Louisiana Supreme Court clarifi

On May 5, 2015, in *Kelly v. State Farm Fire & Cas. Co.*, 14-1921 (La. 5/5/15); __ So.3d __, 2015 WL 208254, the Louisiana Supreme Court issued a landmark decision answering the following two certified questions in the affirmative:

> (1) Can an insurer be found liable for a bad faith failure to settle claim under Section 22:1973(A) when the insurer never received a firm settlement offer; and
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> (2) Can an insurer be found liable under Section 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage?

In answering the questions, the Supreme Court made clear that liability insurers owe their insureds a duty to timely gather information during the claims process, to advise their insureds of significant developments in the claim process and litigation, and to protect their insureds from liability in excess of the policy's limits by taking some positive step to settle their insureds' claims. Perhaps more importantly, the Court adopted the United States Court of Appeals for the Fifth Circuit's holding in *Stanley v. Trinchard*, 500 F. 3d 411 (5th Cir. 2007), that "an insured's cause of action for a breach of the implied covenant of good faith and fair dealing are not limited to the prohibited acts listed in La. R.S. 22:[1973](B)."

The Court began with the language of La. R.S. 22:1973, which provides, in pertinent part, as follows:

> A. An insurer . . . owes to his insured a duty of good faith and fair dealing. The insurer has an affirmative duty to adjust claims fairly and promptly and to make a reasonable effort to settle claims with the insured or the claimant, or both. Any insurer who breaches these duties **shall** be liable for any damages sustained as a result of the breach.
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> B. Any one of the following acts, if knowingly committed or performed by an insurer, constitutes a breach of the insurer's duties in Subsection A of the Section:
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> (1) Misrepresenting pertinent facts or insurance policy provisions relating to any coverages at issue;
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> . . . .

The Court then turned to the following facts. On Nov. 21, 2005, Danny Kelly was injured in an automobile collision with Henry Thomas Jr., who had liability insurance with State Farm. Thomas and Kelly were driving in opposite directions, when Thomas turned left and struck Kelly. Kelly contended that Thomas had failed to yield to oncoming traffic, but Thomas maintained he was not at fault. Kelly was hospitalized and treated for a fractured femur at a cost $26,803.17.

On Jan. 6, 2006, Kelly's attorney mailed a letter to State Farm that included copies of Kelly's hospital records and bills, and stated that he "will recommend release of State Farm Insurance Company and your insured, Henry Thomas Jr. for payment of your policy limits." Kelly's attorney requested that State Farm call him within 10 days to discuss the matter.

State Farm did not respond to the letter and, more than two months later, offered to settle the case for $25,000, the policy's limit, and sent Kelly's attorney a letter memorializing the offer. Kelly rejected the offer and filed suit against Thomas. The same day State Farm received word that the offer was rejected, it sent Thomas a letter informing him of the possibility of personal liability and suggesting that he retain independent counsel. The letter from State Farm did not mention the January 2006 letter from Kelly's attorney, State Farm's offer to Kelly or the amount of Kelly's medical bills.

Kelly's suit against Thomas proceeded to trial, and Thomas was cast in judgment for $176,464.07, plus interest. State Farm paid Kelly the policy limit of $25,000. Thereafter, Thomas entered into an agreement with Kelly, assigning his right to pursue a bad faith action against State Farm to Kelly in exchange for Kelly's agreement not to enforce the judgment against Thomas' personal assets.

Kelly filed suit against State Farm and asserted two causes of action against State Farm as the assignee of Thomas' rights: (1) Failing to accept Kelly's 2006 settlement offer ("failure to settle claim"); and (2) failing to notify Thomas of Kelly's January 2006 letter ("failure to inform claim"). With respect to the failure to settle claim, State Farm argued that it could not be liable where Kelly's attorney did not submit an "actual offer to settle" and where State Farm's conduct did not fall within the ambit of conduct specifically prohibited by Section 22:1973(B)(1) – (6). With respect to the failure to inform

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BY MICHAEL DeBARROS

claim, State Farm argued that its failure to keep Thomas fully informed of the status of settlement negotiations and other developments affecting his excess exposure was not a "misrepresentation" under La. R.S. 22:1973(B)(1) and was merely one factor to be considered in a multi-factored "bad faith" analysis. The Supreme Court rejected all of State Farm's arguments.

On Kelly's failure to settle claim, the Court noted that its resolution of the issue required a twofold analysis. First, is an insured's cause of action against its insurer for a breach of the implied covenant of good faith and fair dealing limited to the prohibited acts listed in La. R.S. 22:1973(B), or does an independent cause of action exist under La. R.S. 22:1973(A)? Second, must an insurer receive "a firm settlement offer" as a condition for an insured to recover for the insurer's bad-faith failure-to-settle?

The Court found that the plain language of La. R.S. 22:1973(A) supported an independent cause of action. Most notably, after describing the duties owed by an insurer, La. R.S. 22:1973(A) concludes with mandatory, rather than permissive language: "Any insurer who breaches these duties shall be liable for any damages sustained as a result of the breach." Further, while a third-party claimant has no cause of action under La. R.S. 22:1973(A), an insured does because the duty of good faith and fair dealing referenced in La. R.S. 22:1973(A) is an outgrowth of the contractual and fiduciary relationship between the insured and insurer—a relationship not present between the insurer and third-party claimant.

The Court also found that, for three reasons, the language of La. R.S. 22:1973(A) did not require the insurer's receipt of a "firm settlement offer" before the insurer had a duty to make a reasonable effort to settle claims. First, the plain language of La. R.S. 22:1973(A) specified that the insurer's duty to make a reasonable effort to settle claims was an affirmative duty. The Court reasoned that the phrase "affirmative duty" is a legal term of art, which "requires taking positive action(s) to comply with a legal standard." Second, the requirement of "a firm settlement offer is not listed anywhere in the statute [and] [t]o impose the requirement of a firm settlement offer would essentially amount to adding words not included in the statute." Third, as a practical matter, "[t]he insured has no control over whether a firm offer will be submitted" and yet "the insurer has undertaken the obligation to protect the insured." Thus, there is "no practical reason why the insurer's obligation to act in good faith should be made subject to the tenuous possibility that an insurer will receive a firm settlement offer." Accordingly, the Court held that an insurer can be found liable for a bad -faith-failure-to-settle claim under La. R.S. 22:1973(A), notwithstanding that the insurer never received a firm settlement offer.

The second certified question asked the Court to decide whether an insurer can be found liable under La. 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage (*i.e.*, whether State Farm can be found liable under La. 22:1973(B)(1) for its failure to keep Thomas fully informed of the status of settlement negotiations and other developments affecting his excess liability). The Court again viewed the question as requiring a twofold analysis. First, is a failure to communicate a "misrepresentation"? Second, must the misrepresentation relate to the insurance policy's coverage? On the first issue, the Court reasoned that because La. R.S. 22:1973(A) requires the insurer to take some positive action, and because La. R.S. 22:1973(B) delineates certain breaches of the insurer's La. R.S. 22:1973(A) duties, "[a] communication from the insurer that either states an untruth or fails to state the truth is contemplated by La. R.S. 22:1973(B)." On the second issue, the Court gave a disjunctive meaning to the word "**or**" in La. R.S. 22:1973(B)'s prohibition of "[m]isrepresenting pertinent facts **or** insurance policy provisions relating to any coverages at issue" (emphasis added). The Court noted that if the word "or" was not given a disjunctive meaning, the first phrase ("pertinent facts") would be both redundant and meaningless, because misrepresentations about insurance policy provisions are addressed in the second phrase, which follows the word "or."

While the Court noted that "tight [reins] must be kept on a cause of action for insurer settlement practices," *Kelly* is a significant win for insureds, and the case serves as a stark reminder that "a liability insurer is the representative of the interests of its insured and the insurer, when handling claims, must carefully consider not only its own [self-interest], but also its insured's interest so as to protect the insured from exposure to excess liability."