Insurance Bad Faith: Maryland

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CAUSES OF ACTION

Is there a statutory basis for an insured to bring a bad faith claim?

A claim against first-party insurers for failure to act in good faith exists under Md. Code Ann., Cts. & Jud. Proc. §3-1701. The statutory cause of action for failure to act in good faith "applies only to first-party claims under property and casualty insurance policies issued, sold, or delivered in the State [of Maryland]." Md. Code Ann., Cts. & Jud. Proc. §3-1701(b). Some federal decisions and a Maryland Insurance Administration ("MIA") decision have construed the term "first-party claims" in the statute to include claims by an insured against its own insurer for defense and indemnity costs. *Whiting-Turner Contracting Co. v. Liberty Mut. Ins. Co.*, 912 F. Supp. 2d 321, 339 (D. Md. 2012) (*dicta*); *Eyes for You, LLC v. Zurich Am. Ins. Co.*, Case No. 27-1001-12-0001 at 6–7 (Md. Ins. Admin. May 9, 2012). This broad construction of the term "first-party" claims has not been tested in the Maryland appellate courts.

Before seeking relief pursuant to Section 3-1701, the insured must first exhaust its administrative remedies before the MIA pursuant to Md. Code Ann., Ins. §27-1001. However, if a case fits within one of the following exceptions, it may be filed in court and is not subject to the jurisdiction of the MIA: (1) a small claim within the jurisdiction of a Maryland District Court, (2) where the insurer and insured agree to waive the MIA requirement; or (3) where a claim involves a commercial insurance policy with policy limits that exceed $1,000,000. *Lanham Servs. Inc. v. Nationwide Prop. & Cas. Ins. Co.*, No. PWG-13-3294, 2014 WL 2772227, *4 (D. Md. June 18, 2014) (permitting insured to aggregate limits for each building insured under policy in order to meet $1,000,000 exception even though claim itself was only for $637,100).

Whether an insurer acted in good faith involves assessing the "totality of the circumstances" including:

> (1) efforts or measures taken by the insurer to resolve the coverage dispute promptly or in such a way as to limit any potential prejudice to the insureds; (2) the substance of the coverage dispute or the weight of legal authority on the coverage issue; and (3) -the insurer's diligence and thoroughness in investigating the facts specifically pertinent to coverage.

Cecilia Schwaber Trust Two v. Hartford Acc. & Indem. Co., 636 F. Supp. 2d 481, 487 (D. Md. 2009) (citation omitted).

Can a third party bring a statutory action for bad faith?

A third party may not bring a bad faith claim unless specifically authorized in the policy. *See, e.g.*, *Bean v. Allstate*, 285 Md. 572, 577, 403 A.2d 793, 796 (1979). However, an action for bad faith may be assigned. *Med. Mut. Liab. Ins. Soc'y of Md. v. Evans*, 330 Md. 1, 25, 622 A.2d 103, 114 (1993).

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Is there a common law cause of action for bad faith?

The sole cause of action for third-party bad faith thus far recognized by the Maryland appellate courts is one for wrongful refusal to settle within policy limits. *Kremen v. Md. Auto. Ins. Fund*, 363 Md. 663, 675, 770 A.2d 170, 177 (2001); *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 259, 725 A.2d 1053, 1061 (1999).

There is no common law cause of action for first-party bad faith in Maryland. *Johnson v. Federal Kemper Ins. Co.*, 74 Md. App. 243, 246, 536 A. 2d 1211, 1212–13 (1988), *cert. denied*, 313 Md. 8, 542 A.2d 844 (1988); *Harris v. Keystone Ins. Co.*, Civil No. CCB-13-2839, 2013 WL 6198160, *2 (D. Md. Nov. 26, 2013) (unreported).

What cause of action exists for an excess carrier to bring a claim against a primary carrier?

An excess carrier may bring an action for bad faith against a primary liability carrier based upon equitable subrogation. *Fireman's Fund Ins. Co. v. Cont'l Ins., Co.*, 308 Md. 315, 320–21, 519 A.2d 202, 205 (1987) (court did not decide whether direct action for bad faith lies).

What causes of action for extracontractual liability have been recognized outside the claim handling context?

None.

DAMAGES

Are punitive damages available?

In Maryland, third-party bad faith is a tort. *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 262–63, 725 A.2d 1053, 1063 (1999). In a tort action, a plaintiff may recover punitive damages only if he or she proves by clear and convincing evidence that the defendant acted with actual malice. *Owens-Illinois, Inc. v. Zenobia*, 325 Md. 420, 460, 601 A.2d 633, 652–53 (1992). The same standard applies in both non-intentional and intentional torts. *Ellerin v. Fairfax Sav., F.S.B.*, 337 Md. 216, 228, 240, 652 A.2d 1117, 1123, 1129 (1995).

Punitive damages are not available in first-party failure to act in good faith actions under Md. Code Ann., Cts. & Jud. Proc. §3-1701.

Are attorney's fees recoverable?

Attorney's fees are not recoverable in third-party bad faith cases. *See Kremen v. Md. Auto. Ins. Fund*, 363 Md. 663, 682–83, 770 A.2d 170, 181–82 (2001).

Attorney's fees are recoverable in first-party failure to act in good faith cases. If the MIA finds that an insurer failed to act in good faith, the insured may recover its reasonable attorney's fees, which may not exceed one-third of the insured's actual damages. Md. Code Ann., Ins. §27-1001(e).

Although not a bad faith claim, attorney's fees may be recovered by a prevailing insured in an action to enforce the insurer's duty to defend. *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 264, 725 A.2d 1053, 1064 (1996); *Bankers & Ship. Ins. Co. v. Electro Enter.*, 287 Md. 641, 648, 415 A.2d 278, 282 (1980); *Govt. Emps. Ins. Co. v. Taylor*, 270 Md. 11, 22, 310 A.2d 49, 55 (1973).

Are consequential damages recoverable?

The sole measure of damages in a wrongful refusal to settle case is the difference between a bona fide judgment and the policy limits. *Kremen v. Md Auto. Ins. Fund*, 363 Md. 663, 675, 770 A.2d 170, 177 (2001); *Med. Mut. Liab. Ins. Soc'y of Md. v. Eva ns*, 330 Md. 1, 25, 622 A.2d 103, 114 (1993).

A successful plaintiff in a failure to act in good faith case can recover actual damages, expenses, litigation costs, interest on those expenses and costs and reasonable attorney's fees. Md. Code Ann., Ins. §27-1001(e)(2)(ii); Md. Code Ann., Cts. & Jud. Proc. §3-1701(d)(1)–(2). *See also Cecilia Schwaber Trust Two v. Hartford*

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Acc. & Indem., Co., 636 F. Supp. 2d 481, 484–85 (D. Md. 2009).

Can a plaintiff recover damages for emotional distress?

No.

ELEMENTS OF PROOF

What is the legal standard required to prove bad faith in a first-party case?

The plaintiff must prove that the insurer failed to act in good faith in determining coverage or in determining the amount of payment for a first-party claim. Md. Code Ann., Cts. & Jud. Proc. §3-1701(d). "Good faith" is defined as "an informed judgment based on honesty and diligence supported by evidence the insurer knew or should have known at the time the insurer made a decision on a claim." *Id.* §3-1701(a)(4).

The MIA's decision must contain the following five findings:

1. whether the insurer is obligated under the applicable policy to cover the underlying first-party claim;
2. the amount the insured was entitled to receive from the insurer under the applicable policy on the underlying covered first-party claim;
3. whether the insurer breached its obligation under the applicable policy to cover and pay the underlying covered first-party claim, as determined by the Administration;
4. whether an insurer that breached its obligation failed to act in good faith; and
5. the amount of damages, expenses, litigation costs, and interest, as applicable and as authorized under paragraph (2) of this subsection.

Md. Code Ann., Ins. §27-1001(e)(1)(i).

What is the legal standard required to prove bad faith in a third-party failure to settle a claim?

Where there is an excess verdict, an insurer who unreasonably refused to settle within policy limits when there was an opportunity to do so is liable in bad faith. *State Farm Mut. Auto. Ins. Co. v. White*, 248 Md. 324, 333–34, 236 A.2d 269, 274 (1967). The obligation to act in good faith requires an insurer's refusal to settle a claim within policy limits to be an informed judgment based upon honesty and diligence. *Id.* at 333, 236 A.2d at 273. The insurer's negligence is one of several factors relevant to a determination of whether the insurer acted in good faith. Other factors include:

> the severity of the plaintiff's injuries giving rise to the likelihood of a verdict greatly in excess of the policy limits; lack of proper and adequate investigation of the circumstances surrounding the accident; lack of skillful evaluation of plaintiff's disability; failure of the insurer to inform the insured of a compromise offer within or near the policy limits; pressure by the insurer on the insured to make a contribution towards a compromise settlement within the policy limits, as an inducement to settlement by the insurer; and actions which demonstrate a greater concern for the insurer's monetary interests than the financial risk attendant to the insured's predicament.

Id. at 332, 236 A.2d at 273.

Maryland does not recognize a cause of action for bad faith refusal to settle where the insurer has erroneously denied its duty to defend. *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 266–67, 725 A.2d 1053, 1065–66 (1999).

Is there a separate legal standard that must be met to recover punitive damages?

An action for bad faith in Maryland is a tort. *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 266, 725 A.2d 1053, 1065 (1999). Thus, punitive

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damages are available only if the plaintiff can prove actual malice. *OwensIllinois v. Zenobia*, 325 Md. 420, 460, 601 A.2d 633, 652–53 (1992).

Does a bad faith claim require evidence of a pattern or practice of unfair or deceptive conduct?

No.

On what issues is expert evidence required to establish bad faith?

There are no reported Maryland appellate cases requiring expert testimony to establish bad faith. Expert testimony is admissible in Maryland, even on ultimate issues, if it will assist the trial of fact. Md. Rules 5-702, 5-704. Expert testimony was admitted, for example, in *Kremen v. Md. Auto. Ins. Fund*, 363 Md. 663, 770 A.2d 170 (2001).

On what issues is expert evidence precluded?

There are no reported Maryland appellate cases precluding expert testimony on any issue in a bad faith case. Generally, experts are not permitted to testify as to their interpretation of the policy. *Truck Ins. Exch. v. Marks Rentals, Inc.*, 288 Md. 428, 434, 418 A.2d 1187, 1190 (1980). However, expert testimony has been permitted concerning the complexity of certain policy provisions. *Johnson & Higgins of Pa., Inc. v. Hale Shipping Corp.*, 121 Md. App. 426, 446–47, 710 A.2d 318, 328–29 (1998).

Is a bad faith claim viable if a coverage decision has been determined to be correct?

There is no cause of action for bad faith refusal to settle where the insurer has refused to defend. *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 262–63, 725 A.2d 1053, 1063–64 (1999).

Is a third-party bad faith claim asserted in connection with a policy that provides third-party coverage viable if the third-party claimant does not prevail in the underlying claim?

The only recognized third-party bad faith claim is for a judgment in excess of the policy limits where the insurer wrongfully refused to settle for an amount within the policy limits. *See*, *e.g.*, *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 262–63, 725 A.2d 1053, 1063–64 (1999).

PRACTICE AND PROCEDURE

Statute of limitations

An insurer's wrongful refusal to settle is a tort. *See*, *e.g.*, *Mesmer v. Md. Auto. Ins. Fund*, 353 Md. 241, 266, 725 A.2d 1053, 1065 (1999). The Maryland statute of limitations for tort causes of action is three years. Md. Code Ann., Cts. & Jud. Proc. §5-101. The cause of action accrues upon a final excess judgment. *Allstate Ins. Co. v. Campbell*, 334 Md. 381, 397, 639 A.2d 652, 659 (1994); *see also Luppino v. Vigilant Ins. Co.*, 110 Md. App. 372, 381, 677 A.2d 617, 621 (1996), *aff'd*, 352 Md. 481, 723 A.2d 12 (1999).

Under what circumstances will bad faith claims be dismissed or stayed pending the resolution of the underlying claims?

Not applicable.

Under what circumstances will the compensatory and punitive damage claims be bifurcated?

Although not required, courts frequently bifurcate claims for compensatory and punitive damages. *Darcars Motors of Silver Springs, Inc. v. Borzym*, 379 Md. 249, 273–74, 841 A.2d 828, 842–43 (2004). Md. Code Ann., Cts. & Jud. Proc. §10-913(a) prohibits the admission of evidence of the defendant's financial condition in personal injury actions unless the jury first finds

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that "punitive damages are supportable under the facts."

DEFENSES AND COUNTERCLAIMS

Is evidence regarding the reasonableness of the conduct of the insured or third-party claimant admissible?

Yes. The actions of the third-party claimant, such as failure to make a demand within policy limits, bear on the reasonableness of the insurer in not settling the case. Contributory negligence of the insured may also be a defense. For example, whether the insured requested that his or her insurer settle the case or agreed that a case should not be settled may be considered by the jury. *Kremen v. Md. Auto. Ins. Fund*, 363 Md. 663, 682, 770 A.2d 170, 181 (2001); *Am. Mut. Ins. Co. of Bos. v. Bittle*, 26 Md. App. 434, 439, 338 A.2d 306, 309 (1975). However, a bad faith suit is not barred by the insured's wish to litigate where it is not based upon a fully informed judgment. *Schlossberg v. Epstein*, 73 Md. App. 415, 434, 534 A.2d 1003, 1012 (1988).

Is "advice of counsel" a recognized defense?

There are no reported Maryland insurance cases on point. However, advice of counsel is a defense to tort actions. *VF Corp. v. Wrexham Aviation Corp.*, 112 Md. App. 703, 715, 686 A.2d 647, 654 (1996), *aff'd in part*, *rev'd in part on other grounds*, 350 Md. 693, 715 A.2d 188 (1998). Hence, it should be one factor the trier of fact may consider in determining the reasonableness of the insurer's conduct in not settling the case.

What other defenses are available?

Since bad faith is a tort action, any defense to a tort may be asserted in a bad faith action, including contributory negligence or assumption of risk.

No case has found bad faith where there was an offer of policy limits prior to trial. *See*, *e.g.*, *Cook v. Nationwide Ins. Co.*, 962 F. Supp. 2d 807, 821 (D. Md. 2013); *Allstate Ins. Co. v. Campbell*, 334 Md. 381, 391–92, 639 A.2d 652, 656–58 (1994).

In first-party cases, the MIA may not find that the insurer failed to act in good faith "solely on the basis of delay in determining coverage or the extent of payment to which the insured is entitled if the insurer acted within the time period specified by statute or regulation for investigation of a claim by an insurer." Md. Code Ann., Cts. & Jud. Proc. §3-1701(f).

Is there a cause of action for reverse bad faith?

No such cause of action has been recognized.

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