

DEFENDING BAD FAITH CLAIMS - - THE INSURER'S PERSPECTIVE

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**Updates and Hot Trending Topics
Affecting Insurance Coverage
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INTRODUCTION

Expanding Theories of Insurer Extra-Contractual Liability

- Bad faith failure to settle.
- Bad faith denials of coverage.
- Bad faith delays in payment.
- Consequential Damages.
- Punitive Damages.
- General Business Law, §349.

Initial Receipt of Claim for Extra-Contractual Damages

- Analyze theories of liability and determine potential defenses.
- Collect appropriate documents from insurance company client (claims files, underwriting files, electronic files).
- Obtain files from insured's third-party administrators or other agents, if any.
- Determine if motion to dismiss is warranted.

- Identify all claims representatives involved with the claim, including decisions on coverage, and including former employees, supervisors and management.
- Determine if there is any potential relevant claims handling manual. Limit to the one in effect during the claims handling and used by the claims unit which actually handled the claim.
- If underwriting issues are relevant, identify all involved underwriters (including underwriting agents).

- Consider subpoena of broker's files.
- Determine if there are any potentially relevant underwriting guidelines (including submissions to regulators or guidelines sent to agents).
- Determine what facts need to be gathered through discovery.
- Analyze factual and legal basis for all client coverage decisions.

- If broker/producer is agent of insurance company, need to get copy of agency agreements (in effect at the time of agent's conduct).
- If agent is involved, consider contractual indemnification claim against agent.
- Issue litigation holds to appropriate persons within company and its agents.

- Discuss with insured's counsel to potentially limit or dismiss extra-contractual claims, and to identify what damages are being sought (if not clear from complaint).
- Prepare a detailed timeline of known facts and events.
- Interview relevant persons from claims, underwriting, and agents.
- Determine need for immediate corrective action, if any (including payment of all or part of claim).

- Identify any choice of law issues.
- Obtain copies of all potentially applicable insurance policies, and all coverage-related correspondence.
- If any company documents are no longer in existence, need to obtain copy of insurance company's document retention policy.
- Determine whether insured's choice of venue is proper and also evaluate whether to remove State Court action to Federal Court.

Bad Faith Failure to Settle Claims

Pavia v. State Farm

- Gross disregard standard.
- Bad faith is established any “where liability is clear and potential recovery far exceeds the insurance coverage”.
- Consider totality of circumstances.
- Underlying claimant’s chance of success.

- Bad faith claim can be assigned to claimant.
- Potential magnitude of damages.
- Did insurer properly investigate the claim?
- Did insured delay settlement negotiations by failing to cooperate or by misrepresenting the facts?
- The claimant's time-restricted settlement demand is not controlling.

OTHER CONSIDERATIONS

- Failure to keep the insured informed of settlement negotiations is evidence of bad faith.
- Under New York law, a primary carrier owes a direct duty to an excess carrier.
- Lack of settlement demand within policy limits.
- No bad faith if coverage is reasonably disputed.

- May be a defense to bad faith, if the insurer needs further information to evaluate the claim (medical records, independent medical examinations of claimant, or depositions).
- Advice of counsel (dangerous defense because it always results in waiver of attorney-client privilege). Tactical considerations – jury may not believe insurance company relied solely on advice of counsel.
- Be careful in responding to “hammer letters” from excess carrier or insured’s personal counsel.

Bad Faith Denial of Coverage

- The test is whether the insurance company has a reasonable or arguable basis for disclaiming coverage (insurer's negligence or mistakes are not equivalent to bad faith).
- If applicable, insurer should argue that particular coverage issues are novel or unsettled.
- Insurer should argue, to the extent possible, that its investigation was prompt, fair, reasonable and thorough.

- If applicable, insurer should rely on reasonable advice of its retained qualified experts (for technical issues, etc.)
- Insurer should conduct its coverage investigation with no predetermined outcome. Claims technicians should be open to reevaluating the case as new facts are developed.
- Potential defense if insured misrepresented or concealed facts or did not cooperate with the investigation.

- The insurer must document need to obtain or clarify certain facts.
- The insurer must carefully document all information/documents sought from insured.
- Insurer must treat insured with courtesy and professionalism (and avoid personal attacks or criticisms).

- Insurer should adhere to its internal claims handling procedures (or document reasons for any deviation).
- Insurer should consult coverage counsel on complex or difficult policy interpretation questions.
- Insurer should invite insured/broker to provide additional or contrary facts/information

Defenses to Consequential Damages Claims

- No bad faith if denial of coverage was correct or at least arguable or reasonable.
- Some or all of the damages sought by the insured are not within the reasonable contemplation of the parties.
- Some or all of the damages are speculative or not caused by the insurer's alleged bad faith.

- The insured did not use reasonable efforts to mitigate damages.
- No recovery allowed for fees incurred in the prosecution of consequential damages claim.
- Consider retention of qualified damages experts.

Defenses to Punitive Damages Claims

- No bad faith.
- No tortious conduct independent of breach of contract.
- No egregious or morally culpable conduct.
- No pattern of conduct directed at the public (only private coverage dispute).
- Argue that other unproven claims of bad faith are irrelevant.
- Argue that mere fact of other similar coverage disputes is not evidence of bad faith.

Insurer's Discovery Demands

Use of Interrogatories Directed to Insured:

- The decisions/events which allegedly constitute bad faith.
- The basis for each claim of bad faith.
- All communications with the insurer that is allegedly evidence of bad faith.
- Each item of alleged consequential damages.

- How each item of alleged consequential damages is calculated.
- Each policy provision allegedly violated.
- Each witness the insured relies on to prove bad faith and consequential damages.

Use of Documents Demands

- All documents relied on to prove bad faith.
- All documents relied on to prove consequential damages.
- All documents relating to communications with the insurer.
- All documents relating to communications with the broker.
- Expert witness disclosure demands.
- Use of Notices to Admit (particularly during later stages of discovery).

Responding to Insured's Discovery Demands

- Use due diligence to obtain entire claims file and underwriting file (and documents kept by any agents of company).
- Seek to prevent or limit discovery of other claims. Use of burden affidavits (difficulty to obtain the documents outweighs the benefits).

- Seek to avoid disclosure of
 - a) Reserve information,
 - b) Communications with reinsurers,
 - c) Attorney-client privileged communications,
 - d) Proprietary information,
 - e) Insurer employee personnel files, and
 - f) Insurer employee training materials.

- Need contact person within insurance company to assist in the collection of documents.
- May need to discuss document production with insurance company IT person (e.g. what types of document searches are feasible).
- May need to obtain insurance company's record retention policy (for long-tail claims, etc.).

- May want to provide appropriate claim manuals or guidelines if the claim handling complied with such protocols.
- Care should be given to assess insurance companies' designation of witnesses at deposition and trial (including experience in testifying, credibility, composure, temperament and ability to withstand cross-examination).

Summary Judgment Motions

- Lack of standing for bad faith denial of coverage (if plaintiff is not an insured).
- No bad faith if coverage position was at least arguable or reasonable.
- Dismissal of punitive damages claims.
- Dismissal of claims for attorney's fees to prosecute bad faith action.

- Dismissal of GBL §349 claims (only private contract dispute with no broad impact on consumers at large).
- Dismissal of bad faith failure to settle (if no lost opportunity to settle or no clear liability).
- Use motion for summary judgment to limit extra-contractual claims, if not outright dismissal.