



## Bad-Faith Insurance Claims in Minnesota Real Estate Policies

By Stacy Kabele

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**I**nureds are allowed to bring claims for penalties or taxable costs against insurers where claims are denied with a lack of good faith. These claims often arise pursuant to homeowners' or other property policies for damage occurring to buildings from fire, storms and water intrusion.

Bad faith claims are actionable if the insured can prove two things: (1) there was no reasonable basis to deny benefits; *and* (2) the insurer knew of a lack of a reasonable basis for denying the benefits *or* acted in reckless disregard of the lack thereof. An insured's claim for taxable costs arises out of the underlying tort claim against the insurer. Procedurally, an insured must seek leave of court to amend a complaint to include a claim for first-party bad faith. If the insured prevails, the court may award: (1) either half the proceeds awarded that exceed the insurer's offer made 10 days or more before the start of trial or \$250,000, whichever is less; *and* (2) reasonable attorney's fees up to \$100,000 incurred to prove the violation.

During the last five years, Minnesota courts have not allowed many insureds to pursue first-party bad faith claims. The following seven cases are some recent examples.

### United States District Court (District Of Minnesota)

***Hackbarth v. State Farm Fire and Cas. Co.*** – Insurer paid damages for insureds' fire loss. Insureds filed a lawsuit, claiming the home was a "total loss" and that they were entitled to the policy limits. Insurer counterclaimed, contending insureds committed fraud. The jury agreed that insureds committed fraud. The court decided that insurer had a reasonable basis to conclude that a total loss did not occur. Insured was ordered to repay insurer the amount that had been paid on claim.

***Friedberg v. Chubb and Son, Inc.*** – In December 2006, insureds discovered extensive water damage to their home. After receiving its expert's opinion, insurer denied the claim citing the faulty workmanship exclusion, among others. Court held that insureds failed to show that the insurer's denial of the claim was unreasonable, noting that insurer did not seek to "shield itself from the facts and otherwise refused to learn the true

nature of [the insureds'] claim. Instead, the record indicates that [the insurer] conducted a thorough inspection of [the insureds'] property.... [B]ad-faith does not arise where the insurer is simply wrong about the factual basis for its denial of the claim.... Nor can bad faith arise simply because the insurer's construction of the policy was subsequently found to be legally incorrect."

***Davis v. Grinnell Mut. Reinsurance Co.*** – Insured claimed hail damage to multiple buildings. Insurer's initial adjuster told insured the roofs were "totaled" and that insurer would replace the roofs. Insurer's roofing expert later determined the roofs could be repaired and did not need replacement. After allowing the insured to bring a claim for first-party bad faith, the court later granted insurer's motion for summary judgment, deciding the first adjuster's opinion does not mean that the offer to merely repair the roofs lacked a reasonable basis.

### Minnesota Court Of Appeals

***Homestead Hills Homeowner Ass'n v. American Family Mut. Ins. Co.*** – Insured sustained hail and wind damage to its condominium roofs. Insurer denied the claim after determining that the shingle damage was caused by a manufacturing defect, not hail. On appeal on a number of issues, the Minnesota Court of Appeals held that insured failed to present sufficient evidence in support of its motion for leave to amend and held that the trial court did not clearly abuse its discretion when it decided that the insured's hail damage claim was "fairly debatable."

***N. Nat'l Bank v. N. Star Mut. Ins. Co.*** – Mortgagee claimed benefits under homeowners' policy for a fire loss. Insurer paid the actual cash value loss at the time of the loss. Insurer denied the mortgagee's demand for an appraisal because the mortgagee was not a named insured. The mortgagee sued. During litigation, an appraisal was conducted. The trial court decided that the insurer acted in bad faith by not agreeing to the appraisal process and for the delay in making payment, but then concluded that taxable costs were not appropriate because the claim was resolved or confirmed by appraisal. The Minnesota Court of Appeals reversed the trial court's finding of



bad faith, noting that the insurer promptly adjusted the loss and tendered payment in a certain amount; that the mortgagee waited two years after the loss before it advised that it was disputing the amount paid; that there was a legitimate dispute about whether the mortgagee could appraise the loss; that the insurer paid the balance of the actual cash value loss into court after the appraisal award; and that the delay was occasioned by matters “unquestionably” out of the insurer’s control.

### Minnesota District Courts

*Auto-Owners Ins. Co. v. Second Chance Investments LLC* – The insured’s home sustained a fire loss. The insured claimed a total loss to its insurer. The insurer eventually paid the mortgage amount, and later tendered to the insured an undisputed amount, but disputed the total amount of the loss and the forum to resolve the dispute. The trial court decided that it had the authority to determine whether there was a total loss, and ordered a jury trial. The trial court allowed the insured to bring a claim for taxable costs, noting that other courts

outside Minnesota have found that a delay in payment is tantamount to a denial.

*King’s Cove Marina, L.L.C. v. St. Paul Mercury Ins. Co., et al.* – The insured suffered damage to its marina due to a windstorm. The insurer denied coverage for a large portion of the claim. First, the insured claimed that the insurer acted in bad faith by not paying the difference between the depreciated cost of replacing an overhead electrical system and the actual cost. The trial court held that there is no basis for a claim for taxable costs because the payment of the difference is not triggered until repairs are completed and actual costs are incurred. Second, the insured claimed that the insurer acted in bad faith by denying claims for the costs of demolition and debris removal. The insurer did not pay for these claims because what items may be covered would be clarified “through the discovery process in this lawsuit.” The trial court held, “The mere statement that the pending lawsuit may clarify coverage issues does not strike the Court as a reasonable basis for the [insurer] not paying a portion of those costs which are indeed covered and are not in dispute.

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