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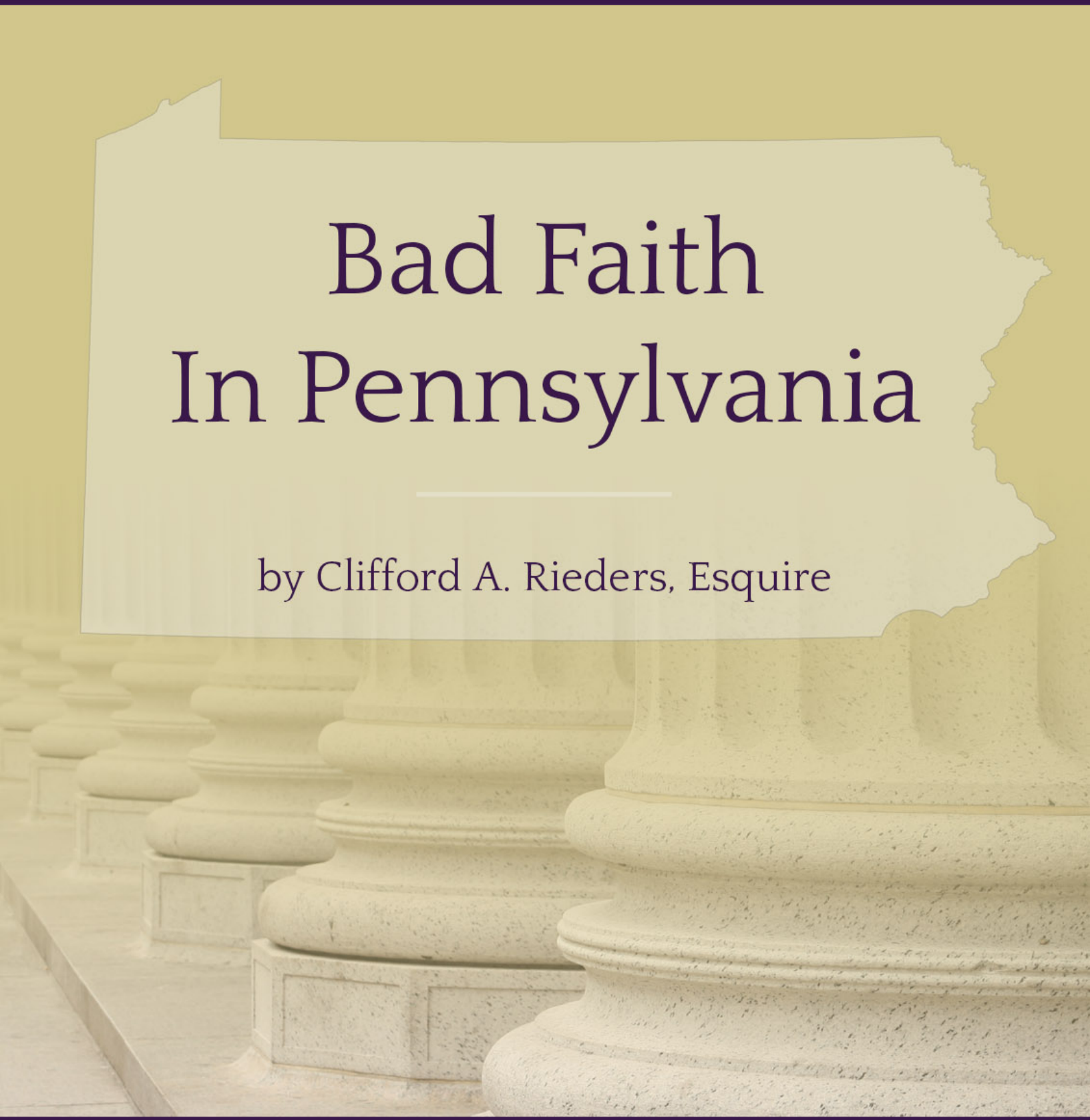

Bad Faith In Pennsylvania

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Updated February 21, 2019

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1. What is Bad faith

1.1 Statute. Bad faith is a statutorily created tort action. 42 Pa.C.S. Section 8371 states:

> In an action arising under an insurance policy, if the court finds that the insurer has acted in bad faith toward the insured, the court may take all of the following actions:
>
> (1) Award interest on the amount of the claim from the date the claim was made by the insured in an amount equal to the prime rate of interest plus 3%.
>
> (2) Award punitive damages against the insurer.
>
> (3) Assess court costs and attorneys fees against the insurer.

1.2 Not a Common Law Tort Action. Bad faith is not a common law action in tort. DiGregorio v. Keystone Health Plan East, 840 A.2d 361 (Pa. Super. 2003), D'Ambrosio v. Penn. Nat. Mut. Cas. Ins. Co., 431 A.2d 966 (1981).

1.2.1 Two-Prong Test. Rancosky v. Washington National Insurance Co., 642 Pa. 153 (Pa. Sup. Ct. 2017) Baer, J. In this discretionary appeal, we consider, for the first time, the elements of a bad faith insurance claim brought pursuant to Pennsylvania's bad faith statute found at 42 Pa.C.S. § 8371. For the reasons set forth below, we adopt the two-part test articulated by the Superior Court in Terletsky v. Prudential Property & Cas. Ins. Co., 649 A.2d 680 (Pa. Super. 1994), which provides that, in order to recover in a bad faith action, the plaintiff must present clear and convincing evidence (1) that the insurer did not have a reasonable basis for denying benefits under the policy and (2) that the insurer knew of or recklessly disregarded its lack of a reasonable basis. Additionally, we hold that proof of an insurance company's motive of self-interest or ill-will is not a prerequisite to prevailing in a bad faith claim under Section 8371, as argued by Appellant. While such evidence is probative of the second Terletsky prong, we hold that evidence of the insurer's knowledge or recklessness as to its lack of a reasonable basis in denying policy benefits is sufficient. Therefore, we affirm the judgment of the Superior Court, which partially

> vacated the trial court's judgment and remanded for further proceedings on Appellee's bad faith claim.

Though the trial court found that Conseco was "sloppy and even negligent" in its handling of Rancosky's claim, it ultimately found in favor of Conseco on the bad faith claim.

Because we agree with the legal test for bad faith claims under Section 8371 articulated by the Superior Court in this case and agree that the trial court misapplied that test by considering Conseco's subjective motivation in determining whether it had a reasonable basis for denying Rancosky's claim, we affirm the Superior Court's ultimate disposition to vacate the trial court's judgment and remand for further proceedings on Rancosky's bad faith claim. However, we respectfully believe that the Superior Court erred in making a specific determination as to whether the record in this case demonstrates Conseco's lack of a reasonable basis for denying Rancosky benefits, i.e., the first Terletsky prong. The Superior Court premised its holding in this regard upon credibility determinations the trial court made in its Rule 1925(a) opinion. However, because it is unclear to what extent the trial court's findings on the reasonable basis prong of Terletsky were intertwined with its erroneous belief that proof of Conseco's motive of self-interest or ill-will was required, upon remand the trial court should consider both prongs of the Terletsky test anew.

> In summary, we hold that, to prevail in a bad faith insurance claim pursuant to Section 8371, a plaintiff must demonstrate, by clear and convincing evidence, (1) that the insurer did not have a reasonable basis for denying benefits under the policy and (2) that the insurer knew or recklessly disregarded its lack of a reasonable basis in denying the claim. We further hold that proof of the insurer's subjective motive of self-interest or ill-will, while perhaps probative of the second prong of the above test, is not a necessary prerequisite to succeeding in a bad faith claim. Rather, proof of the insurer's knowledge or reckless disregard for its lack of reasonable basis in denying the claim is sufficient for demonstrating bad faith under the second prong. For these reasons, we affirm the judgment of the Superior Court, which vacated the trial court's judgment in part and remanded for further proceedings on Appellee's bad faith claim. On remand, the trial court should consider anew whether the above test has been met.

Thus, in Rancosky, the Pennsylvania Supreme Court concluded that the Pennsylvania Superior Court's long-standing two-pronged test, first articulated in

Terletsky, presents an appropriate framework for analyzing bad faith claims under 42 Pa.C.S. § 8371 since the Terletsky test, and its imposition of a recklessness standard for liability under the second prong, comports with the historical development of bad faith in Pennsylvania and effectuates the intent of the Pennsylvania General Assembly in enacting § 8371. Accordingly, the Court held that proof of an insurer's motive of self-interest or ill-will, while potentially probative of the second prong, is not a mandatory prerequisite to bad faith recovery under § 8371.

Pennsylvania federal courts have also followed the two-prong test in Terletsky. See, e.g., Long v. State Farm Mut. Auto Ins. Co, 2018 U.S. Dist. Lexis 367779 (M.D. Pa. Mar. 7, 2018).

1.3 UIM Claims. Bad faith includes handling of UIM claims, despite their similarity to third-party claims. Insurers have a duty of good faith and fair dealing with insureds regardless of first-party or third-party settings. The duty is one of good faith and fair dealing; it is not higher for first-party claimants. Condio v. Erie Ins. Exchange, 899 A.2d 1136 (Pa. Super. 2006). Bonenberger v. Nationwide Mut. Ins. Co., 791 A.2d 378 (Pa. Super 2002). The duty of the insurer is the same no matter what the party's status.

1.4 No Heightened Duty. Insurance companies do not have a heightened duty toward insureds in UIM/UM claims as opposed to purely first-party claims or third-party claims. Condio v. Erie Ins. Exchange, 899 A.2d 1136 (Pa. Super. 2006).

1.5 Misrepresentations. It is bad faith where insurer misrepresented the amount of coverage, arbitrarily refused to accept evidence of causation, secretly placed the insured under surveillance, auctioned in a dilatory manner, and forced the insured into arbitration be presenting an arbitrary "low ball" offer which did not bear a reasonable relationship to the expenses, and was 29 times lower than eventual arbitration award. Hollock v. Erie Ins. Exch., 842 A.2d 409 (Pa. Super. 2004), appeal granted in part by 878 A.2d 864 (2005) and 893 A.2d 66 (2005), appeal dismissed as improvidently granted, 903 A.2d 1185 (2006).

1.6 Reconsideration of Position. If evidence arises that discredits an insurer's reasonable basis for denying a claim, the insurer must reconsider its position. Bonenberger v. Nationwide Mut. Ins. Co., 791 A.2d 378 (Pa. Super 2002).

1.7 Investigative Practices. Bad faith applies to investigative practices and actions of insurer during litigation. O'Donnell v. Allstate Ins. Co., 734 A.2d 901 (Pa. Super. 1999). Insured, who contended that insured's litigation actions were evidence of bad faith, challenged court's jury instruction in bad faith trial. The trial court had erroneously ordered the jury to only consider the insurer's conduct prior to the initiation of the lawsuit.

1.8 Disclosure of Election. Insurance Company acted in bad faith when it failed to disclose or misrepresented the existence of insured's original unsigned UIM election form until the day of arbitration, when it notified its attorney of the form. Insurance Company did not make a reasonable effort to research its files to locate the form, which was requested by insured's attorney, and showed that insured's reduced coverage of $35,000 was not valid as he had not signed the form. Hayes v. Harleysville Mut. Ins. Com., 841 A.2d 121 (Pa. Super. 2003).

1.9 Settlement Factors. Insurance Company acts in bad faith when it refuses to settle merely because it believes that its insured is not liable for the claim asserted. Haugh v. Allstate Ins. Co., 322 F.23d 227 (3rd. Circ. 2003). Insurance Company must consider all factors bearing on settlement, including, the anticipated range of verdict, strengths and weaknesses of all evidence, history of the geographic area in similar cases, and the appeal, appearance, and persuasiveness of the injured and the witnesses at trial. An unreasonable settlement officer can be evidence of bad faith precluding summary judgment. Webber v. Erie Ins. Exch, PICS Case No. 13-3227 (C.P. Northampton Nov. 14, 2013).

1.10 Evasion of Obligation. Discovery violations may be "bad faith" if there is evidence that the violation was intended to evade the insurer's obligation under the insurance contract. W.V. Realty, Inc. v. Northern Ins. Co., 334 F.3d 306 (3rd Cir. 2003). At trial, plaintiffs had introduced evidence that the insurance company had violated rules of discovery by neglecting to disclose other bad faith cases. Plaintiffs failed to allege how the discovery violations were intended to "evade a duty owed under the policy"; therefore, the discovery violations should not have been admissible in court. Moreover, the fact that the discovery violation dealt with other bad faith cases was unfairly prejudicial.

1.11 Post-Lawsuit Conduct. Conduct by an insurance company after the filing of a lawsuit by insured, such as filing a counterclaim to the insured's lawsuit and alleging the insured committed fraud in his applications, may

be considered bad faith. Krisa v. Equitable Life Assur. Soc., 109 F. Supp.2d 316 (M.D.Pa.2000).

1.12 Disregard of Evidence. Insurance company which disregards insured's medical records, conducts no independent medical examination and makes no reasonable evaluation based on insured's presentment is liable for bad faith. Bonenberger v. Nationwide Mut. Ins. Co. 791 A.2d 378 (Pa. Super. 2002).

1.13 Lack of Supporting Evidence. When an insurer continues to advance its reasons for denial of a claim, without any supporting evidence, it commits bad faith. Zimmerman v. Harleysville Mut. Ins. Co., 860 A.2d 167 (Pa. Super. 2004).

1.14 Discovery Dispute. Misrepresenting the insured's coverage amount may be bad faith by an insurance company, and is not merely a discovery dispute; a discovery dispute could not be a basis for a bad faith claim. Adams v. Allstate Ins. Co., 97 F.Supp. 2d. 657 (2000). Insurance Company allegedly informed insured that his coverage was $50,000 less than the actual amount.

1.15 Court Order. An insurer's refusal to arbitrate a claim, despite the policy language, a court order, and advice of counsel, is clear and convincing evidence of bad faith. Anderson v. Nationwide Ins. Enterprise, 187 F. Supp. 2d 447(W.D. Pa. 2002).

1.16 Failure to Respond to Summons and Complaint. An insurer's refusal to respond to a summons and complaint, which resulted in a default judgment against insured, may be bad faith. Sichler v. General Accident Ins. Co. of America, 43 Pa. D&C 4th 529 (1999). Court denied insurer's motion to dismiss bad faith claim and held that a jury should decide if insurer's failure to respond to summons and complaint was a reckless disregard for its duty to defend prompted by improper purposes; thereby rising to the level of was bad faith.

1.17 Animal Strike. Insurer acted in bad faith in denying claim for damages incurred when insured's car hit deer. Insurer disregarded findings of its special investigative unit, ignored the finding of its appraiser that a deer had hit the vehicle, and denied portion of claim based on insured's driving of vehicle to repair shop, despite a lack of evidence that defendant should have known not to drive the vehicle after the accident. Rutkowski v. Allstate Ins. Co., 69 Pa. D&C 4th 10 (2004).

1.18 Expert Reports. Bad faith may exist where there is evidence that an expert deleted a key portion of his report after speaking to an insurance company consultant. Simon v. UnumProvident Corp. PICS Case No., 02-0842 (E.D. Pa. 2002). Psychologist's original report of insured was that insured was "totally disabled and unable to return to his former profession"; after speaking with insurance consultant, psychologist prepared a second report in which he deleted key phrases and the word "totally". Motion for summary judgment denied. Regarding an expert report, courts have allowed an expert's analysis of facts that the expert believed showed that the defendant deviated (or did not deviate) from insurance industry standards, but courts have not allowed the expert to offer an opinion on the ultimate issue in the case, i.e., whether the defendant insurance company acted in bad faith. Further, courts have not allowed expert opinions regarding subjective issues, such as the insurance company's state of mind. *See* Mirarchi v. Seneca Specialty Ins. Co., 2013 U.S. Dist. LEXIS 40513, 2013 WL 1187065, *5-*6 (E.D.Pa. March 22, 2013) (citations omitted). Thus, the court will not consider any expert opinion on the ultimate legal issue in this case as to whether defendant acted in bad faith. Nor does the court agree that a bad faith claim requires expert testimony. Shaw v. USAA Cas. Ins. Co., 2018 U.S. Dist. LEXIS 80101, *12-13, (M.D. Pa. May 11, 2018) (holding that Plaintiff had failed to prove with clear and convincing evidence that Defendant acted in bad faith. Rather, the extensive record indicates that defendant had reasonably attempted to gather all of the information necessary to properly evaluate the value of plaintiff's underlying claim against the tortfeasor).

1.19 Internal Procedures. Insurance Company acted in bad faith when it disregarded its internal procedures and failed to make a proper investigation. Insurance Company denied insured's claim based on the theory that the vehicle in dispute was an additional vehicle under the policy, despite evidence to the contrary, and the policy language. Galko v. Harleysville Pennland Ins. Co., 71 Pa. D & C. 4th 236 (Lackawanna 2005).

1.20 Treating Physicians. Although insured's two treating physicians pled guilty to insurance fraud, there was no evidence that physician who had reviewed records regarding insured's injuries was in error or that insured had not been in an accident; therefore, a jury could reasonably find that the insurance company acted in bad faith by not having a reasonable basis for denying benefits to insured. Insurance Company's motion for

summary judgment denied. Murrell v. Allstate Ins. Co., PICS Case No. 00-1494 (E.D. Pa. 2000).

1.21 Setting Reserve. Grossi was a passenger in a vehicle owned by Tarquinio Brothers Bakery, driven by Michael Tarquinio. Grossi was severely injured and made a UIM claim against his parents' policy, where he was an insured. Tortfeasor had total coverage of $3 million. Travelers paid on the UIM claim $500,000 in first-party medical expenses and $25,000 in lost income to Grossi. Travelers set an initial reserve of $1,000 for any potential UIM claim. Grossi, through counsel, notified Travelers of his demand for the full UIM policy limits of $300,000. The question is whether the total value of the losses exceeded $3,300,000. Grossi's demand included an expert's analysis of his future earnings which alone were valued at $4,252,725. Without adjusting the $1,000 reserve, the claim was transferred to an adjustor who suggested that Grossi's future earnings lost estimate was highly speculative. The trial court's finding of bad faith including punitive damages was sustained. Grossi v. Travelers Personal Insurance Company, 79 A.3d 1141 (Pa. Super. 2013). The court identified a number of principles:

- Whether the insured had a reasonable basis for denying benefits under the policy and whether the insurer knew of or recklessly disregarded its lack of reasonable basis in denying the claim;
- Mere negligence or bad judgment is not bad faith;
- The insured must show that the insurer breached a known duty, the duty of good faith and fair dealing, through a motive of self-interest or ill-will;
- Bad faith extends to the handling of UIM claims;
- An action for bad faith may extend to the insurer's investigative practices;
- Bad faith conduct also includes lack of good faith investigation into facts, and failure to communicate with the claimant;
- Trial court may consider the insurer's claims manual when considering bad faith.

Central to the trial court's conclusion that Travelers acted in bad faith in its treatment of Grossi's UIM claim was its finding that Travelers established

and maintained only a $1,000 reserve throughout the life of the claim, without sufficient justification. The adjuster did not perform an independent analysis and did not question Grossi's vocational and economic expert or its estimate of future lost earnings. Travelers was not justified in postponing an independent evaluation while it monitored Grossi's third-party claim. Travelers never secured a report from an economist after having specified the need to do so.

1.22 The trial court properly looked at the following factors:

1.22.1 Not performing an initial independent analysis in its worksheet pursuant to its own manual;

1.22.2 Delaying its investigation while it monitored the third-party action, when the action was independent of the UIM claim;

1.22.3 Rejecting Grossi's future earnings and lost claim in expert opinion and setting an arbitrarily low reserve without any other basis for so doing;

1.22.4 Committing to arbitration without having commenced its investigation; and

1.22.5 Failing to communicate adequately with Grossi or explain its rejection of his claim.

2 What is not bad faith

2.1 Investigation After a Claim has been Filed. It is not bad faith when an underwriter investigates a policy after a claim has been filed. After insured filed a claim for disability benefits under her insurance policy, the insurance company investigated her medical history and determined it would not have issued the policy had it been aware of insured's history of chronic pain, disc disease and degenerative knee changes. Northwestern Mut. Life Ins. Co. v. Babayan, 430 F.3d 121 (3rd Cir. 2005). A plaintiff may also make a claim for bad faith stemming from an insurer's investigative practices, such as a "lack of a good faith investigation into facts, and failure to communicate with the claimant. Meyers v. Protective Ins. Co., 2017 U.S. Dist. LEXIS 11338, *16 (M.D. Pa. Jan. 27, 2017). Such bad faith investigative practices can include a significant failure to communicate claim status with the plaintiff. Id.