

NO GUARANTEE FOR INSURANCE COMPANY'S "GUARANTEED CONTRACTOR"

By Richard A. Huver

Anyone who has ever been involved with an insurance claim has probably run across the insurance industries' "guaranteed" or "preferred" contractors, repair facilities, service centers, etc. It is standard operating procedure for insurance companies to recommend or suggest "their" people to repair your car, rebuild your home, and refurbish your personal property. And the insurance company usually guarantees the work. Does the insurance company have any tort liability, however, if "their" people are negligent in the repair of your car, the rebuilding of your home, or the refurbishing of your property? Stated differently, does the covenant of good faith and fair dealing implied in every insurance contract extend to the tortious conduct of an insurance company's agent - the "preferred" contractor?

1. Guaranteed Workmanship

This question was recently answered by our local Fourth District in Rattan v. United Services Automobile Assoc'n (2000) 101 Cal.Rptr.2d 6. Plaintiff's home sustained severe structural damage and many contents had been destroyed or damaged as a result of a fire. Rattan's insurance company, USAA, recommended a specific general contractor (Baker Pacific) to perform the necessary structural repairs to the home. Baker Pacific, in turn, recommended a local company to remove, clean and store plaintiff's personal belongings while the home was being repaired. The work of both companies was guaranteed by USAA. Id. at 8.

Baker Pacific's performance, however, was less than satisfactory. Numerous structural repairs were inadequately performed, work was completely slowly, poorly or not at all, and some employees even made long distance phone calls using the Rattan's phone. Eventually, USAA fired Baker Pacific and retained another general contractor, Integrity Builders, to finish the repairs. Id.

Unfortunately, Integrity Builders did not perform much better. Many defects were left unremedied and several major electrical problems arose after their work was completed. To make matters worse, the Rattan's personal property that had not been ruined in the fire was damaged or destroyed because of improper cleaning, storage and packing by the restoration and storage company originally recommended by Baker Pacific. Id.

The Rattans sued USAA for bad faith, alleging breach of contract and breach of the implied covenant of good faith and fair dealing. It appears the basis for their claim was solely the negligent work by USAA's "preferred" contractors, and USAA's guarantees of the contractors' work. Plaintiff contended that USAA could be held liable for bad faith for the general contractors' conduct under principal/agency rules of law. Id. at 9.

Plaintiff's request that the trial court instruct the jury that USAA could be liable for bad faith as principal of their agents' (contractors) negligence was rejected. Plaintiff also requested

several jury instructions which quoted various sections of the Code of Regulations based on his expert's testimony regarding an insurance company's obligations and responsibilities under the Code of Regulations, title 10, §2695 *et seq.* These regulations mimic many of Insurance Code §790.03(h)'s provisions dealing with fair claims handling practices. These requested instructions were likewise refused by the trial court. *Id.* at 9-10. USAA's motion for a directed verdict on punitive damages was then granted. *Id.* at 10.

On appeal, plaintiff contended the trial court erred in refusing to instruct the jury on principal/agency rules of law, and in refusing to read the instructions quoting California's Code of Regulations. Neither avenue of appeal was successful.

2. No Tort Liability For Guarantee Contracts

While acknowledging that all insurance contracts contain an implied covenant of good faith and fair dealing, the breach of which supports a tort cause of action, the appellate court refused to extend this covenant to the separate "guarantee" contracts. Specifically, the court noted that the recovery of tort damages for breach of an insurance contract was "a major departure from traditional principles of contract law." *Id.* at 11, quoting *Foley v. Interactive Data Corp.* (1988) 47 Cal.3d 654, 690. The California Supreme Court has been unwilling to permit tort recovery for breach of a contract "unless in addition to the breach of the covenant a defendant's conduct violates a fundamental public policy of the state." *Rattan*, 101 Cal.Rptr.2d at 11.

Although the insurance contract entered into between the Rattans and USAA included an implied covenant of good faith and fair dealing, the Rattans' remaining contracts with USAA for the repair of their residence and refurbishing/storage of their personal belongings did not. Further, USAA's guarantee of the general contractors and restoration company's work was neither a contract of insurance nor part of the original insurance policy. Extending tort liability against USAA for the contractors' negligence would have, in essence, transformed USAA into the liability insurer for the contractors, something neither party intended or contemplated. *Id.*

The Court found support for its decision on two separate grounds. First, the Court did not believe enforcement of USAA's guarantees of workmanship required a tort remedy.

. . . the insured who has been provided a policy's financial benefits but is unhappy with the paint job performed by an agent of the insurer has contractual remedies against the painter, as well as any insurer, such as USAA, acting as a guarantor of workmanship. The insured may, as was the case here, simply find another painter and require that the insurer pay for it. In this situation it is difficult to see any substantial public interest which supports any additional tort remedy.

Id. at 11-12.

Secondly, the Court was concerned that extending tort liability against an insurer for guaranteeing the repair work would lead to insurers refraining from acting as guarantors in the

future. The Court believed “this might deprive less sophisticated insureds. . . valuable protection from incompetent or unscrupulous contractors.” Id. at 12.

Turning to the requested jury instructions quoting California’s Code of Regulations, the Court again upheld the trial court’s decision. Citing to California law which holds that, “at most the regulations . . . may be used by a jury to infer a lack of reasonableness” on the part of the insurer, the Court stated,

[b]ecause given as instructions the regulations would have suggested to the jury that any violation of the regulations was per se a breach of contract or an act of bad faith, rather than only evidence of a breach or bad faith, the trial court was fully warranted in rejecting them.

Id.

Thus, if your client encounters a similar situation, it will take more than just the insurance company’s guarantee of the contractor’s workmanship to hold the insurer liable in tort for the contractor’s negligent conduct.