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BAD FAITH BLOG

No Covered Loss, No Vexatious Refusal to Pay

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BSI Constructors, a general contractor, had to replace the roof installed by one subcontractor and improperly protected by other subcontractors. After having to replace the roof at a cost of approximately $174,000, Hartford denied its claim. That denial was supported by the district court on summary judgment and the Eighth Circuit affirmed on appeal on both the breach of contract claim and the vexatious refusal to pay claim.

BSI Constructors obtained builders risk coverage from Hartford Fire Insurance Company. After one of BSI's subcontractors finished installing the roofing system, its project manager advised other subcontractors to properly protect the roofing structure while they completed their contracts. They failed to do so, the roof was severely damaged, and because of hundreds of hole patches in the roof and the penetration of water into the roofing system and insulation, the roof had to be replaced.

Hartford denied the resulting claim under the faulty workmanship exclusion which provided that Hartford would not pay "for 'loss' caused by or resulting from any of the following... defective, deficient or flawed workmanship or materials...." The exclusion also included an exception that it would "pay for 'loss' to other covered property that results from such defective workmanship..." (Slip Op at 3) The district court granted Hartford's summary judgment motion on both the breach of contract and vexatious refusal claims.

The Eighth Circuit noted that the Supreme Court of Missouri had never addressed the specific policy language at issue so it had to predict how that court would rule if confronted with the same coverage dispute. It concluded the Missouri Supreme Court would follow the rulings of other courts which had addressed the same issue and held "the Supreme Court of Missouri would read the faulty workmanship exclusion to encompass both a flawed product and the flawed process and thus exclude coverage under the circumstances of this case." (Slip Op. at 5) The Eighth Circuit further noted that the ensuing loss exception was not ambiguous and declined to "adopt a 'strained interpretation of the language of the policy in order to create an ambiguity where none exists.'" (Slip Op. at 7)

Increasingly insureds and their counsel are arguing the insurance company has acted in bad faith and/or is subject to a penalty for vexatious refusal to pay even though the court has determined that there was no coverage. The district court in the BSI case granted summary judgment in favor of Hartford on the vexatious refusal to pay claim because Hartford had no duty to cover the loss in the first place. In affirming the district court the Eighth Circuit stated:

Not only is the logic of the district court's decision irrefutable but, more importantly, Missouri precedent compels the result. See, *Fisher v. First Am. Title Ins. Co.*, (No. WD 74633, 2012 WL 4074418 at *6(Mo.Ct.App. Sept. 18, 2012) ("Where an insurer had no duty to defend or indemnify under the insurance policy, there cannot be a claim for vexatious refusal to defend or indemnify.")

Although some state courts and federal courts have adopted a different rule, Missouri's rule continues to be if there is no coverage there can be no vexatious refusal to pay as a matter of law. We will continue to read and report on this issue in which courts across the country seem to be divided on this "hot topic" in the insurance bad faith arena.

See our recent post on the California case involving Lehman Commercial Paper which addresses a closely related issue. Westlaw users can find that case at 2003WL26741.

By Anthony Martin

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