

ARBITRATION CLAUSES: IS IT BAD FAITH TO REQUIRE MUTUAL CONSENT?

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The Honorable James M. Munley of the United States District Court for the Middle District of Pennsylvania recently held that a bad faith claim could proceed based on an insurance company's removal of a mandatory arbitration clause from a policy. *Bukofski v. USAA Casualty Ins. Co.*, 2009 WL 1609402 (M.D.Pa. June 9, 2009).

In 2005, the Pennsylvania Supreme Court ruled in a case—generally referred to as "Koken"—that the Insurance Commissioner did not have the authority to require mandatory arbitration provisions for underinsured motorist (UIM) or uninsured motorist (UM) claims. *Insurance Federation of Pennsylvania, Inc. v. Com., Dept. of Ins.*, 889 A.2d 550 (Pa. 2005). After the Koken case, many insurance companies, including USAA Casualty, changed the terms of their Pennsylvania insurance policies so that mutual consent was required in order to go to arbitration. Also like USAA Casualty, many companies did this by simply replacing the mandatory arbitration clause in each insurance policy with a mutual consent to arbitrate clause.

In *Bukofski*, the plaintiff was involved in an automobile accident and filed a personal injury protection (PIP) claim and a (UIM) claim with the defendant. The defendant did not pay either claim to the plaintiff's satisfaction, and the plaintiff filed a bad faith lawsuit. One of the grounds alleged by the plaintiff as the basis for the bad faith claim was the fact that the defendant removed the mandatory arbitration clause from the plaintiff's insurance policy several months before the accident at issue. The defendant removed the case to federal court and filed a motion to dismiss on the grounds that a change to the terms of an insurance policy did not fall within the purview of the bad faith statute. Judge Munley denied the defendant's motion to dismiss and held that the plaintiff had stated a claim for bad faith.

Judge Munley referred to the mandatory arbitration clause as a "material benefit under the policy that provided plaintiff with an expedited and cost effective means of resolving UIM disputes." *Bukofski*, at *5. Judge Munley also stated that the defendant insurer might have removed the arbitration clause in order to gain "settlement leverage by necessitating protracted expensive litigation." *Id.* Judge

Munley viewed mandatory arbitration as a "material benefit" to an insured and implied that the use of litigation to resolve UIM disputes is akin to bad faith.

Judge Munley also implied that the lack of notice to the plaintiff of the unilateral policy change was indicative of bad faith. "If the change was done unilaterally without notice to the plaintiff there would be no way for the plaintiff to know about the change until a claim was made." *Id.* at *6. This suggests that insurance companies who wish to change the arbitration provisions of their Pennsylvania policies might avoid bad faith claims by providing notice to their insured before making a change.

It is unclear whether Judge Munley's decision in *Bukofski* is the beginning of a new trend in case law or is simply an anomaly. Clearly, the plaintiff in *Bukofski* will have a difficult burden in proving that USAA altered its arbitration clause to gain leverage in UM and UIM negotiations. As all Pennsylvania courts know, the mandatory arbitration clause was altered as a consequence of the now well-documented corruption scandal in the Luzerne County judicial system. In any event, it is clear that insurance companies would be wise to provide adequate notice to their insured before changing an arbitration clause so as to require mutual consent to arbitrate.

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