



IN THE COURT OF APPEALS OF IOWA

MICHAEL HEYN and JUDY HEYN,)

Plaintiffs-Appellees,)

vs.)

KENNETH R. HORN, IDA M. HORN,)

Defendants,)

and **CHARLIE RUGGLES,**)

Defendant-Appellant.)

Filed June 28, 1983

2-424
2-68091

Appeal from Jefferson District Court - James C. Rielly, Judge.

Defendant appeals from the trial court's refusal to set aside the default judgment entered against him after his insurance company failed to appear and defend him in this personal injury tort action. REVERSED.

Timothy J. McKay of McKay & Moreland, Ottumwa, for defendant-appellant Ruggles.

Ronald K. Watkins of McGrath & McGrath, Keosauqua, for plaintiffs-appellees.

Heard by Oxberger, C.J., and Donielson, Snell, and Schlegel, JJ. Hayden, J., takes no part.

DONIELSON, J.

Defendant appeals from the trial court's refusal to set aside the default judgment entered against him after his insurance company failed to appear and defend him in this personal injury tort action. On appeal defendant asserts (1) that there was not substantial evidence to support two trial court findings of fact; (2) that trial court abused its discretion by entering a default judgment against the insured, Ruggles, while focusing on the conduct of the insurer, and allegedly not considering the evidence that defendant was diligent in pursuing the case; (3) that, even if the notice of suit reached defendant's insurer, the inadvertent loss of suit papers by a large insurance company is not inexcusable neglect and, therefore, should not have been the basis for entry of a default judgment; (4) that the trial court should not have imputed the neglect of the insurance company, if any, to defendant; and (5) that the trial court should not have held, in the alternative, that there was no good defense shown since defendant did show a good defense to plaintiffs' allegations by filing a general denial of the petition and by raising the affirmative defense that defendant Horn's negligence was the sole proximate cause of the injury. We reverse and remand.

Our scope of review is on assigned errors. Iowa R. App. P. 4.

I.

On October 14, 1981, plaintiffs, Michael and Judy Heyn, filed a petition at law in which they asserted that plaintiff Michael Heyn had been injured when the bicycle he was riding was struck by a truck driven by defendant, Kenneth Horn, on November 15, 1979. Plaintiffs alleged that the Horn truck was being pushed by an automobile driven by defendant, Charlie Ruggles, at the time of impact. Plaintiffs sought \$90,000 actual, \$50,000 punitive, and \$10,000 loss of consortium damages. Defendant Ruggles was served with original notice of the action on October 14, the day the petition was filed.

On October 22, 1981, Mrs. Ruggles called the insurance agency which had written Ruggles' insurance policy, and told them that her husband was being sued. At the request of the agency, Ruggles delivered copies of the suit papers to them that day. No appearance or answer was filed on defendant Ruggles' behalf.

On November 12, 1981, plaintiffs filed a demand for an entry of default, which was entered that same day by the district court clerk. See Iowa R. Civ. P. 231. Additionally, on that same day the district court held a hearing to establish damages, which were awarded in a total amount of \$100,000 compensatory and \$25,000 punitive.

On November 19, Ruggles filed a petition to vacate the judgment pursuant to rule 236. He alleged that he had dealt promptly with the suit papers, but that his insurer, Farm & City, never received them and that, therefore, no action was taken. He also alleged that he had a good defense to the claim. The court denied the motion in an extensive ruling. Ruggles now appeals the ruling.¹ Because defendant's assignments of error are closely-related, we shall consider them together.

II.

Rule 236 provides, in part, that the court may set aside a default judgment "for mistake, inadvertence, surprise, excusable neglect or unavoidable casualty." The burden is on the party seeking relief to establish that he is entitled to it. Gateway Transportation Company v. Phillips & Phillips Company, 261 N.W.2d 175, 177 (Iowa 1981). The rules governing review of this type of case were summarized

¹ Since claims against defendants Kenneth and Ida Horn have not been disposed of, this appeal may not have been taken from a final judgment. However, the issues raised in this appeal are applicable only to the default judgment and, thus, the judgment may be considered separable and final for appeal purposes. See Shoemaker v. City of Muscatine, 275 N.W.2d 206, 208 (Iowa 1979). We note further that no purpose would be served by requiring the underlying tort cause to be tried before entertaining this appeal; we allow the appeal to proceed under Iowa Rules of Appellate Procedure 1(c) and 2.

in Paige v. Chariton, 252 N.W.2d 433, 437 (Iowa 1977):

A trial court is vested with broad discretion in ruling on a motion to set aside a default judgment. Such a ruling will be reversed on appeal only if this discretion is abused. Generally abuse will be found only where there is a lack of substantial evidence to support the trial court's ruling. We view the evidence in the light most favorable to the trial court's ruling and will uphold the same even where the trial court made no findings of fact or based its ruling upon a different ground. (citations omitted)

"Because trial on the merits is favored, a liberal approach is to be taken in granting relief from defaults." First National Bank in Lenox v. Claiser, 308 N.W.2d 1, 3 (Iowa 1981). Accordingly, we are more reluctant to interfere with the grant of such motion than with its denial. Flexsteel Industries, Inc. v. Morbern Industries Limited, 239 N.W.2d 593, 596 (Iowa 1976).

In the instant case we find there is substantial evidence to support the trial court's findings of fact. The evidence regarding the mailing and receipt of suit papers reveals the following chain of events took place: The accident occurred on November 15, 1979, when defendant Ruggles was in his vehicle pushing the pickup truck which defendant Horn was steering and trying to "push-start." Ruggles claims that he had stopped pushing Horn's truck at the time the truck hit plaintiff's bicycle.

Thereafter, in May, 1980, an adjuster for Allstate Insurance Company, the company which insured the Horns, spoke with Ralph Summa from Farm and City Insurance Company, with whom defendant Ruggles had his policy. It was agreed between them that the adjuster for Allstate would handle the claim for all defendants. The adjuster attempted to negotiate a settlement with plaintiffs' attorney, but failed to reach an agreement. The adjuster notified someone other than Ralph Summa at Farm and City Insurance Company that Ruggles was going to be sued and that she had received a copy of the petition from plaintiffs' attorney. The person from Farm and City indicated that they would take over the

defense of their insured, defendant Ruggles. The Allstate adjuster never sent a copy of the petition to the Farm and City Insurance Company.

Thereafter, on October 14, 1981, Ruggles was served with an Original Notice. Seven days later he notified Karen Clay at the Burlington insurance agency which had written Ruggles' policy with Farm and City Insurance. That same day Ruggles delivered the suit papers to Karen Clay in Burlington. Karen Clay testified that she called Robert Linebacker at Farm and City Insurance Company in West Des Moines. The evidence regarding this conversation is conflicting. She testified that she informed Linebacker of the suit and of the appearance date, and told him she would send the suit papers and the accident report. She further testified that she sent the papers by mail that same day. Linebacker testified that he never received the phone call from Karen Clay. Both Linebacker and Ralph Summa testified that they never received the papers which Karen Clay sent on October 22. In light of this conflicting evidence, the trial court found that Linebacker was notified and that the papers were sent by Karen Clay. However, the court made no finding regarding whether the papers were ever received by Farm and City or whether they were lost in the mail; the court only found that they were sent by, but never returned to Karen Clay.

On November 12, 1981, plaintiffs motioned for a default judgment against defendant Ruggles. That same day the court granted the motion and assessed damages in the total amount of \$100,000 compensatory and \$25,000 punitive. It appears that the clerk of court notified defendant Ruggles of the default on November 13th. Mrs. Ruggles immediately called the Burlington agency and Karen Clay told her to call Farm and City directly.

Mrs. Ruggles then called the company and told Robert Linebacker about the default. Linebacker called plaintiffs' attorney's office and spoke to James McGrath about the possibility of setting aside the default. Linebacker testified

that he told McGrath that they had never received the suit papers. McGrath testified that Linebacker told him that he had spoken to the agent and that the suit papers had never been sent. Karen Clay testified that she never spoke to Linebacker on November 13th, the day Ruggles notified her of the default.

On November 19th, defendant Ruggles moved to have the default set aside. The court denied defendant's motion because he had failed to show that "mistake, inadvertence, surprise, excusable neglect, or unavoidable casualty" were involved, and that there was "an absence of evidence in the record to show . . . a good defense to the allegations contained in the plaintiffs Petition."

We believe there is substantial evidence to support the court's findings of fact that defendant's insurance company was notified, at least by phone, of the pending suit against Ruggles. We cannot be sure that the suit papers were ever received by Farm and City, especially in light of Karen Clay's testimony that, in the past, she had mailed items which were never delivered, nor ever returned to her. Some of the other items lost in the mail were also important documents. However, we agree that Farm and City were notified of the suit by both the Allstate adjuster and Karen Clay. It was their failure to act on Ruggles' behalf which resulted in the default judgment being entered against him.

While we agree that there is support for the court's findings, we disagree with the trial court's conclusions. "We are not bound by trial court determinations of law or precluded from inquiring into whether the trial court applied erroneous rules of law which materially affected its decision." Kurtenbach v. TeKippe, 260 N.W.2d 53, 54-55 (Iowa 1977); see also Flexsteel Industries, Inc., 239 N.W.2d at 598; Whewell v. Dobson, 227 N.W.2d 115, 117 (Iowa 1975). In this regard, the instant case is similar to Flexsteel Industries, Inc., where the court found that the failure to appear and defend was not due to the defendant himself, but to his insurance carrier's negligence. Flexsteel Industries, Inc., 239 N.W.2d at 597. The court then

noted that because "the trial court made a finding defendant failed to account for the delay the conclusion is inescapable in the present case it applied a rule of law imputing an insurer's negligence in determining the date of appearance to its insured." Id. at 598. Whether this was a correct statement of the law was an issue of first impression for the court.

Our cases have consistently recognized that the purpose of rule 236 "is to allow determination of a controversy on its merits rather than on the basis of non prejudicial inadvertence or mistake." Hannan v. Bowles Watch Band Company, 180 N.W.2d 221, 222 (Iowa 1970); see also Edgar v. Armored Carrier Corporation, 256 Iowa 700, 706-07, 128 N.W.2d 922, 925-26 (1964). The rights of a litigant should not be denied proper hearing by strict application of legal formality. See Newell v. Tweed, 241 Iowa 90, 95, 40 N.W.2d 20, 23 (1949). Our rules of civil procedure and the cases applying them favor trial on the merits so long as they are not "stretched to the point where a judgment will be vacated when the petitioner, through his counsel, has ignored plain mandates of the rule with ample opportunity to abide by them." Wharff v. Iowa Methodist Hospital, 219 N.W.2d 18, 22 (Iowa 1974)(quoting Windus v. Great Plains Gas, 255 Iowa 587, 600, 122 N.W.2d 901, 909 (1961), which involved a petition to vacate a dismissal for want to prosecution).

Due to the great variety in factual circumstances, whether there has been excusable neglect or inadvertence in a rule 236 situation must be decided on a case by case basis. Flexsteel Industries, Inc., 239 N.W.2d at 596; Wharff, 219 N.W.2d at 22. Moreover, because of the varying factual situations under which such grounds have been urged, "the results of the various cases do not always appear to be entirely consistent." Hannan, 180 N.W.2d at 223. The court in Hannan attributed this "in large part to the difficulty in carrying out both the spirit and the letter of a rule which is designed to relieve a litigant from the disastrous effect of what is often a relatively slight nonprejudicial omission." Id.

- 7 -

While the Iowa Supreme Court before Flexsteel Industries, Inc., had never decided the issue in terms of imputing the insurer's negligence to the insured, similar factual circumstances had been addressed in numerous cases. In Edgar v. Armored Carrier Corporation, 256 Iowa 700, 706, 128 N.W.2d 922, 925 (1964), the court affirmed the lower court's ruling setting aside a default judgment against the defendant who, "with reasonable promptness," had sent the suit papers to his insurance company, who lost the papers and failed to file an appearance on its insured's behalf. The court emphasized that:

No approval should be given to gross neglect or wilful procrastination; but under the circumstances shown here, when the defendant has acted promptly, and in good faith, intends to defend and shows a meritorious defense, and there has been no prejudice to the plaintiff and no delay of an expeditious trial, we hold that at least the trial court has discretion to set aside the default and judgment.

Id. at 926.

Later that same year the Iowa Supreme Court reversed the lower court's refusal to set aside a default judgment against a defendant who had forwarded the suit papers to his insurer, but the papers were apparently lost in transit and no appearance was entered. Hobbs v. Martin Marietta Company, 257 Iowa 124, 131 N.W.2d 772 (1964). In holding that the default should have been set aside, the court discussed the responsibility of the insured in this type of situation:

Under such circumstances, is one required to obtain a receipt from one's insurance agent upon delivery to him of a notice of suit, and does a failure to check up on the agency to see that it was taking steps to protect one's interest amount to such carelessness or negligence on the part of the one sued as would permit a denial of his motion to set aside a default and judgment entered against him some seven days after the date set for his appearance in the district court? We think not.

* * *

We are not prepared to hold that in the operation of such large business enterprises the law requires constant checking to see that papers sent through the regular channels are

received and acted upon, nor do we think the failure to do so here amounted to carelessness within the meaning of our rule. To be careless and inattentive, as the terms are applied here, means to give the matter no care, no attention, approaching gross neglect or willful procrastination. Edgar v. Armored Carrier Corp., supra, Iowa, 128 N.W.2d 922, 926; Sioux City Vinegar Mfg. Co. v. Boddy, et al., 108 Iowa 538, 79 N.W. 350.

Id. at 131-32, 131 N.W.2d at 777-78.

In Hannan v. Bowles Watch Band Company, 180 N.W.2d 221 (Iowa 1970), the court affirmed the lower court's order setting aside the default judgment. In Hannan, the defendant had notified his insurer of the suit, but for some "unexplained reason," the matter was not brought to the attention of the attorney handling the matter until after the time for appearance had expired. Id. at 222. The lower court set aside the default finding that the handling of the original notice by the insurer was "inexcusable negligence" but not gross neglect or willful procrastination. On appeal, the court disagreed with the trial court's finding of "inexcusable neglect," but affirmed the trial court in all other respects:

In light of what was said in Hobbs v. Martin Marietta Co., (1964) 257 Iowa 124, 131 N.W.2d 772, the record is not sufficient to support the finding of "out and out inexcusable negligence." The excusable neglect in Hobbs was loss of the original notice after the principal defendant had forwarded it to its insurance carrier. We noted the size of modern business organizations and the difficulties of handling mail as factors to be considered in determining whether the neglect was excusable or not. The case does not hold, as the trial court implies, that large organizations, including insurance companies, are entitled to special treatment. It does recognize the problems of modern business as a legitimate factor in determination of the effect to be given to the inadvertent or negligent failure to handle the matter within the time allowed.

Viewed in this light the evidence here supports a finding of negligence or neglect but does not support a finding of inexcusable neglect. Stated otherwise, it supports the court's later refusal to find "gross neglect or willful procrastination." It also supports the ultimate action setting aside the default so trial could proceed on the merits.

Id. at 223. Nevertheless, the court stressed that its holding would "not allow

defendants to default with impunity . . . 'no approval should be given to gross neglect or willful procrastination.' " Id. at 224 (quoting Edgar, 256 Iowa at 707, 128 N.W.2d at 926). Indeed, subsequent cases demonstrate the seriousness of this assertion. See Gateway Transportation Company v. Phillips & Phillips Company, 261 N.W.2d 175 (Iowa 1978)(misconstruction of proper legal notice by party of time to appear insufficient to show good cause to set aside default); First National Bank in Lenox v. Claisher, 308 N.W.2d 1 (Iowa 1981)(Uhlenhopp, J., dissenting, joined by Reynoldson, C.J., and Larson, J.)(affirming denial of motion to set aside default where evidence supported finding that movant's attorney's affidavit was not true).

Only in Flexsteel did the court discuss the issue in terms of imputing the negligence of the insurance carrier to the insured so as to bar the opening of a default judgment. After noting that the "[d]efendant had no reason to anticipate the failure of its insurer to attend to the case," the court approved the following language from Hinz v. Northland Milk & Ice Cream Co., 237 Minn. 28, 31, 53 N.W.2d 454, 456 (1952):

"Where a defendant with reasonable promptness delivers the summons and complaint to its insurer which by contract is obligated to defend the suit, the negligence of the insurer in failing to forward the papers to the attorney for answering until shortly after the time for answering has expired is not to be imputed to defendant so as to bar the opening of a default judgment where, in the exercise of a sound judicial discretion, it appears that defendant after receiving notice acted with diligence, has a defense on the merits, and where, as here, no substantial prejudice will result to plaintiff."

Flexsteel Industries Inc., 239 N.W.2d at 597.

While there are some examples to the contrary, an examination of similar cases decided under comparable statutes in other jurisdictions, and in the federal courts under federal rules 55(c) and 60(b), reveals that this is the majority position today. Laguna Royalty Company v. Marsh, 350 F.2d 817, 823 (5th Cir. 1965)(rule

60(b)(1) should be liberally construed and doubt resolved in favor of setting aside default judgment so that case may be tried on the merits); see also Standard Oil Company v. Iowa, 408 F.2d 1711 (8th Cir. 1969); Wilkerson v. City Sales Company of Mobile, Inc., 374 So.2d 1333 (Ala. 1979)(set aside default where insurer's inadvertence caused delay in getting suit papers to the attorney in charge); Oliver v. Sawyer, 359 So. 2d 368, 370 (Ala. 1968)(not unreasonable for defendant to rely upon insurer to perform contractual obligation to defend and default should be set aside where insurer misplaced papers attempting to act on insured's behalf); Cobb v. County Fair Association, Inc. v. Boyle, 143 Ga. App. 754, 240 S.E.2d 136 (1977)(reversing refusal to set aside default when defendant showed good faith handling of matter and reasonable reliance on third party to defend); Spencer v. American United Cab Association, 59 Ill. App. 2d 165, 208 N.E.2d 118 (1965)(power to set aside default is based upon substantial principles of right and wrong and is to be exercised in furtherance of justice to permit defendant to have his day in court); King v. Montz, 219 N.W.2d 836 (N.D. 1974)(abuse of discretion found in not setting aside default where insurer mislaid papers sent by insured and no appearance was filed on his behalf); Abrams v. Barnes, 229 N.Y.S.2d 657, 16 A.D.2d 936 (1962)(carelessness of insurer in losing copy of complaint served should not be attributed to insured, especially since plaintiff was not prejudiced because action was still pending against codefendant); Colley v. Bazell, 64 Ohio St. 2d 243, 416 N.E.2d 605 (1980)(error not to set aside default where defendant sent suit papers to insurer, papers were delayed in mail, and an answer was not timely filed); Wagar v. Prudential Insurance Company of America, 276 Or. 827, 556 P.2d 658 (1976)(reversing refusal to set aside default entered when answer not filed due to negligence of insurer, defendant acted promptly to set aside default, and no significant delay of trial on merits); Brooks v. Surman Dental Lab., Inc., 262 Pa. Super. 369, 396 A.2d 799 (1979)(abuse of discretion in not setting aside default

where suit papers forwarded by insurer were lost in mail and was not a strategic decision or intentional misconduct, but was mere inadvertence in misplacing complaint).

A number of these cases relied, in part, on the Hobbs case decided by the Iowa court, and on the Hinz case decided in Minnesota and subsequently relied on by the Iowa court in Flexsteel. A number of cases follow this approach only when it was reasonable for the insured to rely on the insurer's agreement to protect his interest. See Cyrus v. Haveson, 135 Cal. Rptr. 246 (1976); Schutte v. Valley Bargain Center, Inc., 248 Pa. Super. 532, 375 A.2d 368 (1977). Thus, where the insured knew that the insurance company was not acting to protect his interest, the default judgment was upheld. Cyrus at 252; see also Baskerville v. Philadelphia Newspaper, Inc., 278 Pa. Super. 59, 419 A.2d 1355 (1980)(generally, insured can rely on insurer but where he is notified that his interests are not being protected default is appropriate). We agree that the insured's reasonable belief that his interests are being protected is one factor to be considered in determining whether the default should be set aside. This is similar to the reference in Hobbs regarding defendant's good faith intent to defend. In Colley, 64 Ohio St. 2d at 249, 416 N.E.2d at 609, the Ohio court suggests other circumstances bearing on this determination:

... whether the defendant promptly notified his carrier of the litigation. A second circumstance is the lapse of time between the last day for the filing of a timely answer and the granting of the default judgment. A third circumstance is the amount of the judgment granted. A fourth, but not decisive, circumstance is the experience and understanding of the defendant with respect to litigation matters.

In the instant case, the defendant notified his insurance agent that he was being sued, took the suit papers to the agent, and understood that his insurer would undertake his defense. The insurance company was notified of the suit, agreed to undertake the defense, but failed to act within the time for filing an

answer. Shortly after learning of the default, both the defendant and the persons acting on his behalf moved quickly to have the default set aside. In short, defendant's insurance company lost or never received the suit papers and failed to file an appearance on his behalf. We do not believe defendant was dilatory in taking the suit papers to his agent; he was not experienced in litigation matters and, after notifying his agent of the suit, acted quickly to deliver papers to her. In light of this fact, the fact that the motion to set aside the default was filed shortly thereafter, and in light of the \$125,000 judgment amount, we believe the court erred in imputing the insurer's neglect to the insured and by not finding the neglect excusable under the circumstances.

III.

The trial court also found that defendant did not show a good defense to the allegations alleged in plaintiffs' petition. In Flexsteel Industries Inc., the court considered whether a general denial in a pleading would constitute a prima facie showing of a meritorious defense. There the court noted that

[s]ince "good cause" does not exist without a defense this court has held that a movant to set aside a default under rule 236, R.C.P., is required at least to assert in good faith a claimed defense to plaintiffs' action or as some courts state at least a prima facie showing of a meritorious defense. . . . However, this principle does not require the allegations of a defense which can be guaranteed to prevail at trial. See Kirby v. Holman, 238 Iowa 355, 375, 25 N.W.2d 664, 675.

Flexsteel Industries Inc., 239 N.W.2d at 601.

Adopting a liberal standard to determine what constitutes a meritorious defense, the Flexsteel court held that the general denial constituted a prima facie showing of a meritorious defense since it "served to put in issue existence of those elements essential to plaintiffs' maintenance of its action." Id. The court relied, in part, on Springer Corporation v. Herrera, 85 N.M. 201, 510 P.2d 1072 (1973), but noted that in Springer a tougher standard was applied since a final judgment had

been entered on the entry of default. Id. at 600-601. In this regard, the instant case is similar to Springer in that final judgment has been entered. However, in this case, as in Springer, the defendant, in addition to the general denial, made an affirmative statement regarding its defense. Here, the defendant affirmatively asserts that he was not pushing the Heyn vehicle at the time of impact and that defendant Horn was the sole cause of the accident. We believe this statement of the underlying facts supports defendant's allegation that a meritorious defense exists. He should have an opportunity to present his defense at a trial on the merits.

Having found that defendant presented a prima facie showing of a meritorious defense and that the court erred in not granting defendants' motion to set aside the default, we reverse and remand for trial in accordance with the rules of civil procedure.

REVERSED AND REMANDED.