Bad Faith in First Party Property Claims

By: Everette Lee Herndon, Jr.

The insurance industry has recognized the concept of "Bad Faith" for many years and has acknowledged that an insurance policy carries with it a covenant of good faith and fair dealing.

The Fire, Casualty & Surety Bulletins, an insurance industry publication recognized nationwide by insurance companies, says that:

> *At heart, bad faith is the intentional failure by an insurer to perform the duty of good faith and fair dealing implied at law. Generally, an insurer may be acting in bad faith when it refuses to pay a claim and (1) has no reasonable basis for refusing to pay and has actual knowledge of that fact, or (2) has intentionally failed to determine whether it had a reasonable basis for so refusing.*

The courts in various states have recognized the concept of a covenant of good faith and fair dealing between the insurance company and the insured. A breach of this implied covenant or duty is a violation of the insurance policy itself and of good claims handling practices. This breach may (or may not) be recognized by a state as a cause of action entitling the insured to sue the insurance company for Bad Faith.

Bad Faith is more than ordinary negligence or breach of contract.

Mike Johnston, a trial lawyer from Oklahoma, has developed a list of his "Top 40" types of acts of Bad Faith by insurance companies. Recognition of these acts or types of acts as Bad Faith will depend on your local state court. Mr. Johnston's list can be found at: http://www.quatloos.com/traps/badfaith.htm

The actual implementation of the concept of Bad Faith varies from state to state. Some states recognize Bad Faith as either a tort or contract cause of action (or both); others states do not - i.e. you can sue an insurance company for Bad Faith in some states but not in others. However, each lawsuit that goes to trial could change the state's view on Bad Faith.

For a quick summary of where your state may stand on Bad Faith as a cause of action, either tort or contract, check out the Policyholders of America web-site at http://www.policyholdersofamerica.org/does_your_state_punish_bad_faith.pdf for a chart covering the 50 states. For definite information on your state, consult a local attorney as laws change frequently.

One of the earlier cases allowing a Bad Faith claim against an insurer was the California case of Gruenberg v. Aetna Ins. Co., 510 P.2d 1032 (1973). In Gruenberg, the court allowed the insured to pursue a first party Bad Faith action when the insurer failed to deal fairly and in good faith by

refusing, without proper cause, to compensate its insured for a covered loss.

An Arizona court, in the case of Hawkins v. Allstate Ins. Co., 733 P.2d 1073 (1987), stated that first party Bad Faith actions are allowed if insurer intentionally denied a claim without a reasonable basis.

In Texas, the case of Universal Life Ins. Co v Giles, A.W. 2nd 48 (1997) refined the Texas standard to say that an insurer acts in Bad Faith when it denies or delays payment of a claim after it should have become reasonably clear that the claim was covered.

Recovery of damages for Bad Faith lawsuits also varies from state to state. Some states allow punitive damages (above and beyond the policy limits), while other states restrict damages to actual policy coverage or contract damages.

Check with your local attorney to determine what causes of action (if any) are allowed in your state and what types of damages are recoverable.

Originally published in: The Advocate, a newsletter published by Policy Holders of America, September 2004