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The Bad Faith Sentinel

Standing guard on developments in the law of insurance bad faith around the country

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Western District of Washington: Insured That Violated Duties of Notice and Cooperation Could Not Make Out Claim for Bad Faith Based on Insurer's Lengthy Investigation

Granite State Ins. Co. v. Integrity Structures, LLC, No. C14-5085BHS, 2015 WL 136006 (W.D. Wash. Jan. 9, 2015).

The U.S. District Court for the Western District of Washington held that an insurer did not act in bad faith where the insured assigned its rights against the insurer to the underlying plaintiff before it provided notice to the insurer and then provided minimal information in response to the insurer's requests for nearly a year.

In 2006, Integrity Structures, LLC ("Integrity") contracted with a developer to serve as general contractor for the construction of a 30-unit condominium project in Westport, Washington. When construction deficiencies with the condos emerged, the condominium homeowners' association (the "Association") sued the developer and Integrity in Washington state court. Integrity had several insurance policies covering the relevant period. One of Integrity's insurers, Gemini Insurance Company ("Gemini"), appointed defense counsel.

In September 2012, Integrity entered into a contingent settlement with the Association. Among other things, the agreement called for Integrity to tender its defense to its three remaining primary general liability insurers, including Granite State Insurance Company ("Granite State"). If neither Granite State nor Integrity's other two insurers (other than Gemini) agreed to defend Integrity within 60 days of the tender, Integrity agreed to consent to judgment in favor of the Association for \$4.1 million and assign all claims it had against the insurers (other than Gemini) to the Association. In turn, the Association agreed not to execute on the consent judgment.

Granite State received Integrity's tender requesting a defense on November 29, 2012. The tender included the most recent version of the Association's complaint but not the contingent settlement agreement. On December 7, 2012, Granite State wrote to Integrity's lawyer and requested several categories of information in order to evaluate the coverage claim. The lawyer for Integrity referred Granite State to counsel for the Association. Between late December 2012 and November 2013, Granite State repeatedly sought information from Integrity and the Association but received no substantive response.

On September 30, 2013, a stipulated consent judgment for \$4.1 million was entered against Integrity in the state court action. Two months later, on November 20, 2013, Integrity finally disclosed to Granite State the contingent settlement agreement and the consent judgment.

In January 2014, Granite State filed suit against Integrity in the U.S. District Court for the Western District of Washington, seeking a declaratory judgment that it had no duty to defend Integrity or provide coverage for the \$4.1 million consent judgment. Integrity filed counterclaims for breach of contract and bad faith, as did the Association when it intervened in the case in June 2014. The parties filed cross-motions for summary judgment.

The court ruled that although Granite State did have a duty to defend Integrity, because the allegations in the state court lawsuit were “conceivably” covered by the policy, Integrity and the Association had failed to make out a bad faith claim. The court stated that an insurer acts in bad faith if its breach of the duty to defend “was unreasonable, frivolous, or unfound-

ed.” Further, a Washington statute provides that an insurer must complete its investigation within 30 days if doing so is reasonably possible, and that violation of that statute would also signal bad faith. While Granite State’s investigation took far longer, the court noted that Granite State’s prompt and repeated attempts to gather information from its insured were met with “virtual silence.” Thus, Granite State did not act in bad faith.

Further, the court held that Integrity and the Association had violated their duties of notice and cooperation under the Granite State policy by failing to provide Granite State with notice of the state court lawsuit for 15 months and keeping silent about their settlement until even more time had passed. Stating that Granite State may in the future be able to show that it had been prejudiced by Integrity’s lack of cooperation (and more than likely collusion), the court denied Granite State’s motion for a declaration that Integrity had forfeited its coverage, but did so without prejudice, noting that fact issues remained as to whether Granite State had been “actually and substantially prejudiced.”

Western District of Washington: No Bad Faith Where Insurer Refuses to Provide a Defense Where Facts Confirmed Insured’s Actions Were Intentional and Criminal

Wargacki v. W. Nat’l Assurance Co., No. C13-5373RBL, 2015 WL 74111 (W.D. Wash. Jan. 6, 2015).

The U.S. District Court for the Western District of Washington grants summary judgment to an insurer ruling that the insurer had no duty to defend a complaint arising out of an insured’s intentional killing of his girlfriend despite the fact that the girlfriend’s estate had characterized the incident as “negligence.”

On June 27, 2010, Michael Erb (“Erb”) shot his pregnant girlfriend, killing her and their unborn child. Erb then took his own life. Following an investigation, the police concluded that Erb had murdered his girlfriend and intentionally killed himself. Erb had a homeowner’s insurance policy with Western National Assurance Company (“Western”). The policy contained an exclusion barring coverage for criminal and intentional acts.

The girlfriend’s estate sued Erb’s estate for wrongful death. The suit alleged that Erb caused his girlfriend’s death “either negligently, intentionally or recklessly.” The suit further alleged that Erb’s actions constituted the tort of outrage. The attorney for Erb’s estate informed Western of the lawsuit and requested

a copy of the homeowner’s policy. The attorney then wrote to Western and requested a “coverage determination.” Upon investigation, Western concluded that because the shooting was not an accident, it was not covered by the policy. Accordingly, Western did not defend or have any other role in the lawsuit.

In the underlying litigation, Erb’s estate conceded liability to the girlfriend’s estate and judgment was entered against it. Almost a year after judgment was entered, the girlfriend’s estate demanded payment from Western. Western responded by filing a declaratory judgment action in the United States District Court for the Western District of Washington. Western moved for summary judgment and sought a determination that it had

no duty to defend in the underlying litigation. The girlfriend's estate filed a cross motion for summary judgment, arguing that the complaint in the underlying litigation triggered Western's duty to defend, and that its failure to provide a defense was bad faith.

The court had previously ruled that the policy's intentional and criminal acts exclusion applied. Because the shooting was intentional, Western had no duty to indemnify the Erb estate. Nevertheless, the girlfriend's estate argued that Western still had a duty to defend the Erb estate in the underlying case and that its failure to do so was bad faith resulting in coverage by estoppel. The court rejected the estate's argument and entered summary judgment in Western's favor. The estate

had argued that because the complaint in the underlying case characterized the shooting as "negligence," the duty to defend was triggered and the exclusion did not apply. The estate further asserted that because it was impossible to know exactly what transpired, it was arguably conceivable that the shooting was non-intentional and non-criminal. The court reasoned that while the complaint did use the term "negligence," it did not allege any facts that would suggest that the shooting was an accident. The mere conceivable possibility that the shooting might have been accidental was not sufficient to trigger coverage where all facts and Western's investigation led to the necessary conclusion that the killing was an intentional and criminal act. Accordingly, Western had no duty to defend and there was no bad faith as a matter of law.

District of Arizona: Employee's Intentional, Incorrect, and Unreasonable Handling of Claim Subjects Insurer to Finding of Bad Faith

Haney v. ACE Am. Ins. Co., No. CV-13-02429-PHX-DGC, 2015 WL 58670 (D. Ariz. Jan. 5, 2015).

District of Arizona: Court Grants Partial Summary Judgment on Bad Faith Claim for Failure of Insurer to Make Retroactive Payments, but Question of Fact Remained with Respect to Insurer's Initial Miscalculation of Benefits.

Plaintiff Jane Haney fell on a cement surface and injured her head and knee; as a result, she was out of work for two years. Haney's worker's compensation coverage was administered by ACE American Insurance Company and Sedgwick Claims Management Services. After a ten-month delay in receiving her correct benefit amount, Haney sued ACE, Sedgwick, and Sedgwick employee Lori Hasty for bad faith.

Sedgwick assigned Defendant Hasty to manage Haney's workers compensation claims. Hasty made two errors in calculating Haney's claims; first, Hasty based the benefits on Haney's annual salary, as opposed to her monthly salary, and second, Hasty miscalculated Haney's annual salary as the amount she earned in just the first few months of the year. These errors resulted in Haney receiving \$1,247 monthly, as opposed to the \$4,966 for which she qualified. This amounted to a \$20,000 deficiency before the mistake was corrected.

The District of Arizona found that this miscalculation did not amount to bad faith. Under Arizona's bad faith law, which is analyzed as a breach of the duty of good faith and fair deal-

ing, a plaintiff must prove that the defendant's actions were "objectively unreasonable and intentional." The Court held that under the facts, a genuine dispute existed as to whether the miscalculations amounted to a conscious failure to investigate, or were mere negligence. As such, the miscalculation itself was not bad faith as a matter of law.

However, Haney also argued a second basis for bad faith: that Sedgwick's employee Hasty failed to make retroactive payments to Haney that would compensate her for the initial miscalculation, even though Hasty was repeatedly notified of this issue over a period of ten months. The undisputed evidence shows that Hasty and Defendants failed to respond for the entire ten month period. When deposed, Hasty acknowledged she received emails from Haney and her representatives, but when asked why she didn't respond, Hasty stated that "the only [reason] would be the workload."

The Court found that Hasty's behavior was objectively unreasonable, as there was no dispute that Haney was owed the benefits. Moreover, Hasty's conduct was intentional; the

requisite “intent” need not be “intent to harm”, but rather that the party “either knows that its position is groundless or . . . fails to undertake an investigation adequate to determine whether its position is tenable.” The Court further found that

Hasty’s supervisor’s attempts to correct the situation were not a defense for ACE; the duty of good faith is non-delegable for the insurer, and thus if an employee or delegate of ACE handled the claim in bad faith, ACE would be liable.

Court of Appeals of New Mexico Reverses Bad Faith Judgment for Insured and Remands for New Trial on Bad Faith Claim

Progressive Casualty Ins. Co. v. Vigil, No. 32,171 (N.M. Ct. App. Jan. 21, 2015).

Court of Appeals of New Mexico rules that district court abused its discretion in excluding evidence of previous coverage ruling in favor of insurer and insurer’s settlement of third-party claims against insured, and remands for new trial on bad faith claim.

Progressive Casualty Insurance Company filed a declaratory judgment action against Defendants Nancy Vigil and her son, Martin Vigil, asking the district court to determine that the Vigils had no coverage on the day Martin was involved in an automobile accident. The Vigils filed a counterclaim for bad faith. Nancy Vigil added a car to her automobile insurance policy in late September 2002. She paid the premium on October 3, even though it was not due until October 15. Later, Nancy Vigil received a notice from Progressive stating that her policy would renew on November 3. She called Progressive’s automated system to verify the renewal date, and the system told her that the next premium was due on November 15. As a result, she did not pay the premium on November 3. On November 4, Martin Vigil got into an automobile accident which killed one passenger and seriously injured another. Progressive initially advised the Vigils that they had coverage. A couple of weeks later, however, Progressive advised the Vigils that they did not have coverage because the policy had lapsed on November 3.

In December 2002, Progressive filed a declaratory judgment action on the coverage issue and the Vigils counterclaimed, alleged bad faith, among other claims. While the declaratory judgment action was pending, Progressive settled the underlying wrongful death and personal injury claims against Martin Vigil for \$100,000 each, subject to a reservation of rights. Progressive then amended its complaint to seek reimbursement from the Vigils for the \$200,000 in the event the factfinder determined that the Vigils did not have coverage on the day of the accident. The district court granted partial summary judgment for Progressive on the coverage issue and a jury

found that Progressive was entitled to reimbursement from the Vigils in the amount of \$200,000. The Vigils appealed, and the Court of Appeals reversed the district court’s grant of partial summary judgment, finding that the issue of whether the Vigils had coverage involved disputed material facts. The Court of Appeals remanded for a new trial on the coverage and reimbursement claims.

The case was reassigned to a new judge while the appeal was pending. On remand, the district court granted summary judgment for the Vigils on the reimbursement issue. The district court concluded as a matter of law that Progressive did not have a right to seek reimbursement for the payments it made to settle the claims, even if the Vigils did not have coverage on the date of the accident. The district court also entered an order before trial prohibiting Progressive from introducing evidence or making any reference to the earlier proceedings, including the \$200,000 Progressive paid to settle the third-party claims. During closing arguments at the second trial, the Vigils’ counsel stated that “[t]his case ha[d] been going on for nine years” and that during that time, Progressive “wouldn’t even pay for [Martin’s] truck, let alone all the other coverages they should have provided under the policy” (emphasis in opinion). The jury found that the Vigils had coverage on the date of the accident and that Progressive acted in bad faith regarding the coverage claims. The jury awarded approximately \$40,000 in damages under the policy, \$37,000 in compensatory damages and \$11.7 million in punitive damages for their bad faith claim. The district court awarded the Vigils approximately \$1.4 million in attorney fees and \$35,000 in costs. Progressive appealed.

On appeal, Progressive argued that the district court erred by prohibiting Progressive from admitting evidence of (1) the previous judge's ruling that the Vigils were not covered on the date of the accident, and (2) Progressive's payment of \$200,000 to settle third-party claims against the Vigils. In support of the first issue presented on appeal, Progressive argued that even though the coverage ruling was reversed on the first appeal, the fact that the district court initially ruled in Progressive's favor indicates that Progressive did not act in bad faith and should not be liable for punitive damages.

The Court of Appeals agreed. "In New Mexico, an insurer acts in bad faith when it refuses to pay a claim of the policyholder for reasons which are frivolous or unfounded," but "does not act in bad faith by denying a claim for reasons which are reasonable under the terms of the policy" (internal quotations and citations omitted). The Court of Appeals concluded that the exclusion of evidence of the previous judge's ruling on the coverage issue was an abuse of discretion because that evidence was relevant to the issue of whether it was reasonable for Progressive to question the Vigils' coverage. The Court of Appeals reached this conclusion for five reasons: (1) whether Progressive acted reasonably in disputing coverage was an important fact in determining whether Progressive acted in bad faith; (2) the fact that the previous judge determined that there was no coverage tends to make the fact that Progressive acted reasonably more probable than it would be without the evidence because it suggests that the coverage issue was fairly debatable; (3) cases from other jurisdictions have ruled that a district court's previous rulings on coverage, even where they were later reversed, are dispositive of whether an insurer acted reasonably in disputing coverage; (4) exclusion of evidence regarding the prior ruling prevented the jury from considering that Progressive's decision to persist with its coverage position may have been reasonably influenced by the fact that a judge had validated this position; and (5) the Vigils did not argue that any exceptions to the general rule that relevant evidence is admissible should apply in this case. The Court of Appeals added that its "decision regarding the admissibility of the previous

ruling is only relevant to the issue of Progressive's reasonableness under the bad faith claim and has no application to the jury's prior determination of coverage."

The Court of Appeals also concluded that the district court abused its discretion by excluding evidence of Progressive's payment of \$200,000 to settle claims against the Vigils. This evidence, too, was relevant to the Vigils' bad faith claim against Progressive because "it tends to make it less probable that Progressive acted in bad faith over the course of the coverage dispute." The Court explained that "[i]n making these payments, Progressive both compensated the third-party claimants and prevented the Vigils from having to defend themselves against personal injury and wrongful death claims." The Court also noted that "the Vigils took advantage of [the district court's] exclusionary ruling during closing arguments and gave the jury the false impression that Progressive had failed to pay anyone during the long nine-year time period that it had taken to litigate the insurance coverage dispute." Thus, the Court of Appeals concluded that "it was unfair and an abuse of discretion to exclude evidence that was relevant to rebut the Vigils' claim that Progressive acted unreasonably over the long course of the coverage dispute, especially where this exclusion presented the jury with an incomplete and one-sided picture of Progressive's actions."

The Court of Appeals reversed the judgment on the bad faith claim and the compensatory and punitive damages awarded on that claim, and remanded the case to the district court for a new trial on the bad faith claim. The Court of Appeals also vacated the award of attorney fees and costs because the applicable statute awards attorney fees and costs only upon a finding that the insurer acted unreasonably in refusing to pay a claim: "Because the reasonableness of Progressive's actions in addressing the insurance coverage issue and pursuing a declaratory judgment decision remains to be resolved under the bad faith claim that is now remanded for a new trial, the award of attorney fees and cost[s] . . . must also be redetermined after the bad faith proceedings are resolved."

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