

News & Alerts

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Gimme One Reason: Alabama Supreme Court Concludes Insurer Only Needs One Debatable Reason To Overcome Bad Faith Claim

Taking your insurer to task for bad faith handling of a claim just became harder in Alabama. Bad faith lawsuits traditionally have allowed policyholders to recover their costs and additional damages when an insurer improperly mishandled or denied a covered claim and, by doing so, help maintain fair and prompt claim resolution. The recent decision of the Alabama Supreme Court in *Brechbill v. State Farm Fire & Cas. Co.*, 2013 WL 5394444 (Ala. Sept. 27, 2013), however, has made it easier for insurers to defeat bad faith claims.

The Alabama Supreme Court's opportunity to refine the bad faith cause of action came when a homeowner filed a claim with State Farm for windstorm losses including damaged roof shingles, interior wall cracks, crooked door frames, and extensive floor squeaking. Just months before the windstorm, State Farm's own representative had inspected the home, noted no interior damage, and confirmed that it was sufficiently sound to meet State Farm's underwriting guidelines.

In response to the homeowner's windstorm claim, a State Farm adjuster inspected the home and observed the roof shingle damage, cracked drywall, and separated door jams for which the homeowner sought coverage. The adjuster accepted that the roof shingle damage was covered by the policy, but recommended an engineer inspect the remainder of the home to determine the cause of interior damages. A third-party engineer concluded upon visual inspection that the interior damage pre-existed the windstorm due to misaligned load bearing walls and settlement of the home over time. Based on these conclusions, State Farm denied coverage for the interior damage. The homeowner then hired his own engineer, who disputed the findings of State Farm's engineer. State Farm's engineer responded, in turn, contradicting the findings of the homeowner's engineer. State Farm then reissued a claim denial.

The homeowner filed suit against State Farm alleging breach of the policy, bad faith failure to pay claims, and bad faith failure to investigate. State Farm moved to dismiss both bad faith claims prior to trial. The trial court granted the motion in part, dismissing only the bad faith failure to pay claim. The case proceeded to trial on the breach of the policy and failure to investigate claims. The jury awarded the homeowner \$150,000 in compensatory damages on each of the two remaining claims. State Farm appealed only the failure to investigate bad faith award.

In considering the appeal, the Alabama Supreme Court first reviewed conflicting and confusing law arising out of prior bad faith cases. To clear this confusion, the Court noted that there is only one cause of action for bad faith in Alabama: not separate torts for "bad faith failure to pay" and "bad faith failure to investigate" (also sometimes called "normal" and "abnormal" in prior Alabama cases).

The Court then clarified the elements of the single cause of action:

1. Breach of an insurance contract by the insurer;
2. Insurer's intentional refusal to pay the claim;
3. The absences of any reasonably legitimate or arguable reason for the refusal to pay;
4. The insurer's actual knowledge of the lack of any reason; and
5. If failure to investigate is alleged, the insurer's intentional failure to determine whether there is a legitimate or arguable reason to refuse to pay the claim.

By clarifying the elements of bad faith, the Alabama Supreme Court put to rest the notion that there were two separate torts for bad faith with differing elements.

The Court's analysis also laid clear the path for insurers to escape from bad faith claims: development of any "legitimate or arguable reason" on which it could refuse to pay the claim. The Court called such evidence a "sufficient condition" by which a bad faith claim is defeated. Notably, the Court also stated that insurers are not held to a standard of perfection in their review and coverage conclusions. Rather, all that will be required is the "existence of a debatable reason for denying the claim at the time the claims was denied" *Id.* (citing *Weaver v. Allstate Ins. Co.*, 574 So. 2d 771, 775 (Ala. 1990)). Continuing, the Court opined that "more than bad judgment or negligence is required" for a bad faith claim, suggesting instead conduct involving dishonest purpose, breach of a known duty, dishonesty, self-interest, or ill will also must be present.

The homeowner had no such claims. While State Farm's investigation may not have been perfect, the Court found that State Farm repeatedly reviewed and reevaluated the work from its investigation and the fact shared by the homeowner. Because the trial court also found that there was a reasonably legitimate or arguable reason for refusing to pay the claim (based on the State Farm investigation) when it dismissed the bad faith failure to pay claim, the Alabama Supreme Court held that this finding was dispositive of the failure to investigate a bad faith claim as well.

Brechbill likely will be cited for years to come within and beyond Alabama as insurers defend bad faith claims brought by their policyholders. *Brechbill* provides a roadmap to insurers of how to undertake claims review in a manner that maximizes the ability to defeat bad faith claims. By doing so, however, it also is instructive to policyholders: policyholders must always be prepared to question and push back against coverage denials until a fair reason – or no reason – is revealed. By doing so, a policyholder will have the most information available with which to determine its rights, options, and next steps in the pursuit of coverage for losses.

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This update is not legal advice and reflects only some information which may be of interest to policyholders. Additional information may be obtained by contacting Chandra Lantz at clantz@hf-law.com or 804.771.9586.