Virginia

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Bad Faith for a Bad Investigation

The US District Court in Alexandria recently found a carrier acted in bad faith. In this case, the insured, a power plant, suffered a loss to a large turbine. A piece of metal got inside the turbine and forced the insured to disassemble the turbine. The insured reported the loss to its insurer.

Initially, the insured reported an estimate for repair of $450,000. The insurer's adjuster responded that the loss did not exceed the power plant's deductible. The power plant responded quickly, listing costs far in excess of the deductible associated with the disassembly, removal, repair and re-assembly. This response gave an estimate total cost of over $1 million.

The carrier hired an engineer to go onsite and inspect the turbine. This engineer found that the damage reported came from covered losses. He also felt that the insured's cost estimates could be audited and lowered some.

Unsatisfied, the carrier hired two other engineers. Each found different causes of loss for most of the turbine damage. However, neither engineer physically inspected the turbine nor had either engineer repaired turbines. Both engineers determined that the loss to the turbines did not meet the $500,000 policy deductible. Without further research into the insured's estimates or obtaining other information on the damage or the cost to repair, the carrier denied coverage.

After a jury held for the insured and awarded more than $770,000 in damages, the Court turned to the bad faith allegations. The Court applied the venerable test of bad faith: *"In evaluating the conduct of an insurer, courts should apply a reasonableness standard. A bad-faith analysis generally would require consideration of such questions as whether reasonable minds could differ in the interpretation of policy provisions defining coverage and exclusions; whether the insurer had made a reasonable investigation of the facts and circumstances underlying the insured's claim; whether the evidence discovered reasonably supports a denial of liability; whether it appears that the insurer's refusal to pay was used merely as a tool in settlement negotiations; and whether the defense the insurer asserts at trial raises an issue of first impression or a reasonably debatable question of law or fact."*

The District Court held that the insurer committed bad faith. While noting that an insurer's investigation "need only be reasonable, not perfect", the Court found neither. In particular, the Court held that the insured made an unreasonable attempt at investigation by relying on experts that did not actually physically inspect the damage nor obtain competing cost estimates while dismissing what the insured asserted as the value of the claim. Based on the poor investigation, the insurer did not have evidence that reasonably supported a denial of liability.

The opinion found fault with the carrier from the beginning of the claim. The Court suggested that the carrier's response of asserting the deductible at the initial report of loss set the tone for the handling of the claim. For instance, the Court wrote that when the final amount arrived at by the insurer "skirts just below the deductible [the claims handling] reeks of bad faith." The Court believed the carrier attempted to steer the investigation and claims handling to match its initial determination rather than considering the evidence at hand.

In this instance, we do not know the entirety of the investigation, just the mistakes referenced by the Court in making its determination of bad faith. In large losses, it is imperative to rely on experts that have inspected the damaged parts, property and/or components. Further, these experts need experience in performing the work needed to repair or replace the property. Hiring competent experts and thoroughly vetting a claim can avoid a finding of bad faith even if a jury finds coverage for the insured.