The Supreme Court of New Jersey just issued an important pair of decisions for policyholders with bad faith claims against their first-party insurance companies in Badiali v. New Jersey Manufacturers Insurance Group and Wadeer v. New Jersey Manufacturers Insurance Company. In Badiali and Wadeer, both decided last Wednesday, the Court reiterated the narrow “fairly debatable” standard as the threshold for bad faith claims in New Jersey. But, the Court also opened the door to modify this standard in the Badiali decision by recognizing the relevance of the actual claims handling in a particular case.

New Jersey has long recognized that the covenant of good faith and fair dealing is implied in every contract, and that an insurance company owes a duty of good faith to its policyholders in processing claims. See Pickett v. Lloyd’s, 131 N.J. 457 (1993); Sensient Colors, Inc. v. Allstate Ins. Co., 193 N.J. 373, 393–394 (citing Pickett). The standard set by the Supreme Court in Pickett is known as the “fairly debatable” standard—a policyholder must show that the insurance company had no reasonable basis to deny the claim to prevail on a bad faith claim (i.e., if it a claim is “fairly debatable,” there can be no bad faith). Pickett 131 N.J. at 473–74. Under the test, “a claimant who could not have established as a matter of law a right to summary judgment on the substantive claim would not be entitled to assert a [bad faith] claim…. “ Id.

The fundamental flaw of the “fairly debatable” standard, as some courts have applied it, is that it allows actual bad faith to go unpunished; indeed, an insurance company could act in bad faith, utterly fail to make any investigation in breach of its fiduciary duty, for example, yet still avoid the resulting bad faith claims if it turned out that coverage for the claim happened to be “fairly debatable.” Amicus Curiae urged the Court to consider clarifying the rule to avoid this unintended paradox, suggesting that the actual investigation is relevant to a bad faith determination and that courts should not dismiss bad faith claims without discovery on the issue. The Supreme Court did “recognize [the] suggestion that Pickett’s ‘fairly debatable’ standard should include at least some focus on the [claims handling],” but “express[ed] reservation about the potential discovery complications associated with such an approach and thus [did] not adopt such an approach at this time.” Badiali at *8 (emphasis added). Ultimately, the Court found no need “to alter the salutary test set forth” in Pickett based on the facts of the cases before it.

Both cases involved bad faith claims against New Jersey Manufacturers Insurance Group ("NJM") related to uninsured motorist claims under automobile insurance policies. In Badiali, the policyholder suffered injuries when rear-ended by an uninsured motorist. An arbitrator...
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awarded $29,148.62 to Badiali, which was to be split between NJM and another carrier. A provision in the NJM policy provided that such an arbitration decision is binding “unless the arbitration award exceeds [$15,000],” in which case, either party may demand a jury trial. Badiali claimed that NJM acted in bad faith because its share of the claim was less than $15,000 and it should have paid the claim. The Court found Badiali’s claim was fairly debatable because of a prior unreported decision allowing rejection of an arbitration award in nearly identical circumstances; NJM was the carrier in that case, as well. Importantly for policyholders, though, the Court did hold that, in the future “any reference in a policy of insurance to the statutory $15,000 policy limit as the basis for rejecting an arbitration award applies only to the amount that the insurance company is required to pay, not to the total amount of the award.” Badiali at *11.

In Wadeer, the NJM rejected several arbitration awards in favor of its policyholder, two within policy limits, one in excess of the $100,000 policy limits. At trial, a jury awarded the policyholder over $250,000, but molded the verdict to policy limits. Previously, the policyholder made a $95,000 offer of judgment under Rule 4:58-2, which provides attorneys’ fees to an offering party where the award exceeds 120% of the offer. The Court refused to uphold the lower court’s award of attorneys’ fees under this rule because, after molding the verdict, the award was below 120% of the offer of judgment. The Court also rejected Wadeer’s bad faith claims on res judicata grounds; NJM argued that the entire controversy doctrine barred the claim, as well. In considering the entire controversy doctrine, the Court observed that “[a]cts of first-party bad faith in the UM context can, and often will, continue throughout the course of the underlying legal proceedings” and “an insurance carrier’s acts of bad faith may often not cease until a verdict is returned, and this is only after the plaintiff has been forced to fully litigate the matter through arbitration and trial.” Wadeer at *10. The Court, thus, iterated its belief that “viewing bad faith claims as separate and distinct actions promotes judicial efficiency and economy.” Id.

The Supreme Court in Wadeer recommended that the Civil Practice Committee consider several issues that would inure to the benefit of policyholders, if adopted: (1) whether to allow policyholders to first assert party bad faith claims after resolution of an underlying uninsured motorist action under the entire controversy doctrine; (2) whether the trigger for the offer of judgment rule in the uninsured/underinsured motorist context should be an actual damages verdict instead a molded verdict entered by the court; and (3) whether to expand Rule 4:42-9(a)(6)’s allowance for counsel fees “in an action upon a liability of indemnity policy of insurance, in favor of a successful claimant” to first-party insurance claims. New Jersey policyholders should keep an eye on the Committee for any changes to these rules that would bolster a policyholder’s ability to recover against its insurance company.

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