INSURANCE BAD FAITH IN OHIO AFTER *ZOPPO* WHERE ARE WE?

I. INTRODUCTION

In *Zoppo v. Homestead Insurance Company* (1994), 71 Ohio St. 3d 552, the Ohio Supreme Court clarified the standard to be applied in determining whether or not an insurance company has acted in bad faith. Paragraph one of the syllabus held:

> An insurer fails to exercise good faith in the processing of a claim of its insured where its refusal to pay the claim is not predicated upon circumstances that furnish reasonable justification therefore.

The *Zoppo* decision approved and followed the cases of *Hart v. Republic Mutual Insurance Co.* (1949), 152 Ohio St. 185, 87 N.E. 2d 347 and *Staff Buildings, Inc. v. Armstrong* (1988), 37 Ohio St. 3d 298, 525 N.E. 2d 783, which had both endorsed the "reasonable justification" standard. *Zoppo* specifically overruled *Slater v. Motorists Mutual Ins. Co.* (1962), 174 Ohio St. 148, 187 N.E. 2d 45, paragraph two of the syllabus, which had held:

> A lack of good faith is the equivalent of bad faith, and bad faith, although not susceptible of concrete definition, embraces more than bad judgment or negligence, it imports a dishonest purpose, moral obliquity, conscious wrongdoing, breach of a known duty through some ulterior motive or ill will partaking of the nature of fraud. It also embraces actual intent to mislead or deceive another.

The *Zoppo* case also overruled *Motorists Mutual Ins. Co. v. Said*, (1992), 63 Ohio St. 3d 690, 590 N.E.2d 1228, which had abandoned the "reasonable justification" standard for one requiring "an intentional failure by the insurer to perform" its contractual obligation. Justice Francis Sweeney, writing in *Zoppo* for the five-justice majority, held:

> Intent is not and has never been an element of the reasonable justification standard. Hence, in deciding *Said, supra,* and in relying upon the erroneous *Slater* decision, this court

> departed from forty-five years of precedent. By expressly overruling *Said* and *Slater*, we will be following the logical progression of case law that has developed over the years.

Now that the standard for proving bad faith has been clarified, what questions remain to be answered in Ohio in this still developing area of law?

II. WHAT CONSTITUTES REASONABLE JUSTIFICATION?

The *Zoppo* case did not attempt to define what constitutes reasonable justification. Jurisdictions outside of Ohio have held that an insurer may breach its duty of good faith in many ways. The most common charges against insurers include failing to conduct an adequate investigation of a claim, exploiting the insured's vulnerable financial condition, and unnecessarily delaying the handling of a claim.

A. Inadequate Investigation

Inadequate investigation is the basis of many bad faith cases. In *Staff Builders,* the insured was improperly denied health benefits by Aetna Life Insurance Company, resulting in a medical provider bringing suit against the insured. The insured filed a third party complaint against Aetna and was awarded compensatory damages by the jury based on its finding that Aetna had acted in bad faith. The award was affirmed by the Ohio Supreme Court, which noted that:

> (T)here was ample evidence to sustain the jury finding of bad faith in the processing of the insurance claim of appellee. It is abundantly clear that information relevant to the claim was either reviewed by persons unskilled in its evaluation or disregarded by those who possessed such skills.

In *Netzley v. Nationwide Mutual Ins. Co.* (1971), 34 Ohio App.2d 65, the court agreed that one fact indicative of an insurer's bad faith was when "the insurer fails to properly investigate the claim so as to be able to intelligently assess all of the probabilities of the case."

Inadequate investigation was also the primary basis for the bad faith award in *Zoppo*. Homestead Insurance Company accused Zoppo of intentionally burning his bar in order to collect the insurance. Homestead based this conclusion on certain inconsistencies in the several statements Zoppo gave Homestead after the fire and the financial motive Homestead claimed Zoppo had to commit arson: Zoppo's tax returns showed the bar was losing money; and the fact that Zoppo paid $10,000 for the building where the bar was located but insured the building with Homestead for $50,000.

Despite Homestead's claims, the Ohio Supreme Court had no trouble finding "ample evidence to support the jury's finding that Homestead failed to conduct an adequate investigation and was not reasonably justified in denying Zoppo's claim." The Court emphasized that Homestead's investigators focused on Zoppo, did not seriously investigate individuals who had threatened to burn the bar down, did not follow up on leads that indicated that a man ousted from the bar had bragged that he was responsible for the fire, and did not attempt to verify Zoppo's alibi. With regard to the claim of over-insurance, the Court noted that Homestead, in its initial underwriting report, had stated that the building had an insurable value of $95,798 and was *underinsured*. Therefore, the $50,000 in insurance was not excessive.

The adequacy or inadequacy of an investigation will turn on the facts of each particular case. This will usually be a fact question for a jury to resolve.

B. Exploitation of Insured's Vulnerable Position

An insured is often most vulnerable financially when he submits his insurance claim. He may be injured, disabled, and have no means of income to support himself and his family other than the expected insurance benefits. An insurer who takes advantage of the insured's

vulnerable position in order to force him to accept an unfair settlement of his claim is liable for bad faith.

In *Ali v. Jefferson Insurance Co.* (1982), 5 Ohio App.3d 105, 449 N.E.2d 495, the insured brought suit against his insurance company following an accident that damaged the insured's tractor and trailer and led to the insured's hospitalization. The insurance company obtained several estimates to repair the tractor and trailer ranging from $6,994 to $13,056. The insurance company first submitted a proof of loss to the insured for $6,994, but later increased this amount to $8,731.

The negotiations dragged on for several months, during which time the insured made numerous long distance telephone calls to the insurance adjuster to try and get the matter resolved. Due to his injuries, the insured stopped making payments on the tractor and trailer. When negotiations were not concluded within five months of the date of the accident, the tractor and trailer were repossessed. The insured subsequently filed suit against the insurance company and recovered compensatory and punitive damages as well as attorney fees. The court of appeals noted that the insurance company had received information indicating that the necessary repairs greatly exceeded the original estimate, but that it did not substantially increase its offer until shortly before the tractor and trailer were repossessed. The court went on to hold:

> Considering the foregoing, we find that appellant, by virtue of its superior bargaining position, and with knowledge of appellee's economic vulnerability, unreasonably delayed settling this case and acted in a manner so oppressive as to constitute a willful breach of its duty to perform its contractual obligations in good faith.

In the leading California bad faith case of *Neal v. Farmer's Insurance Exchange* (Cal. 1978), 582 P.2d 980, the court summarized the evidence against an insurer that had "lowballed" its insured's claim:

> [The] evidence, in brief, indicated that Farmer's refusal to accept (Mrs. Neal's attorney's) offer of settlement, and its subsequent submission of the matter to its attorney for opinion, were all part of a conscious course of conduct, firmly grounded in established company policy, designed to utilize the lamentable circumstances in which Mrs. Neal and her family found themselves, and the exigent financial situation resulting from it, as a lever to force a settlement more favorable to the company than the facts would otherwise have warranted.

In order to prove that the insurer was attempting to exploit the insured's vulnerable position, the *Neal* court held that the insured may introduce evidence of what the insurer knew about the insured's financial situation:

> Thus, in determining whether Farmer's, in breaching its duty to the insured to make a reasonable settlement, did so in a spirit of oppression, the jury was clearly entitled to consider the evidence of the situation of the insured at the time of the proffered settlement insofar as it might be considered to have motivated its actions.

C. Delay

An insurer that fails to promptly pay an undisputed insurance claim may be guilty of bad faith. As the court stated in *Craft v. Economy Fire & Casualty Co.*(7th Cir. 1978), 572 F.2d 565 :

> It is certainly a reasonable expectation of the insured that if the insurer had no honest doubts concerning its liability, it will promptly pay over the amount owing.

In *Veverka v. Prudential Property Casualty Insurance Co.*, 1983 WL 4791 (8th District), the insured brought a bad faith action against Prudential due to a three-month delay in repairing her car following an accident. The repair shop was delayed because Prudential only allowed the use of cannibalized or used parts, which were not always available. There was also evidence that Prudential's adjuster had harassed the insured into using this particular repair facility.

The trial court granted summary judgment in favor of Prudential and the insured appealed. The court of appeals reversed, holding that there was a fact issue as to whether or not Prudential had acted in bad faith:

> The actions of an insurer, in forcing a customer to accept unreasonable methods of repair, may result in a willful breach of contract which justifies compensatory as well as punitive damages.

II. COMPENSATORY DAMAGES FOR BAD FAITH

The *Zoppo* court held that "an insurer who acts in bad faith is liable for those compensatory damages flowing from the bad faith conduct of the insurer and caused by the insurer's breach of contract".

The *Zoppo* court did not specifically state which items of compensatory damages are recoverable for breach of the duty of good faith. However, courts have traditionally allowed an insured to collect damages for emotional distress, economic harm, and in some instances, attorney fees and costs.

A. Emotional Distress

The bad faith award in the *Zoppo* case was based on testimony of Zoppo's emotional distress following the denial of his insurance claim. The trial court allowed this evidence and charged the jury that it could consider emotional distress in setting the amount of the bad faith award. The court of appeals reversed the jury award, stating "Ohio does not recognize emotional distress as a damage element in bad faith cases". The Ohio Supreme Court reinstated the bad faith award entered by the jury, so it apparently endorsed the awarding of bad faith damages for emotional distress.

The *Zoppo* rationale is in line with the majority view. The victim of insurance company bad faith may generally recover damages for emotional distress caused by the insurer's misconduct. See ASHLEY, *Bad Faith Actions,* § 8.04.

Earlier bad faith cases decided in Ohio had agreed that bad faith damages included mental distress. In *Eastham v. Nationwide Mutual Ins. Co.* (1990), 66 Ohio App.3d 843, the court of appeals affirmed a jury verdict which awarded $425,000 in compensatory damages for bad faith based on the insured's "humiliation, embarrassment, nervousness, and loss of self-worth while being harassed by collectors about bills that they were unable to pay."

In *LeForge v. Nationwide Mutual Fire Ins. Co.* (1992), 82 Ohio App.3d 692, the court of appeals affirmed an award of $60,000 for the bad faith denial of a fire insurance claim. The trial court had instructed the jury that it could award "reasonable compensation for the mental anguish and inconvenience caused by the lack of insurance benefits".

Both *Eastman* and *LeForge* noted that an insured's own testimony is sufficient to establish his entitlement to damages for emotional distress since such consequences were within the common knowledge of jurors.

B. Economic Damage

Recovery is allowed in bad faith cases for all economic harm caused by the insurer's conduct. Economic harm includes compensation for lost profits, loss of a business, lost rents, and loss of the use of property. *Asmaro v. Jefferson Ins. Co.* (1989), 62 Ohio App.3d 110, 574 N.E.2d 1118.

C. Cost of the Lawsuit and Attorney Fees

Although some states allow the recovery of attorney fees as damages for bad faith, the *Zoppo* court did not endorse this position. Rather, *Zoppo* reaffirmed the Ohio rule that attorney

fees may be awarded as an element of compensatory damages where the jury finds that punitive damages are warranted. Whether attorney fees are recoverable for simply a breach of a duty of good faith remains an open question.

Zoppo did not address the issue of costs. However, several decisions by Ohio's appellate courts suggest that litigation costs are automatically recoverable as a part of damages for bad faith. In *Eastham,* the insured was allowed by the trial court to present evidence of litigation costs. In *Spadafore v. Blue Shield* (1985), 21 Ohio App.3d 201, 486 N.E.2d 1201, the court held in a bad faith case that "an obvious loss to Spadafore was the cost of the lawsuit to enable recovery of his claim".

D. Interest

The *Zoppo* court held that pre-judgment interest is recoverable pursuant to the statutory procedures set forth in R.C. 1343.03. Under R.C. 1343.03(A), a creditor is entitled to interest when money becomes due and payable on any instrument of writing. This has been held to include an insurance contract. See *Clevenger v. Westfield Cos.* (1987), 60 Ohio App.2d 1, 395 N.E.2d 377. R.C. 1343.03(C) provides for prejudgment interest when the losing party has not made a good faith effort to settle the case. *LeForge* affirmed the award of prejudgment interest under this provision of the statute.

In *Outdoor Outfitters, Inc. v. Fireman's Fund Insurance Company* (1994), 98 Ohio App.3d 733, 649 N.E.2d 871, the court of appeals reversed a trial court that had failed to give prejudgment interest for breach of an insurance claim. Fireman's Fund had denied coverage based on an arson defense in a property damage claim. Outdoor Outfitters obtained a jury award, and then moved for prejudgment interest. The trial court denied the motion, but its decision was

reversed on appeal and the court of appeals awarded interest at ten percent (10%) from the date coverage was denied.

Although prejudgment interest was awarded by the court in *Outdoor Outfitters*, it is within the discretion of the trier of fact to include an element of interest within the damage award. *DeSantis v. Smedley* (1986), 34 Ohio App. 3rd 218, 517 N.E.2d 1038. In this case, the court of appeals held that the prejudgment interest statute, R.C. 1343.03(C), does not limit the trier of fact's power to award interest as a portion of compensatory damages. In such a situation, it is the trier of fact that has discretion to award or not to award interest as an element of damages for breach of contract.

Other Ohio cases have similarly allowed an insured to collect interest as part of the compensatory damages resulting from an insurance company's denial of a claim. *Mundy v. Roy*, 2006-Ohio-993 (2nd District) reversed a trial court's decision not allowing pre-judgment interest on an uninsured motorist award since "prejudgment interest is payable even for periods of time when the amount of underinsured-motorist damages remains undetermined." *Eldridge v. Grange Mutual Casualty Company* (1997), 86 Ohio Misc. 2d 112, 685 N.E. 2d 1332, held that an insured was entitled to prejudgment interest in connection with the breach of an underinsured motorist insurance contract. In *Clevenger v. Westfield Companies* (1978), 60 Ohio App.2d, 395 N.E. 2d 377, the plaintiff filed suit against her automobile insurer when they could not agree as to the value of her damaged automobile. The Court held that an insurance policy is an "instrument of writing" under R.C. 1342.02(A) and further stated:

> The jury may assess prejudgment interest in favor of the insured under an automobile insurance policy where the insurer does not make a reasonable offer of settlement on or before the date the loss is due and payable.

In *Essex House v. St. Paul Fire and Marine Insurance Co.* 404 F.Supp. 978 (S.D. Ohio), the court held that the insured could recover statutory interest under R.C. §1343.03 in an action against an insurer that had refused to pay a claim even in the absence of bad faith or purposeful delay on the part of the insurer where the award was necessary to make the insured whole. To the same effect are *Kelley v. Smith* (1964), 7 Ohio App.2d 142, 219 N.E. 2d 231 and *Haas v. Pacific Mutual* (1941), 70 Ohio App.332, 41 N.E.2d 263.

In the event that the time and manner of payment is not specified in the contract, the legal obligation of the insurer is to pay the debt in accordance with the usual and customary manner. 59 *O.Jur.3d*, Insurance 1182.

IV. PUNITIVE DAMAGES ARE RECOVERABLE FOR BAD FAITH

In *Hoskins v. Aetna Life Insurance Company,* 6 Ohio St. 3d 272, 452 N.E.2d 1315 (1983), the Ohio Supreme Court held:

> Punitive damages may be recovered against an insurer who breaches his duty of good faith in refusing to pay a claim of its insured upon proof of actual malice, fraud or insult on the part of the insurer.

The *Zoppo* court reaffirmed that punitive damages are recoverable in bad faith cases by reinstating the jury's finding that Zoppo was entitled to punitive damages and by remanding the matter to the trial court for a hearing to determine the amount of the punitive damages.

Significantly, the *Zoppo* case held that R.C. 2315.21(C)(2), which allows the jury to determine whether or not the plaintiff is entitled to punitive damages but gives the trial court the power to set the amount of the punitive damages, is an unconstitutional violation of the plaintiff's right to trial by jury under Section 5, Article 1 of the Ohio Constitution. Therefore, punitive damage claims must be submitted to the jury to both determine initially whether plaintiff is entitled to such damages and, if so, the amount of the punitive damage award. As

mentioned above, if the jury decides to award punitive damages, it could also then award reasonable attorney fees, which become part of the compensatory damages for bad faith.

V. CONCLUSION

Zoppo addressed many of the issues that arise in bad faith cases, but there are still questions to be answered. The exact damages recoverable for bad faith are still open to some debate, but the court's language adopting the tort theory of proximate cause will allow insureds to argue for broad based damages.

The reasonable justification standard will probably make the determination of whether an insurer acted in good faith a fact question for a jury to decide in most cases, as opposed to a legal issue for a judge to resolve since, as one court has noted:

> Inherently, whether a reasonable basis exists taking into account all of the facts and circumstances and whether plaintiff [insurance company] knew of such or simply failed to obtain such knowledge, is factually oriented. While even a showing by the defendants [insureds] that the plaintiff was erroneous does not make out an action for bad faith, questions regarding reasonableness and knowledge inherently include factual questions.

See *State Farm Fire and Casualty Co. v. Trumble* (Idaho 1987), 663 F. Supp. 317.

REFERENCE IN *ZOPPO* TO PRIOR OHIO SUPREME COURT CASES ON BAD FAITH

Case	Syllabus	Reference to Case in *Zoppo*
Hart v. Republic Mutual Ins. Co.(1949), 152 Ohio St. 185, 87 N.E. 2d 347	"¶2. Such [a liability insurance] company is liable to respond in damages to its insured if it fails to act in good faith with respect to the settlement of such a claim."	Approved and Followed
Staff Builders, Inc. v. Armstrong (1988), 37 Ohio St. 3d 298, 525 N.E. 2d 783	"¶ 1. An insurer has a duty to act in good faith in the processing and payment of the claims of its insured. A breach of this duty will give rise to a cause of action in tort against the insurer irrespective of any liability arising from breach of contract."	Approved and Followed
Slater v. Motorists Mutual Insurance Co. (1962), 174 Ohio St. 148, 187 N.E. 2d 45	"¶ 2. A lack of good faith is the equivalent of bad faith, and bad faith, although not susceptible of contract definition, embraces more than bad judgment or negligence. It imports a dishonest purpose, moral obliquity, conscious wrongdoing, breach of a known duty through some ulterior motive or ill will partaking of the nature of fraud. It also embraces actual intent to mislead or deceive another."	¶ 2 of Syllabus, overruled
Motorist Mutual Insurance v. Said (1992), 63 Ohio State 3d 690, 590 N.E. 2d 1228	"¶ 3. A cause of action arises for the tort of bad faith when an insurer breaches its duty of good faith by *intentionally* refusing to satisfy an insured's claim where there is either (1) no lawful basis for the refusal coupled with *actual knowledge* of that fact or (2) an *intentional* failure to determine whether there was any lawful basis for such refusal. Intent that caused the failure may be inferred and imputed to the insurer when there is a reckless indifference to facts of proof reasonably available to it in considering the claim."	"overruled to the extent inconsistent herewith"

REFERENCE IN *ZOPPO* TO PRIOR OHIO SUPREME COURT CASES ON PUNITIVE DAMAGES FOR BAD FAITH

Case	Syllabus	Reference to Case in *Zoppo*
Hoskins v. Aetna Life Insurance Co. (1983), 6 Ohio St. 3d 272, 452 N.E. 2d 1315	"¶2. Punitive damages may be recovered against an insurer who breaches his duty of good faith in refusing to pay a claim of its insured upon proof of actual malice, fraud or insult on the part of the insurer."	Followed
Staff Builders, Inc. v. Armstrong (1988), 37 Ohio St. 3d 298	"¶2. Punitive damages may be recovered against an insurer that breaches its duty of good faith in refusing to pay a claim of its insured upon proof of actual malice, fraud or insult on the part of the insurer."	Followed
Preston v. Murty (1987), 32 Ohio St. 3d 334, 512 N.E. 2d 1174	"¶2. Actual malice, necessary for an award of punitive damages, is (1) that state of mind under which a person's conduct is characterized by hatred, ill will or a spirit of revenge, *or* (2) a conscious disregard for the rights and safety of other persons that has a great probability of carrying substantial harm."	Followed

Zoppo v. Homestead Insurance Co. at a Glance

Syllabus	**Quote**
1. An insurer fails to exercise good faith in the processing of a claim of its insured where its refusal to pay the claim is not predicated upon circumstances that furnish reasonable justification therefor. *Hart v. Republic Mut. Ins. Co.* (1949), 152 Ohio St. 185, 39 0.0. 465, 87 N.E.2d 347, *and Staff Builders, Inc. v. Armstrong* (1988), 37 Ohio St.3d 298, 525 N.E.2d 783, *approved and followed*; *Slater v. Motorists Mut. Ins. Co.* (1962), 174 Ohio St. 148, 21 0.0.2d 420, 187 N.E.2d 45, paragraph two of the syllabus, *overruled*; *Motorist Mut. Ins. Co. v. Said* (1992), 63 Ohio St.3d 690, 590 N.E.2d 1228 (over-ruled to the extent inconsistent herewith)	"Intent is *not* and has never been an element of the reasonable justification standard." p.555 "The record reveals a one sided inquiry by Homestead investigators as to who was at fault. They did not adequately question suspects or follow up on leads. Homestead breached its affirmative duty to conduct an adequate investigation. The award for punitive damages was justified."