THE WALTZ LAW GROUP

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Memo

From: **Jeffery J. Waltz**

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Re: **Louisiana Supreme Court Opinion—*Kelly v. State Farm Fire & Casualty Co.*, No. 2014-cq-1921 (La. 05/05/15)**

The Louisiana Supreme Court recently issued an important opinion concerning the duties imposed on insurers pursuant to Louisiana bad faith statutes. In *Kelly v. State Farm Fire & Casualty Co*., 2014-1921 (La. 5/5/15). –So.3d– (La. 2015), the Louisiana Supreme Court answered two certified questions of law directed to it by the United States Court of Appeals for the Fifth Circuit, addressing the issues of:

> (1) Whether an insurer can be liable to its insured for a bad faith failure to settle under La. R.S. 22:1973(A) in the absence of a "firm" settlement offer, and;
>
> (2) Whether an insurer can be liable under La. R.S. 22:1973(B)(1) for misrepresenting or failing to disclose pertinent facts that are not related to the insurance policy's coverage.

After a thorough analysis of the facts and issues of the case, the Supreme Court found that a firm settlement offer is ***unnecessary*** for an insured to sustain a cause of action against an insurer for a bad faith failure to settle claim because the insurer's duties can be triggered by information other than the fact that a settlement offer has been made. The Supreme Court also found that La. R.S. 22:1973(B)(1) prohibits the misrepresentation of or failure to disclose "pertinent facts", without restriction to facts "relating to any coverages".

A more detailed analysis of the case and opinion is offered below.

I. Factual Summary

At issue were the claims handling procedures of State Farm after an automobile accident in which State Farm's insured struck and hit the plaintiff. The plaintiff and a witness told police that the insured failed to yield, but the State Farm insured maintained he was not at fault. State Farm had issued a policy to its insured with limits of $25,000.

On January 6, 2006, the plaintiff's lawyer sent correspondence to State Farm regarding the extent of his client's injuries and hospital bills, which totaled $26,803.17, and stated in the letter, "I will recommend release of State Farm Insurance Company and your insured…for payment of your policy limits". State Farm did not respond to the letter until over two months later on March 22, 2006. At that time, State Farm offered to settle the case for the $25,000 limit. The plaintiff rejected the offer and filed suit.

On the same day State Farm learned its offer was rejected, it sent its insured a letter informing him of possible personal liability, but it did not inform him of the January letter from the plaintiff's attorney, State Farm's settlement offer to the plaintiff, which was rejected, or the amount of the plaintiff's medical bills.

II. Procedural Posture

At trial, judgment was rendered against State Farm and its insured in the amount of $176,464.07 plus interest. After judgment, State Farm tendered its policy limits. State Farm's insured then entered into a compromise with the plaintiff assigning the insured's rights to pursue a bad faith claim against State Farm to the plaintiff, in exchange for the plaintiff's promise not to enforce the judgment in excess of the policy limits against the insured.

As ***assignee*** of the bad faith claims, the plaintiff then filed suit against State Farm alleging that State Farm breached its duties of good faith and fair dealing by failing to notify its insured of the January 2006 letter and failing to accept the January 2006 settlement offer for policy limits. The district court granted summary judgment in State Farm's favor, finding that the January 2006 letter did not constitute a "firm" settlement offer, and, as such, State Farm did not have a duty to notify the insured of the letter. Further, the court found that, as the letter was not an actual settlement offer, State Farm could not be liable for bad faith failure to settle because it did not fail to accept an actual offer. The plaintiff appealed this decision.

On appeal, the U.S. Fifth Circuit noted that La. R.S. 22:1973(A) did not give a third party claimant a right to sue an insurer for generalized breach of good faith, but recognized that here, the plaintiff was not advancing his own claim but the claim assigned to him by

the State Farm insured. In deciding to certify questions to the Louisiana Supreme Court, the Fifth Circuit noted that the courts of Louisiana have never held that a firm settlement offer was required for a bad faith failure to settle claim, but, then again, no cases were cited that found an insurer liable for bad faith in the absence of a firm settlement offer. As to La. R.S. 22:1973(B), the Fifth Circuit stated that the jurisprudence conflicted as to whether a misrepresentation must relate directly to coverage. Accordingly, the questions were certified to the Louisiana Supreme Court for an opinion.

III. Louisiana Supreme Court's Analysis

In its review, the Louisiana Supreme Court again noted that the plaintiff had been assigned the cause of action, and made clear that the asserted action was not one of a third party claimant, but rather that of an insured. The Court then separated the first certified question into two parts, addressing first whether La. R.S. 22:1973(A) did, in fact, afford an insured a cause of action for a bad faith failure to settle claim.

A. Whether an insured has a cause of action for a bad faith failure to settle claim under La. R.S. 22:1973(A).

La. R.S. 22:1973(A) provides, in relevant part: "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." The Court noted that section B of the statute contained an exclusive list of breaches for which third party claimants could recover. As to section A, however, the Supreme Court cited *Theriot v. Midland Risk Ins. Co*., 694 So.2d 184 (La. 1997) and *Stanley v. Trinchard*, 500 F.3d 411 (5th Cir. 2007), and found that section A of the statute recognized a jurisprudentially established duty of good faith and fair dealing owed to an insured, which is an outgrowth of the contractual and fiduciary relationship between the insured and insurer. In so finding, the Supreme Court held that affirmative duty owed by an insurer to an insured is not limited to the prohibited acts listed in section B of the statute. The Supreme Court noted that the Louisiana legislature essentially codified the holdings of *Theriot* and *Stanley* in 22:1973(A), establishing a cause of action in favor of an insured for an insurer's bad faith failure to settle. The Court reasoned that, to grant third party claimants a statutorily recognized cause of action in section B, while leaving insureds, to whom the insurer is bound to protect, only a jurisprudentially recognized cause of action, would be an absurd and inequitable result. As such, the Supreme Court found that La. R.S. 22:1973(A) represented a legislative recognition of a cause of action in favor of an insured found earlier only in the jurisprudence.

B. Whether an insurer can be liable to its insured for a bad faith failure to settle under La. R.S. 22:1973(A) in the absence of a "firm" settlement offer.

The Court then turned to the second part of the first certified question— whether the insurer was required to receive a "firm settlement offer" as a condition for an insured to recover for the insurer's bad faith failure to settle. The plain language of the statute states that the insurer has an "affirmative duty to adjust claims fairly and promptly and to make a reasonable effort to settle claims…". The Supreme Court noted that an "affirmative duty" requires taking positive action to comply with a legal standard. Following this language concerning the "affirmative duty", the statute contains two further steps to meet that duty; namely, to "adjust claims fairly and promptly" and also to make "a reasonable effort to settle claims". In particular, the Court acknowledged that the statue did not contain any language requiring a "firm settlement offer".

State Farm had argued that a prior decision, *Smith v. Audubon Ins. Co*., 95-2057, at 8 (La. 9/5/96), 679 So.2d 372, 376, enumerated a bright line rule that an insurer is not obligated to compromise just because the claimant offers to settle within the policy limits and its failure to do so is not by itself bad faith, as *Smith* listed several factors used for determining whether an insurer has acted in bad faith in deciding to proceed to trial rather than settle. These factors included (1) the probability of the insured's liability, (2) the extent of damages incurred by the claimant, (3) the amount of the policy limits, (4) the adequacy of the insurer's investigation, and (5) the openness of communications between the insurer and the insured. However, in addressing State Farm's reliance on *Smith*, the Supreme Court noted that *Smith* was decided before the enactment of La. R.S. 22:1220 (now La. R.S. 22:1973). The Supreme Court also noted that the legislature did not include the requirement of a "firm settlement offer" in the language of the statute when it was enacted. Further, the Supreme Court specified that the *Smith* Court did not even include the requirement of a "firm settlement offer" in the list of factors it used to determine bad faith. As such, the Supreme Court opined that to impose the requirement of a firm settlement offer in this case would amount to a rewriting of La. R.S. 22:1973(A).

Additionally, the Supreme Court found that practical considerations support the interpretation that a "firm" settlement offer is not necessary before an insurer can be found in bad faith for failing to settle. The insurer has assumed an obligation to protect the insured and the obligation to act in good faith should not be made subject to a tenuous possibility that an insurer will receive a firm settlement offer. The Supreme Court opined that the insurer's obligation to act in good faith is triggered by "knowledge of the particular situation, which knowledge 't[he] insurer has an affirmative duty' to gather during the claims process". *Kelly*, 2014-1921 at 11, citing La. R.S. 22:1973(A) and *Smith*, 95-2057 at

9-10, 679 So.2d at 377. The Court did find *Smith* instructive, and pointed out that the five factors enumerated in *Smith*, when used in a case by case determination, should adequately address the insurer's desire for clearly defined ways to measure whether an insurer has made a "reasonable effort to settle claims". Therefore, the Supreme Court found that an insurer may be held liable for a bad faith failure to settle claim under La. R.S. 22:1973(A), even if the insurer never received a "firm" settlement offer.

C. Whether an insurer can be liable under La. R.S. 22:1973(B)(1) for misrepresenting or failing to disclose pertinent facts that are not related to the insurance policy's coverage.

As to the second certified question— whether an insurer can be liable under La. R.S. 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to coverage— the Supreme Court concluded that an insurer can be found liable for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage. In its analysis, the Supreme Court found that "pertinent facts" are not restricted to facts "relating to any coverages".

The relevant language of La. R.S. 22:1973(B) prohibits "misrepresenting pertinent facts or insurance policy provisions relating to any coverages at issue". The Supreme Court reasoned that the interpretation of the statute hinged on the word "or". The appellate courts differed on their interpretation of the language of the statute. *Talton v. USAA Cas. Ins. Co*., 06-1513 (La. App. 4 Cir 3/19/08), 981 So.2d 696 and *Strong v. Farm Bureau Ins. Co*., 99-3362 (La. App. 2 Cir 10/29/99), 743 So.2d 949, held that a misrepresentation is limited to a misrepresentation that relates to a coverage issue, while *Arvie v. Safeway Ins. Co. of Louisiana*, 06-1266 (La. App. 3 Cir 2/07/07), 951 So.2d 1284 and *McGee v. Omni Ins. Co*., 02-1012 (La. App. 3 Cir. 3/15/03) 840 So.2d 1248 held that an actionable misrepresentation was not factually limited to dealing with a coverage issue. The Supreme Court took guidance from La. R.S. 1:9, which states:

> Unless it is otherwise clearly indicated by the context, whenever the term "or" is used in the Revised Statutes, it is used in the disjunctive and does not mean 'and/or'".

Relying on this precept of statutory interpretation, the Supreme Court held that an insurer can be liable for misrepresenting either: (1) "pertinent facts", or (2) "insurance policy provisions relating to any coverages at issue."

D. Conclusion

To answer the certified questions posed by the United States Court of Appeals for the Fifth Circuit, the Louisiana Supreme Court held that an insured has a cause of action for bad faith failure to settle under La. R.S. 22:1973(A). To that end, a firm settlement offer is *unnecessary* for an insured to sustain the cause of action against an insurer for a bad faith failure to settle because the insurer's duties can be triggered by information other than the fact that a settlement offer has been made. Such factors to be kept in mind by insurance companies when analyzing a duty to settle, other than receipt of any settlement offer, if applicable, are the probability of the insured's liability, the extent of damages incurred by the claimant, the amount of the policy limits, the adequacy of the insurer's investigation, and the openness of communications between the insurer and the insured.

Additionally, the Supreme Court found that La. R.S. 22:1973(B)(1) prohibits the misrepresentation of or failure to disclose "pertinent facts", without restriction to facts "relating to any coverages", effectively overruling *Talton, supra,* and *Strong, supra*.

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