motor Carrier Endorsements. The first, the Federally mandated MCS-90 Endorsement,[2] states, in pertinent part:

> [T]he insurer (the company) agrees to pay, within the limits of liability described herein, any final judgment recovered against the insured for public liability resulting from <u>negligence</u> in the operation, maintenance or use of motor vehicles subject to the financial responsibility requirements of sections 29 and 30 of the Motor Carrier Act of 1980 regardless of ... whether or not such <u>negligence</u> occurs on any route .... (Emphasis added.)
>
> It is understood and agreed that no condition, provision, stipulation, or limitation contained in the policy, this endorsement, or any other endorsement thereon, or violation thereof, shall relieve the company from liability or from the payment of any final judgment, within the limits of liability herein described, irrespective of the financial condition, insolvency or bankruptcy of the insured.

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[2]/ Federal Motor Carrier Safety Regulations require minimum levels of financial responsibility for motor carriers. See, FMCSR Part 387; see also, 49 U.S.C. § 10927, 49 U.S.C. § 13906, and 49 CFR 1.48. Proof of financial responsibility consists of an "'Endorsement(s) for Motor Carrier Policies of Insurance for Public Liability Under §§ 29 and 30 of the Motor Carrier Safety Act of 1980' (Form MCS-90) issued by an insurer(s)." FMCSR Part 387, § 387.7(d).

> However, all terms, conditions, and limitations in the policy to which the endorsement is attached shall remain in full force and effect as binding between the insured and the company. The insured agrees to reimburse the company ... for any payment that the company would not have been obligated to make under the provisions of the policy except for the agreement contained in this endorsement.

The state-mandated Form F Endorsement[3] states:

> [The policy is] amend[ed] to provide insurance for automobile bodily injury and property damage liability in accordance with the provisions of such law or regulations to the extent of the coverage and limits of liability required thereby; provided only that the insured agrees to reimburse the company for any payment by the company which it would not have been obligated to make under the terms of this policy except by reason of the obligations assumed in making such certification.

The phrase “in accordance with the provisions of such law or regulations” is initially confusing because of the conflict between Ala.Code § 37-3-18 and Rule 4.1 of Alabama’s Motor Carrier General Orders Rules and Regulations. Section 37-3-18 provides:

> . . . no motor carrier ... shall in any operation on any highway of this state, unless such carrier complies with such reasonable rules and regulations as the commission shall prescribe governing the filing and approval of . . . policies of insurance, . . . in such reasonable amounts as the commission may require, conditioned to pay . . . any final judgment recovered against such motor carrier for bodily injuries to or the death of any person resulting from the ***negligent*** operation, maintenance or use of motor vehicles under certificate or permit ....

Ala.Code § 37-3-18 (emphasis supplied). The statute does not require insurance for wantonness or for punitive damages. However, the Public Service Commission went beyond the enabling statute and promulgated a regulation providing:

> No person shall transport . . . property by motor vehicle . . . for compensation . . . unless and until there shall have been filed . . . a . . . certificate of insurance . . . conditioned to pay any final judgment recovered against such person for bodily injuries to or the death of any person resulting from the ***negligent or wanton***

3/ Ala. Code § 37-3-18 also requires minimum levels of financial responsibility in the form of "insurance ... conditioned to pay ... any final judgment ... for bodily injuries ... resulting from the negligent operation, maintenance, or use of motor vehicles under certificate or permit ...."

operation, maintenance or use of motor vehicles on the highways of this State . . . .

Motor Carrier General Orders Rules and Regulations Pamphlet No. 1989 Rule 4.1 (emphasis supplied).

Thus, Rule 4.1 apparently obligates the insurer to pay "any" final judgment for bodily injury caused by the motor carrier's wantonness. Presumably, or at least arguably, that includes judgments for punitive damages.

In the *Ross Neely* case, the insurer argued:

> Negligence and wantonness are two "`qualitatively different tort concepts of actionable culpability.'" ....
>
> Given the fact that under Alabama law negligence and wantonness are two entirely different tort concepts, it follows that *Rule 4.1* not only exceeds, but actually contradicts the enabling statute. Established rules of construction provide that, under these circumstances, the statute should govern: "The provisions of the statute will prevail in any case of conflict between a statute and an agency regulation." "A regulation . . . which operates to create a rule out of harmony with the statute, is a mere nullity. This is because an administrative board or agency is purely a creature of the legislature, and has only those powers conferred upon it by its creator."
>
> The Public Service Commission exceeded its statutory authority by expanding upon the statutory policy expressed in section 37-3-18. ...[T]he Public Service Commission is making law by adding a requirement that carriers insure a "qualitatively different tort" for which the Alabama Legislature did not require coverage. This is an "unconstitutional usurpation of the legislature's authority to make law." ...Thus, *Rule 4* is a nullity.
>
> Neely cites to a general statute (*Ala. Code § 37-3-7*) within the Alabama Motor Carrier Act enabling the APSC to regulate various matters. However, the specific statute enabling the APSC to issue regulations regarding insurance, *Ala. Code § 37-3-18*, only enables the commission to prescribe "reasonable rules ... governing ... policies of insurance ... conditioned to pay ... any final judgment ... for bodily injuries ... resulting from the <u>negligent</u> operation, maintenance, or use of motor vehicles under certificate or permit ...." (Emphasis added.) The enabling statute does not allow the commission to require coverage for wanton conduct, which as pointed out above, it a

> "qualitatively different tort."
>
> The insurance policy was amended by Alabama law, *Ala. Code § 37-3-18*, to include coverage for "negligent operation ... of motor vehicles ..." only. Alabama law does not require payment of punitive damages.

Appellee's Brief, pp. 33-35 (internal quotations and citations omitted).

The District Court agreed with Occidental Fire, holding that the "provisions of the statute [i.e., Ala.Code § 37-3-18] will prevail in any case of conflict between a statute and an agency regulation [i.e., Rule 4.1]." Thus, the District Court read Rule 4.1 as "imposing no further liability on motor carrier insurers that the Legislature directs in the enabling statute ...." That is, no liability to insure anything but negligence. The Eleventh Circuit avoided that whole issue by following the District Court's alternative ground for holding the insurer was not obligated to the motor carrier for punitive damages. *Ross Neely,* 196 F.3d at 1351. The Eleventh Circuit found the insurer's duty to pay was never triggered because the motor carrier endorsements "serve as a guarantee to the public that the insurer will be liable for any damages awarded if the insured is unable to pay. Form F does not alter the relationship between the insured and the insurer. Therefore, Occidental served only as a surety to Ross Neely's performance." 196 F.3d at 1351 (citations omitted).

That holding is consistent with the many cases which hold the motor carrier endorsement is for the benefit of the motoring public, and not the motor carrier itself. *Service Stages, Inc. v. Central Surety & Ins. Co.*, 231 Ala. 417, 418 (1936), quoting *Fidelity & Cas. Co. of New York v. Jacks*, 231 Ala. 394, 397-398 (1936); see also, *Command Transp., Inc. v. B.J.'s Wholesale Club, Inc.*, 62 F.3d 18, 20 (1st Cir. 1995). In fact, the MCS-90 Endorsement states, "upon failure of the [insurance] company to pay any final judgment recovered against the insured [motor carrier] as provided herein, the judgment creditor [i.e., the injured motorist] may maintain an action in any court of competent

jurisdiction on against the [insurance] company to compel such payment." However, the MCS-90 does not allow the motor carrier to bring an action to compel payment; only the injured motorist is allowed to do so pursuant to the terms of the MCS-90. The Motor Carrier Endorsements are simply not applicable to disputes between the motor carrier and the insurance company.

In an Alabama case decided under the Alabama Motor Carrier Act of 1931, the Alabama Supreme Court noted the legislative intent of that requirement was to protect the public, but that "as between the insured and the insurer, the parties were left free to contract uninfluenced by the provisions of said act." *Service Stages, Inc. v. Central Surety & Ins. Co.*, 231 Ala. 417, 418 (1936), quoting *Fidelity & Cas. Co. of New York v. Jacks*, 231 Ala. 394, 397-398 (1936). That interpretation is consistent with the terms of the MCS-90 Endorsement: "All terms, conditions, and limitations in the policy ... shall remain in full force and effect as binding between the insured and the company." Form F also only serves as a guarantee to the public that the insurer will be liable for any damages awarded if the insured is unable to pay. Form F, like the MCS-90, does not alter the relationship between the insured and the insurer. Therefore, the insurance company serves only as a surety to the motor carrier's performance. See also, *Command Transp., Inc. v. B.J.'s Wholesale Club, Inc.*, 62 F.3d 18, 20 (1st Cir. 1995); *Harco Nat'l Ins. Co. v. Bobac Trucking, Inc.*, 107 F.3d 733, 735, (9th Cir.1997) ("The purpose of the MCS-90 is to protect the public, not to create a windfall to the insured."); *Canal Ins. Company v. First General Ins. Co.*, 889 F.2d 604, 611 (5th Cir.1989) (observing that the MCS-90 protection "serves no purpose as against the insured."). Where the motor carrier can satisfy the judgment, the insurance company's duty to pay never arises. *See, e.g., Service Stages, Inc. v. Central Sur. & Ins. Co.*, 165 So. 248 (Ala. 1936); *Fidelity & Cas. Co. v. Jacks*, 165 So. 242 (Ala. 1936).

If the insurance company satisfies the judgment on the sole basis of coverage provided by

the Motor Carrier Endorsement, the motor carrier is still ultimately liable. Both the MCS-90 and Alabama's Form F contain reimbursement provisions requiring the motor carrier to reimburse the insurer for any payments made solely by virtue of the endorsement. *Ross Neely,* 196 F.3d at 1351. If, despite a punitive damage exclusion, an insurer is required to directly pay punitive damages to a member of the motoring public solely because of the Form F endorsement, the motor carrier would immediately be obligated to reimburse the insurer for that payment. Similarly, if an insurer is required to directly pay any damages caused by an excluded driver or an unscheduled vehicle because of the Motor Carrier Endorsement, the motor carrier would be obligated to reimburse the insurer for that payment.

Punitive damage exclusions are clearly enforceable in disputes between the motor carrier and its insurance company. They are also probably enforceable in disputes with third parties. Further, an insurer could pay a punitive damage award under a reservation of rights and then seek reimbursement from the motor carrier.

Thus, assuming the motor carrier has sufficient assets, the insurance company has no ultimate exposure for punitive damages in Alabama if such damages are specifically excluded from coverage. In the context of other policies, such as automobile and general liability policies, it is even clearer that punitive damage exclusions will eliminate the insurer's exposure for punitive damages in Alabama, except in cases involving wrongful death.

Biography: Lane Finch practices in the Litigation Section at the law firm of Haskell Slaughter & Young, L.L.C. in Birmingham. His areas of practice include insurance coverage and defense, business litigation, and intellectual property law. Mr. Finch received his B.S. Degree in Business Administration from California Polytechnic State University, San Luis Obispo, and received his J.D. degree from the University of California, Hastings College of the Law, where he was a Note and Comment Editor for the Hastings Constitutional Law Quarterly. He served internships for United States Congressman Leon E. Panetta and California Court of Appeals Associate Justice Howard B. Weiner. Mr. Finch practiced law in California before coming to Alabama. He is a member of the Alabama Bar, State Bar of California, American Bar Association, Birmingham Bar Association, Defense Research Institute, and Alabama Defense Lawyers Association.

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