IADC COMMITTEE NEWSLETTER

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IN THIS ISSUE

In this article, Mr. Weiss discusses a case pending before the Washington Supreme Court involving the liability of claims adjusters for bad faith. Although the Court of Appeal interpreted various Washington statutes to allow for such liability, it is presently up on review. The article discusses the ramifications of this decision both in Washington and beyond.

Bad Faith Personal Liability of Claims Adjusters Arising Out of Claims-Handling Conduct

ABOUT THE AUTHOR

Bryan M. Weiss is a Partner and Co-Chair of Murchison & Cumming's Insurance Law Practice Group in San Francisco, California. He specializes in providing coverage advice to insurers and representing insurers in declaratory relief and bad faith actions, as well as handling appeals in insurance-related matters. Mr. Weiss' expertise includes intellectual property and Coverage B coverage matters, first party property matters, and coverage issues arising under general and professional liability policies. He can be reached at bweiss@murchisonlaw.com.

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Bryan D. Bolton
Vice Chair of Newsletters
Funk & Bolton
bbolton@fblaw.com

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w: www.iadclaw.org p: 312.368.1494 f: 312.368.1854 e: mmaisel@iadclaw.org

A recent decision from the Court of Appeals in the State of Washington, *Keodalah v. Allstate Ins. Co.*, 413 P.3d 1059 (Wash. 2018) ("*Keodalah*") has sent "shock waves within the claim industry[1]" by holding that individual insurance adjusters can be held liable for "bad faith" with respect to their conduct in handling a claim, in addition to possible liability under the state's consumer protection statute. While *Keodalah* has been accepted for review by the Washington Supreme Court, it is nevertheless an important decision that insurance practitioners should follow. This article will address that decision, as well as decisions in other jurisdictions addressing this issue.

Bad Faith Principles in General

In order to put the *Keodalah* decision in proper perspective, it is necessary to briefly examine the principle of insurance bad faith in general.

A policy of insurance, while certainly invested with special features, is nevertheless a contract and is subject to the same principles of contractual interpretation applicable to "ordinary" contracts.[2] Yet, "every contract imposes on each party a duty of good faith and fair dealing in its performance and its enforcement.[3]" This includes, of course, contracts of insurance. Thus it has been stated that "[i]n every insurance contract there is an implied covenant of good faith and fair dealing that neither party will do anything which will injure the right of the other to receive the benefits of the agreement.[4] The breach of that covenant is coined "bad faith," which in many jurisdictions gives rise to tort remedies, in addition to damages for breach of the insurance contract.

However, such bad faith remedies nevertheless are anchored in contract since a breach of the covenant of good faith and fair dealing cannot exist without an underpinning contract.[5] It is for this reason that courts have struggled with the notion of imposing bad faith liability on a stranger to the contract, such as the insurance adjuster handling the insurance claim. The California Supreme Court in *Gruenberg*, *supra* at 1042, held that "[w]here non-insurer defendants are not parties to the insurance agreement

[1] See "*The Impact of the Keodalah Decision on Insurers, Adjusters*", https://www.claimsjournal.com/news/west/2019/01/02/288527.htm

[2] *Rohlman v. Hawkeye-Security Ins. Co.*, 502 NW2d 310 (Mich. 1993), quoting 12A Couch, *Insurance*, 2d (rev ed), § 45:694, pp 331-332.

[3] Restatement (Second), Contracts, § 205

[4] *Gruenberg v. Aetna Ins. Co.*, 510 P.2d 1032 (Cal. 1973)

[5] See, e.g., *Guz v. Bechtel National, Inc.*, 8 P.3d 1089 (Cal. 2000): "The covenant of good faith and fair dealing, implied by law in every contract, exists merely to prevent one contracting party from unfairly frustrating the other party's right to receive the benefits of the agreement actually made. The covenant thus cannot ' " 'be endowed with an existence independent of its contractual underpinnings.' " ' It cannot impose substantive duties or limits on the contracting parties beyond those incorporated in the specific terms of their agreement."

they are not, as such, subject to an implied duty of good faith and fair dealing. . . . The insurer's agents are not parties to the insurance contract and are not subject to the implied covenant of good faith and fair dealing."

Thus, for "common law" bad faith, in which the covenant of good faith and fair dealing is necessarily tied to a contractual relationship between the parties, it would seem that there should be no cause of action against an individual adjuster who was not a party to the insurance contract. But the result may be different in jurisdictions, like Washington, which have a statutory basis for bad faith claims. It is against this backdrop that we turn to the *Keodalah* decision.

The *Keodalah* Decision

The facts in *Keodalah* arose out of a traffic accident involving the insured, Keodalah, and the driver of an uninsured motorcycle. After Keodalah had stopped at a stop sign in his truck and began moving into the intersection, he was struck by the motorcyclist. According to the police report and witnesses, the motorcycle had been traveling at an excessive speed and was "cheating" between cars in the lanes at the intersection. There was also no evidence that Keodalah had been using his cell phone at the time of the accident. The police report placed the sole blame for the accident on the uninsured motorcyclist.

Keodalah then filed a UIM claim with his insurer, Allstate, and promptly asked for the $25,000 policy limit. Allstate rejected that demand and instead offered $1,600, asserting that Keodalah was 70 percent at fault. Keodalah asked Allstate to explain its position and in response, it increased its offer to $5,000. Keodalah then filed suit against Allstate on his UIM claim. In that suit, the adjuster claimed that Keodalah had run the stop sign and was on his cell phone, but later admitted that was not true. The insured again demanded the $25,000 policy limit, to which Allstate offered $15,000. The case proceeded to a jury trial, with the jury finding the motorcyclist to be 100 percent at fault and awarding Keodalah the sum of $108,868.20.

Keodalah then filed a second lawsuit against Allstate and the individual adjuster who handled the UIM claim, this time including causes of action for insurance bad faith and violation of the state's Consumer Protection Act ("CPA.") The trial court dismissed that part of the suit which named the adjuster as a defendant, while seeking discretionary review in the Court of Appeals.

In its decision filed on March 26, 2018, the Court of Appeals of Washington, Division One, reversed the trial court's decision with respect to liability of the individual adjuster and held that under both the state's bad faith statute (*RCW 48.01.030)* and the CPA (*RCW 19.86.020*,) the adjuster could be held liable for her claims-handling related conduct. The Washington Supreme Court accepted review of this decision on September 5, 2018 and it remains pending.

As noted above, there were two separate grounds for upholding a claim against the individual adjuster: (1) the state's statutory bad faith scheme; and (2) the state's CPA.

Bad Faith

Washington's bad faith statute, *RCW 48.01.030*, provides as follows:

> "The business of insurance is one affected by the public interest, requiring that all persons be actuated by good faith, abstain from deception, and practice honesty and equity in all insurance matters. Upon the insurer, the insured, their providers, and their representatives rests the duty of preserving inviolate the integrity of insurance."

The court noted that the statute applies to any "person" who violates its terms and that the adjuster was a "person." Thus, "under the plain language of the statute, she had the duty to act in good faith. And she can be sued for breaching this duty." (*Keodalah*, 413 P.3d at 1061.) In part, the court relied on prior decisions holding that third party claims adjusting companies constituted "persons" within the meaning of the statute. It rejected Allstate's argument that there should be a distinction made between such third party corporate entities and an individual sued because of her claims handling activities, holding "[t]he duty of good faith applies equally to individuals and corporations acting as insurance adjusters." (*Id.* at 1062.) Lastly, the court rejected the adjusters argument that she cannot be held liable because she was simply acting within the scope of her employment, holding that the statute extends to persons and that "Smith cannot avoid personal liability for bad faith on the basis of her employment." (*Id.* at 1063.)

The CPA

The court next turned its attention to the CPA, which prohibits "[u]nfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce.[6]" Allstate argued that prior decisions by Washington courts have required the parties to have a contractual relationship in order for the CPA to apply. However, that argument had previously been rejected by the Washington Supreme Court in *Panag v. Farmers Ins. Co. of Washington,* 204 P.3d 885 (Wash. 2009.) The *Keodalah* court indicated that it was bound by this decision. (*Keodalah*, 413 P.3d at 1064.) Ultimately, the court held that "Keodalah need not show the existence of a contractual relationship with [the adjuster] to establish a CPA claim against her." (*Id*. at 1065.)

Based on the above results, the court reversed the trial court's ruling and remanded the case back to the court for further proceedings. As noted above, this

[6] *RCW 19.86.020*

decision has been accepted for review by the Washington Supreme Court.

Commentary on the *Keodalah* Decision

One question that must be asked is what purpose is there for including the individual adjuster as a defendant in a bad faith suit given that the insurer itself is also a defendant and the entity that will ultimately satisfy any judgment. Commentators have identified a few reasons behind this strategy. First, naming an individual adjuster as a defendant may defeat diversity jurisdiction, thereby thwarting removal to federal court which is seen as more insurer-friendly than state courts. Second, it may create leverage in settlement negotiations by allowing a policyholder counsel to "remind" the adjuster that he or she can be named as a defendant in a bad faith suit. Third, a suit naming both the adjuster and the company may require the company to retain separate counsel for the defense of the adjuster in order to avoid a conflict, thereby increasing defense costs and creating another leverage factor for settlement negotiations.

Given the fact that the adjuster is likely to be indemnified by the company for any bad faith judgment, should the adjuster really be concerned if he or she is named as a defendant? According to Kevin Quinley of Quinley Risk Associates, the answer is "yes.[7]" Most adjusters do not have the "deep pockets" to satisfy a large bad faith judgment should it come to that. The adjuster would have to disclose that he or she is a party to a lawsuit in any applications for a loan or membership in organizations. And it may be something that ends up in the adjuster's personnel file, thereby impacting his or her advancement within the company or hiring prospects at another company. So yes, the fear is real, according to Mr. Quinley.

Looking Beyond the *Keodalah* Decision

There is no question that should the *Keodalah* decision be affirmed by the Washington Supreme Court, persons adjusting claims in the State of Washington will be faced with this heightened liability. But is this a decision with a national impact? Perhaps not. It must be recalled that the *Keodalah* decision is based on the interpretation of two state statutes that may be unique to the State of Washington. The "bad faith" statute, on its face, extends to "persons" who fail to adjust claims in "good faith." Likewise, there is nothing in the state's CPA statute that limits its reach to corporate entities and not individuals. Thus, to some degree, the court's decision is a natural and logical interpretation of the statute leaving it to the Legislature to address any inequities occasioned by the statutory language. Missing from the *Keodalah* decision is any extra-statutory decree that may be felt beyond the borders of the state, especially in jurisdictions which do not have statutory bad faith laws.

[7] See n.1, *supra*.

Looking beyond *Keodalah*, courts in Kentucky have ruled that "claims adjusters fall under the category of agents engaged in the business of insurance" such that claims against the adjuster were proper[8]. Similar results were reached by courts in Montana, Texas, and Mississippi. It should be noted that these states, like Washington, have statutes regulating the handling of insurance claims which arguably extend to persons adjusting those claims. Courts in other states (e.g., Oklahoma, Indiana, Hawaii, Alabama, Tennessee, New Mexico, West Virginia, New York, and Pennsylvania) have generally held that absent conduct unrelated to general claims handling, adjusters cannot be liable for bad faith.

In California, the courts are guided by the decision in *Gruenberg v. Aetna Ins. Co.*, *supra,* holding that an adjuster cannot be held liable for contractual-based bad faith. However, at least one court has held that an adjuster can be held liable for the separate and independent torts of negligent misrepresentation and intentional infliction of emotional distress.[9] In *Bock*, the court described an adjuster's behavior in adjusting a first party property claim "appalling," including altering the scene of the damage prior to taking pictures, speaking derogatorily to the insured, misrepresenting the terms of the policy and conspiring with an unlicensed contractor to create a false report. The court had no difficulty finding that the insured had at least plead tort causes of action against the adjuster beyond contractual bad faith.

Lastly, the Supreme Court of Iowa has recently held that under Iowa law, a common law cause of action for bad-faith failure to pay workers' compensation benefits is not available against a third-party claims administrator of a worker's compensation insurance carrier.[10]

In conclusion, the issue of personal liability of an adjuster for bad faith remains an issue that continues to be pushed for many of the strategical reasons outlined above. The Washington Supreme Court's decision in *Keodalah* will certainly add another chapter in this saga but is not likely to be the last word.

[8] *Marsh, et al. v. Starns, et al.*, Civil Action No. 17-CI-00042 (Jessamine Cir. Ct., Mar. 27, 2017) and *Haskins v. Good, et al.*, Civil Action No. 15-CI-01122 (Fayette Cir. Ct., June 24, 2015).

[9] *Bock v. Hansen*, 170 Cal. Rptr. 3d 293 (Cal. 2014)

[10] *De Dios v. Indem. Ins. Co. of N. Am.*, 2019 Iowa Sup. LEXIS 56

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