

***KELLY V. STATE FARM FIRE & CASUALTY  
COMPANY: PRACTICAL EFFECTS  
RESULTING FROM AN EXPANSION OF  
INSURERS' BROAD GOOD-FAITH DUTY***

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## I. INTRODUCTION

In *Kelly v. State Farm Fire & Casualty Co.*, the Louisiana Supreme Court examined an insurer’s statutory duty to adjust an insurance claim in good faith.<sup>1</sup> The court settled disputes regarding two issues: (1) whether an insurer can be found liable for a bad-faith failure-to-settle claim when the insurer never receives a firm settlement offer and (2) whether an insurer can be found liable for failure to disclose facts unrelated to the insurance policy’s coverage.<sup>2</sup> After a careful review of the relevant statutes and case law, the Louisiana Supreme Court answered both questions affirmatively.<sup>3</sup>

While the court’s decision in *Kelly* clearly seeks to protect insureds by expanding insurers’ good-faith duty, the decision has the potential to lead to disquieting practical effects on insurance-related litigation in Louisiana. Specifically, the decision expands the duty of insurers by placing an affirmative duty on them to make reasonable efforts to evaluate and attempt to settle from the outset of the claim. Moreover, insurers are left with little guidance as to what information they are obligated to present to the insured. This lack of guidance is likely to result in the transmittal of unnecessary information, which in turn is likely to directly result in increased costs of litigation. The loss of profits which accompanies increased litigation costs is likely to be offset by an increase in insurance premiums for Louisiana insureds.

The following section presents the facts of the lawsuit, the procedural history leading to the Louisiana Supreme Court’s decision, and the court’s ultimate holding. Section III discusses the legal background, including the pre-existing disagreements among the Louisiana appellate courts. Section IV outlines the Louisiana Supreme Court’s analysis utilized to arrive at its

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1. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921 (La. 5/5/15); 169 So. 3d 328; *see also* LA. STAT. ANN. § 22:1973 (Supp. 2015) (imposing the duty).

2. *Id.* at p. 1; 169 So. 3d at 330.

3. *Id.* at pp. 21, 25; 169 So. 3d at 341, 344.

decision. Lastly, Section V examines the effects the court's decision will have on both pre-existing and future law and policy.

## II. FACTS AND HOLDING

This section is divided into two subsections. Subsection A provides the underlying factual background of the incident, while simultaneously outlining the insurer's alleged breach of its statutory requirements in the case. Subsection B begins with a discussion of the procedural history of the case and concludes with the Louisiana Supreme Court's ruling on the underlying issues.

### A. FACTUAL BACKGROUND

*Kelly* arose from allegations that State Farm handled an insurance claim in bad faith.<sup>4</sup> Danny Kelly and Henry Thomas were involved in a motor vehicle accident.<sup>5</sup> As a result of the accident, Kelly obtained legal representation to conduct settlement negotiations with Thomas and Thomas's insurer, State Farm.<sup>6</sup> At the time of the accident, State Farm provided insurance coverage to Thomas with a liability limit of \$25,000.<sup>7</sup> On January 6, 2006, Kelly's attorney mailed a letter to State Farm, enclosing copies of hospital records and medical bills totaling \$26,803.17.<sup>8</sup> In the letter, Kelly's attorney indicated a willingness to "recommend" the release of State Farm and Thomas from all liability in exchange for payment of full policy limits.<sup>9</sup> State Farm failed to respond to the letter and did not communicate again with Kelly's attorney until two months had passed.<sup>10</sup> On March 22, 2006, State Farm offered to settle Kelly's

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4. See *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 4 (La. 5/5/15); 169 So. 3d 328, 331.

5. *Id.* at p. 3; 169 So. 3d at 331.

6. *Id.*

7. *Id.* at pp. 3-4; 169 So. 3d at 331.

8. *Id.* at p. 3; 169 So. 3d at 331.

9. *Id.* ("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." (quoting Plaintiff's letter)). At this time, had State Farm and its insured obtained a release of liability in exchange for payment of full policy limits, Kelly's claim would have been settled and neither Thomas nor State Farm would have been exposed to additional damages.

10. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 3 (La. 5/5/15); 169 So. 3d 328, 331.

claim for full policy limits; however, Kelly rejected the offer.<sup>11</sup> At that time, State Farm informed Thomas of the possibility of personal liability and suggested he retain independent counsel.<sup>12</sup> State Farm, in this communication with Thomas, failed to mention Kelly's attorney's "offer to recommend settlement" and the amount of Kelly's medical bills.<sup>13</sup> Kelly later filed suit against Thomas and State Farm as his insurer.<sup>14</sup>

## B. PROCEDURAL HISTORY

Following Kelly's rejection of State Farm's settlement offer, the case proceeded to trial.<sup>15</sup> The trial court rendered judgment in Kelly's favor in the amount of \$176,464.07 plus interest.<sup>16</sup> State Farm, as the insurer of the party cast in judgment, paid Kelly the full policy limit of \$25,000.<sup>17</sup> Thomas, State Farm's insured, assigned Kelly his right to pursue a bad-faith action against State Farm in exchange for a promise not to enforce the excess judgment against his personal assets.<sup>18</sup>

Kelly then instituted a bad-faith action against State Farm in state court.<sup>19</sup> State Farm removed the action to federal court, and the court recognized the following two potential claims for bad faith: (1) the duty to inform claim and (2) the duty to settle claim.<sup>20</sup> The "duty to inform claim" pertained to State Farm's failure to notify Thomas of the letter received from Kelly's attorney indicating a willingness to recommend settlement for

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11. Kelly v. State Farm Fire & Cas. Co., 2014-1921, p. 3 (La. 5/5/15); 169 So. 3d 328, 331.

12. *Id.* at pp. 3-4; 169 So. 3d at 331.

13. *Id.* at p. 4; 169 So. 3d at 331.

14. *Id.*

15. *Id.*

16. *Id.*

17. Kelly v. State Farm Fire & Cas. Co., 2014-1921, p. 4 (La. 5/5/15); 169 So. 3d 328, 331.

18. *Id.* The plaintiff, because he was assigned the rights of State Farm's insured, stepped into the insured's shoes and was able to proceed by exercising the rights of a first-party bad-faith claimant. See LA. CIV. CODE ANN. art. 2642 (2015) ("All rights may be assigned, with the exception of those pertaining to obligations that are strictly personal. The assignee is subrogated to the rights of the assignor against the debtor."); see also Pontchartrain Gardens, Inc. v. State Farm Gen. Ins. Co., No. 07-7965, 2009 U.S. Dist. LEXIS 3734, at \*8, \*15 (E.D. La. Jan. 13, 2009) (noting that "[t]he right to pursue bad-faith damages against an insurer is not a strictly personal obligation" and hence, under Article 2642, an insured's claim for bad-faith penalties against an insurer can be assigned to a third-party).

19. *Kelly*, 2014-1921, p. 4; 169 So. 3d at 331.

20. *Id.* at pp. 4-5; 169 So. 3d at 331-32.

payment of full policy limits.<sup>21</sup> The “duty to settle claim” concerned State Farm’s failure to accept Kelly’s settlement offer contained in the letter.<sup>22</sup> State Farm moved for summary judgment on both claims.<sup>23</sup>

The district court originally granted summary judgment on the “duty to inform claim” but denied summary judgment on the “duty to settle claim.”<sup>24</sup> Specifically, the district court determined that the letter did not constitute a firm settlement offer; therefore, State Farm had no duty to inform its insured of the letter and could not be found to have acted in bad faith.<sup>25</sup> On the other hand, the district court denied summary judgment on the “duty to settle claim” after recognizing that there are multiple factors to consider when evaluating whether an insured breached its duty to timely pay a third-party claim.<sup>26</sup>

On motion for reconsideration, State Farm, as it did in its initial motion for summary judgment, contended that it could be liable for a bad-faith failure-to-settle claim only by failing to accept an actual settlement offer in bad faith.<sup>27</sup> Because the district court previously concluded the letter did not constitute a firm settlement offer,<sup>28</sup> State Farm argued it had no duty to settle the claim and could not have acted in bad faith.<sup>29</sup> The district court agreed and granted full summary judgment in favor of State Farm.<sup>30</sup> Kelly then appealed to the United States Fifth

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21. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 4 (La. 5/5/15); 169 So. 3d 328, 331.

22. *Id.*

23. *Id.*

24. *Id.* at pp. 4–5; 169 So. 3d at 331–32; *see Kelly v. State Farm Fire & Cas. Co.*, No. 09-619-BAJ-SCR, 2011 WL 5403470, at \*5–6 (M.D. La. Nov. 8, 2011), *reh’g granted and modified in part*, No. 09-619-BAJ-SCR, 2012 WL 4498884 (M.D. La. Sept. 28, 2012), *vacated*, 605 F. App’x 420 (5th Cir. 2015) (per curiam).

25. *Kelly*, 2011 WL 5403470, at \*6 (“[T]he jurisprudence does not support Kelly’s claim that State Farm was obligated to inform [its insured] of correspondence which does not amount to an actual offer to settle.”).

26. *Id.* at \*5.

27. *Kelly v. State Farm Fire & Cas. Co.*, No. 09-619-BAJ-SCR, 2012 WL 4498884, at \*1 (M.D. La. Sept. 28, 2012), *vacated*, 605 F. App’x 420 (5th Cir. 2015) (per curiam); *see also* Memorandum in Support of Motion for Summary Judgment at 5–8, *Kelly v. State Farm Fire & Cas. Co.*, No. 09-619-BAJ-SCR, 2011 WL 5403470 (M.D. La. Nov. 8, 2011) (citing *Commercial Union Ins. Co. v. Mission Ins. Co.*, 835 F.2d 587 (5th Cir.1988)) (arguing that State Farm cannot be liable for bad-faith failure to settle unless the plaintiff proves the letter constituted an “offer/demand” for settlement).

28. *Kelly*, 2011 WL 5403470, at \*5–6.

29. *Kelly*, 2012 WL 4498884, at \*2.

30. *Id.* at \*3–4.

Circuit Court of Appeals.<sup>31</sup>

The Fifth Circuit reversed the district court's judgment in part and affirmed in part.<sup>32</sup> The court affirmed the dismissal of the "duty to settle claim" after acknowledging that "Kelly [could not] maintain a cause of action as a matter of law" because a firm settlement offer was not received by State Farm.<sup>33</sup> However, the court reversed dismissal on the "duty to inform claim."<sup>34</sup> The court emphasized that it was questionable whether State Farm communicated all "pertinent facts" to its insured, as is required by law, so that the insured could determine what was in his best interest.<sup>35</sup>

After both parties filed petitions for rehearing, the Fifth Circuit withdrew its opinion and certified the following two questions to the Louisiana Supreme Court:

Can an insurer be found liable for a bad-faith failure-to-settle claim under [Louisiana Revised Statute] Section 22:1973(A) when the insurer never received a firm settlement offer?

Can an insurer be found liable under [Louisiana Revised Statute] Section 22:1973(B)(1) for misrepresenting or failing to disclose facts that are not related to the insurance policy's coverage?<sup>36</sup>

The Louisiana Supreme Court answered both questions affirmatively.<sup>37</sup>

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31. Brief for Appellant, Danny Kelly, *Kelly v. State Farm Fire & Cas. Co.*, 559 F. App'x 316 (5th Cir. 2014) (No. 12-31064).

32. *Kelly*, 559 F. App'x at 321 n. 4, *withdrawn*, 582 F. App'x 290 (5th Cir. 2012), *certifying questions to* 2014-1921 (La. 5/5/15); 169 So. 3d 328, *answers to certified questions conformed to by* 605 F. App'x 420 (5th Cir. 2015) (per curiam).

33. *Id.* (citing *Brown v. Liberty Mut. Fire Ins. Co.*, 168 F. App'x 588 (5th Cir. 2006) (requiring a firm settlement offer before imposing liability for bad-faith failure to settle); *Commercial Union Ins. Co. v. Mission Ins. Co.*, 835 F. 2d 587 (5th Cir. 1988) (same)).

34. *Kelly*, 559 F. App'x at 322.

35. *See id.* ("At no point did State Farm inform Thomas the extent to which Kelly's medical bills exceeded his policy limits, nor did State Farm tell Thomas that it had made a settlement offer that was rejected by Kelly.")

36. *Kelly v. State Farm Fire & Cas. Co.*, 582 F. App'x 290, 296 (5th Cir. 2014), *certifying questions to* 2014-1921 (La. 5/5/15); 169 So. 3d 328, *answers to certified questions conformed to by* 605 F. App'x 420 (5th Cir. 2015) (per curiam).

37. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, pp. 21, 25 (La. 5/5/15); 169 So. 3d 328, 341, 344.

### III. LEGAL BACKGROUND

In the world of insurance, a first-party claim is a claim filed by an insured against his own insurer for “damage to property or person”; whereas a third-party claim is “made by a claimant against the insured for damages allegedly caused by the insured.”<sup>38</sup> Under Louisiana law, an insurer owes a duty of good faith and fair dealing when adjusting claims.<sup>39</sup> Although an insurer owes duties of good faith and fair dealing to both the insured and third-party claimants, the duties run primarily in favor of the insured; the duties to a third-party claimant are more limited.<sup>40</sup> The Louisiana Supreme Court expressly limited third-party claimant causes of action under Section 22:1973 to allegations of the insurer’s “commission of the specific acts listed in [Section 22:1973(B)],” while refusing to similarly restrain first-party claimants.<sup>41</sup>

In *Kelly*, the Louisiana Supreme Court provided a detailed examination of two sections of Louisiana Revised Statute § 22:1973.<sup>42</sup> These sections provide:

- A. An insurer . . . owes to his insured a duty of good faith and fair dealing. The insurer has an affirmative duty to adjust claims fairly and promptly and to make a reasonable effort to settle claims with the insured or the claimant, or both . . .
- 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 Subsection A of this Section:
  - (1) Misrepresenting pertinent facts or insurance policy provisions relating to any coverages at issue.<sup>43</sup>

#### A. LOUISIANA REVISED STATUTE § 22:1973(A)

Section 22:1973(A) outlines an insurer’s broad duty of good

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38. 1 TOD I. ZUCKERMAN & MARK C. RASKOFF, ENVTL. INS. LITIG.: L. AND PRAC. § 2:6 (2d ed. 2009).

39. See LA. STAT. ANN. § 22:1973(A) (Supp. 2015).

40. See *Theriot v. Midland Risk Ins. Co.*, 95-2895, p. 15 (La. 5/20/97); 694 So. 2d 184, 193 (“[A] cause of action directly in favor of a third-party claimant against a tort-feasor’s insurer is not generally recognized absent statutory creation.”).

41. *Id.* at pp. 15–16 & n.15; 694 So. 2d at 192–93 & n.15.

42. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, pp. 9–25 (La. 5/5/15); 169 So. 3d 328, 334–44; see LA. STAT. ANN. § 22:1973(A)-(B)(1) (Supp. 2015).

43. LA. STAT. ANN. § 22:1973(A)-(B)(1) (Supp. 2015).

faith and fair dealing.<sup>44</sup> The concern regarding this section of the statute was a lack of clarity as to whether an insurer's receipt of a firm settlement offer was required before holding an insurer liable for bad-faith failure to settle.<sup>45</sup>

Before the enactment of Section 22:1973, the United States Fifth Circuit Court of Appeals, interpreting Louisiana law, determined that an insurer could not be found liable for bad-faith failure to settle unless it had received a firm settlement offer from the claimant.<sup>46</sup> On the other hand, though Louisiana courts never expressly held that a firm settlement offer is required, there appears to have been no Louisiana Supreme Court or appellate court decisions holding an insurer liable for bad-faith failure to settle without the presence of a firm settlement offer.<sup>47</sup>

### B. LOUISIANA REVISED STATUTE § 22:1973(B)(1)

Before *Kelly*, there was a decisive split among Louisiana appellate courts as to whether an insurer could be held liable under Section 22:1973(B)(1) for misrepresenting or failing to disclose facts unrelated to the insurance policy's coverage. To hold an insurer liable under Section 22:1973(B)(1), the second and fourth circuits required the insurer's misrepresentation to be related to the insurance policy's coverage.<sup>48</sup> In contrast, the third circuit ruled that a factual misrepresentation unrelated to insurance coverage was sufficient for a bad-faith claim brought under Section 22:1973(B)(1).<sup>49</sup>

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44. See LA. STAT. ANN. § 22:1973(A) (Supp. 2015).

45. See *Commercial Union Ins. Co. v. Mission Ins. Co.*, 835 F.2d 587, 588 (5th Cir. 1988) (per curiam) (determining that an insurer cannot be liable for bad-faith failure to settle unless it received a firm settlement offer from the claimant); see also *Kelly v. State Farm Fire & Cas. Co.*, 582 F. App'x 290, 295 (5th Cir. 2014) ("[T]he Supreme Court of Louisiana and the Louisiana intermediate appellate courts have never held that a firm settlement offer is required for a bad-faith failure-to-settle claim. But [the plaintiff] has not directed us to any Louisiana cases that find an insurer liable for bad-faith failure-to-settle in the absence of a firm settlement offer."), certifying questions to 2014-1921 (La. 5/5/15); 169 So. 3d 328, answers to certified questions conformed to by 605 F. App'x 420 (5th Cir. 2015) (per curiam).

46. *Commercial Union*, 835 F. 2d at 588 (citing *Bailey v. Hardware Mut. Cas. Co.*, 322 F. Supp. 387, 393 (W.D. La. 1969), *aff'd*, 439 F.2d 763 (5th Cir. 1971)).

47. See *Kelly*, 582 F. App'x at 295.

48. See *Strong v. Farm Bureau Ins. Co.*, 32,414, p. 5 (La. App. 2 Cir. 10/29/99); 743 So. 2d 949, 953, *overruled by Kelly v. State Farm Fire & Cas Co.*, 2014-1921 (La. 5/5/15); 169 So. 3d 238; *Talton v. USAA Cas. Ins. Co.*, 2006-1513, 2007-1414, p. 20 (La. App. 4 Cir. 3/19/08); 981 So. 2d 696, 710, *overruled by Kelly*, 2014-1921; 169 So. 3d 238.

49. See *McGee v. Omni Ins. Co.*, 2002-1012, pp. 10-11 (La. App. 3 Cir. 3/5/03); 840 So. 2d 1248, 1255-56; *Arvie v. Safeway Ins. Co.*, 06-1266, pp. 2-3 (La. App. 3 Cir.

Specifically, in *Strong v. Farm Bureau Insurance Co.*, the second circuit held that an insurer could not be found in bad faith for misrepresenting a fact concerning liability.<sup>50</sup> Rather, the court ruled that a reading of the statute requires the misrepresentation of a pertinent fact relating to the insurance policy's coverage.<sup>51</sup> The court even provided examples of pertinent facts relating to insurance coverage, including: (1) exclusions from coverage; (2) lapses or expirations of the insurance policy; and (3) the amount of insurance coverage.<sup>52</sup> The court found that the insurer misrepresented to the plaintiff that its insured had a green arrow to turn when it knew or should have known that was untrue.<sup>53</sup> Nevertheless, because this fact was not related to the insurance coverage (even though it was pertinent to liability), the insurer could not be subjected to bad-faith penalties.<sup>54</sup>

Similarly, in *Talton v. USAA Casualty Insurance Co.*, the fourth circuit required the insureds to prove that the insurer misrepresented facts related to an insurance coverage issue.<sup>55</sup> The insureds argued that their insurer was in bad faith for concealing "evidence reflecting the true extent of damage to [their] dwelling."<sup>56</sup> The court determined that, even if the insured was able to prove that the insurer "concealed evidence regarding the replacement of the roof on the main dwelling structure," the bad-faith statute would not apply because applying the statute would require an expansion of "the clear and unambiguous wording of the statute to include matters not related to coverage."<sup>57</sup>

Conversely, in *McGee v. Omni Insurance Co.*, the third circuit held that an insurer could be found liable for misrepresenting or failing to divulge pertinent facts to the insured, even if those facts were unrelated to the insurance

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2/7/07); 951 So. 2d 1284, 1286.

50. *Strong v. Farm Bureau Ins. Co.*, 32,414, p. 5 (La. App. 2 Cir. 10/29/99); 743 So. 2d 949, 953, *overruled by Kelly v. State Farm Fire & Cas. Co.*, 2014-1921 (La. 5/5/15); 169 So. 3d 238.

51. *Id.*

52. *Id.*

53. *Id.*

54. *Id.*

55. *Talton v. USAA Cas. Ins. Co.*, 2006-1513, 2007-1414, p. 20 (La. App. 4 Cir. 3/19/08); 981 So. 2d 696, 710, *overruled by Kelly*, 2014-1921; 169 So. 3d 238.

56. *Id.* at p. 18; 981 So. 2d at 709.

57. *Id.* at p. 20; 981 So. 2d at 710.

coverage.<sup>58</sup> The court found that the insurer's failure to inform its insured "that she could be relieved of potential excess liability by simply paying a small amount of interest"—though unrelated to the insurance coverage—was sufficient to impose bad-faith liability because it robbed the insured of a chance to mitigate her damages owed.<sup>59</sup>

The third circuit ruled the same way in a subsequent case, *Arvie v. Safeway Insurance Co.*, when it imposed bad-faith penalties on an insurer for failure to inform its insured of the extent of the opposing party's medical damages and the probability that judgment would exceed the underlying policy limits.<sup>60</sup> The insurer's failure to communicate facts necessary for the insured to determine his personal interest in the case, though unrelated to a coverage issue, was enough to subject the insurer to bad-faith penalties.<sup>61</sup>

All in all, before *Kelly* the Louisiana appellate courts were split as to whether the insurer's misrepresentation in Section 22:1973(B)(1) was strictly limited to misrepresentations relating to the insurance policy's coverage.

#### IV. THE COURT'S DECISION

The Louisiana Supreme Court, tasked with answering the two certified questions posed by the United States Fifth Circuit Court of Appeals, analyzed each certified question separately.<sup>62</sup> The court comprehensively analyzed the first certified question and provided an answer, before moving onto the Fifth Circuit's second certified question.

##### **A. QUESTION 1: CAN AN INSURER BE FOUND LIABLE FOR A BAD-FAITH FAILURE-TO-SETTLE CLAIM UNDER SECTION 22:1973(A) WHEN THE INSURER NEVER RECEIVED A FIRM SETTLEMENT OFFER?**

The court broke the first certified question down into two

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58. *McGee v. Omni Ins. Co.*, 2002-1012, pp. 10–11 (La. App. 3 Cir. 3/5/03); 840 So. 2d 1248, 1255–56; (noting the insurer's failure to communicate with their insured about the status of the claim robbed the insured of the ability to mitigate her damages).

59. *Id.* at p. 11; 840 So. 2d at 1256.

60. *Arvie v. Safeway Ins. Co.*, 06-1266, pp. 2–3 (La. App. 3 Cir. 2/7/07); 951 So. 2d 1284, 1286.

61. *See id.*

62. *See Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, pp. 9–25 (La. 5/5/15); 169 So. 3d 328, 334–44.

operative clauses.<sup>63</sup> The first clause asked whether or not an insurer could be found liable under Section 22:1973(A) for a bad-faith failure-to-settle claim.<sup>64</sup> If the court's answer to this clause was yes, it would proceed to the second clause: whether a firm settlement offer must be received before an insurer can be found liable for bad-faith failure to settle.<sup>65</sup>

### 1. DOES SECTION 22:1973(A) PROVIDE AN INSURED WITH A CAUSE OF ACTION FOR BAD-FAITH FAILURE TO SETTLE ?

The court began by determining who is afforded a cause of action under Section 22:1973(A).<sup>66</sup> While Louisiana jurisprudence found that third-party claimants do not have a cause of action under Section 22:1973(A),<sup>67</sup> there was no extant Louisiana jurisprudence analyzing a first-party cause of action under that specific statute.<sup>68</sup>

The court recognized that an insurer's relationship with its insured is different from an insurer's relationship with a third-party claimant.<sup>69</sup> An insurer's relationship with and duties owed to its insured arise from the contract between the two parties,<sup>70</sup> and this relationship has been characterized as "fiduciary in nature."<sup>71</sup> On the other hand, the relationship between the insurer and a third-party claimant is, by its very nature, fundamentally adversarial.<sup>72</sup> Because the insurer's relationships

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63. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 10 (La. 5/5/15); 169 So. 3d 328, 335.

64. *Id.*

65. *Id.* at p. 16; 169 So. 3d at 339.

66. *Id.* at pp. 11–16; 169 So. 3d at 335–38.

67. *Id.* at p. 11; 169 So. 3d at 335 (citing *Theriot v. Midland Risk Ins. Co.*, 95-2895, p. 14 (La. 5/20/97); 694 So. 2d 184, 193) (noting that section 1973(A) does not provide third-parties with a cause of action; rather, an exclusive list of an insurer's actionable breaches available to a third-party claimant is contained in section 1973(B)). The court also noted that the U.S. Fifth Circuit Court of Appeals's assumption in *Stanley v. Trinchard*, 500 F.3d 411, 427–28 (5th Cir. 2007) (that a first-party claimant is entitled to a cause of action for an insurer's breach of good faith and fair dealing) was nothing more than a non-binding "Erie guess" as to how state law would apply. *Kelly*, 2014-1921, pp. 10–11; 169 So. 3d at 335.

68. *Kelly*, 2014-1921, pp. 14–15; 169 So. 3d at 337–38.

69. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 12 (La. 5/5/15); 169 So. 3d 328, 336.

70. *Id.* at p. 11; 169 So. 3d at 335–36 (quoting *Theriot*, 95-2895, p. 15; 694 So. 2d at 193).

71. *Theriot*, 95-2895, p. 15; 694 So. 2d at 193 (citing *Pareti v. Sentry Indemn. Co.*, 536 So. 2d 417, 423 (La. 1988)).

72. *Kelly*, 2014-1921, p. 11; 169 So. 3d at 336 (quoting *Theriot*, 95-2895, p. 15; 694 So. 2d at 193).

with first-party claimants and third-party claimants are different, it stands to reason that the duties owed are also different.<sup>73</sup>

Next, the court turned to an analysis of the plain language of the statute to determine whether or not a first-party claimant is afforded a cause of action for failure to settle a claim in bad faith.<sup>74</sup> The last portion of Section 22:1973(A) provides: “Any insurer who breaches these duties shall be liable for any damages sustained as a result of the breach.”<sup>75</sup> The court found this language favorable to finding a cause of action for an insured under Section 22:1973(A), because the word “shall” is mandatory in statutory interpretation.<sup>76</sup> The fact that an insurer’s breach of its duties outlined in Section 22:1973(A) mandatorily renders it liable for damages sustained as a result of that breach indicates that an insured has a cause of action under that section of the statute.<sup>77</sup>

Furthermore, the court noted that Section 22:1973(A) is remedial in nature.<sup>78</sup> In enacting Section 22:1973(A), the legislature codified a cause of action in favor of insured parties that had been previously recognized by a long line of cases dating back to at least 1967.<sup>79</sup> The court noted that the legislature’s enactment of a law is presumed to (1) take into account existing laws on the subject and (2) add, rather than remove, claimants’ rights.<sup>80</sup> The court refused to believe that the legislature would codify a law regarding bad-faith failure to settle without granting

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73. See *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 11 (La. 5/5/15); 169 So. 3d 328, 335–36 (quoting *Theriot v. Midland Risk Ins. Co.*, 95-2895, p. 14 (La. 5/20/97); 694 So. 2d 184, 192 n.15 (refusing to limit an insured to the same exclusive list of actionable breaches contained in Louisiana Revised Statute § 22:1973(B) to which a third-party claimant is limited)).

74. *Id.* at pp. 13–16; 169 So. 3d at 336–38.

75. LA. STAT. ANN. § 1973(A) (Supp. 2015).

76. *Kelly*, 2014-1921, p. 12; 169 So. 3d at 336 (citing LA. STAT. ANN. § 1:3 (2003)).

77. *Id.*

78. *Id.* at p. 13; 169 So. 3d at 336. (citing *Manuel v. La. Sheriff’s Risk Mgmt. Fund*, 95-0406, p. 7 (La. 11/27/95); 664 So. 2d 81, 85 (finding that the ancestor to Louisiana Revised Statute § 22:1973 is remedial in nature and applicable to all pre-existing insurance policies)).

79. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 14 (La. 5/5/15); 169 So. 3d 328, 337 (citing *Roberie v. So. Farm Bureau Cas. Ins. Co.*, 194 So. 2d 713 (La. 1967); *Hodge v. Am. Fid. Fire Ins. Co.*, 486 So. 2d 223 (La. App. 3 Cir. 1986); *Fertitta v. Allstate Ins. Co.*, 439 So. 2d 531 (La. App. 1 Cir. 1983); *Domangue v. Henry*, 394 So. 2d 638 (La. App. 1 Cir. 1980)).

80. See *id.* at p. 13; 169 So. 3d at 336–37 (citing *Fontenot v. Reddell Vidrine Water Dist.*, 02-0439, 02-0442, 02-0478, p. 13 (La. 1/14/03); 836 So. 2d 14, 24).

a claim for that cause of action to first-party claimants, when at the time of enactment there existed ample jurisprudence granting that right to first-party claimants.<sup>81</sup> Thus, the plain language of Section 22:1973(A), along with the jurisprudence available and the remedial intent of the statute, supported a conclusion that an insured has a cause of action under that section of the statute.<sup>82</sup>

## 2. MUST AN INSURER RECEIVE “A FIRM SETTLEMENT OFFER” AS A CONDITION FOR AN INSURED TO RECOVER FOR THE INSURER’S BAD-FAITH FAILURE TO SETTLE?

In analyzing the necessity of a firm settlement offer, the court again turned to the language of the statute.<sup>83</sup> Of particular importance was the fact that the statute describes the insurer’s duty as “affirmative.”<sup>84</sup> Accordingly, because “affirmative duty” is a legal term of art, the court was required to apply the phrase’s “meaning commonly employed in the law.”<sup>85</sup> The phrase “affirmative duty” in the Louisiana Insurance Code is interpreted to mean “taking positive action[s] to comply with the legal standard.”<sup>86</sup>

The statute lists two “affirmative acts” that an insurer must take to comply with the legal standard: (1) “adjust claims fairly and promptly”; and (2) “make a reasonable effort to settle claims with the insured or the claimant, or both.”<sup>87</sup>

The court listed multiple reasons for determining that a firm settlement offer is not a required condition for an insured to recover for an insurer’s bad-faith failure to settle.<sup>88</sup> First,

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81. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 15 (La. 5/5/15); 169 So. 3d 328, 338.

82. *Id.* at pp. 15–16; 169 So. 3d at 337–38 (citing LA. STAT. ANN. § 1:4 (2003) (“When the wording of a Section is clear and free of ambiguity, the letter of it shall not be disregarded under the pretext of pursuing its spirit”).

83. *Id.* at p. 17; 169 So. 3d at 339.

84. *Id.* (quoting LA. STAT. ANN. § 22:1973(A) (Supp. 2015) (“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.”)).

85. *Id.* (citing LA. STAT. ANN. § 1:3 (2003) (“Technical words and phrases, and such others as may have acquired a peculiar and appropriate meaning in law, shall be construed and understood according to such peculiar and appropriate meaning.”)).

86. *Id.* (citing LA. STAT. ANN. § 22:1931.12(D) (Supp. 2015) (requiring persons liable for insurance fraud to affirmatively “disclose all property and liabilities and all transfers of property which meet the criteria” of a prior portion of the statute)).

87. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 19 (La. 5/5/15); 169 So. 3d 328, 340 (citing LA. STAT. ANN. § 22:1973(A) (Supp. 2015)).

88. *Id.* at pp. 19–21; 169 So. 3d at 340–41.

requiring a firm settlement offer would essentially amount to adding words to the statutory language, given that a firm settlement offer is not listed as a requirement in the statute.<sup>89</sup> The court reasoned that such rewriting of a statute is not allowed by Louisiana courts.<sup>90</sup>

Second, the court cited practical reasons for not making a firm settlement offer a required condition before finding that an insurer acted in bad faith.<sup>91</sup> Specifically, neither the insured nor the insurer has control over whether a claimant will submit a firm settlement offer.<sup>92</sup> The court found it impractical to determine that an insurer's obligation to act in good faith is triggered by receipt of a firm settlement offer, over which neither the insured nor the insurer has any control.<sup>93</sup> As mentioned earlier, insurers have an "affirmative duty" to comply with the legal standards outlined in Section 1973(A)—not a duty that is inactive until a firm settlement offer is received.<sup>94</sup>

After answering both operative clauses of the Fifth Circuit's first certified question, the Louisiana Supreme Court ruled that "an insurer can be found liable for a bad-faith failure-to-settle claim under La. R.S. 22:1973(A), notwithstanding that the insurer never received a firm settlement offer."<sup>95</sup>

**B. QUESTION 2: CAN AN INSURER BE FOUND LIABLE UNDER SECTION 22:1973(B)(1) FOR MISREPRESENTING OR FAILING TO DISCLOSE FACTS UNRELATED TO THE INSURANCE POLICY'S COVERAGE?**

Again, the court answered this question by analyzing the statute's language and applying Louisiana's rules for statutory interpretation.<sup>96</sup> The court started by examining the pertinent language: "misrepresenting pertinent facts or insurance policy

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89. Kelly v. State Farm Fire & Cas. Co., 2014-1921, pp. 19–20 (La. 5/5/15); 169 So. 3d 328, 340.

90. *Id.* at p. 20; 169 So. 3d at 340 (citing *Cacamo v. Liberty Mut. Fire Ins. Co.*, 99-3479, 99-3480, p. 4 (La. 6/30/00); 764 So. 2d 41, 44 ("Courts are not free to rewrite laws to effect a purpose that is not otherwise expressed.")).

91. *Id.* at p. 20; 169 So. 3d at 341.

92. *Id.*

93. *Id.*

94. *Id.*

95. Kelly v. State Farm Fire & Cas. Co., 2014-1921, p. 21 (La. 5/5/15); 169 So. 3d 328, 341.

96. *Id.* at pp. 21–22; 169 So. 3d at 341–42 (quoting LA. STAT. ANN. § 1:3 (2003) ("Words and phrases shall be read with their context and shall be construed according to the common and approved usage of the language.")).

provisions relating to any coverages at issue.”<sup>97</sup> Applying the standard legal definition of the word “misrepresentation,” the court concluded that the statute prohibited “communication from an insurer that either states an untruth or fails to state the truth.”<sup>98</sup>

The main issue with a proper interpretation of the relevant portion of the statute revolved around the application of the word “or.”<sup>99</sup> To that end, the Louisiana Supreme Court preferred the implicit interpretation of the word “or” taken by the Louisiana third circuit in *McGee* and *Arvie* over the implicit interpretation of the Louisiana second and fourth circuits in *Talton* and *Strong*.<sup>100</sup> In essence, the third circuit interpreted the word “or” disjunctively and found that an insurer could be found liable for misrepresenting either (1) pertinent facts unrelated to coverage issues or (2) facts specifically related to coverage issues.<sup>101</sup> Conversely, the Louisiana second and fourth circuits interpreted the word “or” conjunctively and found that an insurer could be found liable for “[1] misrepresenting pertinent facts [*relating to any coverages at issue*] or [2] insurance policy provisions relating to any coverages at issue.”<sup>102</sup>

In reaching this conclusion, the court noted that proper statutory interpretation of the use of the word “or” is outlined by Louisiana Revised Statute § 1:9, which provides that, “[u]nless 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.’”<sup>103</sup> The court recognized that the only time courts can interpret the word “or” to mean “and/or” is when the context of the statute clearly indicates that conclusion.<sup>104</sup>

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97. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, pp. 21–22 (La. 5/5/15); 169 So. 3d 328, 342 (quoting LA. STAT. ANN. § 22:1973(B) (Supp. 2015)).

98. *Id.* at p. 22; 169 So. 3d at 342 (citing *Misrepresentation*, BLACK’S LAW DICTIONARY (6th ed. 2009)).

99. *See id.* at pp. 22–25; 169 So. 3d at 342–44.

100. *Id.* (citing *Talton v. USAA Cas. Ins. Co.*, 2006-1513, 2007-1414, p. 20 (La. App. 4 Cir. 3/19/08); 981 So. 2d 696, 710; *Arvie v. Safeway Ins. Co.*, 06-1266, p. 2 (La. App. 3 Cir. 2/7/07); 951 So. 2d 1284, 1286; *McGee v. Omni Ins. Co.*, 2002-1012, p. 11 (La. App. 3 Cir. 3/5/03); 840 So. 2d 1248, 1256; *Strong v. Farm Bureau Ins. Co.*, 32,414, p. 5 (La. App. 2 Cir. 10/29/99); 743 So. 2d 949, 953).

101. *See id.* at p. 23; 169 So. 3d at 343.

102. *Id.* at p. 23; 169 So. 3d at 342–43 (quoting LA. STAT. ANN. § 22:1973(B)(1) (Supp. 2015)).

103. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 24 (La. 5/5/15); 169 So. 3d 328, 343 (quoting LA. STAT. ANN. § 1:9 (2003)).

104. *Id.* (citing LA. SENATE LEGISLATIVE SERVS., DRAFTING MANUAL 102 (2007)).

Taking the statutory interpretation rules into account, the court found that a clear reading of the statute supported an application of the word “or” in the disjunctive sense.<sup>105</sup> Therefore, the court ruled that the statute should be read to mean that “an insurer can be liable for misrepresenting either: (1) ‘pertinent facts,’ or (2) ‘insurance policy provisions relating to any coverage at issue.’”<sup>106</sup> Thus, an insurer can be held liable under Section 22:1973(B)(1) for misrepresenting facts that are not related to the insurance coverage.

## V. ANALYSIS

For years it has been clear that an insurer owes a broad duty of good faith and fair dealing to its insured.<sup>107</sup> The *Kelly* decision expands that duty. While the decision is clear that an insurer can be found in bad faith (1) without receiving a firm settlement offer or (2) for failing to disclose pertinent facts unrelated to the insurance policy’s coverage, the decision has the potential to have some concerning effects on the handling of insurance-related litigation.

This analysis begins by explaining what pre-existing law the decision affirms and overrules. Next, it predicts the practical effects of expanding the insurer’s duty, including the possibility that the decision will cause an influx of bad-faith claims and increased costs of litigation and insurance premiums.

### A. KELLY’S IMPACT ON PRE-EXISTING LAW

*Kelly* makes it clear that insurers conducting business in Louisiana must “make a reasonable effort to settle claims with the insured or the claimant, or both” before receipt of a firm settlement offer.<sup>108</sup> Before *Kelly*, it was unclear whether an insurer could be liable for a bad-faith failure-to-settle claim without receiving a “firm settlement offer” from the claimant.<sup>109</sup>

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105. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 25 (La. 5/5/15); 169 So. 3d 328, 343.

106. *Id.* at p. 25; 169 So. 3d at 343–44 (quoting LA. STAT. ANN. § 22:1973(B)(1) (Supp. 2015)).

107. *See Theriot v. Midland Risk Ins. Co.*, 95-2895, pp. 6–16 (La. 5/20/97); 694 So. 2d 194, 188–93 (acknowledging that the wording of Louisiana Revised Statute § 22:1973(A) is “broad”).

108. LA. STAT. ANN. § 22:1973(A) (Supp. 2015).

109. *See Commercial Union Ins. Co. v. Mission Ins. Co.*, 835 F.2d 587, 588 (5th Cir. 1988) (per curiam) (determining that an insurer cannot be liable for bad-faith failure-to-settle unless they received a firm settlement offer from the claimant); *see also Kelly v. State Farm Fire & Cas. Co.*, 582 F. App’x 290, 295 (5th Cir. 2014) (“[T]he

The decision indicates that an insurer can be found to have breached its good-faith duty even when the claimant submits a vague “offer to recommend” settlement. Moving forward, Louisiana courts will not require the presence of a firm settlement offer from the claimant before holding an insurer liable for bad-faith failure to settle.

Moreover, before *Kelly*, Louisiana appellate courts were split as to whether an insurer could be assessed bad-faith penalties under Section 22:1973(B)(1) for misrepresenting or failing to disclose facts unrelated to the insurance policy’s coverage.<sup>110</sup> *Kelly* overrules the decisions of the Louisiana second and fourth circuits—which only held an insurer liable for misrepresenting or failing to disclose facts related to a coverage issue.<sup>111</sup> Now, an insurer can be found liable for failing to disclose any “pertinent fact,” even if that fact is unrelated to the policy of insurance covering the insured.<sup>112</sup>

#### **B. KELLY’S EFFECT ON FUTURE LAW AND POLICY: EXPANSION OF INSURERS’ BROAD GOOD-FAITH DUTY**

While *Kelly* adequately answers the certified questions posed by the Fifth Circuit, the decision is likely to have numerous practical implications on insurance-related litigation in Louisiana. Specifically, *Kelly* is likely to affect the handling of insurance claims in two major ways moving forward. First, the decision changes the way insurers must respond to claims in Louisiana by placing a clear duty on insurers to affirmatively reach out to the claimant and make a reasonable effort to settle the claim before a firm settlement offer is received, which is not a

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Supreme Court of Louisiana and the Louisiana intermediate appellate courts have never held that a firm settlement offer is required for a bad-faith failure-to-settle claim. But [the plaintiff] has not directed us to any Louisiana cases that find an insurer liable for bad-faith failure-to-settle in the absence of a firm settlement offer.”), *certifying questions* to 2014-1921 (La. 5/5/15); 169 So. 3d 328, *answers to certified questions conformed to by* 605 F. App’x 420 (5th Cir. 2015) (per curiam).

110. Compare *Strong v. Farm Bureau Ins. Co.*, 32,414, p. 5 (La. App. 2 Cir. 10/29/99); 743 So. 2d 949, 953 and *Talton v. USAA Cas. Ins. Co.*, 2006-1513, 2007-1414, p. 20 (La. App. 4 Cir. 3/19/08); 981 So. 2d 696, 710 (requiring the insured to prove that the insurer misrepresented or failed to disclose facts relating to a coverage issue) with *McGee v. Omni Ins. Co.*, 2002-1012, p. 11 (La. App. 3 Cir. 3/5/03); 840 So. 2d 1248, 1256 and *Arvie v. Safeway Ins. Co.*, 06-1266, p. 2 (La. App. 3 Cir. 2/7/07); 951 So. 2d 1284, 1286 (imposing bad faith penalties for an insurer’s failure to disclose pertinent facts unrelated to a coverage issue).

111. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, pp. 23–25 (La. 5/5/15); 169 So. 3d 328, 343–44.

112. *Id.*

duty mandated in a number of other jurisdictions.<sup>113</sup> Second, the lack of clarity as to what constitutes a pertinent fact unrelated to coverage could lead to unnecessary acts attempting to comply with the ruling, which in turn could lead to increased costs of litigation and increased insurance premiums. Both of these concerning aspects of the ruling have the potential to lead to an influx of bad-faith claims in future litigation.

The decision, which attempts to protect insureds involved in claims handling by expanding the good-faith duty of insurers, could adversely impact the overall class of insureds in Louisiana. It is undoubtedly important to protect insureds from bad-faith claims handling by insurers; however, Louisiana courts should be extremely careful when expanding the already broad good-faith duty of insurers.

**1. INSURERS MUST NOW MAKE AN AFFIRMATIVE AND REASONABLE EFFORT TO SETTLE THE CLAIM BEFORE A SETTLEMENT DEMAND IS RECEIVED.**

The holding in *Kelly* establishes that an insurer can be assessed penalties for bad-faith failure to settle even without receiving a firm settlement offer from the claimant.<sup>114</sup> The ruling places a clear duty on insurers to affirmatively take the necessary steps to evaluate and attempt to settle from the outset of the claim.

However, *Kelly* does not stand for the proposition that a settlement offer has no place in the analysis for determining whether an insurer acted in bad faith. In a footnote, the court indicates that the presence of a firm settlement offer would still factor into an analysis for determining whether to impose bad-faith penalties against an insurer.<sup>115</sup> This footnote indicates that an insurer's mere awareness that "the matter can be resolved" in a way that "shield[s] the insured from an excess judgment" is a major factor to consider when deciding whether to impose bad-faith penalties.<sup>116</sup>

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113. See 1 ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES § 5:2 n.1 (6th ed. 2012) (collecting decisions from Illinois, California, Missouri, Texas, New York, Iowa, Florida, Oregon, Kansas, Georgia, Hawaii, and Montana requiring a firm settlement offer before holding an insurer liable for bad-faith failure to settle).

114. See *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 21 (La. 5/5/15); 169 So. 3d 328, 341.

115. *Id.* at p. 19 n.29; 169 So. 3d at 340, n.29.

116. *Id.*

For example, in the immediate case, although Kelly did not submit a “firm settlement offer” to State Farm, he did express a willingness to settle his claim for a sum which would have shielded State Farm’s insured from an excess judgment.<sup>117</sup> This seemingly put State Farm on notice of an opportunity to settle; the fact that the opportunity to settle was lost factors into the analysis for imposing bad-faith penalties on State Farm.<sup>118</sup>

Even though the court never explicitly stated that in order to be subject to bad-faith penalties the insurer must be on notice that the claim can be settled for an amount that would shield the insured from personal liability, such a factual scenario seems to have a major place in the analysis.<sup>119</sup> All in all, though a firm settlement offer, as well as many other additional factors, will factor into an analysis for determining whether to hold an insurer liable for bad-faith practices, a firm settlement offer is not a requirement for subjecting an insurer to bad-faith penalties. Therefore, insurers must now be sure to make an affirmative effort to settle the claim even before a firm settlement offer is received from the claimant.

## **2. THE DECISION HAS THE POTENTIAL TO LEAD TO AN INFLUX OF BAD-FAITH CLAIMS.**

While the Louisiana Supreme Court acknowledges that Section 22:1973 does not “contemplate gamesmanship, such as having unrealistic offers . . . presented through carefully ambiguous demands coupled with sudden-death timetables in order to ‘set up’ the insurer for an excess liability judgment,” the *Kelly* decision has the potential to lead directly to that result.<sup>120</sup>

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117. See *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 3 (La. 5/5/15); 169 So. 3d 328, 331 (referring to Kelly’s letter in which his lawyer informed State Farm that he would recommend release of State Farm and its insured for full policy limits).

118. See *id.* at p. 19 n.29; 169 So. 3d at 340 n.29 (noting that a firm settlement offer has a place in a bad-faith analysis because it “would unmistakably put the insurer on notice the matter can be resolved and, if the offer were within policy limits, shield the insured from an excess judgment”). Though Kelly did not submit a “firm settlement offer,” it seems he put State Farm on notice that the matter could be resolved in a manner that would shield the insured from an excess judgment, which factors into a bad-faith analysis.

119. See *supra* notes 115–18.

120. *Kelly*, 2014-1921, p. 25 n.34; 169 So. 3d at 344 n.34 (internal quotation marks omitted) (citing *Parich v. State Farm Mut. Auto. Ins. Co.*, 919 F.2d 906, 912 (5th Cir. 1990)); see also Shannon Howard-Eldridge, *Bad Faith Failure to Settle*, MCCRANIE SISTRUNK ANZELMO HARDY MCDANIEL & WELCH (May 8, 2015), <http://mcsalaw.com/kelly-v-state-farm-bad-faith-failure-to-settle/> (predicting that, post-*Kelly*, “insurers may see an increase in the assignment of the insured’s ‘bad faith’ rights against an

Louisiana courts have determined on multiple occasions that insurers have the right to litigate questionable claims.<sup>121</sup> On many occasions, an adequate evaluation of an insurance claim requires a significant amount of time. Factors that must be considered include (1) liability, (2) coverage of the claim under the policy, (3) injury, and (4) the amount of damages.<sup>122</sup>

The decision may incentivize counsel for plaintiffs to submit to the insurer an ambiguous demand for policy limits with a short deadline to accept in the majority of cases they handle.<sup>123</sup> Even if legitimate questions regarding causation or the amount of damages exist in the case, the plaintiff loses nothing by doing this, but has the potential benefit of submitting a bad-faith failure-to-settle claim later on. Worst case scenario, the plaintiff's claim for bad-faith penalties would be denied by the court, and the plaintiff would simply be liable for the miniscule court costs that accompany filing suit. On the other hand, in the event of a later excess judgment rendered against an insured, the court may factor the ambiguous demand into the analysis for determining whether to impose bad-faith penalties against the insurer. If so, the plaintiff's gamble would pay off, and he could be in line for a large damage award accompanying a bad-faith judgment.

Therefore, while the Louisiana Supreme Court acknowledged that unrealistic demands with sudden-death timetables are not contemplated by Section 22:1973,<sup>124</sup> it is likely that the decision will lead to an influx of these unrealistic demands. While it is unlikely that the majority of these claims will be successful, the minuscule costs of bringing them and the potential for high

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insurer").

121. See, e.g., *Calogero v. Safeway Ins. Co.*, 1999-1625, p. 5 (La. 1/19/00); 753 So. 2d 170, 173 (citing *Darby v. Safeco Ins. Co.*, 545 So. 2d 1022, 1029 (La. 1989)).

122. See George E. Allen, *Evaluation and Settlement of a Personal Injury Claim for Damages*, 14 WASH. & LEE L. REV. 1, 4-8 (1957) (describing factors to consider in case evaluation of a personal injury claim).

123. Even if the plaintiff is making a third-party claim, and, therefore, does not possess the ability to bring a bad-faith failure-to-settle claim against the insurer, see *supra* note 67, he is still incentivized to submit such an offer because an assignment of rights from the insured. It is highly likely that an insured faced with personal liability in the wake of an excess judgment will be willing to assign his rights to pursue a bad-faith claim against his insurer to the plaintiff in exchange for an agreement not to enforce the judgment against his personal assets. This was the factual scenario in *Kelly*.

124. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 25 (La. 5/5/15); 169 So. 3d 328, 344 n.34 (citing *Parich v. State Farm Mut. Auto. Ins. Co.*, 919 F.2d 906, 912 (5th Cir. 1990)).

penalty awards is likely to result in more being brought. An influx of bad-faith claims is not inherently bad, given that those very claims are intended to protect insureds from bad-faith conduct by insurers and deter similar conduct in the future. However, it is likely that some legal representatives may, in the wake of *Kelly*, be incentivized to utilize the very bad-faith “set up” tactics that the decision seeks to prevent.

### 3. THE LACK OF GUIDANCE AS TO WHAT CONSTITUTES A “PERTINENT FACT” COULD RESULT IN INCREASED COSTS OF LITIGATION AND INCREASED INSURANCE PREMIUMS.

It is important to remember that in *Kelly*, the Louisiana Supreme Court was simply tasked with answering the certified questions posed by the United States Fifth Circuit Court of Appeals.<sup>125</sup> Though the court did not decide the case on the merits, the decision still effectively imposes new duties on insurers in Louisiana. Therefore, the lack of guidance as to what constitutes a pertinent fact has ramifications on the actions insurers take in claims handling.

Looking back at the facts of *Kelly*, it would not be unreasonable for the court to find that the insurer acted in bad faith. The initial letter sent by plaintiff’s counsel to State Farm enclosed medical bills totaling \$26,803.17, while the policy of insurance had liability limits of \$25,000.<sup>126</sup> At that point, the insurer likely should have made a reasonable effort to settle the claim. In any event, the insurer or counsel for the insurer, at the very least, should have provided a timely response to the plaintiff’s letter rather than simply ignoring the correspondence. Instead, the insurer appears to have blatantly disregarded the letter, subjecting its insured to an excess judgment.<sup>127</sup> Based on the extreme facts of the case, the insurer likely should have disclosed the contents of the plaintiff’s letter and informed the insured of a likely excess judgment.

However, the language and rulings in *Kelly* make it unclear exactly what “pertinent facts” an insurer, who is attempting to adjust a claim in good faith, is required to disclose to its insured as the case develops. The decision warns insurers that they can be liable for bad-faith penalties for failing to disclose pertinent

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125. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 1 (La. 5/5/15); 169 So. 3d 328, 329–30.

126. *Id.* at p. 3; 169 So. 3d at 331.

127. *See id.*

facts unrelated to coverage issues,<sup>128</sup> but fails to provide guidance as to what constitutes a “pertinent fact.” Therefore, *Kelly*’s applicability is not as clear in situations involving less obvious factual scenarios, and it is likely that insurers will be forced to wait for later court decisions to define the scope of what constitutes a pertinent fact.

One example of the confusion *Kelly* may create can be seen by examining the different types of medical records that may be obtained by an insurer during the discovery phase of litigation. Are all new significant medical records received by the insurer pertinent facts that should be forwarded to the insured? Are only medical records which could substantially increase the claimant’s recovery pertinent facts? Or, are medical records considered pertinent facts only when they have the potential to lead to an amount of damages which exceeds the underlying policy limits? Additionally, it is unclear if the amount of available policy limits affects what information, including medical records, should be forwarded to the insured.

It is easy to see that the lack of guidance as to what constitutes a pertinent fact could lead to confusion among insurers and attorneys representing insurers. Those representatives making every effort to handle a claim in good faith may disagree about what must necessarily be conveyed to their insureds. For example, one insurer’s reading of *Kelly* may lead to the determination that all medical records resulting in a major increase in potential recovery should be forwarded to the insured, even if the damage award appears unlikely to exceed the available policy limits. Other insurers may simply forward medicals only when the possibility of an excess judgment presents itself. In each of the above scenarios, the insurer is attempting to adjust a claim in good faith, yet, depending on the courts’ determination of what constitutes a “pertinent fact,” one insurer may be assessed bad-faith penalties while another may not.

While it is undoubtedly important that insurers keep their insureds adequately informed of their personal interest in litigation, in reality, *Kelly* could force insurers and their legal representatives to provide, out of an abundance of caution, more information to their insured than is necessary. Since there is little guidance as to what constitutes a pertinent fact, insurers may simply decide to forward everything remotely questionable to

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128. *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, p. 25 (La. 5/5/15); 169 So. 3d 328, 344.

their insureds. Although this may seem like a reasonable requirement, there is one major concern: cost.

If insurers choose to forward everything to their insureds, a substantial increase in the cost of litigation is likely to result. Insurers' legal representatives generally charge an hourly fee, and every receipt and transmittal of information comes with a cost. For example, when a lawyer defending an insurer receives information that may be classified as a pertinent fact, that lawyer is unlikely to simply scan the documents and forward them to the insured. Rather, the lawyer is likely to provide a report to the insured explaining how the insured's interest in the case may be affected. In some instances, it is reasonable to believe that insureds, now concerned that they may be personally liable at some point in the future, will request phone conferences or in-person meetings with their lawyers.

The more an insurer's legal representative is required to report to and meet with the insured, the more hours are billed in legal services, which leads directly to increased costs of litigation for insurers in Louisiana. Insurers faced with increased legal costs are unlikely to absorb these profit losses; rather, a more likely alternative is that they will increase their premiums to offset the costs.<sup>129</sup>

A recent report listed Louisiana as the state with the fourth highest car insurance rates in the country.<sup>130</sup> The fact that "Louisiana drivers who get in wrecks file more injury claims than motorists in other states" has a substantial impact on these high insurance rates.<sup>131</sup> Accordingly, Louisiana courts should be extremely careful to adequately define the requirements insurers must follow in claims handling and litigation practices. Increased protection for insureds involved in litigation is an extremely

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129. See Renita D. Young, *High Claims, Litigation Continue to Drive Louisiana Auto Insurance Rates Up*, NOLA.COM/TIMES-PICAYUNE (Feb. 14, 2014, 11:35 AM), [http://www.nola.com/business/baton-rouge/index.ssf/2014/02/high\\_claims\\_litigation\\_continu.html](http://www.nola.com/business/baton-rouge/index.ssf/2014/02/high_claims_litigation_continu.html) ("[A]ccording to State Farm spokesman Gary Stephenson, insurance rates in Louisiana are primarily driven by claims costs, which is directly connected to the high number of accidents. Another factor is the high volume of lawsuits and bodily injury claims filed in the state.").

130. See *10 States With the Most Expensive Car Insurance Rates in 2015*, INS. BUS. (Apr. 20, 2015), <http://www.ibamag.com/news/10-states-with-the-most-expensive-car-insurance-rates-in-2015-22160.aspx>.

131. See Chance Ryan, *Louisiana Has the Nation's Highest Auto Insurance Rates—Again*, WWLTV.COM (Apr. 21, 2013, 5:11 AM), <http://www.wwltv.com/story/news/local/lafourche-terrebonne/2014/09/03/14585906/>.

important concern; however, lack of clarity regarding insurers' duties could increase insurance rates and harm the overall class of insureds in Louisiana, who already pay some of the highest insurance rates in the country.

Accordingly, while insureds should always be kept informed of their interest in the case, more guidance as to what constitutes a pertinent fact unrelated to the insurance policy would have helped prevent unnecessary actions by insurers and their representatives when responding to claims.

## VI. CONCLUSION

*Kelly* makes it clear that insurers in Louisiana can be found liable for bad-faith failure to settle without receiving a firm settlement offer or for failing to disclose pertinent facts unrelated to a coverage issue.<sup>132</sup> A “new” duty to affirmatively respond to insurance claims and make a reasonable effort to settle before receipt of a firm settlement offer from the claimant is now clearly imposed on Louisiana insurers. While the decision informs insurers that they must advise their insureds of all “pertinent facts,” there is little guidance provided as to what constitutes a “pertinent fact.” This lack of guidance could lead to increased costs of litigation, which in turn is likely to result in increased insurance premiums. In sum, *Kelly*—while it attempts to protect insureds involved in the claims handling process—has the potential to negatively impact the overall class of insureds in Louisiana.

Gary Langlois, Jr.

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132. See *Kelly v. State Farm Fire & Cas. Co.*, 2014-1921, pp. 21, 25 (La. 5/5/15); 169 So. 3d 328, 341, 44.