Westlaw Today
powered by Reuters

Top bad faith cases of 2021

By Michael W. Melendez, Esq., and Chad A. Pasternack, Esq., Cozen O'Connor

JULY 8, 2022

Totality of the circumstances

Case: *Pelaez v. Government Employees Insurance Company*, 13 F.4th 1243 (11th Cir. 2021).

The 11th Circuit, interpreting Florida law, ruled that in determining whether an insurer's conduct is in bad faith, a court must review the "totality of the circumstances," not merely one aspect of the insurer's conduct.

An insured driver and a motorcyclist were involved in an accident, resulting in serious injuries to the motorcyclist. Seven days later, the motorcyclist's attorney requested statutory disclosures, but did not make a demand. Six days after that, the driver's liability insurer proactively tendered its bodily injury limit. The tender package included a proposed release and a letter explaining that the motorcyclist's attorney should call if he wished to revise the release. The motorcyclist rejected the settlement offer, asserting that the release was overbroad, but without proposing any revisions. The claimant and insured subsequently entered into a $15 million stipulated judgment, over the insurer's objection.

The 11th Circuit held bad faith is determined by the "totality of the circumstances." Because the insurer diligently investigated the claim, proactively tendered its limit, and offered to change the release language, the court held that it did not act in bad faith. The court noted that the insurer did not escape bad faith liability merely because the claimant's attorney's actions hindered the settlement, but stated that those actions were relevant to the totality of the circumstances.

Insurers should be mindful of the applicable laws regarding what constitutes bad faith. Where the insurer's overall conduct is reasonable, that may provide a defense against a bad faith claim.

No bad faith per se

Case: *Pinto v. Farmers Insurance Exchange*, 61 Cal. App. 5th 676 (Cal. Ct. App. 2021).

The California Court of Appeal addressed whether a liability insurer's declination of a reasonable settlement offer constitutes bad faith per se. The court held that it did not.

A one-car accident caused injury to each of the occupants. The auto insurer promptly tendered bodily injury limits to each occupant, except the permissive driver, who was determined to be at fault. One seriously injured passenger made a policy limit settlement demand with a short deadline. That demand required a sworn declaration that the driver had not been driving in the course of her employment and a copy of any other applicable insurance policy.

The insurer promptly offered the policy limit to globally settle all claims against all insureds. The insurer retained a private investigator to locate the driver, who refused to sign a declaration. The day before the deadline, the insurer advised the claimant's attorney that the driver stated she had no other insurance and requested a 30-day extension because the insurer had insufficient time to comply with all the conditions. The claimant's attorney refused the extension.

The 11th Circuit, interpreting Florida law, ruled that in determining whether an insurer's conduct is in bad faith, a court must review the "totality of the circumstances," not merely one aspect of the insurer's conduct.

Nevertheless, prior to the deadline, the insurer tendered a settlement check for the limit and a form release of the driver and the owner. The claimant rejected the tender because the insurer failed to unconditionally accept and provide the requested documentation.

The claimant sued the driver. The lawsuit settled for approximately $10 million, including the driver's assignment of her claims against the insurer. The claimant brought a bad faith action against the insurer. The jury found that the insurer was responsible for the judgment because the claimant made a reasonable settlement demand, the insurer failed to accept it, and an excess monetary judgment was entered against the driver. The jury did not find that the insurer's conduct was unreasonable.

The appellate court reversed, explaining that the critical issue was the reasonableness of the insurer's conduct under the facts of the particular case. A settlement offer may be multidimensional, including the amount demanded, conditions, and the scope of the release. The court found that the insurer was not in bad faith because it did all it could to achieve a settlement, especially where

the condition with which it could not comply — obtaining the declaration from the driver — was beyond its control.

The insurer's reasonableness generally is the key consideration in a bad faith action. *Pinto* exemplifies that if the insurer acts reasonably to protect the insured's interests, the insurer should not be liable in bad faith.

Compliance with notice provisions

Case: *GEICO Indemnity Company v. Whiteside*, 857 S.E.2d 654 (Ga. 2021).

The Georgia Supreme Court addressed whether an auto insurer that did not receive a contractually required notice of a lawsuit against a permissive driver could be liable for a bad faith failure to settle. The court held that in limited circumstances, it could be.

Pinto exemplifies that if the insurer acts reasonably to protect the insured's interests, the insurer should not be liable in bad faith.

The driver was involved in an accident that resulted in injuries to a cyclist. The insurer received pre-litigation notice of the accident, and advised the driver that it was responsible for the accident and would deal directly with the cyclist's attorney.

The driver, however, did not have a copy of the policy, and the insurer knew that she was unsophisticated and lived an unstable lifestyle. The insurer did not advise her to promptly forward any legal papers to the insurer.

The cyclist made a pre-litigation policy-limit demand. The insurer made a counter-offer and followed up with the cyclist's attorney, who ignored the insurer. Without informing the insurer, the cyclist filed suit. The driver threw the summons in the trash because she assumed the insurer was handling the claim. The cyclist obtained an excess default judgment and pursued a bad faith claim.

The court concluded that the insurer could be liable in bad faith because it should have foreseen that the driver would breach her contractual notice obligation because she did not know about it and the insurer knew she was unsophisticated. The court emphasized that the failure to settle occurred before the driver breached that obligation.

A good practice for insurers is to inform or remind insureds of their obligations under the policy to avoid any misunderstandings.

Requirement of excess judgment

Case: *West Virginia Mutual Insurance Company v. Salango*, 866 S.E.2d 74 (W.Va. 2021).

The West Virginia Supreme Court held that an insured cannot state a claim for a common law bad faith failure to settle where no judgment exceeding the policy limit is entered against the insured.

A doctor reported a lawsuit to his malpractice insurer, which provided $2 million in coverage. The patient demanded $300,000. The insurer rejected the demand, so the parties proceeded to trial, The jury returned a $6 million verdict, which was reported in local newspapers. After the verdict, but before the court entered final judgment, the insurer settled the suit for $950,000.

The doctor filed a bad faith action, alleging that the failure to settle before trial caused him to lose approximately $1.2 million in business. The court rejected the doctor's argument, explaining that the insured must face personal liability for an excess judgment before the insured can recover bad faith damages. Although the excess verdict might have supported a bad faith action, the doctor did not face personal liability because the insurer settled the claim within the policy limit before the judgment was entered.

Case: *Reeves v. South Carolina Municipal Insurance & Risk Financing Fund*, 862 S.E.2d 248 (S.C. 2021).

The South Carolina Supreme Court ruled that an insurer cannot be liable for a bad faith failure to settle where it satisfies an excess judgment rendered against the insured.

A Cottageville police officer shot and killed the former Cottageville mayor. The mayor's estate filed a wrongful death and survival lawsuit against Cottageville and numerous people involved. Cottageville was insured under a "self-insurance liability fund" established pursuant to South Carolina Code. The Fund argued that the coverage provided was limited to $1 million. A jury ultimately awarded $7.5 million in actual damages and $90 million in punitive damages. The estate and the Fund agreed to settle all the lawsuits for $10 million. The settlement agreement provided, among other things, that if the state court determined in a declaratory relief action that the South Carolina Tort Claims Act applied to a bad faith claim against the Fund, the Fund would pay the estate another $1 million.

The West Virginia Supreme Court held that an insured cannot state a claim for a common law bad faith failure to settle where no judgment exceeding the policy limit is entered against the insured.

The South Carolina Supreme Court refused to answer that question because it found that the Fund's position on coverage, though wrong, was reasonable. The court noted that the liability issues in the underlying lawsuits were hotly contested and that there was no indication of any certainty that the estate would prevail. A key consideration was that after the verdict exceeded available limits, the Fund settled the case, leaving the insured insulated from any excess judgment. The court explained that it "do[es] not condone the idea an insurer may incur bad faith liability for simply taking a case to jury, when the insurer satisfied the judgment after trial without exposing the insured to excess liability."

Salango and *Reeves* show that an insurer may be able to avoid a bad faith claim for failure to settle by eliminating the insured's personal exposure to excess liability.

Consequential damages in coverage actions

Case: *Citizens Property Insurance Corp. v. Manor House, LLC*, 313 So. 3d 579 (Fla. 2021).

The Florida Supreme Court held that an insured under a first-party insurance policy cannot seek breach of contract damages and extra-contractual consequential damages in the same lawsuit. Following Hurricane Francis, an insured apartment complex filed a property damage claim. The insurer made payments, totaling about $2.3 million. The insured invoked appraisal, resulting in an approximately $8.4 million award.

The insured sued the insurer for breach of contract and fraud. The insured, who did not have business interruption coverage, sought extra-contractual damages on its breach of contract claim for lost rental income based on the alleged delay in rebuilding caused by the insurer's failure to promptly pay $8.4 million. The court held that "extra-contractual consequential damages are not available in a first-party breach of insurance contract action because the contractual amount due to the insured is the amount owed pursuant to the express terms and conditions of the insurance policy." To recover extra-contractual damages, the insured would have to seek relief in a separate bad faith action pursuant to Florida Statutes section 624.155.

Consenting to settlement under indemnity policy

Case: *Apollo Education Grp, Inc. v. National Union Fire Insurance Company*, 480 P.3d 1225 (Ariz. 2021).

The Arizona Supreme Court addressed a certified question from the Ninth Circuit regarding the reasonableness of an insurer's decision to withhold consent to a settlement under an indemnity policy that does not include a duty to defend. The court held that such reasonableness must be viewed from the insurer's — not the insured's — perspective.

The insured was sued in a class action following reports that it improperly backdated stock option grants to its executives. The court dismissed the lawsuit with prejudice for failure to allege falsity with particularity.

While the dismissal was on appeal, the insured and the plaintiffs agreed to settle for approximately $13 million. The policy stated that "[t]he Insured shall not ... enter into any settlement agreement ... without the prior written consent of the Insurer," and that "consent shall not be unreasonably withheld." The insurer refused to consent to the settlement. The insured paid the settlement and then filed a coverage and bad faith action against the insurer.

The court held that under a policy without a contractual duty to defend, the objective reasonableness of the insurer's consent decision is assessed from the insurer's perspective, not the insured's. Namely, the insurer must independently assess and value the claim, giving fair consideration to the settlement offer, but need not approve a settlement simply because the insured believes it is reasonable. The court noted that an insurer is unlikely to reject a settlement if the objective value of the claim is commensurate with the settlement because the insurer likely would have to pay such a claim. Insurers should endeavor to have information that objectively justifies their claim determinations.

Adjusting claims with fraud concerns

Case: *Selective Insurance Company of South Carolina v. Sela*, 11 F.4th 844 (8th Cir. 2021).

The 8th Circuit, applying Minnesota law, addressed the award of taxable costs under the Minnesota statute for bad faith denial of policy benefits.[1] Under the statute, the court can award taxable costs if the insured can show: (1) objectively, that the insurer had no reasonable basis for denying policy benefits; and (2) subjectively, that the insurer knew it lacked a reasonable basis or recklessly disregarded its lack of a reasonable basis.

Salango and Reeves show that an insurer may be able to avoid a bad faith claim for failure to settle by eliminating the insured's personal exposure to excess liability.

An insured sought first-party property coverage for roof damage. The insurer received an anonymous tip that years earlier, the insured submitted a fraudulent claim under a prior policy by not repairing all the property damage for which it was paid. The insurer referred the claim to its special investigation unit and retained a forensic expert. The forensic expert determined that much of the previously claimed damage was not repaired. The insurer denied the claim based on fraud.

Regarding the objective prong, the court found that the anonymous letter would have led a reasonable insurer to open a fraud investigation, and that once it did, it would focus on whether the insured said anything that was untrue.

Here, the insured admitted he did not repair all the prior damage and provided documents showing how much he paid for the prior repairs. Because that information was not provided to the forensic expert, the court found that a reasonable insurer, in denying the claim, would not rely on the expert's opinion regarding whether the prior work was actually performed.

Regarding the subjective prong, the court found that the insurer denied coverage based on the mistaken premise that the insured claimed to have repaired all prior damage. The court concluded that the insurer ignored the facts that supported the insured's claim and recklessly disregarded its lack of a reasonable basis to deny it. The court held that the insured was entitled to taxable costs.

Florida civil remedy notices

Case: *Julien v. United Property & Casualty Insurance Company*, 311 So. 3d 875 (Fla. 4th DCA 2021).

A Florida court decided that a Civil Remedy Notice of Insurer Violation[2] failed to satisfy the requirement that an insured "state with specificity" the policy language and statutory provisions at issue. The insured reported a claim for fire damage to his home. After the insurer learned that the insured previously filed multiple plumbing claims and a fire claim with another insurer, it sent a reservation of rights letter and requested an examination under oath. In response, the insured filed a Civil Remedy Notice. That Notice alleged thirty-five violations of statutory provisions and referenced the entire policy. The court dismissed the insured's bad faith action because the Notice did not include the required specificity of the purported violations to provide the insurer with an opportunity to cure those violations.

Notes

[1] Minn. Stat. § 604.18.

[2] Florida Statutes section 624.155.

About the authors

Michael W. Melendez (L) is the office managing partner of **Cozen O'Connor**'s San Francisco office and is co-chair of its bad-faith practice group. He has practiced insurance coverage law for more than 30 years, primarily handling complex liability insurance and bad-faith issues. He provides coverage advice to liability insurers and represents them in lawsuits brought by insureds. He may be reached at mmelendez@cozen.com. **Chad A. Pasternack** (R) represents insurers in coverage and bad-faith litigation. Based in West Palm Beach, Florida, he focuses his practice on commercial property and general liability insurance. His work also includes advising on complex coverage issues, monitoring potential excess exposure and handling multiple-claimant issues. He may be reached at cpasternack@cozen.com.

This article was first published on Westlaw Today on July 8, 2022.