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BAD FAITH BLOG

Kansas Insurers Are Subrogated to Their Insured's Bad Faith Claim Against the Primary Insurer Even When the Insured Had No Personal Exposure

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The excess insurer subrogated to the insured's bad faith claim was entitled to pursue its counterclaim against the primary insurer although the named insured was fully protected from excess exposure by a high/low agreement.

Stanley Miller rear-ended a car which resulted in injuries to the driver and passenger and ultimately ended up with an arbitration award against him for nearly $1.35 million. His primary insurance company, West American Insurance Company, had liability limits of $250,000 per person and $500,000 per occurrence. He had a separate umbrella policy issued to him by RLI Insurance Company. Early on West American had an opportunity to settle the claims within its liability limits. Thereafter, a tort claim was filed in Kansas City, Missouri against Miller, which was arbitrated after the parties entered into a high/low agreement which provided the recovery would only be against West American and any unknown excess insurers.

Miller lived in Kansas, had West American and RLI Insurance coverage issued to him in Kansas, and had his vehicle garaged in Kansas. Initially, RLI did not defend or otherwise represent Miller in the tort case or the garnishment action which followed.

The district court judge entered a series of orders which resulted in the dismissal of West American's multiple claims against RLI seeking a recovery for costs incurred by West American in the original actions, as well as against RLI's agent which was an independent adjusting firm. RLI counterclaimed seeking a recovery for the amounts it had paid to resolve and partially satisfy the judgment entered against Miller. RLI was subrogated to the claims of its insured, Miller. The district court granted summary judgment against RLI on grounds West American could not have been liable for the bad faith tort of the failure to settle within policy limits because the named insured, Miller, never had any personal exposure due to the high/low agreement, which had fully protected him from personal liability.

The first issue the court had to resolve was whether to apply Missouri or Kansas substantive law. The underlying litigation had been in Missouri giving Missouri courts an interest in the outcome, but the Eighth Circuit ruled that Kansas law governed after analyzing Missouri's choice of law rules. The key factors were that Miller was a Kansas resident and West American's failure to settle within policy limits would have damaged his financial interests in Kansas.

The initial settlement negotiations took place before suit was filed in Missouri. Furthermore, West American was alleged to have failed to apprise Miller of the settlement negotiations. Because Kansas had an interest in protecting individuals residing in that state driving an automobile licensed and insured and garaged in that state and protecting them from economic injury caused by the bad faith or negligent failure to settle, the Eighth Circuit ruled that Kansas law applied.

Kansas insurers have a duty to "not only to act in good faith but also to act without negligence." *Bollinger v. Nuss*, 202 Kan. 326, 449 P.2d 502, 508 (1969). Kansas requires insurers to consider settlement offers by giving "at least the same consideration to the interests of the insured as it does to its own interests." *Glenn v. Fleming*, 247 Kan. 296, 799 P.2d 79, 85 (1990). An insurer's exposure for failing to do so and failing to settle can exceed its policy limits. *Bollinger*, 449 P.2d at 508.

The Eighth Circuit noted that Kansas is like many other jurisdictions which do not recognize an independent duty of care between primary and excess insurers. The Eighth Circuit, like the Tenth Circuit before, predicted that the Kansas Supreme Court will rule that an excess insurer is subrogated to the rights of its insured in order to assert a claim that the primary insurer acted in bad faith by failing to settle a claim within its policy limits. *Ins. Co. of N. Am. v. Med. Protective Company*, 768 F.2d 315, 321 (10th Cir. 1985). The Eighth Circuit also stated that most state courts have adopted that principle, citing to *Nat'l. Sur. Corp. v. Hartford Cas. Ins. Co.,* 493 F.3d 752, 756-57 & n.2 (6th Cir. 2007). The court then followed the Tenth Circuit's lead predicting that the Supreme Court of Kansas will also adopt the "majority rule."

The Eighth Circuit addressed whether the high/low agreement, which had fully protected Miller, insulated West American from bad faith and/or negligent tort exposure to RLI. The court concluded it did not, relying upon the reasoning of the Supreme Court of Kansas in *Glenn* and *Farmers Ins. Exch. v. Schropp*, 222 Kan. 612, 567 P.2d 1359, 1369 (1977). The cases demonstrated that even in situations where the insured was insolvent (and therefore could not pay any excess claim) or where there was a covenant not to execute on the judgment against the insured, the bad faith claim against the primary insurer was not barred. The court concluded that the high/low agreement which insulated the insured from exposure was not substantially different. Accordingly, the bad faith claim could be pursued against any other carrier whose negligent or bad faith refusal to settle within policy limits resulted in an excess judgment against the insured. The court added it would be "sophistry to posit that West protected Miller from the risk created by West's earlier refusal to settle within its policy limits. Miller protected himself against most of that risk by purchasing excess liability insurance from RLI." 698 F.3d at 1076. Because the Eighth Circuit concluded that the Supreme Court of Kansas would likely allow RLI's counterclaim to proceed, it reversed and remanded the district court's grant of summary judgment to West American.

West American cross-appealed the dismissal of its claims against RLI's independent adjusting agent. The Eighth Circuit summarily affirmed most aspects of that dismissal while at the same time noting it might be appropriate for the district court to reconsider the partial summary judgment it had granted RLI on the affirmative defenses West American had raised to RLI's counterclaims. The Eighth Circuit observed that was an interlocutory order which the district court could appropriately reconsider on remand. The court also ruled that the district court had properly dismissed West American's prima facie tort claim against RLI whether analyzed under Kansas or Missouri law.

The primary lesson from this case is that whether there is excess coverage protecting an insured or not, the primary insurance carrier must act to appropriately consider and act on settlement demands and offers on behalf of claimants and keep the insured fully apprised of the settlement negotiations. Failing to do so in Kansas can expose the insurance carrier to excess liability either directly to the insured or possibly on a subrogated claim pursued by an excess carrier asserting the insured's rights

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