EXCESS V. PRIMARY:
THE EXPANSION OF BAD FAITH DEFENSE CLAIMS
IN LOUISIANA

Submitted by Ryan C. Higgins
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I. INTRODUCTION

A. During this presentation we will examine the expansion of bad faith defense claims in Louisiana by focusing on the recent case of RSUI Indemnity Company v. American States Insurance Company.

1. RSUI (excess insurer) brought a subrogation claim against American (primary insurer) arising out of American’s alleged bad faith failure to properly defend a mutual insured in an underlying state court personal injury action.

2. The underlying case resulted in a $2 million excess settlement funded by RSUI.

3. RSUI filed suit against American to recover its excess settlement payment.

II. BAD FAITH IN THE INSURANCE CONTEXT

A. Generally

1. Term “bad faith” is generic term used to describe conduct of insurer who breaches its statutorily imposed duty to act in “good faith” and engage in “fair dealing” in adjusting claims and includes specific acts that are defined by statute. Bourque v. Audubon Ins. Co., App. 3 Cir. 1997, 704 So.2d 808, 1997-522 (La. App. 3 Cir. 11/19/97), writ granted in part, reversed in part, 709 So.2d 766, 1997-3142 (La. 2/20/98).

2. An insurer’s duty to its insured also arises from its policy and the receipt of premiums from the insured in exchange for a defense.

3. An insurer is a professional defender of lawsuits and is held to a higher standard than an unskilled practitioner. What may be neglect on the part of the latter may well constitute bad faith on the part of the insurer. Keith
v. Comco Insurance Company, 574 So.2d 1270, 1277 (La. App. 2nd Cir. 1991), writ denied, 577 So.2d 16 (La.1991); Gourley v. Prudential Property and Casualty Insurance Company, 98-0934, pp. 6-7 (La. App. 1 Cir.5/14/99), 734 So.2d 940, 944, writ denied, 99-1777 (La.10/8/99), 750 So.2d 969.

4. “A liability insurer is the representative of the interests of its insured and the insurer, when handling claims, must carefully consider not only its own self-interest, but also its insured's interest so as to protect the insured from exposure to excess liability.” See Smith v. Audubon Ins. Co., 95–2057, p. 7-8 (La.9/5/96), 679 So.2d 372, 376, citing Holtzclaw v. Falco, Inc., 355 So.2d 1279 (La.1978) (on reh'g).

5. LSA-R.S. 22:1973

   a. Section A provides that insurer owes a duty of “good faith and fair dealing” to its insured.

   b. 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.

   d. R.S. 22:1973(B) contains a non-exclusive list of acts and omissions constituting a breach of the insurer’s duties.

      (i) Misrepresenting pertinent facts or insurance policy provisions relating to any coverages at issue.

      (ii) Failing to pay a settlement within thirty days after an agreement is reduced to writing.

      (iii) Denying coverage or attempting to settle a claim on the basis of an application which the insurer knows was altered without notice to, or knowledge or consent of, the insured.

      (iv) Misleading a claimant as to the applicable prescriptive period.

      (v) Failing to pay the amount of any claim due any person insured by the contract within sixty days after receipt of satisfactory proof of loss from the claimant when such failure is arbitrary, capricious, or without probable cause.

      (vi) Failing to pay claims pursuant to R.S. 22:1893 when such failure is arbitrary, capricious, or without probable cause.
6. Bad faith is determined on a case by case basis.

   a. The Cousins court set forth six factors to be considered in determining whether an insurer acted in bad faith: (1) the probability of the insured's liability, (2) the adequacy of the insurer's investigation of the claim, (3) the extent of damages recoverable in excess of policy coverage, (4) the rejection of offers in settlement after trial, (5) the extent of the insured's exposure as compared to that of the insurer, and (6) the nondisclosure of information between the insurer and insured. Cousins v. State Farm Mutual Automobile Insurance Company, 294 So.2d 272, 275 (La. App. 1st Cir.1973), writ denied, 296 So.2d 837 (La.1974).

   b. Courts have never held that an insured must provide evidence establishing each of the Cousins factors. In fact, courts have found insurers liable for excess judgments where only one of those factors was established, especially when the insurer failed to keep its insured informed. Gourley, 734 So.2d at 945; citing Trahan v. Central Mutual Insurance Company, 219 So.2d 187 (La. App. 3d Cir.), writ denied, 254 La. 12, 222 So.2d 66 (1969).

B. Faith Failure to Settle v. Failure to Defend

   1. Bad Faith Failure to Settle

      a. An insurer can be found liable for failing to settle a claim against its insured when its failure to do so is found to be arbitrary, capricious or in bad faith.

      b. An insurer has an affirmative duty to attempt reasonable settlement efforts.

      c. However, 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.” Smith, 95–2057 at 9, 679 So.2d at 377.

      d. Failure to settle in absence of offer from plaintiff

         i. Recently addressed by Louisiana Supreme Court in Kelly v. State Farm, 2014-1921 (La. 5/5/15), 169 So.3d 328.
ii. 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?

ANSWER = YES!

iii. The Court looked to the language of the statute finding no requirement of a firm settlement offer and instead language that imposes an “affirmative duty” on the insurer to settle.

iv. The Court also found 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.

2. Failure to Defend

a. Distinction between insurer’s failure to defend for coverage reasons and failure to adequately defend the interests of the insured.

b. Breach of duty to handle claim in good faith and put interests of insured ahead of insurer (Cousins factors).

c. Defense Duties of the Insurer:

i. Competently represent the interests of the insured

ii. Investigate the loss

iii. Keep the insured informed of pertinent developments in the case

iv. Resolve the case in good faith to protect the insured from excess exposure

v. Avoid prejudicing the insured by timing of withdrawal from the case

III. THE EXCESS CARRIER’S RIGHT TO RECOVER

A. Direct Duty

2. Therefore, excess carrier has no right to recover directly from primary carrier for actions alleged to have caused damage to excess carrier.

B. Subrogation

1. *Great Southwest v. CNA, supra.*

   a. In *Great Southwest*, the Louisiana Supreme Court held that excess liability insurer became conventionally and legally subrogated to insured's right against primary insurer when excess insurer performed obligation that primary insurer owed insured due to primary insurer's failure to perform in good faith (i.e. excess carrier satisfied excess judgment).

      i. Court relied on principles of solidary liability (“It also seems clear that Transportation [primary insurer] and Great Southwest [excess insurer] were solidarily obliged to the insured to pay on its behalf the portion of the judgment in excess of the primary policy limits”).

      ii. The essential elements of a solidary obligation are that the obligors are obliged to the same thing, that each is liable for the whole performance, and that the payment by one relieves the others of liability toward the obligee. La.C.C. art. 1794

      iii. Transportation's obligation arises from its legal obligation to perform its contractual duties in good faith and to respond in liability for all damages that are a direct consequence of its bad faith failure to perform. Great Southwest's obligation, on the other hand, arises from its agreement to pay damage awards against the insured in excess of Transportation's primary policy limits.

      iv. If the excess insurer is to recover from the primary insurer for acts which make the excess insurer's contract and liability more burdensome, it must do so by asserting the insured's rights after becoming subrogated to them or after acquiring them through assignment.

      v. In a proper case, it may be possible for the excess carrier to recover directly from the primary insurer for damage caused by an abuse of right.
vi. The Court held that Transportation should be liable for reimbursement of the whole debt to Great Southwest because its bad faith failure to perform caused the excess judgment and under the circumstances it should be considered “the principal obligor.” *Id.* at 969.

**Conventional Subrogation** - An obligee who receives performance from a third person may subrogate that person to the rights of the obligee, even without the obligor's consent. That subrogation is subject to the rules governing the assignment of rights.

**Legal Subrogation** – Subrogation takes place by operation of law in favor of an obligor who pays a debt he owes with others or for others and who has recourse against those others as a result of the payment.

*Great Southwest* left open the question of whether an excess insurer can assert a subrogation claim in the absence of an excess judgment in the underlying lawsuit…


   a. **Holding of Great Southwest** recognized by U.S. Fifth Circuit

   “This was, for the first time, an authoritative decision that subrogation is available to the excess insurer where it has made payment on behalf of its insured. In such a circumstance, the excess insurer will be able to recover from the primary insurer for the primary insurer's bad faith failure to settle the case within the primary limits, where such failure resulted in the excess judgment or compromise.” (emphasis added).

   b. **Essential elements of subrogation claim:**

      i. The elements of the subrogation claim are (1) bad faith (by the primary insurer) and (2) payment (by the excess insurer).

   c. **Claims against outside counsel**

      i. Outside law firm representing insured on behalf of primary insurer could not be held independently liable to excess insurer, which was suing both primary insurer and law firm for breach of duty to adequately represent insured.

      ii. No privity of contract with excess insurer.

   a. Primary carrier tendered policy limits shortly before trial. Excess carrier settled for $4 million in exchange for a complete release of the insured.

   b. U.S. Fifth Circuit certified question to the Louisiana Supreme Court:

      i. Does the primary insurer owe a duty to the excess insurer similar to the duty it owes its insured, to act reasonably and in good faith?

      The Louisiana Supreme Court answered the certified question as follows:

      We answer the question in the negative. The reasons for our decision are stated in *Great Southwest Fire Ins. Co. v. CNA Ins. Co.*, 557 So.2d 966 (La.1990), which was argued, considered and decided contemporaneously with this certified question. *Gibbs v. Liberty Mut. Ins. Co.*, 557 So. 2d 972 (La. 1990).

   c. *Gibbs* court recognizes subrogation claim:

      i. The [Great Southwest] court did, however, permit the excess insurer to seek recovery against the primary insurer to the extent the excess insurer was subrogated to the rights of the insured.

   d. Excess insurer stipulates that it has no subrogation claim (for some reason)

      i. “The parties concede in this case that the insured (Cummins) had been fully released and thus had no liability to which the excess carrier could be subrogated. Thus, as plaintiffs concede, the negative answer to the certified question is fatal to plaintiffs' action.”

Note: *Gibbs* became very important in the RSUI case discussed below.

**IV. RSUI v. AMERICAN STATES**

**A. The Underlying Litigation**

The underlying litigation was a personal injury suit entitled *Stacia Barrow v. Ameraseal, LLC and Lamar Thomas* in the 18th JDC for the Parish of West Baton Rouge. The suit arose out of an intersectional collision on a two lane state highway. Plaintiff struck the rear corner of the left-turning Ameraseal flat-bed truck just before the truck cleared the intersection. Plaintiff alleged a traumatic brain injury and severe low back injury requiring implantation of a spinal cord stimulator. She retained several experts to support her claims. RSUI did not receive notice of the suit until just before the close of discovery. The case was ultimately settled by American and RSUI.
B. RSUI’s Subrogation Claim

After its excess settlement, RSUI filed suit against American in the Eastern District of Louisiana alleging American failed to properly defend the underlying lawsuit. American moved for summary judgment on several grounds. The district court granted American’s motion holding that an excess judgment in the underlying litigation is a pre-requisite to the excess insurer’s subrogation claim against the primary insurer. RSUI appealed.

C. RSUI’s First Appeal to the U.S. Fifth Circuit

a. Sole Issue: Whether an excess judgment in the underlying lawsuit is required for an excess carrier to assert a subrogation claim and recover its excess settlement payment from a primary carrier.

ANSWER: NO!

b. Excess carrier can recover from primary carrier for acts which make its contract and liability more burdensome.

c. Excess carrier must prove bad faith and causation.

i. Causation = that the acts or omissions of the primary carrier increased the amount required to settle the case beyond the primary policy limit.

ii. But by how much?

d. Case remanded to district court for further proceedings.

D. Trial

a. 3 day bench trial

b. Court ruled as follows:

i. Assumed for purposes of its analysis that American acted in bad faith

ii. Settlement document American asserted was a Gasquet release was ambiguous but ambiguity resolved by the testimony of the attorneys involved in the settlement

iii. Gasquet release fatal to RSUI’s subrogation claim: RSUI is subrogated to nothing!

iv. Even if no Gasquet, RSUI still did not prove causation
E. Second Appeal to U.S. Fifth Circuit
   a. Judgment Affirmed
   b. Court of Appeal did not reach Gasquet/subrogation issue
   c. Held that failure to prove causation was a factual finding subject to clear error review and declined to reverse

F. Takeaway
   a. What else could RSUI have shown?
   b. Does the excess carrier have to “retry” the underlying litigation?
   c. Importance of an offer within policy limits in establishing causation
   d. Role of Staff Counsel
      i. In the underlying case, the insured was represented by staff counsel for much of the litigation. This is significant because any negligence or substandard conduct of the attorney could be imputed to American, as staff counsel is an employee of the insurer. American argued that it could not be held liable for the independent legal decisions made by an attorney in the defense of the insured.
      ii. No clear ruling, but could be implied from holding.
   e. Gasquet Release (Discussed below).

V. THE ROLE OF THE GASQUET SETTLEMENT

A. What is it?
   - A Gasquet settlement or release takes its name from Gasquet v. Commercial Union Ins. Co., 391 So.2d 466 (La. App. 4 Cir. 1980).
   - Accepted practice among Louisiana attorneys and courts.
   - Typically used when there is exposure beyond primary policy limit and insurer wants to settle for policy limit, or less, and tender defense to excess carrier.
   - Advantage to insurer is that they are completely dismissed and no longer responsible for defense costs.
   - Advantage to insured is complete protection from personal liability.
B. How to confect?

- Insurer is completely released and dismissed.
- Insured is released except to the extent of collectible insurance afforded by an excess policy, with the insured to remain in the case as a nominal defendant only (will never have personal or financial exposure – this is key!)
- Why does insured have to remain as nominal defendant?
- The Louisiana Direct Action Statute generally requires the insured to be a party to the case in order for the plaintiff to pursue the insured’s insurance coverage
- Primary insurer permitted to settle for less than policy limit
- But excess carrier gets credit up to amount of primary policy limit
- Be mindful of cooperation clause in excess policy and timely notice to excess carrier – don’t want excess carrier to deny coverage to insured

C. Implications of the RSUI Ruling

- RSUI was case of first impression
- No ruling from U.S. Fifth Circuit on effect of Gasquet release on excess insurer’s subrogation claim
- But district court ruling is problematic for excess carriers hoping to assert subrogation claims against primary carriers where there is a Gasquet release
- Excess carriers could find themselves subrogated to nothing
- Gasquet release is now an even more attractive exit strategy
- It is clear that excess carriers can now assert subrogation claims against primary carriers even in absence of excess judgment in underlying lawsuit
- Does having an excess judgment make burden of proof easier?
- Will the RSUI ruling increase litigation between insurers?
- Primary carriers should timely notify excess carriers of claims
- Keep insured informed of all significant developments in case