COVERAGE OPINIONS
Judicial Opinions Today - Impact On Counsel's Opinions Tomorrow

THE WALL STREET JOURNAL.
Coverage Opinions Baseball Issue leads to Op-ed in WSJ
Coverage Opinions In The News!
Featured in:
THE PHILADELPHIA LAWYER
The Philadelphia Inquirer
Randy Maniloff's a family insurance man, Philly Deals, A14

Vol. 9 - Issue 8
December 7, 2020

Insurer Liable For Bad Faith -- For Filing A Declaratory Judgment Action

I've said for a long time that when insurers are found liable for bad faith, it is usually not because their coverage determination was erroneous. Courts generally give insurers wide latitude to get a coverage determination wrong – and conclude that it was not done in bad faith. The bad faith standard is usually quite high – too high to be satisfied because an insurer's interpretation of the meaning of "mobile equipment" was not correct. All of this is notwithstanding how some policyholder counsel define "bad faith" -- anything the insurer does that he or she does not agree with.

Insurer liability, for bad faith, is usually tied to the manner in which the insurer handled a claim. In other words, it is not the coverage determination that was made in bad faith, but how it was reached. Often-times this has to do with the insurer's investigation of a claim.

That's what happened in Travelers Property Cas. Co. v. North American Terrazo Co., No. 19-1175 (W.D. Wash. Nov. 13, 2020), but in a different way. Travelers filed a declaratory judgment action, seeking a determination that it had no obligation to provide coverage for a construction defect claim. As Travelers saw it, the claim was excluded by the "your work" exclusion. On its face, this seems relatively straightforward. But it wasn't. The court concluded that the insurer's decision *to file the DJ* was made in bad faith, and the insurer was estopped to deny coverage.

The facts giving rise to the situation started in the kitchen of a restaurant. North American Terrazzo ("NAT"), as a subcontractor to SODO Builders, installed an epoxy flooring at the 13 Coins restaurant in Washington. The epoxy had been supplied by Terrazzo & Marble Supply Co. of Illinois (T&M). The work was completed in December 2017. In May 2018 and later, NAT began to notice damage to the flooring in various places.

Here's the key to the case: T&M undertook a lab analysis, on a sample of the epoxy flooring, in an effort to find the cause of the damage. It identified five possible causes of the damage. Of note, three were related to work performed by NAT: preparation of the existing concrete floors, improper mixture of the epoxy and inadequate thickness of the application. But two other possible causes were not related to NAT's work: exposure to heat above 140 degrees Fahrenheit and standing water.

To make a long story short, NAT reported a potential claim to Travelers. Travelers provided a defense, under a reservation of rights, even though no complaint had been filed. NAT replaced the epoxy flooring with tiles. A mediation to settle the underlying claims was not successful. A settlement was reached after a second mediation. It included no contribution from Travelers. SOTO was to receive $200,000 and 13 Coins was to receive $300,000.

Somewhere along the way, Travelers had filed a declaratory judgment action. The decision is a little complex. But it can be boiled down to this. The court observed that Travelers knew, within a month of getting the claim, that the "your work" exclusion or "your product" exclusion could preclude coverage.

The claim is clearly one involving "your [NAT's] work." There is no dispute about that. But that did not mean that the "your work" exclusion applied. The exclusion applies to property damage to the insured's work, **arising out of the insured's work – and not some other source.**

But, as noted above, T&M's lab analysis identified five possible causes of the damage – three related to work performed by NAT and two other possible causes that were not related to NAT's work. And, if they were not related to NAT's work, then the property damage was not arising out of NAT's work. Therefore, there were reasons why the "your work" exclusion may not have applied.

And, as the court observed, Travelers did not have a definitive answer on the cause of the damaged floor:

"Travelers knew that there was a limited window to investigate the epoxy flooring before it would be removed and replaced. But Travelers sent only one investigator before the flooring was replaced. And she simply made visual observations of the damage and took photographs. Travelers' coverage adjuster did not visit the site, take a sample, or retain an expert before the repairs were made. And Travelers did not retain a flooring expert until after the damaged flooring was replaced. Over two months before Travelers filed this action, its flooring expert, Phillips, put Travelers on notice that only forensic testing of the damaged flooring could allow him to

determine the flooring failure's cause. Phillips stated: '[I] cannot determine the cause of the failure without analyzing a product sample to determine the laboratory results of the mixture of the product' and '[a] forensic laboratory analysis will be able to determine what is the probable cause of failure.' Travelers has not provided any forensic evidence or expert evidence as to the cause of the flooring's damage."

Held: "Both exclusions require evidence that the property damage 'arose out of' the insured's work or product and not some other source. Travelers' failure to investigate meant that it could not make a reasonable determination of coverage. This violated Travelers' quasi-fiduciary responsibilities to investigate the claims. And the undisputed evidence demonstrates that Travelers filed this lawsuit knowing from its own expert that it could not prove the claims it has asserted. Travelers actions were 'unreasonable' and 'unfounded' and constitute bad faith."

The court further concluded that the bad faith finding justified a "presumption of harm" and "coverage by estoppel."