Insurance Coverage Update Pennsylvania

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INSURANCE COVERAGE

BAD FAITH

CIVIL LITIGATION

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ENVIRONMENTAL LAW AND LITIGATION
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Pennsylvania Supreme Court Holds Bad Faith Statute Does Not Encompass Pre-Contract Conduct

In Toy v. Metropolitan Life Ins. Co., 928 A.2d 186, 2007 Pa. LEXIS 1463 (Pa. July 18, 2007) (opinion by Chief Justice Cappy), the Pennsylvania Supreme Court definitively held that the bad faith statute does not apply to conduct that occurs prior to the existence of an insurance contract. The bad faith claim in Toy was based on the manner in which a life insurance policy was allegedly marketed, specifically, that MetLife marketed the life insurance policy as a savings plan in an attempt to disguise the true nature of the policy. The Court based its decision on construction of the statute, tracing the history of bad faith claims and the meaning of bad faith. After providing the history of bad faith claims, both in Pennsylvania and throughout the country, the Court held:

> That is, the term "bad faith" concerned the duty of good faith and fair dealing in the parties' contract and the manner by which an insurer discharged its obligations of defense and indemnification in the third-party claim context or its obligation to pay for a loss in the first party claim context.

Id. at *35 (citations and footnotes omitted). Thus, the bad faith statute does not apply to the manner in which an insurer solicits the purchase of a policy. The Court also made it clear that its holding applied to the nature of the claim available under the statute rather than the applicable standard of conduct used

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Pennsylvania Superior Court Holds That Failure To Warn Is Not A "Completed" Service

In Bombar v. The West American Insurance Company, 2007 Pa. Super. LEXIS 2171 (July 26, 2007) (opinion by Justice Stevens, dissent by Justice Klein), the Pennsylvania Superior Court held that the "Products–completed operations hazard" exclusion contained in West American's policy did not exclude coverage for a lawsuit including negligent failure to warn claims asserted by an individual against a forklift supplier with respect to an injury she suffered at work despite the fact that the definition of "your work" includes failure to provide warnings.

Suzanne Bombar was struck and severely injured by a forklift while at work. The forklift had been sold to Ms. Bombar's employer by Upright Materials Handling, Inc. ("Upright"), which was in the business of selling and servicing industrial equipment. After the sale, an agent of Upright installed a backup alarm and a strobe light on the forklift. Evidence existed that employees intentionally disconnected the alarm on several occasions and that the placement of the wires may have allowed them to disconnect during normal operations. Upright had been called several times to reinstall the alarm before the accident happened.

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to assess the claim:

> As we observe in footnotes 17 and 18, we do not consider what actions amount to bad faith, what actions of an insurer may be admitted as proof of its bad faith, whether an insurer's violations of the UIPA are relevant to proving a bad faith claim or whether the standard of conduct the Superior Court has applied to assess an insurer's performance of contractual obligations in bad faith cases is the correct one.
>
> In this area, the term "bad faith" refers not only to the *claim* an insured brings against his insurer under the bad faith statute, but also, to the *conduct* an insured asserts his insurer exhibited and establishes that it is liable. These matters although related, are nonetheless, separate and distinct. We write to the former. The concurrence appears to write to the latter.

Id. at *36-37 n.16.

The Court also addressed two issues related to the insured's claim under the Unfair Trade Practices and Consumer Protection Law (UTCPL)—whether justifiable reliance had to be shown and whether the parol evidence rule prevented the insured from establishing justifiable reliance. The Court, interpreting the version of the statute in effect at the time the claim accrued and was brought, held that justifiable reliance was a necessary element of the UTPCPL claim, relying on its prior decision in Weinberg v. Sun Co., Inc., 777 A.2d 442 (Pa. 2001). However, the Court held that the parol evidence rule did not prevent the insured from proving her case because the exception to the rule for fraud in the execution applied. The Court also noted that the insured had no duty to read the policy and thus the fact that she did not do so did not preclude her from proving justifiable reliance. Thus, summary judgment was incorrectly entered on this claim. ♦

Product Exclusion Bars Coverage For Defective Workmanship Even When Product Incorporated Into Another Product

In Plasticert, Inc. v. Westfield Ins. Co., 923 A.2d 489 (Pa. Super. 2007), a panel of the Superior Court reiterated that a business risk exclusion bars coverage where the underlying claim alleged the insured's product was defective, even when the product was incorporated into another product. There, the insured sought a coverage determination related to an underlying suit against it brought by a client, Westfalia Technologies, Inc. Westfalia alleged that Plasticert supplied thermoplastic wheels for use in Westfalia's gravity flow product line and after incorporation of the product, Westfalia received complaints from its customers that the wheels were breaking. Westfalia claimed that the wheels were nonconforming and sued, *inter alia*, for breach of contract, breach of warranty and fraud. The court limited its discussion to one exclusion ("'property damage' to 'your product' arising out of it or any part of it"), finding it dispositive of the case.

The court likened this case to Ryan Homes, Inc. v. The Home Indem. Co., 647 A.2d 939 (Pa. Super. 1994), appeal denied, 657 A.2d 491 (Pa. 1995), wherein a similar exclusion was interpreted to bar coverage where the insured's subcontractor's defective product necessitated repairs to the insured's customers' roofs. The court also noted that the underlying complaint did not allege that the wheels caused damage to any other aspect of the gravity flow product and did not allege personal injury or property damage to anything other than the wheels; it merely alleged that the wheels did not conform to specifications. (The court assumed without deciding that the underlying complaint alleged an occurrence and property damage.) ♦

Superior Court Reverses Bad Faith Judgment Entered Against Insurer

In Zappile v. AMEX Assur. Co., 928 A.2d 251 (Pa. Super. 2007), the trial judge entered judgment against the insurer on the plaintiffs' claim that it had handled the husband's UIM claim in bad faith. The court's finding was based on the following actions: failing to make a partial payment of $4000 for the excess wage loss claim, undervaluing the claim and forcing the claim to arbitration, never raising its initial $32,000 offer, and telling trial counsel that plaintiffs would not accept less than the $150,000 policy limits. In reversing, the Superior Court noted that the trial court relied heavily on the plaintiffs' expert, whose testimony contained factual and legal errors. Clear and convincing evidence did not exist to establish that the insurer acted unreasonably or was motivated by ill will.

The Court reiterated that UIM claims are adversarial in nature, a hybrid of first- and third-party claims and

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there is no heightened duty to a first-party claimant over a third-party claimant. The Court further held that Pennsylvania has not recognized a duty on the part of an insurer to make partial payment of undisputed amounts and would not do so in the context of this case, noting the difference between a dispute over coverage limits versus a dispute over the value of the injury and noting that the plaintiffs did not request a partial payment. Thus, the failure to make a partial payment could not properly form a basis for a finding of bad faith. Moreover, no evidence existed to support the court's other findings of bad faith and it was error to base the bad faith decision on the failure to raise the $32,000 offer where no evidence existed that the plaintiffs would have accepted anything but the policy limits.

Finally, the Court held that neither the delay in the arbitration nor the undervaluing of the claim could establish bad faith. The delay was attributable in part to the insurer's late discovery that the husband had a second car accident between the first accident and his shoulder surgery and the insurer was within its rights to investigate this accident's affect on the claimed injury. Other aspects of the delay could be attributed to the insurer, but the Court did not see clear and convincing evidence that the delay was the result of improper conduct. With respect to the value of the claim, the Court noted that, based on the arbitration award, the insurer had undervalued the claim and the plaintiffs had overvalued the claim in approximately the same amount ($62,820 versus $55,000). Moreover, bad faith cannot be established solely on the basis that an arbitration award was more than the insurer's offer. Additionally, the insurer's valuation was based on opinions of counsel and its own assessment of the injury and the evidence did not show that the undervaluation was the result of ill-will or conduct without reasonable basis. Thus, the Court reversed the judgment. ♦

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Ms. Bombar sued Upright for negligence and strict liability. West American refused to provide a defense to the lawsuit based on the products–completed operations hazard exclusion where the hazard was defined, in part, as:

> a. includes all "bodily injury" and "property damage" occurring away from premises you own or rent and arising out of "your product" or "your work" except
>
> * * *
>
> 2. Work that has not yet been completed or abandoned. However, "your work" will be deemed completed at the earliest of the following times:
>
> (a) when all of the work called for in your contract has been completed
>
> * * *
>
> (c) when that part of the work done at a job site has been put to its intended use by any person or organization other than another contractor. . . .
>
> Work that may need service, maintenance, correction, repair or replacement but, which is otherwise complete, will be treated as complete.

After a jury returned a verdict against Upright for negligence, Upright filed a declaratory judgment action claiming that West American should have defended it in the underlying suit, should indemnify it for the verdict, and should pay bad faith damages. Ms. Bombar filed a Petition to Intervene as the real party in interest, which the court granted. Upright subsequently assigned all rights under its policy of liability insurance to Ms. Bombar.

Following cross-motions for summary judgment in the declaratory judgment action, the trial court found coverage existed and held West American liable for bad faith.

On appeal, West American argued that coverage for the underlying suit was excluded based on the products–completed operations hazard exclusion contained in the policy. West American further argued that without coverage, it could not be held liable for bad faith.

The Superior Court disagreed, and adopted the trial court's interpretation of the exclusion that Upright's installation of the backup alarm was a service which, due to the negligent and faulty installation, had never been completed.

The Superior Court held that while the policy referred to "failure to warn," the warnings must be complete to fall within the exception. Specifically, the Court held:

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> Here, the installation of the backup alarm's wiring was not completed at the time of the installation of the wiring because of the negligent failure to warn, and therefore, the operation was not complete.

Consequently, the Superior Court affirmed the trial court's opinion, relying on a prior panel's decision in Keystone Spray Equip., Inc. v. Regis Ins. Co., 767 A.2d 572 (Pa. Super 2001).

In a strongly worded dissent, Judge Klein questioned the majority's holding, stating

> If the circular logic of the majority and trial court is true, then a failure to warn can *never* be excluded. . . . If the majority and the trial court are correct, then even the clear and unambiguous language of the instant policy, following a specific instruction from our Court [referencing Harford Mut. Ins. Co. v. Moorhead, 578 A.2d 492 (Pa. Super 1990) (advising insurance companies if they wanted to exclude failure to warn they should so state)], is still unenforceable. That does not make sense.

Judge Klein also questioned the wisdom of the pronouncements in Keystone and advocated for an *en banc* panel of the Superior Court or for the Supreme Court to revisit that rationale - - a failure to warn means installation is not complete.

The majority's affirmance of the bad faith summary judgment award is also troubling. The opinion does not provide a detailed analysis of the bad faith decision, but apparently did not find the insurer's interpretation of the policy reasonable and agreed with the trial court that the insurer had a duty to investigate the claim despite the insurer's argument that its only duty was to compare the four corners of the complaint to the policy. This opinion was issued one week after Toy, which reiterated that the duty to defend is based solely on the allegations of the underlying complaint. ♦

For any questions on the topics addressed in this newsletter, please call Alan S. Miller at 412-288-4004 or Bridget M. Gillespie at 412-288-4017. ♦

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