Personal Issues—Bad Faith Against Claims Adjusters

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Independent Adjuster Liability for Bad-Faith and Other Tortious Conduct

A Washington state case on appeal to the state’s highest court has garnered a great deal of attention in the last year. Washington’s intermediate appellate court ruled that a Plaintiff may plead a claim for bad faith and violation of the state’s Consumer Protection Act directly against the insurance company’s claims handler. Oral argument were heard before the Washington Supreme Court in February of this year and a decision is expected any time.

Even if the intermediate appellate decision is an outlier, and even though nothing is yet etched in stone in Washington state, the decision could spell trouble on the horizon if courts begin recognizing a special relationship exists between the claims handler dedicated to a specific claim and the claimant or insured.

The issue to be addressed by the Supreme Court in Keodahlah v. Allstate Ins. 413 P.3d 1059 (2018), is whether the Plaintiffs may plead a claim for bad faith and Consumer Protection Act violations directly against the Allstate adjuster, Tracey Smith. Since the Court of Appeals’ decision in Keodalah was published in March 2018, it has become more and more common for insureds to name both the insurance company and the adjuster in lawsuits alleging bad faith claims handling.

At the oral argument hearing, Allstate and the claims adjuster asserted that the only potentially available claim against an adjuster would be based on Washington’s general good faith statute and would require the Court to hold that this statute provided for an implied cause of action. They argued that an adjuster cannot be subject to a common law bad faith claim because there was no quasi-fiduciary relationship between an adjuster and insured.

In response, the insureds asserted that their claim was actually based on common law bad faith and the good faith statute provided the duty which applies to the adjuster for this claim. They argued recognizing a bad faith claim against an adjuster was necessary to prevent the insurance company from avoiding bad faith liability by
asserting that its adjuster’s offending conduct was outside the scope of the adjuster’s authority and employment duties with the insurance company.

Before *Keodolah*, other states had looked at the issue. California’s *Bock* decision was one of the first in the country to have a lasting effect on this issue and has been cited in numerous decisions upholding the right to plead an independent action against a claims handler. In *Bock v. Hansen*, 225 Cal.App.4th 215 (2014) a California appeals court considered whether an adjuster in the employ of an insurance carrier could be found individually liable for negligent misrepresentations in the handling of a claim, and ultimately ruled that such an action was viable under California law. Since the *Bock* decision, these theories have been gaining ground in other jurisdictions.

**Majority” Rule: No Adjuster Liability**

The majority of states do not impose a duty of care on individual adjusters. The “majority rule” was recognized by the Seventh Circuit Court of Appeals in *Lodholtz v. York Risk Servs. Group, Inc.*, 778 F.3d 635, 642, fn. 11 (7th Cir. 2015). The federal court predicted that if Indiana evaluated the issue of employee-adjuster liability, Indiana would follow the “majority rule” and not impose liability. The court specifically noted that the state courts of Alabama, Arizona, California, Connecticut, Florida, Louisiana, Missouri, New York, North Carolina, Oklahoma, South Carolina, Texas, and Vermont have held that a claims adjuster does not owe a duty of care to the insured. The court also noted that a federal court applied the laws of Rhode Island and reached the same conclusion.

The *Lodholtz* court did cite California’s *Bock* decision in its recitation of those states that were willing to hold that an insurance adjuster may be liable “under alternative theories.” The court did not, however, analyze the *Bock* finding of a duty personally owed under a “special relationship” theory. Nevertheless, the overriding majority rule continues to find “no duty” owed by an employee adjuster to an insured.
Adjuster Liability in Other States

California’s *Bock* decision was not the first state appellate court to permit a direct action against an adjuster. The Alaska Supreme Court ruled in *Continental Insurance Company v. Bayless and Roberts, Inc.*, 608 P.2d 281 (Alaska 1980), that an insurance adjuster could be held liable for negligence as a result of failing to investigate a claim adequately. The adjuster there argued that he owed no duty directly to the insured under his contract with the insurance company. In doing so, he relied on California cases including some of those cited in the *Bock* case. The court disagreed and determined that although he could not be held liable for bad faith, the insurance adjuster could be held liable for negligence based on a “breach of the general tort duty of ordinary care.” *Id.* at 287.

Another state that has permitted direct actions against adjusters is New Hampshire. In *Morvay v. Hanover Insurance Companies*, 506 A.2d 333 (N.H. 1986), the plaintiffs had a fire policy with Hanover. Their property was damaged by a fire. Hanover hired a third party to investigate the fire and received reports from an individual named Roberts, the third party that conducted the investigation's employee. Roberts determined that the fire was incendiary, which caused Hanover to deny the claim. The plaintiffs sued the insurer and Roberts, (along with his employer), claiming that Roberts negligently conducted the investigation leading to the denial of the claim. The court was asked to determine whether “investigative agents” of an insurance company, hired to investigate a claim, have a duty to the insured arising out of the insurer's duty of good faith and fair dealing. The New Hampshire Supreme Court noted that Roberts was not in privity with the plaintiffs but that Roberts was fully aware that that the plaintiffs could be harmed financially if Roberts performed his investigation in a negligent manner. Roberts was
also aware that there was a mutual duty of fair dealing between the insurer and insureds. Under those circumstances, the court found that the plaintiffs had stated a cause of action against Roberts (and his employer). Specifically, the New Hampshire Supreme Court held in Morvay that “the investigators owe a duty to the insured as well as to the insurer to conduct a fair and reasonable investigation of an insurance claim....” Id. at 335.

The court went on to say that the “scope of the investigators' duty must be determined in the light of their contract with the insurer.” Id. The court noted that an investigator paid only $200 for an investigation is not obligated to expend the same effort as one paid $2,000. This analysis tempers the court's application of “special duty”. It is also important this case involved a non-employee adjuster.

Other Attempts to Impose Independent Liability on Employee Adjusters

Courts have permitted other liability theories directly against insurance adjusters. Some jurisdictions permit liability but only in those circumstances in which something more than simple negligence is established. For example, in Alliston v. Omega Ins. Co., 983 F. Supp. 675, 677 (S.D. Miss. 1997), the court noted that “under Mississippi law, insurance agents and adjusters, while not liable for ordinary negligence in performing their duties on behalf of the insurers, can incur independent liability... [for]... gross negligence, malice or reckless disregard....”

New York takes a slightly different approach, noting that individual employee-adjuster liability can exist for negligent misrepresentation where an insured sustained “pecuniary loss... as a result of another's negligent misrepresentations [if]... there was either actual privity of contract between the parties or a relationship so close as to approach that of privity.” Ryan v. Preferred Mut. Ins., 38 A.D.3d 1148, 1149 (N.Y. App. Div. 2007) (alteration in original) (internal citations omitted).
More recently, both Kentucky and Texas have permitted actions against employee adjusters on a limited basis. A Kentucky federal court noted that adjusters could be held individually liable for bad faith. *Collins v. Montpelier U.S. Ins. Co.*, 2011 WL 6150583 (E.D. Ky. Dec. 12, 2011). It is noteworthy, however, that the issue remains undecided by the Kentucky Supreme Court.

Texas has limited employee-adjuster liability to a specific statutory violation known as the Deceptive Trade Practices Act. In *Barclay v. State Farm Lloyds*, 2015 WL 1408185 (S.D. Tex. Mar. 26, 2015), the court noted that Texas' statutory language “is broad enough to permit... a cause of action against an insurance agent [or adjuster] who engages in unfair or deceptive acts or practices.” *Id.* at *4 (alterations in original) (internal citation and quotes omitted). Texas differentiates between adjusters employed by insurance companies and independent adjusters. Texas will only permit a cause of action against the employee adjusters because these individuals possess the ability to make a coverage decision. The theory behind this is that the business of insurance is defined in Texas to include the investigation and adjustment of a claim. The courts have reasoned that an adjuster who services a policy for the insurer is, therefore, engaged in the business of insurance and subject to Texas' Insurance Code individually. *Gasch v. Hartford Accident & Indem. Co.*, 491 F.3d 278, 282 (5th Cir. 2007).

In Colorado, a direct action was permitted against a third-party administrator for negligent misrepresentation. The court in *Colorado Pool Systems, Inc. v. Scottsdale Insurance Co.*, 317 P.3d 1262 (Colo. App. 2013), permitted the action when the third-party administrator told the insured that there would be coverage, but the insurer later denied coverage.

**Federal Erie decisions**

Despite the “majority” rule, there have been some applications of California’s *Bock decision*, (either explicitly or based on similar reasoning), in federal courts to expand the potential of employee-adjuster liability. These extensions by federal courts have resulted in other states allowing *Bock*-type lawsuits. One particular area in which
analysis of Bock led to a potential for similar lawsuits has been when a federal court has reviewed state law applicable to the case before it.

For example in Nebraska, a federal court relied on California’s Bock decision to conclude that Nebraska might decide to recognize a similar claim. In Good Shepherd Assisted Living Corp. v. Great American Insurance Co. of New York, 2015 WL 2449161 (D. Neb. May 21, 2015), the court was reviewing a request to remand to the state court. One of the issues was whether the adjuster defendant was a “‘sham” defendant included only for purposes of destroying diversity. The defense argued that because no direct personal liability existed, the inclusion of the adjuster was fraudulent. The court disagreed, noting that the insureds were “advancing a good faith argument for expansion of the law.” Id. at *5. The court relied on Bock and noted that Nebraska could create similar liability. Furthermore, the court noted that the defendants had not provided any authority in Nebraska that absolutely precluded such a claim. Therefore, the court remanded the action. Nebraska, to date, has not voiced an opinion on this issue. Of note, however, is the fact that the adjuster was expressly noted by the insurer not to be an employee.

In Pennsylvania, a federal court also refused to remand an action based on the theory that the employee adjuster was a sham defendant. In Kennedy v. Allstate Prop. & Cas. Ins. Co., 2015 WL 4111816 (E.D. Pa. July 8, 2015), the plaintiffs had an uninsured motorist claim with Allstate. The plaintiffs alleged that the defendants improperly evaluated their claim and engaged in intentional delay, misrepresentation and fraud in processing the claim. The plaintiffs also specifically alleged that the individual adjuster defendants made affirmative misrepresentations and concealed material facts from the plaintiffs to delay the resolution of their claim. The plaintiffs claimed that the misrepresentations were intended to induce a lower settlement of the claim. The defendants removed the action to federal court, arguing that the employee-adjuster defendants were fraudulently joined for the purposes of defeating diversity jurisdiction. The plaintiffs moved to remand, contending that they had colorable claims against the employee adjusters. The court analyzed the arguments and noted that joinder of a non-
diverse defendant is fraudulent when “there is no reasonable basis in fact or colorable ground supporting the claim against the joined defendant....” *Id.* at *2.

The defendants argued that under Pennsylvania law an adjuster owes no duty of care to the insured. However, the court noted that Pennsylvania law “is silent on the question of whether there is a cause of action for negligence” against an employee adjuster arising from the handling of a claim. The court cited *Tippett v. Ameriprise Ins. Co.*, 2015 WL 1345442 (E.D. Pa. Mar. 25, 2015), in which the court dismissed a claim against an independent insurance adjuster because that federal court found it unlikely that the Supreme Court of Pennsylvania would impose a duty of care on an adjuster. However, the *Kennedy* court noted that the standard for evaluating the issue was much different because of the “no reasonable basis” standard applied to the review of the plaintiffs’ motion.

After considering the more liberal standard in evaluating a motion for remand, the court held that “there is at least ‘a possibility’ that the Pennsylvania Supreme Court... could decide that an insurance adjuster owes a duty of care to an insured....” *Kennedy*, 2015 WL 1345442 at *4. In doing so, the court specifically noted that two state supreme courts had come to similar conclusions: New Hampshire with the *Morvay* decision and Alaska with the *Continental* decision. In addition, the court pointed to the lack of “decision law” on the issue. For these reasons, the court granted the remand to state court. It is noteworthy that the court did not explicitly rely on or cite *Bock*.

In *Moun Keodalah, et al. v. Allstate Ins. Co., et al.*, No. 75731-8-I, 2018 WL 1465526 (Wash. Ct. App. Mar. 26, 2018), the court held that a policyholder may directly sue an insurance claims adjuster for insurance bad faith and violations of the Washington Consumer Protection Act (“CPA”), even if the adjuster is acting within the course and scope of his or her employment. Prior to this decision, Washington courts permitted an insurance adjuster to be named individually in cases alleging bad faith or CPA violations only if they were employed by a third party independent adjusting firm.

The underlying case which resulted in the *Keodalah* decision involved a motorcycle accident where the insured, Keodalah, was hit by an uninsured motorcyclist while both were driving. The motorcyclist died and Keodalah suffered injuries. Keodalah had UIM insurance through Allstate.

A police investigation determined that the motorcyclist was speeding and that Keodalah was not on the phone during the time of collision. Allstate’s own investigation also revealed that motorcyclist was speeding and splitting lanes at the time of the accident and that the motorcyclist’s excessive speed caused the collision.

Keodalah requested that Allstate pay its $25,000 UIM limits. Allstate denied, offering $1,600 to settle the claim based on its assessment that Keodalah was 70% at fault. After Keodalah asked Allstate to explain its basis for its position, Allstate increased its offer to $5,000.

Keodalah then sued Allstate, asserting a UIM claim. Allstate designated Tracey Smith, an Allstate insurance adjuster on the claim, as its 30(b)(6) representative. Smith claimed that Keodalah ran the stop sign and was on his cell phone, despite the fact that Allstate had the investigative reports showing the opposite. Smith later admitted that her statements were untrue.
Before trial, Keodalah rejected Allstate’s offer of $15,000 to settle the claim. The case proceeded to trial where the jury determined the motorcyclist was 100% at fault and awarded Keodalah $108,000.

Keodalah then filed suit against Allstate and Smith. Keodalah alleged IFCA violations, insurance bad faith, and CPA violations. After the trial court dismissed Keodalah’s claims against Smith, the Washington Court of Appeals granted discretionary review on two issues.

First, the court looked at whether an individual insurance adjuster may be liable for bad faith, concluding that this is permissible. It reasoned that the pertinent statute, RCW 48.01.030, required that “all persons” involved in insurance act in good faith. The term “person” was defined to include an individual. Therefore, the court determined that under the plain language of the statute, insurance representatives, as individuals, had a duty to act in good faith and could be sued if they breach that duty. The court also cited to two Washington decisions for support – one in federal district court and one in Division Three of the Washington Court of Appeals – which similarly held that the same statute unambiguously applies to corporate insurance adjusters based on the statute’s plain language. The difference in Keodalah was that the insurance adjuster was an individual adjuster employed by the insurer, while the prior cases involved third-party corporate adjusters.

The second issue was whether an individual insurance adjuster could be liable for violation of the CPA, which prohibits “[u]nfair methods of competition and unfair or deceptive acts or practices in the conduct of any trade or commerce.” RCW 19.86.020. The court answered this question in the affirmative, rejecting Smith’s argument that a contractual relationship is required in order for there to be liability under the CPA.

The court did hold that the plaintiff was foreclosed from suing the insurance adjuster under the Washington Insurance Fair Conduct Act (“IFCA”) due to the recent decision in Perez-Cristantos v. State Farm Fire & Casualty Insurance Co, 187 Wn.2d 669, 672 (2017), which held that the IFCA does not create an independent cause of action against insurers for regulatory violations.
Advantages For Claimants In Naming The Adjuster As An Individual Defendant.

- To defeat diversity.

Conventional wisdom is that state courts are better venues for plaintiffs and that federal courts favors insurance companies. So, to lessen the odds that a defendant can successfully remove the case to federal court, where the plaintiffs reside in the state as the local adjuster, the adjuster can be named as an individual defendant.

- Intimidation

Under *Keodalah*, bad faith attorneys, especially at the pre-litigation stage, can tell an adjuster, ‘You’re acting in bad faith and I’m going to sue not just your employer, but you individually.’ That threat might cause an adjuster to pause and reexamine a claim or dispute,” And some adjusters might be understandably intimidated and think twice about contesting a gray area claim that needs to be contested.

- To increase the defendant’s defense costs.

If the adjuster defendant needs separate counsel, that will increase the legal fees involved in defending a bad faith claim. The carrier or the E&O carrier for the insurance company might be paying not just one defense attorney, but two, putting more financial pressure on either the insurer or if it’s professional liability carrier to settle the claim. Adjusters are concerned because they don’t have deep pockets to pay a judgment. A pending lawsuit could have a domino effect of negative consequences for an individual adjuster. There are a number of scenarios in which individuals are required to disclose lawsuit which have brought against them personally i.e. application for a mortgage, a car loan, a home equity line of credit.

The claims handling process and the insurance company’s employee retention and recruitment could all be impacted by the decision.
Developing a plan for defeating these claims

One of the first considerations when facing a claim seeking independent liability against the claims handler is to determine whether there is a potential conflict of interest in representing both the insurance company and the insurance adjuster. If there is the potential that that conduct of the adjuster could be deemed “outside the course and scope” of his or her employment, the lawyer's ability to provide joint representation may be destroyed. However, the general basis for most of these claims relates to conduct by the adjuster that is within the course and scope of the adjusting duties. Consequently, joint representation is usually not at issue. Nevertheless, a lawyer must consider this issue and should advise both clients in writing of potential issues of joint representation before proceeding with the joint representation.

Otherwise, the defense of individual claims against an adjuster should be aggressive at the outset. The underlying problem with a Bock-style claim is that it purports to make the plaintiff's case more valuable for settlement purposes. The plaintiff will believe that having multiple defendants, including an individual employee, will make the insurance company more willing to settle the action, including potentially overpaying the settlement. Forcing the issue up front may eliminate this possibility.

Advice To Claims Handlers In Light Of The Facts Keodalah And Other Cases Finding Individual Adjuster Liability Claims Are Viable.

There are ways to reduce the chances of an adjuster being named in a bad faith

- Take reasoned liability stances. Under the Keodalah facts, no reasonable adjuster would assess liability on the part of the insured, much less 70 percent responsibility of the accident. Align your liability position and claim assessment with the facts of the case.

- Explain the basis for any settlement offer.

In Keodalah the plaintiff policyholder demanded the $25,000 UIM limit. In response, the carrier offered $1,600 based on its assessment that the insured was 70 percent at fault. And when Keodalah asked the insurance company to explain, it simply bumped the offer to $5,000. Just raising the offer from $1,600 to $5,000 doesn’t really explain the insurance company’s evaluation. Absent any explanation, absent any compelling rationale, an increased over with no explanation can be characterized as “low balling” which is the most often cited “bad faith tactic” of insurers.