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Danger ahead: the potential effects of 'progressive legislation' on bad faith claims in New York

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A claim of bad faith in insurance is an accusation directed at the insurance carrier for failing to meet its clients' and plaintiffs' obligations. The bad faith claim can be from either the insurance carrier's refusal to pay a policyholder's legitimate claim or investigate and process a policyholder's claim within a reasonable period.

The National Association of Insurance Commissioners has written their Unfair Claims Settlement Practices Act ("UCSPA"), which 47 states have enacted. The purpose of this act is to set forth standards for the investigation and disposition of claims. The UCSPA does not provide policyholders with the individual right to sue against an insurance carrier.

In the past five years, several states have strengthened bad faith protection for policyholders. This noticeable trend aims to tighten regulation of insurance companies for bad faith in settling claims. In 2017, the Pennsylvania Supreme Court adopted a two-prong test to prove statutory bad faith.

The test requires that a plaintiff present clear and convincing evidence that the insurer did not have a reasonable basis for denying benefits under the policy. It also says that the insurer knew of or recklessly disregarded its lack of a reasonable basis.

Washington, Georgia, and Colorado have enacted regulations that would strengthen protections for policyholders and plug the gap in enforcement of bad faith settlement practices against insurance companies. In 2017, Colorado passed a private right of action for bad faith and allows policyholders to sue insurance carriers for bad faith.

In the New York State Assembly, legislators have introduced two bills relating to bad faith. Bill 7285 creates a new private cause of action against an insurer who has refused or delayed payment of a claim. Bill 5623 would allow a plaintiff to recover interest, costs and disbursements, compensatory damages, consequential damages, and reasonable attorney's fees for bad faith.

In addition, the plaintiff would recover amounts due under the policy when the insurer has refused to pay, settle, and or unreasonably delayed payment of a claim and was not reasonably justified. Variations of these bills have been in the New York State Assembly since 2013.

Both bills would dramatically alter the existing playing field. The proposed law would place insurers on the defensive right away. It would require an insurer to evaluate a claim within six months and allow it 30 days to settle or reject an accusation of bad faith before filing a bad faith suit.

Opponents argue that the legislation goes beyond almost all jurisdictions and allows third parties the right to sue insurers for bad faith. They point to Florida, where there has been a private third-party action against insurance companies since 1993.

A 2018 report by the Insurance Research Council found that the possibility of winning sizeable bad faith settlement act suits has been an incentive for policyholders to file insurance claims that otherwise would not have been filed. The report also found that Florida consumers paid the third highest auto insurance premiums in the United States.

Carriers argue that no proof exists of widespread abuses by New York insurers in the wake of Hurricane Sandy and COVID-19. Furthermore, they say it will be difficult for insurers to comply with the proposed legislation and the legislation would improperly tip the scales against New York insurance companies.

Proponents of the new law argue that New York's current law is archaic and cumbersome. The current law requires a policyholder to assign their bad faith claim to the victim before filing a bad faith action against the insurance company.

Proponents, supported by the plaintiffs' bar, argue that the new law will not increase premiums or unleash litigation floodgates. They point to other states that allow third parties to directly file bad faith claims against insurance companies, which have not seen increased premiums or reduced consumer choice.

Those in favor also point out that when New York passed a law in 2017 that extended the statute of limitations for misdiagnosed cancer patients, no such increase in filings or increased premiums occurred.

Supporters of the legislation argue that liability insurance carriers have earned windfall profits because of COVID-19. They say less driving has reduced auto claims, increasing earnings of the auto insurance carriers by around 8%. They point to the 2016 report by the New York State Attorney General that found widespread

marketing abuses by insurers in adjusting Hurricane Sandy claims left consumers stranded without the coverage they expected, along with widespread insurance litigation as a result.

Supporters of the new proposals argue that the six-month deadline is needed to compel carriers to act. They claim some insurers fail to complete investigations, value cases, and make determinations to pressure claimants who urgently need monetary relief into accepting less than the full value of the claim. Also, they argue that the bill's 30-day deadline is necessary to avoid insurers thwarting the new bad faith law by refusing to engage with a policyholder or injured victim who alleges a bad faith claim.

In my opinion, plaintiffs' lawyers will seek to use the new law, if passed, as a cudgel to force carriers to pay claims and or settle litigation that is defensible on the merits. We feel the best way to achieve prompt and fair settlements for both sides is for insurance companies and their attorneys to negotiate and fairly settle cases aggressively.

Like every industry, insurance companies have different philosophies about how to transact business and approach negotiations. Most insurers do not need a bad faith lawsuit to settle claims in good faith. Insurance companies must evaluate claims promptly to create and set a reserve.

Internally, they are always under scrutiny to ensure claims have a realistic evaluation and a reasonable reserve is in place. Thus, the notion that insurance companies ignore open claims is an exaggeration. Of course, as with every industry, some carriers seek to avoid or delay their fiduciary duties.

These carriers should be held responsible for their claims handling policies. The problem here is that the proposed legislation takes a blunderbuss approach to what is a surgical problem.

Bad faith suits are a threat that the plaintiffs' bar wants to use to gain an unwarranted advantage from insurance carriers. They are the sword of Damocles hanging over a carrier's head.

Forcing insurance companies to write insurance in an even more unfriendly business environment in New York may cause them to stop writing insurance here at all and write more policies in pro-insurance states. And if they do continue to offer insurance policies, the cost will go up to reflect the increased risk in New York.

If the purpose of the bad faith legislation is only to punish insurance companies for past bad experiences, it may accomplish that. If, on the other hand, the objective of the bad faith legislation is to encourage prompt and fair settlements, then it will accomplish nothing.

About the author

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