The New Jersey Supreme Court Rejects Attempt To Alter "Fairly Debatable" Standard To Determine Bad Faith In First-Party Coverage Action

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On February 18, 2015, the New Jersey Supreme Court decided Badiali v. New Jersey Manufacturer's Insurance Group, ____ N.J. ____ (2015), A-48-12, and rejected an attempt to alter the "fairly debatable" standard to determine bad faith in a first-party coverage action.

The Supreme Court further held that New Jersey Manufacturer's Insurance Company's ("NJM") rejection of an arbitration award in an uninsured motorist's (UM) claim precluded a finding of bad faith when there was unpublished non-binding case law supporting NJM's rejection of the arbitration award. It also held "that any reference in a policy of insurance the statutory $15,000 policy limit as a basis for rejecting an arbitration award applies only to the amount the insurance company is required to pay, not to the total amount of the award."

Plaintiff was injured when his car was rear-ended by an uninsured motorist. Plaintiff filed a UM claim under a personal auto policy resulting in an arbitration award in the amount of $29,148.62. NJM, along with Harleysville Insurance Company, shared the award and therefore each insurance company paid half or namely $14,574.31. NJM asserted that the language of its personal auto policy allowed either party to dispute an arbitration award if the total amount exceeded $15,000. Plaintiff filed suit. The trial court confirmed the arbitration award.

Plaintiff commenced a separate bad faith action against NJM arguing that NJM spent more than $28,000 to avoid paying its portion of the arbitration award causing plaintiff to incur substantial expense, years of delay, undue aggravation and attorneys' fees. NJM moved for summary judgment arguing it did not act in bad faith because it relied on an unpublished 2004 Appellate Division decision which held that NJM was entitled to reject an arbitration award and demand a trial de novo. Geiger v. N.J. Mfrs. Ins. Co., No. A-5135-02 (App. Div. Mar. 22, 2004). The trial court and the Appellate Division both held that as matter of law the mere existence of unpublished case law supporting NJM's rejection of the arbitration award precluded a finding of bad faith regardless of whether or not NJM was aware of or relied on that unpublished case.

On certification to the Supreme Court, plaintiff argued that NJM did not have "fairly debatable" reasons for rejecting the arbitration award based on an unpublished Appellate Division opinion. Plaintiff also argued that it was error for the trial court to grant summary judgment when discovery had not yet been completed and that plaintiff was statutorily entitled to counsel fees pursuant to R. 4:42-9(a)(6). The Supreme Court also granted the New Jersey Association for Justice ("NJAJ") leave to appear amicus curiae. NJAJ asserted that in analyzing allegations of first-party bad faith, the

court should be required to engage in more exhaustive examination of claims-handling practices which would include reviewing the actual conduct of the defendant insurance carrier with respect to the investigation, evaluation and processing of the claim, as well as information actually considered in the point of time the decision was made. NJAJ urged the court to depart from its adherence to the "fairly debatable" approach to allow for a bad faith determination when an insurer acts intentionally or recklessly contrary to its fiduciary obligations.

The Supreme Court affirmed the "fairly debatable" standard under Pickett v. Lloyd's, 131 N.J. 457 (1993). The Supreme Court again set forth the standard; namely, "to establish a first-party bad faith claim for denial of benefits in New Jersey, plaintiff must show 'that no debatable reasons exist for denial of the benefits.'" [Citation omitted]. The Supreme Court rejected NJAJ's suggestion that the "fairly debatable standard" should include some focus on the claim handler's investigation, noting the Supreme Court's reservation "about the potential discovery complications associated with such an approach." It rejected that approach "at this time" because the issue did not require an alteration of the existing standard.

The Supreme Court noted that it has consistently upheld an insured's right to reject an arbitration award when the arbitration clause or wording of a policy is clear and express. A prior unpublished opinion of the Appellate Division "will allow a party to avoid a finding of bad faith for actions taken in courts with its holding." The Court further saw no need to address the entitlement to attorney's fee in the uninsured/underinsured context because of its decision. The Supreme Court also rejected Geiger and stated that any reference in a policy of insurance to the statutory $15,000 policy limit would not serve as a basis to reject an arbitration award because that $15,000 policy limit only applies to the amount that the insurance company is required to pay and not to the total amount of the award. To allow the total amount of an award to be the determining factor for rejecting an arbitration award when the insurance company's share is less than the statutory policy limit "would frustrate the legislative intent of expediting resolution of smaller cases in the least costly manner."

Should you have any questions or comments regarding this matter, please feel free to contact Vincent E. Reilly or Mark S. Hanna.