

Policyholders' Statutory Bad Faith Claims Barred Based on Statute of Limitations

July 2006

A Pennsylvania federal district court, applying Pennsylvania law, has granted partial summary judgment to an E&O insurer, holding that one policyholder's statutory bad faith claim against the insurer was barred by Pennsylvania's two-year limitations period, while a second policyholder's bad faith claim was barred because the causes of action asserted against it in the underlying action were not within the policy's coverage. *Nat'l Recovery Agency, Inc. v. AIG Domestic Claims, Inc.*, 2006 WL 1289545 (M.D. Pa. May 9, 2006).

In 2000, a debt collection agency was sued in New Jersey state court by another collection agency with which it had subcontracted to perform work. The defendant-agency sought a defense from its insurer under an E&O policy, but the insurer denied coverage on the ground that the policy did not cover claims "seeking the return of fees or charges for services performed by any 'Insured.'" In 2002, the complaint was amended to add a second defendant, another collection agency that was also an insured under the E&O policy. The insurer again denied coverage, and the insureds filed a coverage action in 2005 alleging breach of contract and bad faith (both statutory and common law). The insurer sought leave to amend its answer to plead the statute of limitations as a defense to the bad faith claims and then sought summary judgment on that issue.

After granting the insurer's motion for leave to amend, the court held that the first insured's statutory bad faith claims were barred by Pennsylvania's two-year limitations period because the limitations period began to run in 2000 when the insurer "provided clear notice" that it would not defend or indemnify the policyholder. In reaching this conclusion, the court found that the insurer's second denial of coverage (after the complaint was amended) was not "a separate act of bad faith that started the statute of limitations running anew." The court also held that the bad faith claim asserted by the second policyholder was barred because there was no "clear and convincing evidence" of bad faith, as none of the underlying counts alleged against the policyholder were within the policy's coverage.