SANDBERG PHOENIX

BAD FAITH BLOG

# Insurer's Conduct in Investigating and Settling Claim against Insured Did Not Constitute Bad Faith

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The West Virginia Supreme Court of Appeals found an insurer, who defended and settled claims brought by downhill homeowners against its insured, a residential construction company, was not liable for first party common law bad faith or statutory bad faith as a matter of law.

*State ex rel. State Auto Property Insurance Companies v. Stucky*, -- S.E.2d -- , No. 17-0257, 2017 WL 4582607 (W.Va. Ct. Oct. 10, 2017)

State Auto Property Insurance Companies ("State Auto") issued a CGL policy to its insured, CMD Plus, Inc. ("CMD"), a residential construction company, with $1 million in policy limits. CMD contracted to build a custom home on a parcel of property uphill from and adjacent to property owned by Barry and Ann Evans ("Plaintiffs"). Plaintiffs claimed CMD was liable for damages to their home resulting from ground slippage caused by CMD's construction activities. CMD promptly notified State Auto of Plaintiffs' property damage claim. State Auto, in turn, inspected the property and investigated the claim, purportedly resulting in delay of potential settlement, increasing the amount of Plaintiffs' property damage, and a lawsuit against CMD.

After Plaintiffs sued CMD, it filed a third-party complaint against State Auto, alleging common law bad faith by its delay in resolving Plaintiffs' claim and failing to protect CMD from litigation. CMD also asserted a statutory bad faith claim premised on violations of the West Virginia Unfair Trade Practices Act ("UTPA"), W.Va. Code, 33-11-1, *et seq.*, and a breach of contract claim for failing to make insurance proceeds available.

State Auto moved to dismiss the third-party complaint twice, which was denied by the trial court both times. Eventually State Auto paid $325,000 to the Plaintiffs on behalf of CMD to settle the property damage claims and obtained a full release of CMD. Subsequently, State Auto moved for summary judgment on CMD's bad faith claims, which was denied, resulting in State Auto filing a petition for writ of prohibition contending the trial court should not permit CMD's claims to proceed.

The appellate court agreed with State Auto, concluding CMD could not maintain a first-party bad faith action against State Auto for common law and statutory bad faith and breach of contract. As to the common law bad faith claim, the court found there was no evidence State Auto failed to exercise good faith in meeting its obligations under the policy given State Auto's continued defense of CMD from Plaintiff's claims, State Auto's settlement of Plaintiffs' claim on CMD's behalf, and the lack of an adverse judgment against CMD. Essentially, the court found State Auto discharged its duties in good faith as CMD was "defended and indemnified by State Auto with respect to the lawsuit as required by the commercial general liability policy."

As to CMD's allegations of statutory bad faith arising out of violations of two subsections to the UTPA, the court determined CMD lacked standing to assert such a claim premised on subsections (9)(b)[1] and (9)(f)[2] of the UTPA. It held "the UTPA protects only the efforts *by the plaintiffs* to recover legally cognizable damages from CMD by way of State Auto's liability policy." (emphasis added). Because CMD was the insured protected by the policy, "CMD itself can make no demand that can be defended, settled or paid by State Auto," such that CMD had no standing to assert such claims.

Similarly, the court concluded CMD lacked standing to assert a breach of contract claim based on violation of subsection (9)(g)[3] because CMD, as the insured, "was entitled to two things: a defense against the liability claim of the plaintiffs and indemnification of any damages within policy limits due to the plaintiffs as a result of CMD's alleged negligent act or omission." CMD, therefore, was not entitled to any right to "recover amounts due" under the policy.

The court ultimately granted State Auto's request for prohibition, set aside the trial court's denial of State Auto's motion for summary judgment, and dismissed CMD's third-party complaint as a matter of law.

Notably, Justice Margaret L. Workman filed a lengthy dissenting opinion, joined by Justice Robin Jean Davis. The dissent found the majority permitted State Auto to employ an extraordinary writ as a substitute for appeal, which was unwarranted based on the circumstances of the case. Furthermore, the dissent found the majority used an "over-simplified approach" to resolving bad faith claims, thereby "implicitly alter[ing] the law without even enunciating a new syllabus point, suggesting that an insurer has only two duties under the commercial general liability policy—provision of a defense and indemnification—and that eventual satisfaction of those two duties precludes any recovery in a bad faith action." Rather, the dissent emphasized "[n]either the absence of an excess judgment nor ultimate settlement for policy limits is necessarily fatal to an insured's claim for bad faith." (citing cases).

The West Virginia Supreme Court of Appeals' decision in *Stucky* suggests an insurer's defense and settlement of a claim against an insured – within policy limits and without a judgment against the insured – precludes a first-party common law bad faith claim by the insured. Additionally, the opinion limits an insured's standing to bring a statutory bad faith claim grounded in violation of the UTPA. However, the dissenting opinion may open the door to additional litigation and clarification on the evidence appropriate for consideration of a first party bad faith claim against an insurer.

[1] *"Failing to acknowledge and act reasonably promptly upon communications with respect to claims arising under insurance policies."*

[2] *"Not attempting in good faith to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear."*

[3] *"Compelling insureds to institute litigation to recover amounts due under an insurance policy by offering substantially less than the amounts ultimately recovered in actions brought by the insureds, when the insureds have made claims for amounts reasonably similar to the amounts ultimately recovered[.]"*