

Winter, 2019

AEI CLAIMS LAW QUIZ

INSURABILITY OF PUNITIVE DAMAGES IN AUTO POLICIES

[ref: *Automobile Liability Insurance, Para. 2.01*]

FACTS: Zuniga, a pedestrian walking on the sidewalk, was struck from behind by a car driven by Medina. The case went to trial and Medina was found liable for negligence and gross negligence. The jury awarded \$93,244.91 in actual damages and \$75,000 in punitive damages against Medina, plus interest and costs. Medina was insured by Farmers Texas County Mutual Ins. Co., which paid all but the punitive damage award. Farmers disputed whether its policy covered the punitive damage award. A number of legal actions followed, initiated by Zuniga, seeking to enforce the judgment as Medina's assignee, and Farmers, which sought a declaration that it did not have an obligation to pay punitive damages under the policy.

QUESTION: Does an automobile policy that promises to "pay damages for bodily injury or property damage" cover punitive damages assessed against an insured?

ANSWER: No according to a Texas appeals court in *Farmers Texas County Mutual Ins. Co. v. Zuniga*, 548 SW3d 646 (Tex. App. 2017). The court held that the policy was clear and unambiguous and did not cover punitive damages.

The court first looked to the policy language. Two policy provisions were at issue in this case. The first was the insuring agreement, which stated:

We will pay damages for bodily injury or property damage for which any covered person becomes legally responsible because of an auto accident. ... Damages include prejudgment interest awarded against the covered person.

The second policy provision involved in the inquiry was the limit of liability, which stated:

If separate limits of liability for bodily injury and property damage liability are shown in the Declarations for this coverage the limit of liability for "each person" for bodily injury liability is our maximum limit of liability for all damages for bodily injury sustained by any one person in any one auto accident.

Using common rules of contract construction, the court stated that the policy language would be enforced as written unless it was ambiguous. Policy language is ambiguous if it is susceptible to two or more reasonable interpretations.

Some of the key terms in the two policy provisions were not defined in the policy and the court looked to the common meaning of the terms to determine their meaning. The court stated that “bodily injury” means “physical damage to a human being’s body.” It also stated that “damages” is “a sum of money to compensate for an injury.” The word “for” means “in exchange as the equivalent of.” The court stated that the policy’s promise to pay damages for bodily injury was a promise by the insurer “to pay a sum of money as compensation in exchange as the equivalent of the physical damage” to the claimant’s body.

All of the policy parts had to be read together to resolve the question posed to the court. The insuring agreement creates and defines the scope of coverage. The policy limits provision simply sets the maximum amount payable under a specific type of coverage provided by the policy. The court stated that the limit of liability language did not expand the policy’s scope of coverage.

Zuniga argued that the lack of an express exclusion for punitive damages in the policy meant that these damages were covered. The court pointed out that decisions that held that punitive damages were covered absent an express exclusion analyzed policies in which the insuring agreements stated the insurer would pay “all sums” for which an insured was liable to pay as damages because of bodily injury. These insuring agreements were not limited to the payment of damages for bodily injury. Punitive damages are not awarded as compensation for bodily injury, although an insured may be liable for them because of a bodily injury. Punitive damages are intended to punish a wrongdoer for conduct that goes beyond mere negligence.

The court referred to an earlier case in which a Texas appellate court had read the “all sums” language into an auto policy with an insuring agreement similar to the one at issue. The court in this case, however, refused to read that language into a policy that did not include it. The court refused to rewrite the policy in this fashion and concluded that because the policy language was clear and unambiguous it must be enforced as written.

The court held that the policy was clear and unambiguous and did not provide coverage for punitive damages.

CONCLUSION

When an auto claim involves a question of coverage for punitive damages, it is important to consider the specific policy language and the way the courts in the jurisdiction have interpreted that language. In this case, the insuring agreement stated “We will pay damages for bodily injury,” and the Texas appeals court ruled that this language unambiguously did not include coverage for punitive damages. Other courts, however, have reached different conclusions on similar language. Some courts, such as the Federal District Court for the District of Delaware in *Valley Forge Ins. Co. v. Jefferson*, 628 F. Supp. 502 (D. Del. 1986), have found that this language unambiguously includes coverage for punitive damages, while other courts have concluded that the policy language is ambiguous. A finding of ambiguity, of course, means that the policy will be interpreted in the insured’s favor and there will be coverage for punitive damages.

The language in some policies is broader than the promise to pay damages for bodily injury. In some policies the insurer promises “to pay on behalf of the insured all sums which the insured shall become legally obligated to pay as damages.” This broader language makes it more likely that a court will find ambiguity that favors the insured as the Mississippi Supreme Court did in *Anthony v. Frith*, 394 So2d 867 (Miss. 1981).

In addition to the language of the insuring agreement and the court cases interpreting that language, something else to consider when faced with a claim for punitive damages is whether the jurisdiction considers insurance of punitive damages to be a violation of public policy. Most states permit the insurability of punitive damages but a significant minority do not. If insuring punitive damages is held to violate public policy, there won't be coverage regardless of what the policy states.