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# The Impact of Kelly v. State Farm:

Clarifying the Insurer's Obligation to its Insured in Claims Involving Potential Liability in Excess of Policy Limits

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# **Duty of Good Faith**



## Specific Impact of Kelly v. State Farm

The information below is not intended to be an all-inclusive discussion of all aspects and nuances of the insurer's duty of good faith. Rather, what follows is exclusively focused on explaining those issues that were squarely addressed in *Kelly*, and how *Kelly* changes, or really clarifies, the interpretation of <u>two</u> subparts of La. R.S. 22:1973. Namely, the discussion in Kelly is focused on the insurer's affirmative duty to investigate and to make a reasonable effort to settle claims under La. R.S. 22:1973(A); and the insurer's duty to keep its insured informed of "pertinent facts" under La. R.S. 22:1973(B)(1). As illustrated above, these particular duties are a fraction of the big picture of the "duty of good faith and fair dealing" owed by insurers under Louisiana law.

## **Introduction**

On May 5, 2015, in *Kelly v. State Farm Fire & Cas. Co.*,<sup>1</sup> the Louisiana Supreme Court issued a significant ruling, opining on two previously unsettled issues of law in the context of bad faith claims. In short, the court held that (1) insurer can be found liable for bad faith even where a claimant has yet to make a firm settlement demand; and (2) require that the insurer convey all "pertinent facts" to its insured, regardless of whether such facts are related to "coverages at issue." These two holdings relate to two specific aspects of the broader duty of good faith owed by the insurer to its insured – namely, the affirmative duty to make a reasonable effort to settle claims, under La. R.S. 22:1973(A), and the duty to inform the insured, under La. R.S. 22:1973(B)(1). In general, these are statutory duties which exist in *all* cases, and which have existed since long before *Kelly*. But the statements and the holdings within supreme court's decision in *Kelly* basically clarify and arguably heighten these duties.

Perhaps most significantly, *Kelly* will cause a shift in the handling and decision making with respect to pre-trial resolution. In years past, it was widely accepted and assumed that an insurer was essentially insulated from bad faith liability where a claimant had yet to make a settlement demand. In this regard, insurers' approach to settlement could be described as "reactive." After *Kelly*, if insurers continue to take this sort of reactive approach, they will be doing so at their own risk. Instead, it will be advisable for insurers to be proactive in exploring settlement options. Separately, in light of *Kelly*'s second holding, insurers will need to increase efforts to keep the insured abreast of the status of the claim, and related progress with settlement or litigation, by timely communicating significant, case-specific developments.

In sum, in order to minimize potential bad faith exposure post-*Kelly*, insurers, adjusters and defense attorneys must develop and/or hone a practice of taking proactive steps (1) toward pretrial resolution of claims, and (2) engaging in regular, thorough communication with the insured concerning pertinent facts. For reasons explained more fully below, these practices will be of particular importance in those cases involving potential for a judgment in excess of the applicable policy limits. It is worth noting, however, that it is often difficult to predict, especially in the early stages of investigation, whether a claim will ultimately develop into one presenting a risk of excess judgment.

In addition to the duty to settle and the duty to inform, the insurer also owes a general duty to protect the insured's interest in all cases. Although an abundance of past Louisiana jurisprudence had already articulated and emphasized this point, it was strongly reiterated by *Kelly*. As the court explained, a liability insurer is the representative of its insured's interests, and therefore "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."<sup>2</sup> When statements such as this one are read in tandem with the *Kelly* court's holdings, there is no room to doubt that the impact of the case will be to essentially heighten the insurer's duties to make reasonable efforts to settle and to keep the insured informed. Conversely, the law now offers increased protection for the insured tortfeasor, who may be neither particularly savvy regarding, or simply not fully aware of, the potential risk of incurring personal liability for an excess judgment.

<sup>&</sup>lt;sup>1</sup> Kelly v. State Farm Fire & Cas. Co., 14-1921 (La. 5/5/15); \_\_\_\_ So.3d \_\_\_\_, 2015 WL 2082540.

<sup>&</sup>lt;sup>2</sup> Id. at \*8 (quoting Smith v. Audubon Ins. Co., 95-2057 (La. 9/5/96); 679 So.2d 372, 376) (emphasis added).

In ruling as it did, the supreme court created an incentive (or disincentive) to prompt the insurer to make the insured's interests a higher priority, to look after the insured's interests above of its own, and to take a more proactive approach to settlement and insured communications. As a consequence, insurers, adjusters and defense attorneys would be wise to take note of *Kelly* and tailor their practices accordingly. The information below provides an overview of the facts and issues presented in Kelly (Section I); a "before and after" look at the broad issues presented in Kelly to highlight how the case clarified the law in Louisiana (Section II); an expanded discussion of certain nuanced issues and issues left open-ended by the *Kelly* court's analysis (Section III); and some big-picture ideas and suggested practice tips that insurers, adjusters and defense attorneys should strongly consider implementing as a result of *Kelly* (Section IV).

#### \* \* \*

### I. Case Brief – Kelly v. State Farm<sup>3</sup>

#### A. Summary of Facts:

\*Note: In the "Law and Analysis" section of the Kelly opinion, minimal reference is made to the facts of this case, as the Louisiana Supreme Court was basically focused on answering certified legal questions presented. Thus, it is difficult to say whether the facts of this case are of particular significance in terms of providing guidance for insurers and adjusters. Nevertheless, we provide a brief summary of the facts for reference:

In November 2005, the plaintiff, Danny Kelly ("Kelly") sustained a fractured femur as a result of an auto-accident caused by the defendant-driver and State Farm insured, Henry Thomas ("Thomas"). State Farm's policy provided coverage with a \$25,000.00 limit.

In relation to the accident, both Kelly and a witness told police that Thomas failed to yield to oncoming traffic, but Thomas maintained he was not at fault. After the accident, Kelly was taken to the hospital, where he underwent surgery to repair his fractured femur and was hospitalized for six days. The related medical bills totaled \$26,803.17.

On January 6, 2006, Kelly's attorney sent a letter to State Farm, together with the hospital records. In the correspondence, Kelly's attorney explained he would be willing to recommend settlement to his client if State Farm would tender its policy limits, and he requested a response within ten days.<sup>4</sup> Initially, State Farm did not respond.

<sup>&</sup>lt;sup>3</sup> In lieu of citation references for each sentence in the Summary of Facts and Procedural History subsections, below, we note that, unless indicated otherwise, the information in these sections is drawn from the corresponding section in the supreme court's opinion. *See generally id.* at \*1-5.

<sup>&</sup>lt;sup>4</sup> *Id.* at \*2. The letter stated in full:

Please find enclosed a copy of Danny Kelly's Medical Summary with attached medical records/reports and bills concerning his hospital treatment for the above referenced incident involving your insured. I will recommend release of State Farm Insurance Company and your insured, Henry Thomas, Jr., for payment of your policy limits.

Please give me a call in the next ten (10) days to discuss this matter.

Two months later, State Farm made a \$25,000 settlement offer – its full policy limit. Kelly rejected the offer. On the same day that State Farm received notice of the rejection, it sent Thomas a letter which generally stated that 'it [wa]s possible" that the insured would bear personal liability and that State Farm would be agreeable if he chose to retain independent counsel.<sup>5</sup> Importantly, the letter did not mention anything about the January 2006 letter from Kelly's attorney, State Farm's offer to Kelly, or the amount of Kelly's medical bills.

### **B. Procedural History:**

The case proceeded to trial, where the Thomas was found liable and Kelly was awarded \$176,464.07, plus interest. State Farm paid its policy limit of \$25,000 to Kelly. This ostensibly left Thomas exposed for the remainder of the judgment – \$151,464.07, plus interest.

After trial, Thomas agreed to a compromise with Kelly. Thomas assigned his right to pursue a bad faith claim against State Farm to Kelly, and, in exchange, Kelly promised not to enforce the judgment against Thomas personally.

Subsequently, Kelly initiated a new suit, asserting Thomas's rights as an insured against State Farm. Specifically, Kelly alleged that State Farm was liable for (1) failing to negotiate a settlement in a timely, good faith manner ("Failure to Negotiate Claim"), and (2) failing to timely communicate sufficient details concerning the status of Kelly's claim and settlement negotiations to Thomas ("Failure to Inform Claim"). This new suit, originally filed in state court, was eventually removed to federal court, where the trial court later granted a Motion for Summary Judgment filed by State Farm seeking dismissal of both claims. In reaching its ruling, the district court reasoned that State Farm could not be held liable for bad faith because Kelly did not submit an "actual offer to settle."<sup>6</sup>

Kelly appealed to the Fifth Circuit, which reversed in part and affirmed in part. Both Kelly and State Farm both filed for a rehearing. On rehearing, the Fifth Circuit withdrew its earlier opinion; and, in doing so, it issued a new opinion which is an example of a rare circumstance in which a federal appellate court will "certify" a question of law to the Supreme Court of Louisiana for review - i.e., request that the supreme court issue an opinion concerning questions of Louisiana law with respect to which "there are no controlling precedents" in supreme court's prior

Id.

<sup>&</sup>lt;sup>5</sup> An excerpt of the content of the letter appears in a brief filed with the Louisiana Supreme Court. *See Brief for United Policy Holders, as Amicus Curiae* at 6-7, *Kelly v. State Farm*, 14-1921 (La. 5/5/15); \_\_\_\_\_ So.3d \_\_\_\_, 2015 WL 2082540. In pertinent part, the letter stated as follows:

Dear Mr. Thomas:

It is our duty to inform you that due to the circumstances surrounding the above accident, it is possible the injuries claimed against you may be in excess of the protection afforded by this policy. State Farm will do everything possible to protect you within those limits, however, you may be held personally responsible for any judgment above those limits.

In view of your personal liability, it will be agreeable with the company for you, if you so elect, to employ attorneys of your own choosing, at your own expense, to represent you personally in this matter. . . .

<sup>&</sup>lt;sup>6</sup> Kelly v. State Farm Fire & Cas. Co., 2012 WL 4498884, at \*3 (M.D. La. 2012).

decisions.<sup>7</sup> In this particular case, the federal court certified the following two questions to the supreme court:

### C. Issues Presented:

(1) Can an insurer be found liable for a bad-faith failure-to-settle claim under [La. R.S.] 22:1973(A) when the insurer never received a firm settlement offer?<sup>8</sup>

(2) Can an insurer be found liable under [La. R.S.] 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage?<sup>9</sup>

### D. Louisiana Supreme Court's Holdings:

(1) 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 to the insured can be triggered by information other than the mere fact that a third party has made a settlement offer;<sup>10</sup> and

(2) An insurer can be found liable under La. R.S. 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage because the statute prohibits the misrepresentation of "pertinent facts," without restriction to facts "relating to any coverages."<sup>11</sup>

### E. Brief Discussion of the Louisiana Supreme Court's Analysis:

In *Kelly*, **two** specific provisions of a much broader statutory scheme are put at issue and interpreted by the court. **The first**, La. R.S. 22:1973(A), relates to the general duties owed by an insurer to its insured. In particular, though, the discussion in *Kelly* hones in on the following underscored language within La. R.S. 22:1973(A), which states:

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.<sup>12</sup>

It is important to recall that the *insured's rights were at issue*. As illustrated by the court's opinion, this is significant because while the insured has a cause of action under La. R.S. 22:1973(A),<sup>13</sup> a third party claimant does not.<sup>14</sup> But, a third party can assert the insured's cause

<sup>9</sup> Id.

<sup>&</sup>lt;sup>7</sup> See La. Sup. Ct. R. XII.

<sup>&</sup>lt;sup>8</sup> *Kelly*, 2015 WL 2082540 at \*1.

<sup>&</sup>lt;sup>10</sup> *Kelly*, 2015 WL 2082540 at \*1 (emphasis added).

 $<sup>^{11}</sup>$  Id.

<sup>&</sup>lt;sup>12</sup> La. R.S. 22:1973(A)

<sup>&</sup>lt;sup>13</sup> See generally Kelly, 2015 WL 2082540 at \*5-8.

of action for Failure to Settle following an assignment of rights akin to the one that followed the judgment in the original personal injury action in *Kelly*. After drawing this distinction and explaining that the insured does have a cause of action for Failure to Settle under La. R.S. 22:1973(A),<sup>15</sup> the court further narrowed the first issue presented under this provision of the statute, as follows: "whether an insurer's affirmative duty to make a reasonable effort to settle claims is triggered only by receipt of a firm settlement offer."<sup>16</sup>

The court held 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."<sup>17</sup> In addition to this specific holding, the decision in *Kelly* is also significant for other guidance provided within the opinion regarding what actions an insurer must take in order to satisfy its "affirmative duty" to make a reasonable effort to settle claims with its insured. Specifically, the court explained that the term "affirmative duty" requires taking "positive action(s)" to comply with a legal standard – or, in this context, taking positive action(s) to make a reasonable effort to settle claims.<sup>18</sup> Thus, as explained in the Introduction section, above, the insurer must be proactive, not reactive, in its settlement efforts.

**The second** statutory provision, La. R.S. 22:1973(B)(1), is related to the insurer's duty to keep the insured informed. It provides as follows:

B. Any one of the following acts, if knowingly committed or performed by an insurer, constitutes a breach of the insurer's duties imposed in [La. R.S. 22:1973(A)]:

(1) Misrepresenting pertinent facts or insurance policy provisions relating to any coverages at issue.<sup>19</sup>

Prior to *Kelly*, conflicting appellate case law existed regarding whether an insurer could be found liable under La. R.S. 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage. While some courts had applied this statute as a prohibition of misrepresentation of "pertinent facts relating to any coverages at issue," others had found that the statute prohibited "misrepresentation of [any] pertinent facts" – i.e., regardless of whether those pertinent facts related to coverage.<sup>20</sup> The *Kelly* found favor with the latter approach, holding that the statute prohibits "misrepresentation of 'pertinent facts,' without restriction to facts 'relating to an coverages."<sup>21</sup>

<sup>&</sup>lt;sup>14</sup> See Kelly, 2015 WL 2082540 at \*6 (quoting *Theriot v. Midland Risk Ins. Co.*, 95-2895 (La. 1997); 694 So.2d 184 (holding that despite the language in the excerpted statute, a third party claimant has no cause of action under La. R.S. 22:1973(A)).

<sup>&</sup>lt;sup>15</sup> See generally Kelly, 2015 WL 2082540 at \*5-8.

<sup>&</sup>lt;sup>16</sup> Kelly, 2015 WL 2082540 at \*10.

<sup>&</sup>lt;sup>17</sup> Kelly, 2015 WL 2082540 at \*1.

<sup>&</sup>lt;sup>18</sup> *Kelly*, 2015 WL 2082540 at \*9.

<sup>&</sup>lt;sup>19</sup> La. R.S. 22:1973(B)(1).

<sup>&</sup>lt;sup>20</sup> *Kelly*, 2015 WL 2082540 at \*12 (citing *Talton*, 981 So.2d at 709–10; *Strong*, 743 So.2d at 953; *McGee*, 840 So.2d at 1256).

<sup>&</sup>lt;sup>21</sup> *Kelly*, 2015 WL 2082540 at \*13 (citations omitted).

As noted above, the Louisiana Supreme Court's opinion in *Kelly* did not make any specific factual findings about whether the insurer in that particular case, State Farm, breached the statutory duties at issue. Rather, the importance of *Kelly* is that it clarifies two issues of statutory interpretation, each of which relates to specific aspects of the insurer's duty of good faith.

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## II. A Before and After Look at the Issues in *Kelly*

Even though *Kelly* does not "change" the law *per se*, the case interpreted and clarified the law as applied to claims for (A) breach of the duty to engage in reasonable settlement efforts ("Failure to Settle Claims") under La. R.S. 22:1973(A); and (B) breach of the duty to keep an insured informed ("Failure to Inform Claims") under La. R.S. 22:1973(B)(1). In order to further illustrate the impact of the case, the following synopsis provides a "before and after" look at Louisiana law with respect to the broad issues presented in *Kelly* under these two statutes:

### A. Failure to Settle Claims – La. R.S. 22:1973(A)

The first statutory provision at issue in *Kelly*, La. R.S. 22:1973(A), relates to the general duties owed by an insurer. In particular, though, the discussion in *Kelly* hones in on the following underscored language within La. R.S. 22:1973(A), which states:

An insurer...owes to his insured a duty of good faith and fair dealing. The insurer has an <u>affirmative duty</u> to adjust claims fairly and promptly and <u>to make a</u> <u>reasonable effort to settle claims</u> 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.

### **Pre-Kelly:**

Before *Kelly*, it was widely presumed and widely accepted *in practice* that it was permissible to be reactive in settlement negotiations. Insurers, adjusters and attorneys often waited on the claimant to make the first move, or settlement demand. But, *Louisiana courts* had yet to squarely address the issue of whether an insurer could be liable for a Failure to Settle Claim in the absence of a settlement demand. Instead, Failure to Settle Claims were basically resolved in Louisiana jurisprudence on a case-by-case basis.

In fact, before the *Kelly* case made its way to the Louisiana Supreme Court, the district court initially granted summary judgment in favor of State Farm, finding that State Farm could not be liable for bad faith where the plaintiff did not submit an "actual offer to settle."<sup>22</sup> In the appellate opinion, on rehearing, the United States Fifth Circuit noted that the plaintiff in *Kelly* was unable to direct the court to "any Louisiana cases that find an insurer liable for bad-faith failure-to-settle in the absence of a firm settlement offer."<sup>23</sup> Again, perhaps as a consequence of the dearth of such cases, practicing attorneys, insurers, and adjusters routinely have, for years, operated under the assumption that the insurer was basically insulated from a bad faith liability in a Failure to

<sup>&</sup>lt;sup>22</sup> Kelly v. State Farm Fire & Cas. Co., 2012 WL 4498884, at \*3 (M.D. La. 2012).

<sup>&</sup>lt;sup>23</sup> Kelly v. State Farm Fire & Cas. Co., 582 Fed.Appx. 290, 296 (5th Cir. 2014), quoted in Kelly, 2015 WL 2082540 at \*4.

Settle Claim until receipt of a settlement demand. In this regard, *Kelly* marks a distinct shift in the law.

Even though the district court has yet to make a factual finding regarding whether State Farm is liable for Failure to Settle as of this date, the district court's prior ruling, granting summary judgment to State Farm, is certainly incorrect in light of the Louisiana Supreme Court's recent decision.

### **Post-Kelly:**

In its submission to the supreme court, State Farm argued that La. R.S. 22:1973(A) could only be breached "when an insurer unreasonably refuses an offer of settlement."<sup>24</sup> The *Kelly* court held that a settlement offer is *not* a prerequisite for an insured, or the insured's assignee, to successfully recover against the insurer on a bad faith in Failure to Settle Claim. Rather, the court explained that the issue of whether an insurer is in bad faith depends upon the insurer's "knowledge of the particular situation."<sup>25</sup> As the court explained, "we see 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. Instead, *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."<sup>26</sup>* 

As has long been the case, the court reiterated that the question of whether an insurer has made "a reasonable effort to settle claims" is a *case-by-case determination*.<sup>27</sup> In particular, when evaluating the issue of bad faith in the context of an insurer's decision to proceed to trial as opposed to pursuing settlement, the following five factors will be weighed by courts applying Louisiana law:

- 1. The probability of the insured's liability.
- 2. The extent of the damages incurred by the claimant.
- 3. The amount of the policy limits.
- 4. The adequacy of the insurer's investigation.
- 5. The openness of communications between the insurer and the insured. $^{28}$

The foregoing factors, however, are not an exhaustive list, but rather are illustrative of a "totality of the circumstances" analysis that courts will utilize when evaluating Failure to Settle Claims.

As alluded to above, insurers who continue to take the reactive approach to investigation and settlement efforts, as many have in years past, will be exposed to a significant risk post-*Kelly*. Indeed, the supreme court placed an overwhelming emphasis on the statutory language which provides that the duty to engage in reasonable settlement efforts is an "*affirmative duty*" – meaning the insurer must take "*positive action(s)*" to comply with the legal standard.<sup>29</sup> Basically,

<sup>&</sup>lt;sup>24</sup> *Kelly*, 2015 WL 2082540 at \*9.

<sup>&</sup>lt;sup>25</sup> *Kelly*, 2015 WL 2082540 at \*11.

<sup>&</sup>lt;sup>26</sup> *Kelly*, 2015 WL 2082540 at \*11 (emphasis added).

<sup>&</sup>lt;sup>27</sup> *Kelly*, 2015 WL 2082540 at \*10.

<sup>&</sup>lt;sup>28</sup> See Kelly, 2015 WL 2082540 at \*10 (quoting Smith, 679 So.2d at 377).

<sup>&</sup>lt;sup>29</sup> Kelly, 2015 WL 2082540 at \*10 (emphasis added).

this means that *the insurer should be proactive*, not reactive, in investigating and evaluating reasonable settlement options.

The net effect of this ruling is that the tide has turned, at least to some degree, in favor of the insured, or the insured's assignee. In particular, it is reasonable to anticipate that following *Kelly*, in those cases which result in excess judgment at trial, plaintiff's attorneys will increasingly seek an assignment of rights from the insured and then proceed to attack those insurers who fail to take a proactive approach to the settlement process. Further, it would not be surprising to see such tactics specifically employed in cases involving large damages, and low-limit policies.

\* \* \*

### B. Failure to Inform Claims – La. R.S. 22:1973(B)(1)

The second statutory provision at issue in *Kelly*, La. R.S. 22:1973(B)(1), under which an insurer may be held liable for "misrepresentation." The statute provides as follows:

B. Any one of the following acts, if knowingly committed or performed by an insurer, constitutes a breach of the insurer's duties imposed in [La. R.S. 22:1973(A)]:

(1) <u>Misrepresenting pertinent facts</u> or insurance policy provisions relating to any coverages at issue.

### Pre-Kelly:

Before *Kelly*, there was a split in Louisiana appellate decisions regarding the proper interpretation of La. R.S. 22:1973(B)(1). Some decisions had ruled that a misrepresentation was only actionable if it related to a "coverage issue" (i.e., facts about the policy itself, such as extent or amount of coverage, lapse or expiration of the policy, or exclusions from coverage).<sup>30</sup> Other Louisiana appellate decisions had ruled that an insurer could be held liable for misrepresentation of any "pertinent" fact, even a misrepresentation of a pertinent fact unrelated to coverage. For instance, in one pre-*Kelly* decision involving evaluation of an insurer's communications regarding facts related to settlement progress, Louisiana's Third Circuit, in *McGee v. Omni Ins. Co.*,<sup>31</sup> held that "[m]isrepresentation can occur when an insurer either makes untrue statements to an insured concerning pertinent facts or fails to divulge pertinent facts to the insured."<sup>32</sup> In light of this split in the appellate jurisprudence, the Fifth Circuit called upon the Louisiana Supreme Court for clarification. As explained below, the *Kelly* court found favor with *McGee*'s interpretation of La. R.S. 22:1973(B)(1).

**Post-Kelly:** 

<sup>&</sup>lt;sup>30</sup> *Kelly*, 2015 WL 2082540 at \*12 (citing *Talton v. USAA Cas. Ins. Co.*, 06–1513 (La. App. 4 Cir. 3/19/08), 981 So.2d 696, 709–10; *Strong v. Farm Bureau Ins. Co.*, 32,414 (La. App. 2 Cir. 10/29/99), 743 So.2d 949, 953).

<sup>&</sup>lt;sup>31</sup> McGee v. Omni Ins. Co., 02–1012 (La. App. 3 Cir. 3/15/03), 840 So.2d 1248, 1253-56.

<sup>&</sup>lt;sup>32</sup> *Kelly*, 2015 WL 2082540 at \*12 (quoting *McGee*, 840 So.2d at 1256).

As a precursory matter, *Kelly*'s discussion of the meaning of "misrepresentation" is noteworthy, as it is not only limited false statements. An insurer's omissions will also be considered. Simply put, based on *Kelly*, the term "misrepresentation" encompasses when an insurer either "states an untruth" or "fails to state the truth."<sup>33</sup>

Turning more directly to the focal point of the *Kelly* court's analysis, the supreme court interpreted the statutory language at issue and declared that an insurer can be found liable for misrepresentation of any "pertinent facts." Thus, in the context of a Failure to Inform Claim under La. R.S. 22:1973(B)(1), the law in Louisiana post-*Kelly* is as follows:

[A]n insurer can be liable for misrepresenting either: (1) "pertinent facts," *or* (2) "insurance policy provisions relating to any coverages at issue."<sup>34</sup>

The second of these two points is not a change in the law and was not an issue in *Kelly*. Rather, the holding in *Kelly* is focused on the first point, which is that the first clause of La. R.S. 22:1973(B)(1) prohibits misrepresentation of any and all "pertinent facts," period – i.e., regardless of whether those facts are related to "coverages at issue."

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### **III.** Further Analysis of Subordinate Issues in *Kelly*: Expanding on the Nuanced Issues in Failure to Settle Claims and Failure to Inform Claims

Although the *Kelly* court did articulate two clear holdings, some subordinate issues were left open-ended by the court. Complicating matters, the court also emphasized the premise that bad faith claims are fact sensitive and thus must be analyzed on a case-by-case basis. Because of this, the importance of certain nuanced issues discussed in *Kelly* may become magnified in some cases more than others, depending on the circumstances.

In recognition of the fact that *Kelly* did not paint particularly bright line rules with respect to certain issues presented in the context of Failure to Settle Claims and Failure to Inform Claims, respectively, the following outline delves into a more detailed discussion of particularly important points. And, where *Kelly* is silent or left questions openended, the authors have attempted to clarify certain issues based on related case law and/or the authors' own independent analysis.

### A. Failure to Settle Claims – La. R.S. 22:1973(A)

- Emphasis on "Affirmative" Nature of Duty to Engage in Settlement Efforts. The *Kelly* opinion repeatedly emphasizes the statutory language stating that an insurer has an "*affirmative duty*" to make a reasonable effort to settle claims.
  - As the court explained, "an affirmative duty *requires taking <u>positive action(s)</u> to comply with a legal standard*."<sup>35</sup>

<sup>&</sup>lt;sup>33</sup> *Kelly*, 2015 WL 2082540 at \*11 (citing BLACK'S LAW DICTIONARY (6th ed. 1990) ("**Misrepresentation**. Any manifestation by words or other conduct by one person to another that, under the circumstances, amounts to an assertion not in accordance with the facts.")) (emphasis original).

<sup>&</sup>lt;sup>34</sup> Kelly, 2015 WL 2082540 at \*13 (citations omitted).

<sup>&</sup>lt;sup>35</sup> *Kelly*, 2015 WL 2082540 at \*10.

- Lower courts will likely interpret *Kelly*'s emphasis on the *affirmative* nature of the insurer's duty as an instruction to apply more rigorous scrutiny to an insurer's efforts in the settlement process, and/or the decision to forgo settlement efforts and proceed to trial.
- Beware if Attempting to Apply *Kelly* and its Progeny by Analogy. Unfortunately for insurers, adjusters and attorneys, the supreme court repeatedly emphasized that the issues presented in *Kelly* are both particularly fact sensitive. Thus, when considering potential exposure in cases involving risk of liability for Failure to Settle Claims and/or Failure to Inform Claims, each claim will need to be evaluated on a case-by-case basis in order to determine the appropriate course of action.
  - As noted above, the supreme court expressly stated in *Kelly* that it was not making findings of fact as to whether the insurer breached either of the two statutory provisions at issue. And, even if the court had, it seems that it may be unwise to review the facts and attempt to draw analogies when analyzing similar issues of bad faith in other cases.
  - As explained in *Kelly*, Failure to Settle Claims involve a "case-by-case" analysis, and a non-exhaustive five factor analysis. Thus, it is certainly conceivable that in future cases, Louisiana courts may consider other facts and circumstances in addition to the five factors, which are excerpted here again for the convenience of the reader:
    - 1) The probability of the insured's liability.
    - 2) The extent of the damages incurred by the claimant.
    - 3) The amount of the policy limits.
    - 4) The adequacy of the insurer's investigation.
    - 5) The openness of communications between the insurer and the insured.
  - Again, these five factors are not new and, in fact, they date back to a 1996 decision by the Louisiana Supreme Court *Smith v. Audubon Ins. Co.*<sup>36</sup>

<sup>&</sup>lt;sup>36</sup> See Smith v. Audubon Ins. Co., 95-2057 (La. 9/5/96); 679 So.2d 372, 377. The fact that the *Kelly* court extensively cited *Smith* with approval is noteworthy, as the Louisiana Supreme Court's opinion in *Smith* provides a general explanation of when an insurer's decision to litigate would be considered reasonable. In doing so, the *Smith* court explained in pertinent part:

<sup>[</sup>T]he determination of whether the insurer acted in bad faith turns on the facts and circumstances of each case. Of course, an insurer is not obliged to compromise litigation just because the claimant offers to settle a claim for serious injuries within the policy limits, and its failure to do so is not by itself proof of bad faith. The determination of good or bad faith in an insurer's deciding to proceed to trial involves the weighing of such factors, among others, as the probability of the insured's liability, the extent of the 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. *Nevertheless, when an insurer has made a thorough investigation and the evidence developed in the investigation is such that reasonable minds could differ over the liability of the insured, the insurer has the right to choose to litigate the claim, unless other factors, such as a vast difference between the policy limits and the insured's total exposure, dictate a decision to settle the claim.* 

- When considering the legal question of whether an insurer can be held liable for Failure to Settle absent a settlement demand, the *Kelly* court stressed that whether the claimant has made a "firm settlement offer" is *not* one of the factors above.
- In practice, based on *Kelly*'s holding, it is advisable for insurers, adjusters and attorneys to routinely reevaluate a claimant's chances of success on liability, and the potential for an excess judgment.
- "Reasonableness" of Settlement Efforts. Basically, the question of whether the insurer acted "reasonably" will be answered by courts based on (1) an evaluation of the extent of the insurer's investigation efforts, and (2) an evaluation of liability and damages in light of the knowledge that an insurer had at particular point(s) in time. Since what is "reasonable" is inherently dependent on the circumstances of each case, we note the following points of discussion in *Kelly* provide some additional insight.
  - Footnote 28 within the *Kelly* opinion, wherein the court cited with approval and excerpted the following quote from a well-respected legal treatise on Louisiana insurance law, is noteworthy because it seems to provide some additional guidance regarding "reasonableness" vis-à-vis settlement evaluation:

Anyone involved in handling claims quickly learns that the evaluation of liability and amount of damages is not an exact science, and reasonable professional judgment may vary (substantially in larger claims) on where to draw the line in settlement negotiations. It is suggested that the insurance company should disregard its policy limits in evaluating the reasonableness of a settlement offer. The insurer should not be motivated by how much it stands to gain or lose, thus disregarding the insured's exposure. Instead, the insurance company should analyze the claim from the viewpoint of how much it would be willing to pay in settlement of the case if its policy limits. On the other hand, if the insurer reasonable settlement up to its policy limits. On the claim, then it should not be required to pay more simply because the insured has purchased inadequate insurance protection.<sup>37</sup>

- Also, *Kelly* reiterated the principle that "*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."<sup>38</sup>
- When an insurer is considering the appropriate course of action to satisfy its duty to engage in reasonable in settlement efforts, the insured's interests and the points made in the excerpted language from Footnote 28, above, should be considered in conjunction with the five factor test from *Smith v. Audubon Ins. Co.*

Id. (emphasis added).

<sup>&</sup>lt;sup>37</sup> *Kelly*, 2015 WL 2082540 at n. 28 (citation omitted) (emphasis added).

<sup>&</sup>lt;sup>38</sup> Kelly, 2015 WL 2082540 at \*8 (citing Smith, 679 So.2d at 376).

#### \* \* \*

#### B. Failure to Inform Claims – La. R.S. 22:1973(B)(1)

- **Expanding on Duty to Inform & Which Facts are "Pertinent".** Although the *Kelly* decision does not provide particularly clear guidance regarding which facts are pertinent, we have attempted to glean some general guidance from *Kelly* and the decisions cited by the supreme court with approval therein.
  - *Kelly* expressly declined to clearly identify which facts will be considered "pertinent," stating as follows: "it is important to recall that the merits of this case are not before this court to decide. ... For these reasons, we do not purport to decide whether State Farm's letter to Thomas addressed all facts that were "pertinent" within the meaning of La. R.S. 22:1973(B), let alone delineate every situation for which an insurer is required to disclose pertinent facts."<sup>39</sup>
  - Despite *Kelly*'s failure to define "pertinent" facts, the following general guidelines seem applicable:
    - As explained in further detail in Section IV, below, insurers should communicate with the insured regarding: facts which have a significant impact on the evaluation of liability or damages; major developments regarding the status of a claim and related litigation or settlement negotiations, if any; and the likelihood *and extent* of the potential risk of liability for an excess judgment.
    - If there is a significant risk of excess judgment and the insurer merely communicates that the insured "might" face personal liability and has a right to independent counsel, the insurer will likely be subject to exposure for a bad faith claim.<sup>40</sup>

\* \* \*

### C. Apparent Attempt to Avoid Opening the Flood Gates for Bad Faith Claims

• Qualifying Language in *Kelly*. Notably, the supreme court incorporated some language which seems to be an effort to restrict an anticipated increase in bad faith claims following Kelly. In doing so, it seems that the court perhaps anticipated potential litigation involving arguments about which facts are "pertinent" and whether they were adequately communicated, and/or what an insurer must do to take an "affirmative" step when making a reasonable effort to settle claims. This qualifying language, which

<sup>&</sup>lt;sup>39</sup> Kelly, 2015 WL 2082540 at n. 31.

<sup>&</sup>lt;sup>40</sup> See McGee, 840 So.2d at 1253-56 (finding insurer in bad faith for failure to inform insured of pertinent facts where insurer did not advise the insured that "she would likely be found liable for causing accident and that an excess judgment was likely to be rendered against her. [Further,] she was never told that the medical expenses and lost wage claims alone...exceeded her policy limits....").

appears in a lengthy footnote incorporated into the discussion of the Failure to Inform Claim in *Kelly*,<sup>41</sup> captures the following points:

- The court recognized that "*tight reigns* must be kept on a cause of action for insurer settlement practices."<sup>42</sup> Further illustrating this point, the court excerpted the following quote from a case which pre-dates the enactment of La. R.S. 22:1973(B)(1): "We are not saying that mere poor judgment is the basis of an award for bad faith failure to settle within policy limits....*the law of bad faith should be cautiously applied*...."<sup>43</sup>
- The court also reiterated the well-established principle that La. R.S. 22:1973 should be strictly construed, and went on to explain that "[a] strict application of the statute does not contemplate gamesmanship" e.g., unrealistic offers "presented through 'carefully ambiguous demands coupled with sudden-death timetables' in order to 'set up' the insurer for an excess liability judgment."<sup>44</sup>
- **Potential Claims Despite Qualifying Language.** Despite the above-referenced language included in *Kelly*, and even though the court strongly emphasized that La. R.S. 22:1973 should be strictly construed, it is reasonable to anticipate that *Kelly* will trigger experimental claims by plaintiff's attorneys alleging misrepresentation of allegedly "pertinent" facts and/or failure to take "positive" action(s) toward settlement.
  - Generally, it would not be surprising to find that some claimant's are more willing to proceed to trial in light of the prospect of a post-judgment assignment of the insured's right to assert bad faith claims against the insurer.
  - Adjusters and attorneys should beware that attorneys representing some claimants may have this tactic in mind from the inception of the claim.
  - From the insurer's perspective, the risks associated with such tactics seem particularly likely to come to fruition in cases involving potential damages awards substantially exceeding relatively low policy limits.

### **IV. Key Takeaways & Suggested Action Steps:** What is the Practical Impact of *Kelly* on Claims Handling?

\* \* \*

By contrast to the information in the sections above, the focal point of which is to explain how *Kelly* impacts the body of law related to potential bad faith liability, the following outline is intended to highlight *Kelly*'s practical impact, or likely practical impact, for insurers. In other words, the information below is intended to answer the following question: How does the law, as applied in *Kelly*, impact the day-to-day handling and evaluation of claims?

<sup>&</sup>lt;sup>41</sup> *Kelly*, 2015 WL 2082540 at n. 32.

<sup>&</sup>lt;sup>42</sup> *Kelly*, 2015 WL 2082540 at n. 32.

<sup>&</sup>lt;sup>43</sup> Kelly, 2015 WL 2082540 at n. 32 (citing Keith v. Comco Ins. Co., 574 So.2d 1270, 1279-80 (La. App. 2 Cir. 1991); Moskau v. Insurance Co. of North America, 366 So.2d 1004 (La. App. 1 Cir. 1978)).

<sup>&</sup>lt;sup>44</sup> *Id.* (citation omitted).

Although it would be impossible to provide an all-inclusive response to this question given the fact sensitive nature of bad faith claims, what follows is intended to provide a big-picture ideas regarding suggested action steps and general issues and topics to keep in mind when deciding what the appropriate course of action is from one case to the next.

- A Settlement Demand is Not a Prerequisite for Bad Faith Liability. Technically, the *Kelly* court's ruling on the Failure to Settle issue does not change the law as much as it clarifies and arguably heightens the insurer's duties in the settlement process. Since *Kelly* held that an insurer can be found liable for bad faith Failure to Settle in the absence of a settlement demand, *insurers may, in certain cases, need to make the first move in settlement negotiations.* 
  - In the course of the claims handling and investigation process, insurers and claims handlers can no longer hope to avoid potential bad faith liability in the absence of a settlement demand.
- **Be Proactive, Not Reactive.** Prudent insurers will be more *proactive* in both the investigation, settlement efforts, and communication with the insured.
  - Before *Kelly*, it was widely assumed that an insurer could not be liable for Failure to Settle where the claimant had yet to make a settlement demand. So, in practice, many *insurers were reactive* rather than proactive with respect to settlement efforts. This general approach is no longer advisable.
  - Considering *Kelly*'s clear holding that a settlement demand is not a prerequisite for bad faith liability, it will be necessary to take "affirmative" i.e., proactive actions in investigation process and to periodically evaluate (or revaluate) settlement prospects in order to consider the appropriate course of action with respect to settlement efforts.
  - In general, where a claimant has yet to make a settlement demand and the insurer discovers facts during its investigation of a claim reasonably indicating that the insured would likely be subjected to personal liability for excess exposure if the case proceeded to trial, the insurer should timely:
    - (1) Communicate all pertinent facts to avoid exposure to a Failure to Inform Claim; and
    - (2) Take positive action(s) to make a reasonable effort to settle, and perhaps even make the first offer in settlement negotiations, in order to avoid exposure to a Failure to Settle Claim.
    - It is also advisable that the communication to the insured should request the insured's input regarding settlement strategy. Although this is not a requirement of Louisiana law, nor was it directly discussed in *Kelly*, the insurer's failure to seek the insured's input on a settlement decision will likely weighed as a fact which favors a finding that the insurer was in bad

faith.<sup>45</sup> Thus, this practical suggestion is incorporated into the outline here because of its relation to the insurer's general duty to consider the insured's interests ahead of its own self-interests.

- Again, in certain instances, it will be necessary for the insurer to extend the first settlement offer in order to avoid liability for breach of the duty to engage in a reasonable effort to settle claims.
- In some cases, as an alternative to making an outright settlement offer where a claimant has yet to make a settlement demand, it seems plausible that an insurer may be able to satisfy its duty to take such affirmative action(s) by eliciting or attempting to elicit a settlement demand from the claimant.
- Additionally, and this cannot be overstated, significant developments in the claims handling process especially the insurer's proactive, affirmative actions with respect to fact investigation and settlement efforts should be *well documented* in the claims file. The same is true with respect to insured communications related to these and other "pertinent facts".
- **Duty to Investigate.** In addition to emphasizing the duty to engage in reasonable settlement efforts, the court emphasized the correlative duty to investigate.
  - As the court explained, when determining whether to litigate or settle, "an insurer has a *duty to conduct a thorough investigation <u>and</u> to consider the evidence developed in the investigation."<sup>46</sup>*
  - Given the *Kelly* court's emphasis on the affirmative duty to investigate and to engage in reasonable settlement efforts, it is now more important than before to periodically reevaluate resolution strategy when significant developments arise during the investigation process.
- Importance of Analyzing Risk from Insured's Perspective. When there is a Failure to Settle Claim akin to the one made in *Kelly*, the key question for the court will be whether the insurer acted reasonably in light of the risk posed to the insured's interests. Accordingly, the court will engage in a fact-finding effort regarding the extent of the insurer's knowledge at a particular point in time, and a related evaluation of insured's risk based on such knowledge. As a result, adjusters and attorneys, whose actions may be put at issue in bad faith claims, should consider the following:
  - $\circ\,$  The insurer has an affirmative obligation to gather knowledge during the investigation process.

<sup>&</sup>lt;sup>45</sup> See Arvie v. Safeway Ins. Co. of Louisiana, 06-1266 (La. App. 3 Cir. 2/07/07), 951 So.2d 1284, 1286 (listing fact that the insurer failed to solicit insured's input as one of several facts which supported the Third Circuit's decision to affirm the trial court's finding of bad faith liability in the context of Failure to Inform Claim).

<sup>&</sup>lt;sup>46</sup> Kelly, 2015 WL 2082540 at \*11 (citing Smith, 679 So.2d at 376) (internal quotation marks omitted) (emphasis added).

- With that knowledge, the insurer must evaluate liability and damages, and then consider the extent of the potential risk that the insured could be cast in judgment for the amount exceeding policy limits. In other words, the insurer must bear the facts of the case in mind and:
  - (1) Evaluate (a) the plaintiff's likelihood of success in establishing liability; (b) the potential range of damages (i.e., verdict potential), and (c) other factors which can reasonably be anticipated to impact outcome of the suit, including credibility issues, venue considerations, etc.
    - Then, if it is determined that there is potential for an excess judgment:
  - (2) Assess whether the choice to litigate rather than settle would expose the insured to a significant risk of incurring personal liability for an excess judgment.
- If the insured's interests are significantly exposed, the insurer must take "positive" action(s) to engage in reasonable settlement efforts in order to avoid liability under La. R.S. 22:1973(A), as interpreted by *Kelly*.
- It is plausible that a court might find that insured's interests were significantly at risk even where (1) there is high risk of a judgment which merely exceeds the policy limit by a nominal amount; or (2) there is a low-to-moderate risk of an judgment which substantially exceeds the policy limit.
- **Document Communications to Insured.** Since *Kelly* held that an insurer has a duty to inform the insured of any and all "pertinent facts," all insured communication should be well-documented because of its potential evidentiary value.
  - In all cases, and especially when there is a possibility of an excess judgment, it would be a prudent course of action to (a) keep the insured abreast of any and all "pertinent facts," and (b) document all such communication so as to compile evidence in case of a bad faith claim.
- Advisable Method, Extent and Nature of Communication. In addition to documenting insured communication, an insurer should regularly and thoroughly communicate "pertinent facts" and all such communication should be carefully drafted, as it may be subject to production in cases involving bad faith claims like those in *Kelly*.
  - In order to manage insured communication, it is generally suggested that insurers should determine who will be the point of contact with the insured for a particular claim. In claims involving litigation, the point of contact could be the TPA, claim adjuster, or claim counsel.
  - Prudent insurers will communicate early and often in cases where there is a risk of excess liability.

- Based on *Kelly* and other cases cited with approval therein, sending a form letter without any specifics regarding the claim/case will likely not be treated favorably by Louisiana courts.
- Instead of a form letter, prudent insurers will consistently communicate "the status of the claim to [the insured] on a regular basis," and, in doing so, will timely communicate "the pertinent facts necessary for [the insured] to consider determining what [i]s in [his or] her personal interest."<sup>47</sup>
- When the information gathered through the insurer's investigation indicates that the insured is at risk of an excess judgment, the safe course of action is to timely prepare and send a detailed letter, sometimes called an "excess letter," to the insured. In light of *Kelly*'s holding that Louisiana law requires all "pertinent facts" be communicated to the insured, such an excess letter should be detailed and carefully drafted in the future. The following details are examples of what the court might consider to be "pertinent facts":
  - (1) A description of the extent and nature of the applicable policy limit(s).
  - (2) Significant details regarding the underlying incident and the status of the claims investigation, including a carefully written, detailed explanation of significant details regarding the claimant's alleged damages and chances of establishing liability.
  - (3) Thorough details regarding status, extent and nature of settlement demands, settlement discussions, opportunities to settle and/or settlement efforts, if any, and also regarding litigation, if any.
    - If the claimant has made a settlement demand, or indicated a willingness to settle within policy limits, that should be clearly stated.
  - (4) Projected settlement range, verdict potential, and the projected range of a potential liability for insured in the event of an excess judgment.
  - (5) If, based on the projected verdict potential and policy limit, there
    is a significant chance that the insured could be held personally liable
    for a judgment, the insured should be put on notice of that fact. This
    includes an explanation regarding the extent and likelihood of
    potential personal liability for the insured.
  - (6) Depending on the case, when explaining the rationale related to settlement valuation, likely verdict range and/or chances of personal liability for the insured, the following factors may also noteworthy:

<sup>&</sup>lt;sup>47</sup> *McGee*, 840 So.2d at 1256.

- Issues of comparative fault that would reduce the projected award of damages, if any;
- Witness credibility issues or conflicting testimony, if any;
- Evidence of malingering or pre-existing medical conditions which could limit the amount recovered by the claimant, if any;
- Anticipated difficulties in pre-trial resolution, including, for example, any reason to expect that the claimant's attorney will be unwilling to reduce an unreasonable settlement demand;
- Details concerning the insurer's prior payments in relation to the claimant's alleged loss;
- Identification and explanation of any other insurance policies which are applicable (and thus may, either directly or indirectly, impact the insured's interest in avoiding personal liability);
- Venue considerations, especially if the venue is particularly liberal or conservative.
- In addition to the foregoing, when preparing an excess letter, the insurer should also advise the insured of its right to obtain separate counsel to protect its interests. Further, the insurer should also expressly inquire into (1) the existence and extent of a policy of excess insurance which might provide coverage for the claim, and (2) the insured's input regarding settlement strategy in written correspondence. Although these are not "pertinent facts," we note these practical points here given their relation to the topic at hand, and also because of the *Kelly* court's general emphasis on the insurer's duty to protect the insured's interests.
- $\circ$  In the short term and until the law is further developed through decisions by Louisiana's intermediate courts on which facts are "pertinent," the best practice post-*Kelly* is to err on the side of being overinclusive regarding insured communications.
- To Litigate or To Settle? How to Handle Close Calls. In borderline cases, where there is a risk of liability and excess judgment, but neither are substantially certain, insurers will be confronted with a difficult decision of whether to litigate or engage in settlement efforts.
  - Some Generally Suggested Guidelines –

- The decision to litigate or settle must be made on a case-by-case basis. This is because of the fact sensitive nature of bad-faith cases in general, and particularly because of the lack of guidance regarding which facts are "pertinent" and thus need to be communicated to the insured.
- If an insurer believes that there is a reasonable basis for choosing to litigate, that should be thoroughly detailed in correspondence to the insured. The same correspondence should also explain, among the other things listed above, the potential risk of excess judgment and projected settlement value of the case.
- Specific Factors to Weigh
  - In addition to any and all factors that an insurer would ordinarily consider, the five factors enumerated in *Smith*, and reiterated in *Kelly* are worthy of consideration (*see* Section III.A., above).
  - In addition to those five factors, it is also clear that the insured's interests must be weighed heavily, and must be prioritized ahead of the insurer's own self-interest. This point is expanded upon immediately below.
- Importance of Considering Insured's Interest
  - An insurer does not necessarily need to settle any and all cases involving potential risk that the insured will be liable for an excess judgment.
  - But, it should be noted in Kelly, the Louisiana Supreme Court emphasized its past cases standing for the proposition that, in "every case, the insurance company is held to a high fiduciary duty to discharge its policy obligations to its insured in good faith-including the duty to defend the insured against covered claims and to consider the interests of the insured in every settlement."<sup>48</sup>
  - Considering the focus on protecting the insured's interest, if there is a substantial risk from the insured's perspective in a particular case, it could be necessary to increase settlement authority above what the case may otherwise seem to warrant based on all other factors. Put another way, there could be value in minimizing the insured's risk of incurring personal liability for an excess judgment where that risk is substantial.
  - On the other hand, in cases where the risk to the insured's interest is only minor, and/or significant questions exist with respect to liability, damages, or both, it may be perfectly reasonable for the insurer to choose to litigate especially where the plaintiff is unwilling to be reasonable in settlement negotiations.

<sup>&</sup>lt;sup>48</sup> See Kelly, 2015 WL 2082540 at \*11 (citing Pareti v. Sentry Indem. Co., 536 So.2d 417, 423 (La.1988); Holtzclaw v. Falco, Inc., 355 So.2d 1279 (La.1978)).

As a general rule of thumb, insurers would be well served take a proactive approach *in all cases* with respect to settlement efforts and insured communications, as detailed above. That said, the cases most directly impacted by *Kelly* are those where it is *substantially certain* that a claimant will be able to *establish liability <u>and</u> recover an excess judgment* at trial. Specifically, the insurer can no longer wait on the claimant to make a settlement demand; and, unless the insurer takes reasonable, positive action(s) attempting to resolve the case up to the policy limits, it will be exposed to Failure to Settle Claims as a consequence of *Kelly*. Thus, the insurer should be proactive and thorough in investigation, settlement evaluation and negotiation, and communication of pertinent facts to the insured – and, as a practical matter, it would be wise to take a similarly proactive approach to documenting all such action in the claims file. Also, it should be noted that the *Kelly* opinion makes it abundantly clear that an insurer's refusal to settle will be considered unreasonable if the only justification is the insurer's own self-interest in saving money. Therefore, insurers should proceed with increased caution where the decision to forgo pre-trial resolution efforts would essentially involve taking a "gamble" with the insured's interest in avoiding personal liability for a judgment in excess of policy limits.

At the other end of the spectrum, in those cases in which there is little to no risk of an excess judgment, the ruling in *Kelly* will have virtually no practical consequences. This should be understood with a caveat, however, as there will be some cases in which the risk of potential for excess judgment only becomes substantially certain after extensive development in the investigation process.

Then there will be borderline cases, which may or may not involve any one or more of the following: (1) serious questions with respect to the claimant's theory of liability; (2) pre-existing medical conditions, or other facts and circumstances clouding the evaluation of damages; and (3) credibility issues and/or conflicting testimony which complicate the evaluation of liability, damages, or both. In such borderline cases, it will be important for insurers and adjusters to work closely with counsel when developing and making decisions related to resolution strategy and also regarding which pieces of information should be communicated to the insured.

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If you have any questions about the opinions or information above, please feel free to contact:

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