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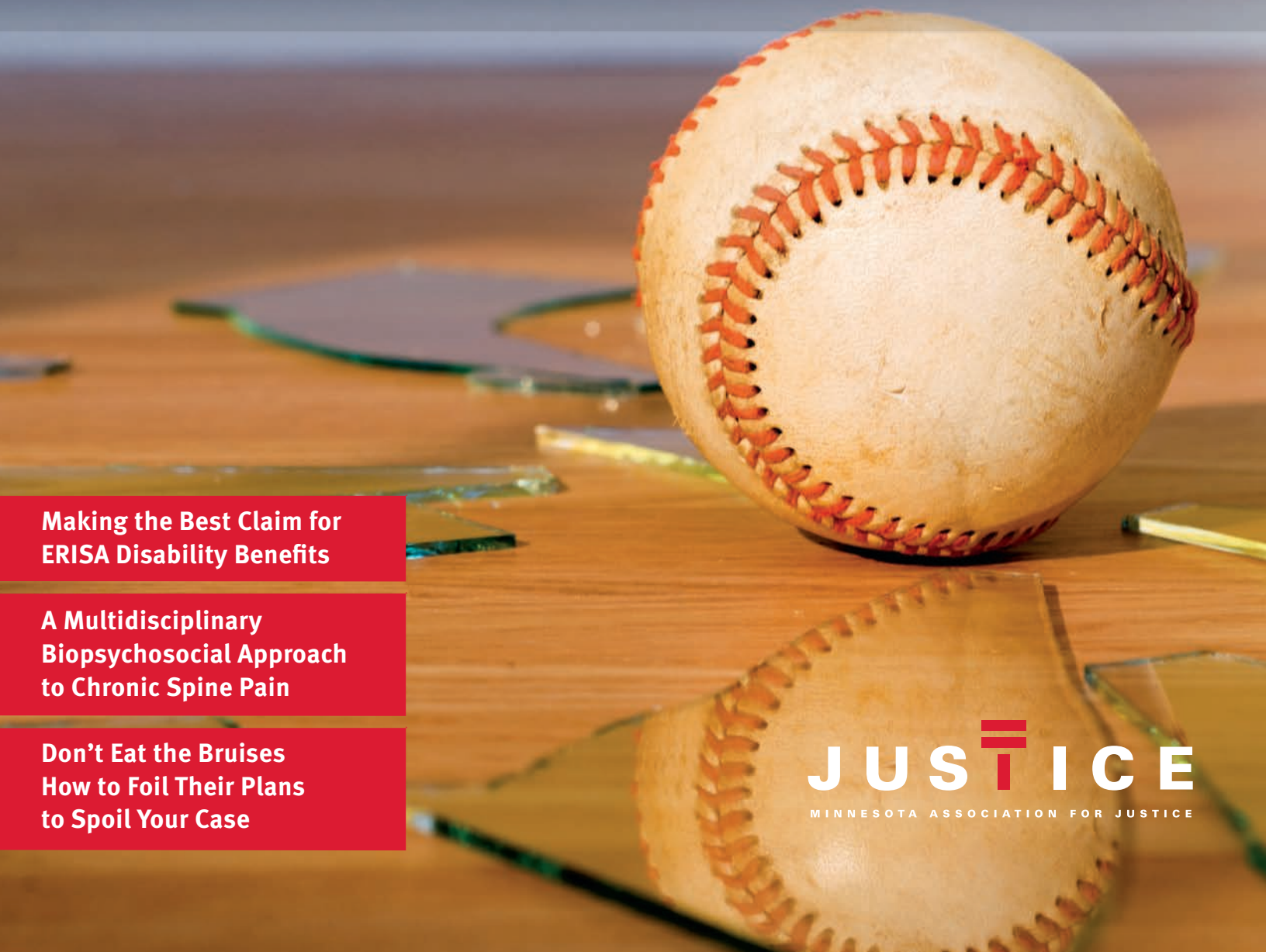
Deterrence of Future Wrongs is at the Heart of Tort Law



Making the Best Claim for ERISA Disability Benefits

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JUSTICE

MINNESOTA ASSOCIATION FOR JUSTICE

The Anatomy of a First-Party "Bad Faith" Claim

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The Minnesota Legislature enacted Minnesota Statute § 604.18, or Insurance Standard of Conduct, to penalize insurers for making unreasonable offers and denials in response to claims by their insureds.[1] Too often, insurers object to plaintiffs' discovery requests regarding insurers' claims investigation and evaluation. Despite courts historically sustaining these objections, there is a growing body of law permitting plaintiff/insureds to obtain discovery regarding insurer's basis for making unreasonable offers and denials. These developments better effectuate the intent of Minn. Stat. § 604.18 to hold insurers accountable for bad-faith claims handling.

The Insurance Standard of Conduct

Pursuant to Minnesota Statute § 604.18, additional damages, costs, and attorneys' fees[2] can be taxed against an insurer that denied an insured's claim in bad faith. In pertinent part, that statute provides:

> A. The Court may award taxable costs to an insured against an insurer in amounts as provided in subdivision 3 if the insured can show:
> 1. the absence of a reasonable basis for denying the benefits of the insurance policy; and
> 2. that the insurer knew of the lack of a reasonable basis for denying the benefits of the insurance policy or acted in reckless disregard of the lack of a reasonable basis for denying the benefits of the insurance policy.[3]

Notably, the meaning of "denial" within § 604.18 is not limited to an outright refusal to offer any payment on the insured's claim. The intent of § 604.18 is to deter unreasonable offers, and the purpose would be defeated if insurers were permitted to escape liability under the statute by making a nominal offer. Minnesota courts have concluded that the phrase "denying the benefits of the insurance policy" means withholding the benefits of the insurance policy from the insured.[4] Therefore, any offer from an insurer that is less than the insured's policy limits is a *denial* of the remaining coverage. In the scenario where the insurer makes a partial offer, a claim under § 604.18 exists where the plaintiff can show that the denial of the remaining coverage was unreasonable.

"Lack of a reasonable basis" has been interpreted to mean that the insurer acted with reckless indifference to the facts and proof provided or that the insurer debated a claim that was not fairly debatable.[5] Reasonableness of a denial is measured against what another reasonable insurer

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would have done with a similar claim.[6] Unfortunately, that standard provides little information, and this area of case law is sorely lacking. Consulting an expert with a background in insurance claims handling or insurance defense will add clout to an argument that the defendant insurer's denial was unreasonable as compared with other reasonable insurers.

Settlement Demands and "Bad Faith" Letters

A bad faith claim begins with the settlement demand. Even if the insurer wrongly denies a first-party claim, a substantial amount can be gained by sending a detailed demand pre-suit.

The settlement demand creates a record of all the information provided to the insurer to pay the claim. Providing all pertinent medical records and bills, relevant prior medical records, expert reports, and collateral source information in the demand phase eliminates any later argument that the insurer did not have sufficient information to evaluate the claim *at the time of* the denial. Concluding the demand by asking the insurer to request any additional information necessary to the evaluate the claim and promptly responding to the insurer's requests should eliminate later arguments from the insurer that there was insufficient information available to make a reasonable offer prior to the lawsuit.

After a demand and denial, a "bad faith letter" can provide as an efficient and persuasive way to notify the insurer of its duty of reasonableness to its insured under § 604.18. The bad faith letter should again document the information made available to the insurer to evaluate the claim as of that date and confirm the insurer has communicated it has all the information and materials it needed to properly evaluate the claim.

Finally, confirming in writing that the insurer has communicated its top offer of settlement may prevent obstacles later in the case. When plaintiff is seeking to amend the claim under § 604.18, the insurer may argue that a low offer was not truly a denial within the meaning of the statute because it was not the final offer (i.e. the insurer intended to continue negotiating). Confirming prior to filing suit that negotiations have failed should diminish this argument.

The Catch-22 in §604.18 Discovery

Discovery in first-party insurance litigation is not a one-way street. Insurers often

see discovery only as an opportunity to dig deeper into plaintiffs' medical, employment, and personal histories to test plaintiff's claims develop defenses to those claims. At the same time, insurers refuse to engage in discovery allowing plaintiffs to test the insurer's claims, often objecting to producing anything other than what was provided to them in the demand. To avoid answering questions about the basis for their evaluations, insurers make relevance and work product objections. Compelling this discovery can be challenging.

Because § 604.18 does not permit pleading a claim in the initial complaint, "bad faith" discovery is, according to some insurers, not relevant prior to the amendment. To amend, a plaintiff must file a motion with one or more affidavits which provide a *prima facie* basis for the bad-faith claim.[7] This amendment standard leads to a catch-22 in the discovery phase: how can a *prima facie* showing of an unreasonable denial be made if the insurer objects to the relevancy of discovery about its claims handling?

The answer: it's not all irrelevant. Parties are entitled to discovery regarding the claims and defenses alleged in the plaintiff's complaint and the defendant's answer.[8] When an injured plaintiff initiates a breach of contract claim against her insurer, the insurer will inevitably respond with an answer holding plaintiff to her burden of proof.[9] Often, the insurer will also assert denials and affirmative defenses about the facts alleged by the plaintiff. If the defendant alleges that plaintiff was injured by her own negligence, failed to mitigate her damages, or did not comply with the terms of her policy, the plaintiff has a right to request discovery of any facts in support of these defenses. This should include obtaining at least the claim file and potentially the insurer's deposition.

To mitigate the effectiveness of objections regarding relevance, interrogatories and Rule 30.02(f) notices should be tailored to the defendant's alleged defenses. In both Minnesota state and federal courts, judges have permitted the discovery of the plaintiff's individual insurance claim file and permitted depositions of the insurer regarding the specific insured's claim.[10] The relevance of this information, where bad faith has not been alleged, is that the claim file and adjuster's mental impressions provided the insurer a basis for the denial and are therefore part of insurer's defense in litigation.

Hennepin County Judge Laurie Miller ordered that a plaintiff *could* not undertake discovery related to a § 604.18 claim before it was pled, but the plaintiff *could* seek discovery regarding the basis for denial of her claim by her insurer.[11] In her memorandum, Judge Miller stated:

> Plaintiff is entitled to discovery on Defendant's defenses and the information relied upon in reaching that conclusion. If Defendant fails to provide information supporting its conclusion not provide coverage, Plaintiff may seek to bring a motion to amend to add a bad faith claim. Such information includes Plaintiffs medical records, as well as any surveillance of Plaintiff. The information relied upon by Defendant in reaching its conclusion that no benefits should be provided on Plaintiff's claim likewise is discoverable. Complete copies of Defendant's claims files for Plaintiff, which presumably contain further information supporting Defendant's decision, are discoverable. The organization and location of these documents bears upon Plaintiffs capability to retrieve the documents from Defendant, so this too is discoverable. Communications between the file handler and non-attorney representatives are discoverable as well, to the extent they contain information regarding Defendant's conclusion not to cover Plaintiffs claim.[12]

Judge Miller's order essentially provides a two-phase approach to discovery in first-party bad faith claims. This model appears to be an appealing compromise for judges and has been followed in a number of orders since Judge Miller's decision.[13] Under this scenario, plaintiffs should be able to obtain their specific claim file and take a Rule 30.02(f) deposition of the insurer or a deposition of the adjuster individually on the bases for the denial. Equipped with the claim file and the adjuster's deposition, plaintiffs can determine whether there are sufficient facts to move for leave to amend under § 604.18. A retained expert, having been supplied with the insurer's claim file and deposition testimony, can provide the affidavit identifying which facts create the *prima facie* claim of bad faith. If the Court permits the amendment, broader discovery regarding the insurer's "best practices" to support a § 604.18 claim should be permissible. In this way, a two-phase approach to discovery in first-party cases may be the most time- and cost-efficient way to approach a potential bad faith amendment.

Venue Selection

In certain cases, it may make sense to consider filing in federal court. In the federal courts, there is a more significant weight of precedent that insurance claim files are relevant to plaintiff's discovery, regardless of whether the plaintiff has alleged a "bad faith" claim.[14] Furthermore, the law regarding "work product" objections from insurers is pretty clear in the federal courts: an insurer's work in the ordinary course of administering a claim prior to the initiation of a lawsuit is not "work product."[15]

Finally, federal courts have determined that the amendment provision in § 604.18, subd. 4 conflicts with Federal Rule 15, and there is developing law in Minnesota federal court applying the more liberal Federal Rule 15 to §604.18 amendments.[16] Under Federal Rule 15, the plaintiff may amend her claim freely where justice so requires. The amendment is subject to Federal Rule 8 and the pleading standards set forth in *Twombly*. In one of the Minnesota decisions applying Rule 15, Magistrate Judge Rau noted that "[u]nder the relaxed pleading standards of the Federal Rules, the idea was not to keep

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litigants out of the court, but rather to keep them in."[17] These relaxed standards for amendment in federal court may expand the scope of a plaintiff's permissible discovery at an earlier phase in litigation and avoid the catch-22 imposed by the § 604.18 amendment standard.

Conclusion

Minnesota Statute § 604.18 was enacted as a means for individual plaintiffs to hold their insurers accountable for bad-faith denials. Unfortunately, the case law surrounding the statute is underdeveloped. If plaintiffs are willing to fight these battles in discovery, it may clear a path to pursue more claims under Minnesota's first-party bad faith statute and prevent insurers from manufacturing frivolous defenses in first-party cases.

[1]*See Wilbur v. State Farm Mut. Auto Ins. Co.*, 880 N.W.2d 874, 881 (Minn. Ct. App. 2016), *review granted* (Aug. 23, 2016), *aff'd*, 892 N.W.2d 521 (Minn. 2017), quoting Senator Tarryl Clark, S. Floor Deb. on S.F. 2822 (Apr. 14, 2008).

[2]Taxable fees are those expended in the pursuit of the § 604.18 claim.

[3]Minn. Stat. § 604.18, subd. 2.

[4]*Wilbur v. State Farm Mut. Auto. Ins. Co.*, 27-CV-10-17956 (Minn. Dist. Ct. Nov. 26, 2014).

[5]*See Freidberg v. Chubb and Son, Inc.*, 800 F. Supp.2d 1020, 1025 (D.Minn. 2011); *Anderson v. Cont'l Ins. Co.*, 85 Wis. 2d 675, 691, 271 N.W.2d 368, 376 (1978); *see also Drake v. Milwaukee Mut. Ins. Co.*, 70 Wis. 2d 977, 984, 236 N.W.2d 204, 208 (1975).

[6]*Freidberg v. Chubb and Son, Inc.*, 800 F. Supp.2d 1020, 1025 (D.Minn. 2011).

[7]Minn. Stat. § 604.18, subd. 4.

[8]Minn. R. Civ. P. 26.02 (b)(2).

[9]A first-party insurance lawsuit is a breach of contract claim, proved by establishing the damages resulting from the underlying tort entitled the insured to payment under the contract. *See Employers Mut. Ins. Companies v. Nordstrom*, 495 N.W.2d 855, 856 (Minn. 1993); *see also Stroop v. Farmers Ins. Ex.*, 764 N.W.2d 384, 386 (Minn. Ct. App. 2009).

[10]*See Carlson v. American Family*, No. 02-CV-14-615 (Minn. Dist. Ct. March 16, 2015); *Kubat v. American Family Ins. Co.*, No. 19HA-CV-10-3967 (Minn. Dist. Ct. June 29, 2011); *Culhane v. American Family Ins. Co.*, No. 19HA-CV-17-1593 (Minn. Dist. Ct. January 2, 2010).

[11]*Perez v. American Family*, No. 27-CV-15-16881, 2016 WL 5408064 (Minn. Dist. Ct. Aug. 24, 2016).

[12]*Id.*

[13]*See Weinke v. State Farm Fire and Casualty Co.*, No. 19HA-CV-18-2418 (Minn. Dist. Ct. Nov. 27, 2018); *Day v. American Family Ins. Co.*, No. 19-HA-CV-12-3015 (Minn. Dist. Ct. Oct. 28, 2016); *Staples v. Farm Bureau*, No. 17-CV-4555 (Minn. Dist. Ct., Sept. 21, 2018).

[14]In Minnesota, *see Staples v. Farm Bureau*, No. 17-CV-4555 (Minn. Dist. Ct., Sept. 21, 2018); *Besser v. Allstate Insurance Co.*, No. 08-5415 (Minn. Dist. Ct., Nov. 20, 2009); *see generally Renfrow v. Redwood Fire and Cas. Ins. Co.*, 288 F.R.D. 514, 521 (D. Nev., Feb. 1, 2013); *Baerla v. Safeco Ins. Co.*, No. 13-1084, 2014 WL 11497826, at *4 (D.N.M. Aug. 22, 2014); *Morrison v. Chartis Prop. Cas. Co.*, No. 13-cv-116, 2014 WL 840597, at *2 (N.D. Okla. Mar. 4, 2014).

[15]*See Peterson v. Douglas County Bank & Trust Co.*, 967 F.2d 1186, 1189 (8th Cir. 1992); *St. Paul Reinsurance Co., Ltd.*, 197 F.R.D at 620, 636 (N.D. Iowa 2000); *Selective Ins. Co. of S.C. v. Sela*, 16-CV-4077 (PHS/SER), No. 16-CV-4077 (PJS/SER), 2017 WL 8315885, at *1 (D. Minn. Oct. 10, 2017); *Collins v. Depositors Ins. Co.*, No. 12-CV-2122 (PAM/LIB), 2013 WL 12142580 (D. Minn. Dec. 12,2013); *Mission Nat. Ins. Co. v. Lilly*, 112 F.R.D. 160, 163 (D. Minn. 1986).

[16]*See Selective Ins. Co. of S.C. v. Sela*, ---F. Supp. 3d. ----, No. 16-cv-4077 PJS/SER, 2018 WL 6181179 (D. Minn. Nov. 27, 2018); *see also Darmer v. State Farm Fire and Casualty Co.*, 17-CV-4309- (JRT/KMM), 2018 WL 6077985 (D.Minn. Nov. 21, 2018).

[17]*See Selective Ins. Co. of S.C. v. Sela*, No. 16-CV-4077 (PJS/SER), 2018 WL 1960450, at *6 (D. Minn. Apr. 26, 2018), vacated, No. 16-CV-4077 (PJS/SER), 2018 WL 6181179 (D. Minn. Nov. 27, 2018) *citing Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 575, 127 S. Ct. 1955, 1976, 167 L. Ed. 2d 929 (2007).