WINNING BAD FAITH JURY TRIALS

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WINNING STRATEGY FOR A BAD FAITH INSURANCE CASE FOR OFFICERS AND DIRECTORS

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I. <u>INTRODUCTION TO BAD FAITH</u>

Every jurisdiction in this country recognizes the potential for a claim by policy holders against their insurance companies for bad faith. The notion that policy holders have a right to assert a bad faith claim against insurance companies originates in both tort and contract concepts. Each jurisdiction has its own view of whether the claim is a tort claim, a contract claim, or a combination of the two, and the characterization of the claim may become important in that jurisdiction for determining the available relief[1].

It is also important to recognize that the nature of the insurance at issue may affect the right to assert a bad faith claim. Typically, bad faith claims first originated in jurisdictions that were concerned about third party liability policies in which the insurance company had provided a policy holder with some protection against claims by third parties. In connection with that protection, typical insurance policies provide the insurance company with substantial control over the defense of the claim, the settlement of the claim, or sometimes both. All jurisdictions recognize bad faith claims by policy holders in connection with third party coverage. That is not true for first party coverage which is ordinarily coverage sold to a policy holder to cover some

[1] There are a number of treatises on the subject of bad faith claims. *See*, e.g., Ashley, <u>Bad Faith Actions – Liability and Damages</u>, (2d Ed.)

policy holder loss such as property loss, business revenue loss, or losses from other sources. While the majority of jurisdictions do recognize a bad faith claim for first party coverages, there are still a number of jurisdictions that do not hold this view[2].

Jurisdictions do vary in their legal requirements for a bad faith claim. The most prevailing requirement among jurisdictions for a bad faith claim is the showing that the insurance company had no reasonable basis for its actions. This is what's called the objective test of bad faith. Other jurisdictions, however, employ a more subjective test and require as an element of bad faith that there be some showing of malice or improper intent[3].

Almost all states have adopted some form of the National Association of Insurance Commissioner's model provisions for regulating the handling of claims by insurance companies. Those standards that govern the handling of claims establish a base line for determining when an insurance company is engaged in an unfair claims handling practice. In some states those standards are embodied in regulations and in others in statutes. In either case, the violation of those unfair claims handling practices usually provides evidence of bad faith. Attached as Exhibit A is an example of a jury instruction incorporating typical claims handling standards into an instruction on bad faith. While a violation of those claims handling standards may provide evidence of bad faith, in most states a violation of the standards does not, by itself, provide as a basis for a private cause of action[4]. In other states, the violation of the claims handling statutes or regulations may result in a private cause of action or constitute evidence of an unfair business

[2] For examples of states that reject the bad faith claim for first party insurance coverage, *see* Beck v. Farmers Ins. Exchange, 701 P.2d 795, 798 (Utah 1985) and Levine v. Selective Ins. Co. of America, 250 VA. 282, 462 S.E. 2d 81 (1985).

[3] For examples, *see* Bullock v. State Farm Mutual Auto Ins. Co., 733 F.2d 63 (8th Cir. 1984) and Aurey v. Progressive Car Ins. Co., 620 F.2d 583, 586 (6th Cir. 1980).

[4] *See* Ashley, Bad Faith Actions – Liability and Damages, § 9:03 for an extensive discussion of this issue with related case citations.

practice and the violation of the laws regarding unfair business practice may give rise to a private cause of action.

For a plaintiff, there will always exist a claim for breach of contract in a circumstance where there is a claim of bad faith but the corollary is not also true. An insurance company's breach of contract does not always rise to the level of bad faith.

The legal significance for plaintiff of the bad faith claim is the availability of remedies that go beyond those available for breach of contract. In states where the bad faith claim is rooted, in whole or in part, in tort, the bad faith claim normally gives rise to a tort measure of damages which entitles the policy holder to recover all damages reasonably foreseeable as a result of the bad faith. In particular, the establishment of bad faith may entitle a policy holder to a claim for punitive damages in states where punitive damages are authorized. In other states, bad faith may establish a claim for recovery of attorneys' fees or a claim for coverage by way of estoppel, even in a circumstance where no coverage otherwise might exist. Finally, some states provide for statutory penalties for bad faith claims. It is the availability of these additional remedies that make the assertion of bad faith claims very attractive to plaintiffs and very controversial for defendants.

II. WINNING THE BAD FAITH CASE FOR DIRECTORS AND OFFICERS

There are a number of third party liability policies that might give rise to a bad faith claim. In evaluating your chances of success, it is important to keep in mind who you represent, the subject matter of the policy and the features of your case for bad faith that might be attractive to a jury.

In some cases, the policy holder is an individual who is similarly situated to your potential jurors. A plaintiff in this position is likely to enlist jury sympathy and support. Additionally, there are certain subject matters that are covered by insurance in which potential jurors are likely to have a direct interest. For example, jurors are interested in health insurance and how insurance companies respond to requests for coverage for what may be deemed experimental treatments. There are some cases, however, in which neither the persons involved nor the subject matter resonates with the jury. Insurance coverage for directors and officers of publicly held companies clearly falls into this category of insurance disputes. In such a case there is likely to be very little jury sympathy. Nevertheless, it is important to identify jury themes that will resonate with jurors who otherwise will have little sympathy for the persons involved and little interest in the subject matter.

In representing officers and directors who seek to enforce their coverage rights, it is important to focus on process. During the handling of an insurance claim that covers many years, there are often communication problems that occur and there are problems getting prompt and efficient responses from the insurance companies. Insurance companies process thousands of claims and it is difficult for them to process all those claims flawlessly. While potential jurors may have no sympathy with your clients or may find the subject matter of your policy irrelevant to their daily lives, they are likely to be concerned with process. How efficiently and promptly has the insurance company acted in responding to the claim? How straightforward has the insurance company been? Has the insurance company withheld information from the policy holder? Has the insurance company "partnered" in the processing of the claim or has the insurance company appeared hostile to processing the claim? These are questions and issues that interest jurors because they are questions and issues which permeate the handling of every single claim no matter what the subject matter or who is seeking coverage.

In July 2007, we represented AT&T Mobility in a jury trial regarding its claim for coverage for defense costs under a director's and officer's investment policy. The setting and circumstances of that case illustrate the importance of process to obtaining a favorable jury verdict for bad faith in a case involving director's and officer's coverage.

AT&T Mobility is a multi-billion dollar plaintiff. AT&T Mobility had been a defendant in a consolidated, class action shareholder case brought in Delaware. The shareholders in the class were shareholders in a company called TeleCorp. AT&T Mobility had owned a significant interest in TeleCorp and had negotiated a price to buy all remaining TeleCorp shares, and certain TeleCorp shareholders challenged the price that AT&T Mobility had paid for TeleCorp's shares in connection with a merger of TeleCorp into AT&T Mobility. The transaction at issue was a multi-billion dollar transaction, and the TeleCorp shareholders brought claims against AT&T Mobility and the TeleCorp officers and directors who had approved the merger. They alleged that the defendants had violated fiduciary duties to TeleCorp, or aided and abetted the breaches of fiduciary duty, by not disclosing key terms of the deal, by approving the deal and by failing to get a "fair price" for the TeleCorp shares AT&T Mobility required.

A number of prominent New York and Delaware law firms were involved in defending AT&T Mobility and the TeleCorp officers and directors in the shareholder litigation. The litigation was settled before trial, but AT&T Mobility paid out approximately $9.5 million in attorneys' fees and defense costs for the TeleCorp directors. When AT&T Mobility sought recovery from the TeleCorp insurer who had issued director's and officer's coverage for these TeleCorp directors, the insurer disputed the reasonableness of the $9.5 million in fees. As a result, AT&T Mobility filed a lawsuit to recover from the insurer the defense costs that it paid. AT&T Mobility tried its claim for those defense costs before a jury in Delaware.

What is most obvious about AT&T Mobility's claims for both breach of contract and for bad faith is that there was little reason for the jurors to be vested in any way in the parties or in the subject matter of the lawsuit. The plaintiff was a multi-billion dollar corporation. The

TeleCorp officers and directors were successful business persons, some of whom were worth tens of millions of dollars personally. The defendant had paid over $9 million dollars to prominent New York and Delaware law firms to defend them in the shareholder litigation. The lawyers who were retained to defend the directors were, by any juror's measure, also extraordinarily successful and wealthy. The key witnesses on the subject of the reasonableness of the attorneys' fees were either the lawyers who had performed the work or experts who had performed similar work who could vouch for the fees. In either case, there was nothing intrinsically attractive about the case, the parties or the witnesses for the jurors. In order to put forward a bad faith case that would resonate with the jurors you need to provide them with some reason to care. Otherwise, it is too easy for any jury to produce the compromise verdict of awarding some damages for breach of contract but finding no bad faith.

At trial, the strategy was to focus on the process. Why?

First, the claims process and the debate over the reasonableness of the attorneys' fees and costs had extended over six years. Over six years there inevitably is going to be some slip-ups. The AT&T Mobility trial strategy was to focus on the slip-ups and to convince the jury that they were important. If the jury has an interest in the process, and most jurors have some experience with the process whereby insurance companies handle claims, the flaws in the process can become of major importance to the jurors. The jurors interest in process enhances your ability to show that the insurance company has acted in bad faith simply because it had no reasonable basis or explanation for different errors in the process.

Second, if the jury focuses on the larger question – did the insurance company have a reasonable basis for disputing $9.5 million of defense costs as reasonable? - you're asking the wrong question because you're asking a question that answers itself. For most jurors $9.5

million is a lot of money to spend on a defense, and it is probably not unreasonable to ask questions about whether that amount of money was needed.

At trial AT&T Mobility was able to present repeated examples of insurance company slip-ups. Repeated slip-ups can become a powerful piece of evidence in a bad faith case. We also were able to categorize the slip-ups and organize the case around those categories. As we examined the six years during which the insurance company had been processing this claim, we could find examples of neglect, delay, stonewalling and, in some cases, a lack of candor. We organized the case around these four flaws in the process and based the bad faith case on the notion that the slip-ups in all these areas showed that the insurer was acting unreasonably.

The point is that you often need to focus on process and not the parties or the subject matter when advancing a claim for bad faith on a directors and officers insurance policy. Too often, the parties you are representing in such cases are not going to be sympathetic, and the subject matter of the dispute - a director's and officer's insurance policy - will be foreign and unfamiliar to jurors. Do not expect them to invested in either your clients or in the coverage at issue. But you can expect that they will care about the process because almost every juror has some experience in trying to process an insurance claim. Too often, their experience with processing an insurance claim is that it is cumbersome, unduly lengthy, and a source of great frustration. You need to capitalize on that real life experience in presenting your bad faith case.

BAD FAITH

Turning now to the bad faith claim, an insurer has a duty to act in good faith in the performance of its obligations under the policy. As such, AT&T has a duty to deal fairly and reasonably in the investigation handling and disposition of any claim under the Policy.

In this vein, AT&T Wireless contends that _________ acted in bad faith by:

1) Failing to promptly and reasonably investigate their claims;

2) Failing to communicate honestly during the handling of the claims;

3) Failing to respond promptly to inquiries or other communications; and

4) Failing to promptly pay the claim once liability became reasonably clear.

In evaluating _________'s conduct, you should apply a reasonableness standard. If you find that _________conducted a reasonable investigation of AT&T Wireless's claim and denied AT&T Wireless's request for payment of the fees and expenses at issue here based upon a reasonable questions of fact or law, or if there was a legitimate controversy as to the validity of AT&T Wireless's claim for payment of the fees and expenses at issue here, then you must find against AT&T Wireless on its bad faith claim. If, however, you find that _________ failed to conduct a thorough investigation of AT&T Wireless's claim for the fees and expenses at issue here or they have failed to promptly and reasonably pay the fees and expenses they were obligated to pay under the policy, then you must find for AT&T Wireless on its bad faith claim. The duty of the insurance company is to act in good faith is a continuing duty that remains until the dispute is resolved.

You will not be asked to determine a separate damage award in regards to the bad faith claim. However, on the verdict sheet that you will be asked to complete there will be a question of whether AT&T has established by a preponderance of the evidence that __________ acted in bad faith as set forth in these instructions.

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Mr. Cronin is a founding partner of the Corr Cronin law firm. Mr. Cronin was formerly co-chair of the Bogle & Gates litigation department from 1995 to 1999. Mr. Cronin is a Fellow in the American College of Trial Lawyers and has been named as one of the top business litigators in Seattle in every one of *Seattle Magazine's* top lawyer surveys since 2001. Mr. Cronin was one of the five named top business litigators in 2001 and 2003 and one of the four named in 2005 (his partner, Kelly Corr, was also named as a top business litigator in each survey). For 8 years in a row Mr. Cronin has been listed in the *Best Lawyers in America*. He has also been selected as a "Super Lawyer" on multiple occasions by *Washington Law & Politics* and has been named as one of the Top 100 Super Lawyers in the state.

Practice / Experience

Mr. Cronin's practice focuses on business litigation, representing both plaintiffs and defendants. He has considerable experience representing law firms, accounting firms, corporate officers and directors, and majority and minority stockholders in securities litigation, professional liability litigation, and corporate control disputes. During his career, Mr. Cronin has represented: Exxon Corp. in a large tax dispute with the State of Alaska involving a claim in excess of $1 billion; Exxon and Arco Alaska in a major dispute with Chevron, Mobil and Phillips over the respective ownership interests in the Prudhoe Bay Oil Field, the largest oil field in North America; Georgia Pacific Corporation, AT&T Wireless, Pendleton Woolen Mills, Todd Shipyards and Champion International as plaintiffs in major insurance coverage disputes; and Amazon.com and AT&T Wireless in major contract disputes.

Representative Clients

- Alyeska Pipeline Service Company
- Atlantic Richfield Company
- Amazon.com
- Aramark
- Arco Alaska, Inc.
- AT&T Wireless
- Champion International
- Earle M. Jorgensen Company
- Exxon and ExxonMobil Corporation
- Georgia-Pacific
- Glacier Northwest
- Longview Fibre Company
- Lynden Transport
- Pendleton Woolen Mills
- The Port of Seattle

Education / Background

- J.D., University of Southern California Law School, 1975
- University of Oregon Law School, 1972-1973
- B.A., cum laude, Brown University, 1970
- Joined Bogle & Gates PLLC in 1978, and was a Member from 1983 to 1999
- Associate Attorney, O'Melveny & Myers, Los Angeles, California, 1975-1978
- Admitted to the Bar in California in 1975 and in Washington State in 1978