

# Kentucky Would Reject Reverse Bad Faith Sixth Circuit Predicts

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**Summary:** State Auto sued Hargis contending she intentionally set fire to her house. She counterclaimed with common law and statutory bad faith claims. State Auto thereafter amended its Complaint alleging damages for insurance fraud as well as a common law claim for reverse bad faith. The district court granted Summary Judgment allowing the insurance fraud claim, but denied the claim for reverse bad faith. The Sixth Circuit affirmed that ruling predicting Kentucky would not recognize a common law tort claim for reverse bad faith.

State Auto Property v. Hargis

State Auto insured Lori Hargis' home in Henderson, Kentucky when it burned to the ground on December 9, 2007. She filed an insurance claim for approximately \$866,000. After State Auto paid out more than \$425,000, Hargis was indicted, admitted she presented a fraudulent insurance claim, was sentenced and ordered to pay restitution. Her claims for common law bad faith and for recovery under Kentucky's Consumer Protection Act and Unfair Claims Settlement Practices Act were denied. The district court judge further dismissed State Auto's claim for reverse of bad faith.

This Sixth Circuit initially ruled there was no reason for it to certify to the Supreme Court of Kentucky the question of whether that court would recognize a reverse bad faith claim. Instead, it ruled it could adequately predict how that court would rule.

Kentucky recognizes four separate categories of bad faith claims, which an insured can assert against an insurance company. There are two common law tort theories for an insurance company's breach of the duty of good faith (both first party and third party) and an assignment of a bad faith claim to a third party. In addition, there are two statutory causes of action, one, under the Kentucky Consumer Protection Act and another under the Kentucky Unfair Claims Settlement Practices Act. Under any of those four bad faith theories, the insured has to first prove that the insurance company was obligated to pay the claim; second, the insurer lacked a reasonable basis in law or fact for denying the claim; and finally, that the insurance company knew it had no reasonable basis to deny the claim or acted with reckless disregard as to whether such a basis existed. *Wittmer v. Jones*, 464 S.W.2d 885, 890 (KY 1993). The Sixth Circuit noted that there can be no bad faith claim asserted against a Kentucky insurance company when it has no obligation under the policy.

The Sixth Circuit found it compelling that the Supreme Court of Kentucky had rejected an insurance company's challenge to the Kentucky Unfair Claim Settlement Practices Act on grounds that the rights or remedies were not the same for insurers as they were for insureds. In light of that rejection, the Sixth Circuit believed it unlikely that the Kentucky Supreme Court would find similar reciprocal rights under a common law bad faith claim. Furthermore, when rejecting the lack of reciprocal statutory claim, the court had noted that insureds are in need of protection while insurance companies are not.

The Sixth Circuit also noted other jurisdictions which have considered whether to recognize a reverse bad faith claim had all rejected the request. Those rulings came from the Supreme Courts of Ohio, Iowa, and Oklahoma. In addition, the California Court of Appeals had rejected such a tort claim for the breach of the covenant of good faith and fair dealing. Finally, the District Court for the Virgin Islands had similarly rejected such a claim.

Finally, the court rejected State Auto's argument that it would be unjust for Kentucky law to fail to recognize a bad faith claim because such a rejection would "allow [the insured] Hargis to escape the consequences of her intentional fraudulent act." The Court noted the insured had not escaped those consequences both in view of her criminal conviction and the order of restitution, as well as State Auto succeeding on its civil fraud action against her. For all of those reasons the Sixth Circuit predicted "that the Kentucky Supreme Court would reject State Auto's invitation to adopt a common law tort claim for reverse bad faith by an insured."

Based upon the Sixth Circuit's ruling regarding Kentucky law as well as the rejection of similar invitations by the courts in Ohio, Iowa, Oklahoma, California, and the Virgin Islands dating back to 1992, it seems unlikely that any court is likely to recognize a reverse bad faith claim any time soon.

By Anthony L. Martin

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