Next Steps For Insurers After Ky. OKs Early 3rd-Party Claims

By **Jason Reichlyn** (August 29, 2023)

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Like most jurisdictions, Kentucky follows the general rule that an insurance bad faith claim cannot be maintained against an insurance company when the underlying claim is not covered by the policy.[1]

Bad faith claims are therefore susceptible to dismissal when the insurer, either on a motion to dismiss or for summary judgment, can establish the absence of coverage in the first instance. Alternatively, bad faith claims may be severed and litigated separately after coverage is definitively established by motion or trial.

Unlike many jurisdictions, however, Kentucky also permits third-party claimants to bring a cause of action for claims of bad faith.[2] Indeed, the Kentucky Supreme Court defined the cause of action in a 1993 third-party bad faith case, Wittmer v. Jones.

Given Kentucky's general limitation on bad faith claims absent coverage, a third party's ability to assert, much less prevail on, such claims seemingly would be limited if the insurer either has declined coverage or reserved its rights. When coverage has not been judicially established, may a third-party claimant bring a bad faith claim against the insurer following an underlying settlement or judgment?

On June 15, Kentucky's highest court answered this question in the affirmative in Estate of Lahoma Salyer Bramble v. Greenwich Insurance Co.[3]

The Estate of Bramble Decision

The heirs of an estate comprising natural land sued J. D. Carty Resources LLC and Anaconda Drilling of Kentucky LLC for trespassing on estate land and drilling natural gas wells, resulting in damage to the land and loss of mineral royalties.

After Carty admitted the alleged conduct, the trial court granted partial summary judgment on liability. Carty then entered an agreed judgment with the heirs that was to be satisfied by monthly installment payments paid by Carty.

Greenwich Insurance Co., which insured Carty during the relevant period, had defended Carty under a reservation of rights. Greenwich agreed to contribute toward Carty's agreed judgment but, in doing so, did not admit coverage for the alleged conduct.

When Carty defaulted on the monthly payments, the heirs sought payment from Greenwich and were granted leave to assert new claims against Greenwich for common-law bad faith and violation of Kentucky's Unfair Claims Settlement Practices Act. Greenwich moved to sever those claims from the others in the case, and the parties subsequently filed summary judgment cross-motions addressing coverage for the underlying claims.

The trial court ruled that Greenwich's policies in fact covered Carty's actions and, therefore, also covered the agreed judgment between Carty and the heirs. Greenwich timely appealed that ruling. The Kentucky Court of Appeals, however, dismissed the appeal; thus, no final determination on coverage had been established.

On remand, the trial court granted the heirs leave to amend their complaint to assert in a declaration of rights that the Greenwich policies covered their claims. Following the trial, judgment was rendered against Greenwich for compensatory and punitive damages.

Greenwich again appealed, reasserting that the bad faith claims were improper absent a final adjudication on coverage. The Court of Appeals agreed.

The Supreme Court, however, granted the heirs' motion for discretionary review and reversed, holding that its precedent does not require a final judicial determination of coverage prior to filing a third-party tort claim against an insurer.

In so holding, the Supreme Court qualified certain statements in its 2013 decision in Pryor v. Colony Insurance as a misapplication of Kentucky bad faith law to the extent they arguably required a final appellate determination of coverage.[4]

In Pryor, the Supreme Court held that a third party may only sue the tortfeasor's insurer for statutory bad faith when there is no dispute as to coverage or when coverage already is established, and that the claimant cannot establish the availability of coverage via a bad faith suit.[5]

The Supreme Court reaffirmed Wittmer's requirement that, to prevail on a bad faith claim, a third-party claimant bears the

> burden of proving the insurer (1) was obligated to pay the claim under the terms of the policy; (2) lacked a reasonable basis in law or fact for denying the claim; and (3) knew it had no reasonable basis for denying the claim or acted with reckless disregard for whether such a basis existed.[6]

Thus, the court reasoned, if the insurer's

> obligation to pay under the policy must be finally and conclusively determined prior to a third party bringing its bad faith claim, then the first element of Wittmer is rendered superfluous.[7]

Kentucky Bad Faith Litigation Going Forward

Following the Bramble decision, insurers may face more and earlier statutory bad faith claims, as third parties seek to join insurers to underlying litigation and separately assert these tort claims. Consequently, protracted litigation, including complex discovery and trial, may lead to increased costs and potentially higher settlements.

But insurers are not left without any recourse. To help prevent or resolve bad faith claims on favorable terms, insurers may consider, for example, commencing a separate declaratory judgment action to establish no coverage. This approach of course assumes that there is a genuine dispute over coverage and that a good faith basis exists to bring a separate action. Other considerations, such as local jurisdiction and venue, may also bear on this approach.

Alternatively, if an underlying settlement appears likely, a global settlement that releases all current and potential claims among the claimant, insured and insurer may be worth exploring.

If a third-party claimant manages to successfully bring bad faith claims, insurers may

consider asserting counterclaims for declaratory judgment, again with the intention of establishing no coverage by motion. Affirmative claims coupled with any prospects of early mediation, may help to reduce or minimize potential exposure.

Conclusion

Whether the Estate of Bramble decision will affect the number and timing of statutory bad faith claims remains to be seen. At the outset of any claim or underlying litigation, however, insurers should bear in mind the two general factual situations potentially giving rise to a third-party bad faith action in Kentucky:

1. Coverage is undisputed; and

2. The insured's liability to the claimant "has been reasonably established" and the insured's policy seemingly covers the underlying matter.

It is the latter situation that typically presents opportunities for bad faith exposure. By considering the approaches outlined above, insurers can be better equipped to act when the circumstances suggest that bad faith claims are likely or inevitable.

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[1] See Davidson v. Am. Freightways Inc., 25 S.W.3d 94, 100 (Ky. 2000).

[2] See State Farm Mutual Insurance Co. v. Reeder, 763 S.W.2d 116, 118 (Ky. 1988).

[3] Estate of Lahoma Salyer Bramble v. Greenwich Insurance Co., Case No. 2022-SC-0043-DG (June 15, 2023).

[4] Pryor v. Colony Insurance, 414 S.W.3d 424 (Ky. 2013).

[5] See id. at 433.

[6] See Bramble, Case No. 2022-SC-0043-DG (June 15, 2023).

[7] See id.