

IN THE SUPREME COURT OF TEXAS

=====
No. D-4095
=====

STATE FARM FIRE & CASUALTY COMPANY, PETITIONER

v.

JAMES AND CYNTHIA SIMMONS, RESPONDENTS

=====
ON APPLICATION FOR WRIT OF ERROR TO THE
COURT OF APPEALS FOR THE NINTH DISTRICT OF TEXAS
=====

Argued October 8, 1997

JUSTICE HECHT, joined by JUSTICE OWEN, dissenting.

The tort of bad faith has two elements, one objective and the other subjective. Plaintiff must prove both "that the insurer had no reasonable basis for denying or delaying payment of the claim, and that it knew or should have known that fact." *Transportation Ins. Co. v. Moriel*, 879 S.W.2d 10, 18 (Tex. 1994). The Court has recently held that the objective element is satisfied by proof that an insurer denied or delayed payment of a claim after liability was reasonably clear. *Universe Life Ins. Co. v. Giles*, 950 S.W.2d 48, 55-56 (Tex. 1997).

Today the Court holds that an insurer who conducts "a biased investigation intended to construct a pretextual basis for denial" of its insured's claim may be liable for breach of its duty of good faith and fair dealing. *Ante* at _____. But that is true only if, in the end, the basis for denying the claim actually *is* pretextual. Bad faith liability requires proof not only of the subjective element but also of the objective element. Before an insurer can be in bad faith for the way it investigated a claim, there must be evidence not only that it was wrongly motivated but that a differently conducted investigation would have shown the claim to be reasonably clear. An insurer who willfully ignores evidence supportive of a claim risks bad faith liability; an insurer who ignores irrelevant evidence does not. An insurer who sets out to fabricate a basis for denying a claim but finds instead solid

grounds for denial is no more in bad faith than the insurer who seeks a pretext for denial but then decides to allow the claim after all. The insurer's bias and intent become relevant only when it appears that the insurer denied a claim when liability was reasonably clear. Then the fact that the insurer was not simply mistaken but wrongly motivated becomes important.

The burden of proving both elements of bad faith is on the insured. In this case, the Simmonses contend that State Farm acted in bad faith because it conducted a biased investigation designed to find some pretext for denying their claim. State Farm argues, I think with some force, that there is no evidence of such misconduct. But even if there were such evidence, State Farm argues that there must also be evidence of the objective element of bad faith liability — here, that but for a biased investigation, it would have been reasonably clear that the Simmonses' claim should have been allowed. As the Court states: "State Farm argues that the deficiencies in its investigation doied any particular step that would have made State Farm's liability reasonably clear." *Ante* at ____.

The Court rejects this argument, not because the Simmonses have proved how State Farm's liability on their claim would have been reasonably clear if only its investigation had not been deficient, but because the Court concludes that the Simmonses are not required to offer such proof. The Simmonses, the Court holds, have met their burden of proof merely by showing that State Farm's investigation was deficient. The Court reasons that because the insurer, not the insured, is obliged to investigate a claim, an insured meets its burden of proof as to both the objective and subjective elements of bad faith liability by showing that the investigation was deficient in some respect. The Court's conclusion is crystal clear:

Under the investigation standards State Farm's own experts identified, there was more than a scintilla of evidence that State Farm's investigation was materially deficient. We hold that the evidence is legally sufficient that State Farm breached its duty of good faith and fair dealing.

Ante at ____.

In other words, proof that an insurer's investigation was deficient in some respect is enough for bad faith liability.

In effect, the Court shifts to the insurer the burden of proving that the insured's claim would not have been reasonably clear even if its investigation had not been deficient. To leave the burden

on the insured, the Court appears to think, would obligate the insured to conduct some investigation of his own. While an insured should be obliged to present his insurer with whatever evidence the insured has or hopes may be supportive of his claim, no duty should fall on an insured to investigate his own claim in the same sense in which the insurer must investigate the claim. But even if an insured has no obligation to investigate his claim, when an insured alleges bad faith he is obliged to prove the elements of that tort to recover. He cannot merely assert that the insurer's investigation was deficient, whatever the insurer's motivation, and then rest his case. To recover for bad faith, he must show that the deficient investigation led the insurer to deny the claim when liability was reasonably clear.

Here, the Simmonses have failed to show how their claim would have been reasonably clear but for State Farm's deficient investigation. The Simmonses' central argument, and the one the Court focuses on, is that State Farm did not interrogate all the people who might have been able to shed light on the origin of the fire that destroyed their home. The Simmonses argue, for example, that State Farm was wrong in failing to question the paper delivery woman who first discovered the fire. But at oral argument the Simmonses' counsel admitted that he had interviewed the woman before trial and that she knew nothing helpful to the Simmonses' case. Undaunted by this partial setback, the Simmonses continue to argue that State Farm should have contacted the neighborhood hooligans who had burgled and perhaps vandalized their home, would have been more helpful to the Simmonses' cause than the paper delivery woman. If anything, one could reasonably expect that the young offenders would have denied arson just as they denied burglary. The Simmonses' decision to interview the paper delivery woman and no one else suggests that they themselves did not expect anything to be gained by further effort. State Farm cannot be faulted for having shared that same expectation.

The Simmonses argue that State Farm's bias was apparent in its persistent belief that they had financial reasons to burn down their home. It is true that State Farm initially overestimated the Simmonses' financial burdens, but the mistake was corrected before State Farm denied the claim.

The facts are that the Simmonses had such trouble making timely mortgage payments that their lender required weekly rather than monthly payments, that from the time of that requirement until seven weeks before the fire the Simmonses made only a little over seventy percent of their payments, that the Simmonses made no mortgage payments at all the seven weeks before the fire, and that the Simmonses owed about as much on their home as it was insured for. The record not does indicate whether the Simmonses knew at the time of the fire what equity they had in their home or that relief from weekly obligations would not be to their benefit. In retrospect, had the Simmonses known their true financial situation, they would not have been justified in thinking that destroying their home would relieve them of any significant financial burden, and thus they would have had no motive for arson. But what they actually knew or thought is surmise. From the facts it is not reasonably clear whether or not the Simmonses had a financial motivation to burn their home. But more importantly, on the issue of bad faith, no different investigation would have shown different facts.

The Simmonses also object to State Farm's initial characterization of the fire's origins *were* suspicious. The Simmonses themselves believe the fire was set. They argue that the proximity of the fire's origin to their time of departure in the wee hours of the morning can be explained by the possibility that arsonists were waiting in the bushes for them to leave. There is strong evidence of arson in this case; what is unclear is who set the fire.

The Court affirms a judgment of over \$1 million against State Farm for deficiencies in its investigation. Yet whatever those deficiencies were, the facts concerning the Simmonses' fire are almost entirely disputed. The Simmonses cannot show how State Farm would have learned something more if only it had been more thorough or more objective in its investigation. Rather, the Simmonses argue that on the facts available, State Farm should have paid their claim. State Farm concedes coverage, but a mistake in determining coverage is not bad faith. There is nothing more here.

Although the Court bases liability in this case squarely and entirely on evidence of what it regards as a deficient investigation, I doubt the Court will apply the same rule in other cases. That

is, the Court does not intend to impose bad faith liability on every insured whose investigation is “deficient” in some particular. The decision in this case, as in most bad faith cases, lamentably, is driven not nearly so much by legal principles as by the belief of individual judges that State Farm was not entirely fair and should pay the Simmonses some money. There is bad faith in insurance claims processing, and when it occurs, insureds should have a remedy. Until we formulate a body of law that defines bad faith sufficiently, we continue with our we-know-it-when-we-see-it approach that does little to change the lottery-like nature of the bad faith cause of action.

I continue to believe that the Court’s bad faith decisions refuse to give adequate definition to the tort of bad faith. *See Giles*, 950 S.W.2d at 58-79 (Hecht, J., dissenting); *State Farm Lloyds v. Nicolau*, 951 S.W.2d 444, 453-464 (Tex. 1997) (Hecht, J., dissenting). I agree with JUSTICE ENOCH that today’s opinion adds to the confusion. I do not agree with him, however, that bad faith liability is based on a failure to act as a reasonable insurer would. That is a negligence test which is not and should not apply in the context of bad faith. *Giles*, 950 S.W.2d at 64-65, 73 (Hecht, J., dissenting). Bad faith is no more negligence than accidentally causing a car wreck is bad faith.

I would hold that there is no evidence of bad faith in this case. Accordingly, I respectfully dissent.

Nathan L. Hecht
Justice

Opinion delivered: February 13, 1998