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Pennsylvania's Bad Faith Statute 42 Pa.C.S.A. § 8371 — After 17 Years Some Questions Are Answered

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Two decisions from the Pennsylvania Supreme Court issued this past year have put to rest at least two of the myriad questions that have intrigued insurance coverage practitioners for 17 years.

In the years since the legislature responded to the high court's invitation to act in *DiAmbrosio v. Pennsylvania Nat'l Mut. Casualty Ins. Co.*, 494 Pa. 501, 431 A.2d 966 (1981), by enacting 42 Pa.C.S.A. §8371, practitioners and courts have struggled with the many ambiguities of the statute. However, 2007 saw some clarification.

Ash v. Continental Ins. Co., 593 Pa. 523, 932 A.2d 877 (2007) answers the question of the applicable statute of limitations. Since the enactment of §8371, the lower courts and the federal courts applying Pennsylvania law, have issued a number of conflicting opinions. Several trial courts applied the two-year statute of limitations, reasoning that the cause of action allowed by § 8371 is more akin to a tort action than a contract action even though the action must be one "arising under an insurance policy." See, e.g. *Susich v. Prudential Prop. & Cas. Ins. Co.*, 35 Pa. D. & C. 4th (1988). Other trial courts have concluded that the § 8371 claim is neither a tort nor a contract action, and have, therefore, employed the six-year "catch-all" statute of limitations. See, e.g. *Trujillo v. State Farm Mut. Auto. Ins. Co.*, 54 Pa. D. & C. 4th 241 (2001), rev'd, 817 A. 2d 1194 (Pa. Super. 2002).

The federal district courts have similarly been divided in their prediction on how the Pennsylvania Supreme Court would rule. In *Haugh v. Allstate Ins. Co.*, 322 F.3d 227 (3d Cir.2003), the Third Circuit predicted that the Pennsylvania high court would apply the two-year statute of limitations.

In *Ash, supra*, decided on October 11, 2007, the Pennsylvania Supreme Court did just that. The Court analyzed the remedies created by

the statute and reiterated that the statutorily created claim is distinct from the common law cause of action for breach of the contractual duty of good faith. *Birth Center v. St. Paul Companies, Inc.*, 567 Pa. 386, 787 A.2d 376 (2001) and *DiAmbrosio, supra*. It concluded that the duty imposed by § 8371 is imposed by law rather than by mutual contract; therefore, an action thereunder derives primarily from tort law. Accordingly, the Court held that the two-year statute of limitations under 42 Pa.C.S.A. § 5524 applies to § 8371 bad faith claims.

In *Toy v. Metropolitan Life Ins. Co.*, 523 Pa. 20, 928 A.2d 186 (2007), the Court was asked to consider whether the bad faith statute was broad enough to provide a remedy to an insured who alleges bad faith in soliciting the purchase of a policy. The Court held that it is not. *Id.* at 200.

In reaching its decision on that issue, the Court articulated the definition of "bad faith" that had developed at common law by 1990 when the statute was enacted. That definition encompasses the insurer's duty of good faith and fair dealing in its obligation of defense and indemnity in a third party claim and its obligation to pay for a loss in a first party claim. *Id.* at 199. The Court, relying on that definition to analyze the types of claims cognizable under § 8371, made it clear that the statute provides a remedy both for first party claims and third party claims, an issue that has been the subject of some debate among practitioners.

There is no doubt that § 8371 provides a remedy to insureds where there was not one at common law, as it was intended to do. However, it left us with unanswered questions, many of which remain unanswered even today. The Court has now answered at least two of these questions in their work this past year.

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