

THE DECLINE OF THE SO-CALLED DOCTRINE OF CONTINUING BAD FAITH

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INTRODUCTION

The covenant of good faith and fair dealing was first recognized in insurance contracts in the early part of the twentieth century and provides that implied in every insurance contract is an obligation on the part of the insurer to act reasonably and in good faith. When an insurer violates this covenant, liability is sometimes imposed for bad faith. Historically, bad faith liability has been imposed to give policyholders an avenue of recovery beyond the policy language when, for example, insurers unreasonably fail to settle claims against their insureds and expose their insureds to excess liability, or when an insurer denies coverage with no reasonable basis. In the 1985 decision, *White v. Western Title Insurance Co.*,¹ the California Supreme Court allowed, for the first time, the use of an insurer's conduct during the course of coverage litigation as evidence of the insurer's alleged bad faith, an idea that has since been labeled by some proponents as continuing bad faith.²

1. 710 P.2d 309 (Cal. 1985).

2. See Douglas R. Richmond, *Bad Insurance Bad Faith Law*, 39 TORT TRIAL & INS. PRAC. L.J. 1, 39 (2003) (indicating that the "doctrine" of "continuing bad faith" includes the "principle that an insurer can commit bad faith in the defense of a coverage action"); Douglas L. Christian & Nathan D. Meyer, *Continuing Bad Faith: Theory of Liability or Rule of Evidence?*, 19 INS. LITIG. REP. 601 (2001) (discussing "the theoretical and practical significance of the concept of continuing bad faith").

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In the twenty-three years since the *White* decision, policyholders and their counsel have regularly attempted to expand this holding by asserting in coverage litigation that various types of insurer conduct in litigating a coverage lawsuit could be used as evidence of an insurer's bad faith. Despite these efforts to define and expand continuing bad faith, most of the recent decisions show that courts are becoming reluctant to allow policyholders to delve into an insurer's conduct in coverage litigation to prove bad faith. Although there are a number of sound reasons for this reluctance, the most significant reason is concern about establishing a different standard of litigation conduct for insurers than for other litigants. Within California, cases subsequent to *White* quickly limited the breadth of its holding, effectively finding that the case only allows for the introduction of evidence of the settlement offers made by insurers during coverage litigation.

This article reviews the holdings of *White*; its progeny in California; and later opinions, such as the 2006 decision by the Kentucky Supreme Court in *Knotts v. Zurich Insurance Co.*,³ which contains an extensive discussion and criticism of efforts to expand continuing bad faith.

This article also responds to *Bad Faith Coverage Litigation: The Insurer's Covenant of Good Faith and Fair Dealing*,⁴ which appeared in the fall 2006 issue of this *Journal*. That article identified and discussed five specific ways in which an insurer can purportedly commit bad faith during the course of coverage litigation. Despite these assertions, there is almost no authority supporting the application of continuing bad faith to the conduct discussed in *Bad Faith Coverage Litigation*. Indeed, as will be seen, in those few instances where courts have directly or indirectly considered the identified categories of conduct, the reviewing court often did not even consider whether the conduct was in bad faith, much less make a finding of bad faith.

Finally, this article considers whether continuing bad faith ever was, or currently is, viable enough to be considered a doctrine and whether courts should ever permit insurers' litigation conduct in coverage litigation to be evidence of bad faith. The authors of this article conclude that the twenty-three years of cases subsequent to *White* show that the decision was ill-conceived in allowing the introduction of any evidence of an insurer's conduct in the course of coverage litigation. Future courts should closely scrutinize *White*'s applicability to classes of an insurer's conduct in coverage litigation because *White*'s holding rests upon questionable or nonexistent legal principles. Accordingly, the authors of this article suggest that no class of an insurer's conduct in the course of coverage litigation should be admissible in a bad faith action to evidence the insurer's alleged continuing bad faith.

3. 197 S.W.3d 512 (Ky. 2006).

4. Brent W. Huber & Angela P. Krahulik, *Bad Faith Coverage Litigation: The Insurer's Covenant of Good Faith and Fair Dealing*, 42 TORT TRIAL & INS. PRAC. L.J. 29 (2006).

I. THE DOCTRINE OF THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING AND THE EXPANSION OF BAD FAITH LAW

The implied covenant of good faith and fair dealing in insurance contracts traces its origin to the early part of the twentieth century.⁵ However, it did not gain practical application until the Wisconsin Supreme Court decided *Hilker v. Western Automobile Insurance Co.*⁶ and used this covenant to resolve the problem of insurers unreasonably refusing to settle third-party claims within applicable policy limits to the detriment of their insureds.⁷

Courts today universally recognize an implied covenant of good faith and fair dealing within every insurance contract.⁸ States accomplish this by recognizing an actionable tort or cause of action based on a breach of the implied covenant of good faith and fair dealing or through the enactment of statutes (typically unfair claims settlement practices acts or similar laws) or through both.⁹ As the nomenclature developed, a variety of types of actions that fall under this broad umbrella have come to be known by the familiar term *bad faith*.¹⁰

Initially, bad faith was only applicable in the third-party context. This situation arises when an insurer, faced with a settlement demand within policy limits, unreasonably (i.e., in bad faith) fails to settle a third-party claim against its insured and thereby exposes the policyholder to a verdict in excess of the limits of its insurance policy. In order to provide the policyholder with a remedy for such misconduct, courts created a bad faith cause of action against the insurer for extracontractual damages. In *Gruenberg v. Aetna Insurance Co.*,¹¹ the California Supreme Court extended the concept to the first-party context to guard against an insurer acting unreasonably and in bad faith in direct dealings with its insured. In considering whether

5. See *Brassil v. Md. Cas. Co.*, 104 N.E. 622, 624 (N.Y. 1914) (finding that it was the obligation of the insurer to “deal fairly and in good faith” with its insured).

6. 231 N.W. 257 (Wis. 1930).

7. *Id.* at 260–61 (finding the insurer liable for an excess judgment when it failed to settle the liability claim brought against the insured for less than policy limits).

8. *Jordan v. Allstate Ins. Co.*, 56 Cal. Rptr. 3d 312 (Ct. App. 2007); see also STEPHEN S. ASHLEY, *BAD FAITH ACTIONS: LIABILITY AND DAMAGES* § 2:15 (2d ed. 1998).

9. See ASHLEY, *supra* note 8 (discussing jurisdictions that have adopted the tort-based and statutory-based mechanisms for bringing a bad faith action against an insurer).

10. See *Best Place, Inc. v. Penn Am. Ins. Co.*, 920 P.2d 334, 338 (Haw. 1996) (finding that the “obligation to deal in good faith is now a well-established principle of contract law”); *Brown v. Patel*, 157 P.3d 117, 121 (Okla. 2007) (finding that [g]enerally, an implied duty of an insurer to act in good faith and deal fairly with its insured is imposed by law upon the insurer-insured relationship, and a breach of that duty arises from a breach of the insurance contract where the breach occurs in a manner constituting a lack of good faith; i.e., constituting bad faith).

11. 510 P.2d 1032 (Cal. 1973).

bad faith could apply to both the insurer's conduct in handling claims by third parties and in the first-party context, the court stated thus:

These are merely two different aspects of the same duty. . . . It is the obligation, deemed to be imposed by the law, under which the insurer must act fairly and in good faith in discharging its contractual responsibilities. Where in so doing, it fails to deal *fairly and in good faith* with its insured by refusing, without proper cause, to compensate its insured for a loss covered by the policy, such conduct may give rise to a cause of action in tort for breach of an implied covenant of good faith and fair dealing.¹²

Thus, in addition to the wide acceptance of bad faith actions in the third-party context, many jurisdictions also recognize bad faith actions for the insurer's conduct towards its insured in the handling of first-party claims.¹³

Further, bad faith doctrine in both the first- and third-party context is predicated on two basic principles. First, the courts creating bad faith law predicated that new law on the special insurer-insured relationship that required the parties to act with good faith toward one another. Thus, for liability policies, most courts recognize that only the insured itself has a viable cause of action for bad faith. Bad faith actions by third-party claimants are not generally permitted because these third parties are not parties to the insurance contract.¹⁴ For first-party coverage lines, only the insured typically has a sustainable cause of action that flows directly from its contractual relationship with the insurer.¹⁵

Second, courts expanding the law to include causes of action for bad faith did so to provide a legal remedy where no adequate contract remedy existed.¹⁶ By implication, the inverse is equally true. The law should not

12. *Id.* at 1037 (emphasis in original).

13. See Douglas G. Houser, Ronald J. Clark & Linda M. Bolduan, *Good Faith as a Matter of Law—An Update on the Insurance Company's "Right to Be Wrong,"* 39 TORT TRIAL & INS. PRAC. L.J. 1045, 1048 (2004) (stating there were at least twenty-seven states recognizing a first-party bad faith cause of action).

14. See, e.g., *Hartman v. United Heritage Prop. & Cas. Co.*, 108 P.3d 340, 345–46 (Idaho 2005); *Gaskins v. S. Farm Bureau Cas. Ins. Co.*, 541 S.E.2d 269, 272 (S.C. Ct. App. 2000).

15. In some limited instances, insurers have been held liable for bad faith to noninsureds such as life insurance policy beneficiaries. Those decisions are few in number and permit the bad faith cause of action because the plaintiff is found to be in privity with the parties to the insurance policy. See, e.g., *Anderson v. Lancaster Aviation, Inc.*, 220 F. Supp. 2d 524, 530–31 (M.D.N.C. 2002) (noting that “a third party who is not the insured and is not in privity with the insurer does not have a cause of action against the insurance company”); *Cannon v. Travelers Indem. Co.*, 994 P.2d 824, 828 (Utah Ct. App. 2000) (indicating that duty of good faith “runs to parties to an insurance contract or their privies”).

16. See Randy Papetti, *The Insurer's Duty of Good Faith in the Context of Litigation*, 60 GEO. WASH. L. REV. 1931, 1935 (1992) (stating that “[t]he flexible concept of the implied covenant of good faith and fair dealing has been used to compensate for the inadequacy of contract law in certain insurance settings,” and a tort remedy is provided in those instances “[t]o ensure that the duty has more than a salutary effect”).

provide duplicative remedies when the policyholder has other avenues to recover or adjudicate its grievances. In these later instances, courts have been reluctant to recognize a bad faith cause of action largely because the policyholder's motive is simply to maximize its recovery. Thus, if the bad faith action is simply a duplicative or alternate mechanism for a litigant to attempt to increase the amount of the ultimate verdict and is not intended to address an unrecognized legal right or to provide an adequate remedy for wrongful conduct, there is no need to create a bad faith cause of action. This is particularly true in instances where the insurer's conduct is not egregious and there is no colorable justification to allow punitive damages as a means to punish the alleged bad behavior. Moreover, as will be shown in the discussion below, the use of an insurer's conduct in coverage litigation is problematic not only because the policyholder has other available mechanisms to address grievances but also because the admission of the conduct subjects the insurer to a different litigation standard.

II. CONTINUING BAD FAITH

For the first fifty-five years after the court in *Hilker* recognized a cause of action for breach of the implied covenant of good faith and fair dealing, no court permitted an insurer's litigation conduct to be used as evidence of bad faith. This changed in 1985, when the California Supreme Court allowed the introduction of an insurer's conduct during coverage litigation to demonstrate bad faith in *White*.¹⁷ *White* held that an insurer's unreasonable offers to settle coverage litigation could be evidence of bad faith.

The ruling effectively set off a maelstrom of litigation by policyholders attempting to extend *White's* holding to apply to insurer conduct that extended far beyond offers to settle litigation. Despite the persistent attempts by policyholders to expand the so-called doctrine, most courts have resisted. Indeed, one California appellate court has even suggested that the California Supreme Court's holding in *White* should be reversed.¹⁸

The courts should continue to question *White's* holding and the admissibility of insurers' conduct toward their insureds after the commencement of coverage litigation because there is simply no justification for treating insurers differently than other litigants. In addition to the unjustifiable disparate treatment, admissibility of settlement conduct after the commencement of coverage litigation will always be unduly prejudicial to the insurer. As such, although the so-called doctrine of continuing bad faith has been on the decline from its inception, its fall is twenty-three years overdue.

17. *White v. W. Title Ins. Co.*, 710 P.2d 309 (Cal. 1985).

18. *See Cal. Physicians' Serv. v. Superior Court*, 12 Cal. Rptr. 2d 95, 98-99 (Ct. App. 1992).

A. *Beginnings*: *White v. Western Title Insurance Co.*

The seminal case of continuing bad faith law arose when Brian and Helen White sued Western Title Insurance Company, alleging breach of a title insurance policy. Six months after the purchase of their property and the policy, the Whites learned that the prior owner had granted an easement for water rights to a local water company, which was not identified on Western's title report.¹⁹ The Whites obtained an appraisal suggesting a loss in value to the property of \$62,947, and they demanded this amount. Western acknowledged its responsibility but denied coverage, asserting that the policy excluded loss due to diminution of value because of loss of groundwater rights.²⁰ The Whites sued, and Western ultimately lost a summary judgment motion that relied upon the aforementioned policy exclusion.²¹ Thereafter, Western offered \$3,000 and then \$5,000 to fully resolve the matter, but the Whites rejected both offers. The Whites then amended their complaint to allege that Western had breached the implied covenant of good faith and fair dealing.²²

The court separated the liability and damages portions of the trial and found Western liable for breach of contract and negligence in the liability portion. In the damages phase, the jury returned a verdict totaling \$8,400 for the breach of contract.²³ The court then turned to the cause of action alleging breach of the covenant of good faith and fair dealing. Over Western's objection, the court allowed the introduction of evidence of Western's settlement offers made after the commencement of coverage litigation. The jury returned a special verdict finding that Western had breached the implied covenant of good faith and fair dealing and awarded the Whites \$20,000, but it declined to award punitive damages.²⁴

On appeal, the California Supreme Court acknowledged that the issue was one of first impression and proceeded to resolve the case as a matter of principle.²⁵ It found that the evidence of postlitigation settlement offers was admissible because the contractual relationship between the insurer and the insured did not terminate with the commencement of litigation.²⁶ The court reasoned that drawing a distinction between the admissibility of an insurer's prelitigation and postlitigation conduct was not desirable because it would encourage insurers to file premature litigation or cause the insurer to induce the insured to initiate litigation.²⁷

19. *Id.* at 311.

20. *Id.*

21. *Id.* at 312.

22. *Id.*

23. *Id.*

24. *Id.*

25. *Id.* at 317.

26. *Id.*

27. *Id.*

Western argued that the trial court should have excluded the evidence of settlement conduct because the parties became adversaries after suit was filed and Western no longer owed the Whites a duty of good faith and fair dealing.²⁸ Western also asserted that a continuation of the duty of good faith and fair dealing would seriously impair insurers' rights if they had to reveal all information learned after the commencement of coverage litigation that might be potentially relevant to the bad faith allegation.²⁹ Further, ethical rules would require the lawyers preparing the defense of the bad faith claim to withdraw from the defense of the insurer in the breach claim because the lawyer could be called as a material witness to testify about the insurer's litigation conduct.³⁰ Finally, Western argued that juries might misunderstand normal litigation tactics or view settlement offers as an admission of liability on the part of the insurer.³¹

Without much analysis, the *White* court rejected each of Western's arguments, citing three reasons to support its conclusion. First, it stated that insurers were effectively obligated to fully investigate the factual basis of claims prior to the commencement of coverage litigation.³² Second, it held that courts have the ability to bifurcate the breach of contract and bad faith trials just like the trial court had done in this instance. Third, the *White* court found that determining liability for bad faith required a fact-specific inquiry but offered no explanation how this rationale justified ignoring the insurer's various arguments.³³

The positions taken by Western in *White* are important because subsequent insurers have made variants of these arguments and courts have increasingly adopted them when policyholders assert continuing bad faith. Moreover, it is significant that the court in *White* was asked to consider the admissibility of a single class of evidence—the insurer's settlement offers in coverage litigation.³⁴ The underpinnings of the holdings in *White* and its progeny start to break down significantly or altogether vanish when policyholders suggest that insurers' other litigation conduct (e.g., pleadings, strategy, and tactics) should also be admissible. As such, most recent decisions preclude the introduction of most categories of insurers' postlitigation conduct. Further, for reasons that will be shown, even the basis supporting the *White* court's rationale for the admission of settlement conduct during coverage litigation rests on questionable grounds because settlement conduct is actually indistinguishable from other classes of conduct.

28. *Id.* at 316.

29. *Id.* at 317.

30. *Id.*

31. *Id.* at n.9.

32. *Id.* at 317.

33. *Id.*

34. *Id.* at 318–19.

B. California Decisions After White

Shortly after the *White* decision, California judges almost immediately refused to expand the decision's breadth. This was particularly true in instances where policyholders sought to introduce evidence of insurers' litigation strategy or tactics in coverage litigation as evidence of insurers' bad faith. Each significant post-*White* decision is discussed below.

In *Palmer v. Ted Stevens Honda, Inc.*,³⁵ a California appellate court refused to apply the holding in *White* to allow evidence of bad faith outside of the insurance context. In that case, one party to a commercial contract asserted a cause of action against the other for bad faith denial (a tort analogous to insurance bad faith). The trial court allowed the plaintiff to submit evidence of the attorney fees it incurred in responding to numerous motions made by defendant and regarding sanctions that defendant received as a result of those motions.³⁶ Based on this evidence, plaintiff obtained a judgment against defendant, including an award of punitive damages for \$150,000.³⁷ On appeal, the trial court was reversed, and the appellate court found that defendant's litigation tactics were not admissible.³⁸ *White* was deemed inapplicable outside of the insurance context, and the court distinguished the nature of the ordinary commercial contract at issue from the special relationship that arises out of an insurance policy.³⁹ Further, the court found it significant that the contractual relationship had not remained intact through the filing of the suit. In deciding not to allow the litigation evidence, the court emphasized that allowing a party's litigation tactics to be used as evidence of bad faith wrongfully "holds the client responsible for the attorney's litigation strategy" and fails to "accord any weight to the right of a defendant to defend itself."⁴⁰ Finally, the *Palmer* court indicated that litigation tactics were not admissible because they were not probative of whether defendant committed bad faith prior to the lawsuit.⁴¹

A second decision by another California appellate court similarly refused to expand *White*. In *Nies v. National Automobile & Casualty Insurance Co.*,⁴² plaintiff was struck by an uninsured driver of a dune buggy. The insurer initially denied uninsured motorist coverage, arguing that the dune buggy did not qualify as a highway vehicle under the policy. Plaintiff sued, alleging breach of contract and bad faith.⁴³ One week after the suit was filed, the insurer's

35. 238 Cal. Rptr. 363 (Ct. App. 1987).

36. *Id.* at 366.

37. *Id.* at 364.

38. *Id.* at 370.

39. *Id.* at 368.

40. *Id.* at 368-69.

41. *Id.* at 369.

42. 245 Cal. Rptr. 518 (Ct. App. 1988).

43. *Id.* at 521.

attorney found authority suggesting that coverage would apply, and the insurer then immediately paid its contractual obligation.⁴⁴ However, plaintiff still maintained its bad faith action. At trial on the bad faith action, plaintiff was allowed to introduce the counterclaim filed by the insurer shortly after the commencement of coverage litigation.⁴⁵ The insurer's attorney was also allowed to be called to testify about his role after the commencement of coverage litigation.⁴⁶ The jury awarded plaintiff \$35,000 in general damages and \$70,000 in punitive damages.⁴⁷ The appellate court reversed. It found that *White* did not address the types of insurer conduct in coverage litigation that "would or would not be relevant or admissible on the issue of bad faith, nor did it address the policy issues involved in permitting a lay jury to impute improper motives to the imposition of a legally proper defense."⁴⁸

*California Physicians' Service v. Superior Court*⁴⁹ is a third California case that applied even further limitations to the *White* holding and suggested that the California Supreme Court should reconsider its decision. In that matter, a health insurer responded to a suit by filing a general denial and asserting eleven affirmative defenses.⁵⁰ Plaintiffs then filed an amended complaint alleging bad faith on the basis that the answer asserted "spurious, untenable and unprivileged defenses."⁵¹ The trial court found generally that bad faith allegations are sustainable in instances when an insurer asserts "patently untenable" defenses, but it did not determine if any of the insurer's particular defenses fit into this category.⁵² Based on this ruling, the insurer sought and obtained immediate appellate review.

The appellate court reversed the trial court and found that all of defendant insurer's pleadings (including affirmative defenses) were protected by the absolute litigation privilege.⁵³ The appellate court focused its analysis on the rights of the insurer as a litigant by first observing that there is no such thing as a tort for malicious defense.⁵⁴ To find otherwise, according to the appellate court, would be tantamount to allowing litigation to go on perpetually. Plaintiff would simply continue to file separate actions after the entry of a judgment if the law recognized a separate cause of action predicated on the way the defense was conducted.⁵⁵

44. *Id.* at 521–22.

45. *Id.* at 522–23.

46. *Id.* at 522.

47. *Id.* at 519.

48. *Id.* at 524.

49. 12 Cal. Rptr. 2d 95 (Ct. App. 1992).

50. *Id.* at 96.

51. *Id.*

52. *Id.*

53. *Id.* at 100.

54. *Id.* at 96 (citing *Bertero v. Nat'l Gen. Corp.*, 529 P.2d 608 (Cal. 1974)).

55. *Id.* at n.2.

The appellate court in *California Physicians' Service* concluded that the only way the trial court's decision was sustainable was to interpret *White* to mean that insurance company defendants "do not have the same privileges in terms of defensive pleadings as do other defendants."⁵⁶ The appellate court categorically rejected such an interpretation and expressed doubt about the "current vitality of *White*," reasoning that insurers' rights to defend themselves would be seriously compromised without equal litigation privileges.⁵⁷ The appellate court then proceeded to limit severely the application of *White*, allowing only the introduction of an insurer's settlement offers made during coverage litigation. Such evidence could be used only to show a continuation of the insurer's prior course of tortious conduct that started before commencement of the litigation.⁵⁸ The appellate court found that plaintiff's effort was "not to use trial tactics as *evidence* of prior bad faith, but to mount a new cause of action for severable damages on the theory of an action for bad faith defense."⁵⁹ Essentially, *California Physicians' Service* and the other aforementioned cases limit the *White* holding to the facts of that case and strongly suggest that *White* may no longer be viable.

C. *Beyond California: Various Categories of Insurer
Litigation Conduct Inadmissible*

In addition to the California cases subsequent to *White* that severely limit continuing bad faith, the majority of courts from other jurisdictions that have addressed this issue have held that most, if not all, of an insurer's conduct in the course of coverage litigation is neither relevant nor admissible.

Some states have adopted an absolute prohibition on admitting insurers' conduct in coverage litigation as evidence of bad faith. For instance, in *Parker v. Southern Farm Bureau Casualty Insurance Co.*,⁶⁰ the insured attempted to introduce evidence of his insurer's coverage litigation conduct to support his bad faith claim, including positions taken in pleadings, briefs, affidavits, and depositions of the insurer's employees.⁶¹ The court held that conduct by the insurer following the filing of the coverage litigation could not provide a basis for a bad faith claim for the simple fact that the bad faith cause of action "must exist and be complete at the time the action is commenced."⁶² Thus, the court precluded consideration of any aspect of an insurer's conduct in coverage litigation.

56. *Id.* at 97.

57. *Id.* at 98–99.

58. *Id.* at 98.

59. *Id.* (emphasis in original).

60. 935 S.W.2d 556 (Ark. 1996).

61. *Id.* at 561–62.

62. *Id.* at 562.

Other jurisdictions have held that, as a general rule, an insurer's conduct in coverage litigation should not be admitted. In *Timberlake Construction Co. v. U.S. Fidelity & Guaranty Co.*,⁶³ the U.S. Court of Appeals for the Tenth Circuit held that the conduct of the insurer's counsel during coverage litigation could not be used as evidence of bad faith.⁶⁴ That evidence included the following:

a letter from [the insurer's] counsel to [the insurance] adjuster; the fact that [the insurer] filed a counterclaim against [the insured] seeking to recover the monies paid pursuant to [a] non-waiver agreement; and the fact that [the insurer] made a motion to join [a third party] in [the insured's] suit as a necessary party.⁶⁵

The *Timberlake Construction* court stated that "if the focus of a bad faith claim is the insurer's knowledge and belief during the time the claim is being reviewed," then the relevance of conduct that takes place after the claim has been reviewed (i.e., in litigation) is "severely diminished."⁶⁶ The court was concerned that allowing litigation conduct into evidence would defeat "an insurer's right to contest questionable claims and to defend itself against such claims."⁶⁷ The court concluded that any concern that the insured may have about improper litigation conduct by the insurer could be addressed by the Federal Rules of Civil Procedure.⁶⁸

The *Timberlake Construction* court stopped short of holding that there should be an absolute bar to evidence of an insurer's litigation conduct in the course of coverage litigation to demonstrate bad faith.⁶⁹ Nevertheless, the court stated that litigation conduct would "generally be inadmissible, as it lacks probative value and carries a high risk of prejudice," and emphasized that instances where such evidence might be admissible were "rare."⁷⁰

63. 71 F.3d 335 (10th Cir. 1995).

64. *Id.* at 341.

65. *Id.* at 339.

66. *Id.* at 340.

67. *Id.* at 341.

68. *Id.*

69. A few courts have relied upon *White* and permitted insureds to present evidence of an insurer's litigation conduct to support a bad faith claim in limited circumstances. *See, e.g., Gooch v. State Farm Mut. Auto. Ins. Co.*, 712 N.E.2d 38 (Ind. Ct. App. 1999) (allowing evidence of claim investigation conduct after the start of coverage litigation); *Downey Sav. & Loan Ass'n v. Ohio Cas. Ins. Co.*, 234 Cal. Rptr. 835 (Ct. App. 1987) (allowing evidence that insurer had a practice of using depositions to harass insureds and force settlement). However, even courts that have allowed limited evidence of litigation conduct acknowledge that it should be the exception rather than the rule. *See, e.g., Gooch*, 712 N.E.2d at 42 (noting that "an insurance company's postfiling conduct, particularly its litigation conduct, has little relevance to proving that the insurer's prefiling actions resulted in the wrongful denial of policy benefits") (citations omitted).

70. *Timberlake Constr.*, 71 F.3d at 341.

Many other courts have applied similar restrictions. For example, in *Sims v. Travelers Insurance Co.*,⁷¹ the Oklahoma Court of Civil Appeals adopted the reasoning from *Timberlake Construction* and held that various aspects of the insurer's litigation conduct could not be the basis of a bad faith claim brought by the insureds.⁷² Specifically, the *Sims* court disagreed with the insureds and determined that the following types of insurer conduct in coverage litigation were not indicative of bad faith on the part of the insurer: treating the insureds as adversaries, filing motions to dismiss, objecting to discovery, misdocketing meetings, failing to agree to deposition times offered by the insureds, and rejecting the insureds' request for mediation.⁷³

In *FDIC v. Aetna Casualty & Surety Co.*,⁷⁴ the insured attempted to use the insurer's discovery tactics to support its bad faith claim. The court rejected the insured's argument, holding that the insurer's "normal and commonly accepted strategic pretrial discovery decisions" could not be used as evidence of bad faith.⁷⁵ Similarly, in a recent Colorado case, *Parsons v. Allstate Insurance Co.*,⁷⁶ the court held that common litigation conduct, such as the insurer's counsel's refusal to submit to a deposition and filing an answer denying coverage was not admissible evidence of bad faith.⁷⁷ Generally, courts that have addressed the issue of the admissibility of insurers' conduct during coverage litigation have come to the conclusion that the rules of civil procedure (not a bad faith tort action) provide the proper remedy for any alleged improper litigation conduct.⁷⁸

*Knotts*⁷⁹ is a recent decision by the Kentucky Supreme Court that contains an extensive synthesis of the case law repudiating continuing bad faith. *Knotts* involved a worker who was seriously injured in a fall at a construction

71. 16 P.3d 468 (Okla. Civ. App. 2000).

72. *Id.* at 471.

73. *Id.*

74. 903 F.2d 1073 (6th Cir. 1990).

75. *Id.* at 1079-80.

76. No. 03CA2051, 2006 WL 3437561 (Colo. Ct. App. Nov. 30, 2006).

77. *Id.* at *9; see also O'Donnell v. Allstate Ins. Co., 734 A.2d 901, 909-10 (Pa. Super. Ct. 1999) (discovery requests and failure to settle following receipt of the insured's sworn deposition testimony do not constitute "bad faith investigatory practices" actionable under the Pennsylvania bad faith statute); Int'l Surplus Lines Ins. Co. v. Univ. of Wyo. Research Corp., 850 F. Supp. 1509, 1528 (D. Wyo. 1994) (noting that "litigation conduct" by insurer's counsel in filing suit and regarding discovery matters is not evidence of "oppressive and intimidating claim practices" as required for a first-party bad faith claim) (emphasis in original); Palmer by Diacon v. Farmers Ins. Co. Exch., 861 P.2d 895, 915 (Mont. 1993) (noting that "actions taken after an insured files suit are at best marginally probative of the insurer's decision to deny coverage").

78. See, e.g., Roussalis v. Wyo. Med. Ctr., Inc., 4 P.3d 209, 257 (Wyo. 2000) (asserting that the Rules of Civil Procedure provide the remedy for improper litigation conduct, disallowing the bad faith tort action based on litigation conduct).

79. *Knotts v. Zurich Ins. Co.*, 197 S.W.3d 512 (Ky. 2006).

site. The worker filed a personal injury suit against the company after denial of workers' compensation coverage by the company's insurer.⁸⁰ The worker ultimately obtained a verdict against the company in his tort suit for over \$1.2 million, which was affirmed on appeal. The worker subsequently pursued a bad faith claim against the company's general liability insurer.⁸¹ The third-party bad faith action alleged that the insurer had violated Kentucky's Unfair Claims Settlement Practices Act (UCSPA) in the course of managing the defense of the underlying tort case and the subsequent appeal.⁸² The trial court ruled that the UCSPA only applied to an insurer's conduct prior to the commencement of litigation, and the appellate court affirmed.⁸³

The Kentucky Supreme Court granted discretionary review and found, as a preliminary matter, that there was nothing in the UCSPA explicitly limiting its application only to allowing admission of an insurer's prelitigation conduct.⁸⁴ The court then specified that the recognition of the "existence of a continuing duty of good faith, however, is not the end of our inquiry," and it immediately endeavored to address the types of an insurer's postfiling conduct that would be deemed admissible in bad faith actions.⁸⁵ Because this was an issue of first impression in Kentucky, the decision contains an extensive discussion of cases from other jurisdictions analyzing the admissibility of an insurer's conduct in coverage litigation.⁸⁶

The *Knotts* court established an absolute prohibition on the introduction of an insurer's conduct in coverage litigation (excluding settlement conduct) and found that the Federal Rules of Civil Procedure provided a remedy for challenging an insurer's litigation conduct:⁸⁷

[G]iven the chilling effect that allowing introduction of evidence of litigation conduct would have on the exercise of an insurance company's legitimate litigation rights, any exception threatens to turn our adversarial system on its head. We are confident that the remedies provided by the Rules of Civil Procedure for any wrongdoing that may occur within the context of the litigation itself render unnecessary the introduction of evidence of litigation conduct. This is particularly true given that the attorneys, who in fact control and perpetuate the litigation conduct on behalf of an insurance company, are subject to direct sanction under the Civil Rules for any improper conduct. Though it goes without

80. *Id.* at 514.

81. *Id.* at 515. The worker was not a party to the insurance contract, but UCSPA, KY. REV. STAT. § 304.12-230, specifically allows third-party bad faith actions in Kentucky.

82. *Id.*

83. *Id.*

84. *Id.* at 517.

85. *Id.* at 518.

86. *Id.*

87. *Id.* at 523 (citing STEPHEN S. ASHLEY, *BAD FAITH ACTIONS LIABILITY AND DAMAGES* § 5A:6 (2005)).

saying, we also note that those attorneys have significant duties under the Rules of Professional Responsibility, which allow for further sanctions for unethical behavior. Thus, we think the better approach is an absolute prohibition on the introduction of such evidence in actions brought under [the UCSPA].⁸⁸

The court concluded that permitting a “jury to pass judgment on the defense counsel’s trial tactics and to premise a finding of bad faith on counsel’s conduct places an unfair burden on the insurer’s counsel, potentially inhibiting the defense of the insurer.”⁸⁹

The extensive analysis by the *Knotts* majority in support of its holding that there should be a prohibition on the admission of an insurer’s conduct in coverage litigation is correct and well supported. Admitting this type of evidence holds insurers in coverage litigation to a different and far more restrictive litigation standard than is applied to other litigants.

However, without much analysis, the majority in *Knotts* ultimately distinguished settlement conduct from all other classes of an insurer’s conduct in coverage litigation. The decision by the *Knotts* majority was based largely upon strict reliance on the language of Kentucky’s UCSPA but also on the familiar argument that settlement conduct is distinguishable because a policyholder has no other mechanism to complain about settlement offers.⁹⁰ Nevertheless, the *Knotts* majority suggests that an absolute prohibition might otherwise apply absent the UCSPA statute:

While such an approach [establishing an absolute prohibition] has some instinctive appeal, especially given that the adversarial nature of litigation undoubtedly makes it difficult for an insurer to fulfill such a demanding duty to what amounts to an opposing party, we ultimately find that the statute simply cannot be read in such a limited manner.⁹¹

As is discussed below, the distinction between an insurer’s settlement conduct and other types of litigation conduct is illusory for a number of reasons, and future courts should adopt an absolute prohibition on the admission of all types of insurers’ conduct in coverage litigation.

D. *Insurer’s Settlement Conduct During Coverage Litigation Not Distinct*

The most prevalent argument for some courts distinguishing between an insurer’s settlement conduct in coverage litigation and all other classes of

88. *Id.* at 522.

89. *Id.* at 523.

90. *Id.* As indicated, *Knotts* involved a bad faith suit by a worker who was a third party to the insurance contract and able to sue only because the UCSPA specifically allows third-party bad faith actions. For this reason, the rationale supporting the *Knotts* majority’s continued recognition of the *White* exception for insurers’ settlement conduct is distinguishable.

91. *Id.* at 515.

conduct in coverage litigation is the assertion that the policyholder has no other means to have its grievances heard. However, neither this argument nor others used by certain courts to support the continuation of the distinction stand up to scrutiny.

First, no litigant typically has the ability to adjudicate grievances that it may have about the opposing party's settlement conduct in litigation. In fact, most suits arise over disputes about case valuation. The mechanism for resolving those disputes is the actual litigation. Thus, holding an insurer liable to its insured for bad faith on the basis of its settlement offers is unquestionably holding that insurer to a higher and different standard than other litigants.

Second, the probative value of settlement offers is minimal or nonexistent as to the issue of bad faith. Moreover, the admission of this type of evidence is always unduly prejudicial to the insurer. For instance, a nominal settlement offer after the commencement of coverage litigation by an insurer that believes there is no coverage has no probative value. Such conduct does not show that the insurer acted in bad faith through its prelitigation failure to respond timely to the insured's demand for coverage. Additionally, the admission of such a settlement offer would be prejudicial to the insurer because it might lead the fact finder to conclude that the extension of a settlement offer was an admission that the insured was entitled to coverage.

Third, the cases subsequent to *White* that adopt the exception rarely (if ever) attempt to examine whether insurer settlement conduct is truly distinguishable from other litigation conduct after the commencement of coverage litigation. Other than the assertion that the law provides no other mechanism for a policyholder to complain about settlement conduct (discussed supra), there is no other widely asserted colorable argument. Many courts simply adopt the *White* postfiling settlement exception without examination. Further, this problem is compounded by the fact that the perpetuation of the exception appears to have occurred, not because of sound judicial reasoning, but only because settlement conduct was the precise conduct at issue in *White*. Therefore, the subsequent appellate California cases interpreting *White* were confined by the holding of that case and effectively forced to leave the settlement conduct portion of the *White* holding intact. Simply put, those courts could not overturn the California Supreme Court although they were critical of the holding and likely would have overturned the decision if they had the power. This view was most clearly articulated in *California Physicians' Service*, the last of the California courts criticizing *White* and providing an in-depth analysis of continuing bad faith. The *California Physicians' Service* court stated:

We have some doubt as to the current vitality of *White*, even for the more restricted view. . . . Commentators have criticized the decision. Justice Brauer in a concurring opinion in *Palmer v. Ted Stevens Honda, Inc.* [internal citations omitted] stated that "*White* . . . seriously compromises the right of [insurance

companies] to defend themselves in court. I hope our Supreme Court will find an early opportunity to reexamine that decision.”

The Supreme Court has to date *not* reexamined *White*. Treatment of the *White* precedent by the Courts of Appeal has, however, to the extent such is possible by the intermediate appellate courts, limited its application. . . .

We will follow the lead of the *Nies v. National Auto. & Casualty Ins. Co.* court. *White* stands for the proposition that ridiculously low statutory offers of settlement may be introduced in a bifurcated trial, after liability has been established, as bearing on the issue of bad faith of the insurance company. . . .⁹²

As the *California Physicians' Service* court states, the time has come for *White* to be reexamined. Courts inside and outside of California should recognize that the holding in *White* creates an illogical disparate standard for insurers. Although *White* has already been rendered largely insignificant or irrelevant for most classes of an insurer's conduct in coverage litigation, the last remaining viable aspect of *White*—addressing settlement conduct after the commencement of coverage litigation—rests on faulty legal principles. Therefore, rather than continuing to perpetuate the *White* exception, future courts should recognize an absolute prohibition precluding all of an insurer's litigation conduct without exception.

III. BAD FAITH COVERAGE LITIGATION: RESPONSE

Against the backdrop of the authority discussed above, the *Bad Faith Coverage Litigation* authors attempt to expand the so-called doctrine of continuing bad faith. They do so by asserting that there are at least five ways by which an insurer can commit bad faith in coverage litigation:

(1) hiring defense counsel to jointly represent two insureds with conflicting interests; (2) suing the insured and the underlying claimant in the same action . . . ; (3) demanding the production of materials that could result in the waiver of the insured's litigation privileges; (4) . . . using confidential and sensitive information . . . to develop coverage defenses; and (5) asserting multiple, unsubstantiated defenses. . . .⁹³

As discussed below, the conduct that is the focus of *Bad Faith Coverage Litigation* neither supports a tort claim for bad faith nor a basis for perpetuating continuing bad faith.

A. *Joint Representation of Two Insureds with Conflicting Interests*

There is no clear support for the argument that an insurer commits bad faith by selecting the same defense counsel to represent two different insureds

92. *Cal. Physicians' Serv. v. Superior Court*, 12 Cal. Rptr. 2d 95, 98–100 (Ct. App. 1992).

93. Huber & Kraulik, *supra* note 4, at 30.

that may have conflicting positions. This is true regardless of whether coverage litigation has commenced. Indeed, the courts that have considered this question have done so by applying straight breach of contract principles and have not suggested that a bad faith analysis was appropriate.

The authors of *Bad Faith Coverage Litigation* cite and analyze *Bituminous Insurance Cos. v. Pennsylvania Manufacturers' Ass'n Insurance Co.*⁹⁴ and *Murphy v. Urso*.⁹⁵ However, those cases did not involve allegations of bad faith, and neither case suggests that an insurer's duty to provide independent counsel to insureds with potential conflicting interests could give rise to a bad faith cause of action. Thus, although these cases provide an interesting and topical overview of this area of law, they are not germane to the issue of bad faith or continuing bad faith.

In actuality, there is no authority holding that an insurer's choice to hire defense counsel to represent multiple insureds with conflicts of interest can constitute bad faith. The cases address such conflict situations in terms of the insurer's duty to defend rather than in terms of bad faith. As noted above, bad faith law was developed to create legal rights and remedies where existing rights and remedies were perceived as inadequate. As such, there is simply no need to allow a bad faith cause of action where a declaratory judgment action to determine the insurers' duties under the policy will suffice.

B. *Concurrent Underlying and Coverage Actions
or Intervention in Underlying Action*

There is no support for the idea that insurers can be liable for bad faith when they "attempt to combine the underlying suit with the coverage action or when insurers attempt to intervene in the underlying case."⁹⁶ The *Bad Faith Coverage Litigation* authors assert that such proceedings harm the insured by introducing prejudice in the insured's defense against the underlying claim and in the coverage action.⁹⁷ Yet, the absence of support cannot be remedied by simply labeling this conduct as continuing bad faith.

Again, there is no need to create a bad faith cause of action when existing legal remedies provide ample methods for dealing with any problems in this area. For example, some jurisdictions address potential prejudice that may arise with concurrent underlying and coverage actions by routinely staying the coverage case during the pendency of the underlying litigation.⁹⁸ In those instances, any potential prejudice is averted by requiring

94. 427 F. Supp. 539 (E.D. Pa. 1976).

95. 430 N.E.2d 1079 (Ill. 1982).

96. Huber & Krahulik, *supra* note 4, at 38.

97. *Id.*

98. See, e.g., *Cincinnati Ins. Co. v. Pro Enters., Inc.*, 394 F. Supp. 2d 1127, 1134 (D.S.D. 2005); *Essex Ins. Co. v. Dembo, Inc.*, 47 F. Supp. 2d 627, 629 (D. Md. 1999).

the resolution of the underlying matter first. Along the same lines, many jurisdictions will not permit the insurer to intervene in the underlying action.⁹⁹ In these instances, there should be no bad faith liability for the attempt to join or intervene. In short, bad faith is an inappropriate and unnecessary remedy to resolve situations where coverage and liability cases threaten to become intermingled.

C. *Production of Materials*

As their third argument, the authors of *Bad Faith Coverage Litigation* assert that an insurer that is not providing a defense or that has reserved its rights and then seeks privileged documents from its insured pertaining to the underlying matter for use in the coverage action may be held liable for bad faith.¹⁰⁰ Again, the cases that the authors cite to support this assertion neither analyze nor even mention bad faith. Insureds can object to producing documents that are improperly sought in discovery, and they can claim privilege if they believe the documents are, in fact, privileged. Insurers that disagree with such claims can, like any other litigant, file a motion to compel. A court that agrees with the insured will deny the motion to compel and end the dispute between the parties on this issue.¹⁰¹ On the other hand, courts often find that insurers are entitled to their insureds' privileged documents.¹⁰² In short, disagreements over objections to producing documents are discovery disputes, not evidence supporting bad faith actions.

The problems that arise from a policyholder attempting to use discovery disputes to support a claim of bad faith are at least twofold. First, as discussed, the insured already has a more appropriate remedy to adjudicate any grievance it may have by refusing a particular request and opposing any resulting motion to compel. Second, if insurers that request documents from their insureds become liable for bad faith, then a higher and more restrictive litigation standard would apply to insurers than would apply to other litigants.¹⁰³

99. See, e.g., *Bucci v. Essex Ins. Co.*, 393 F.3d 285, 295 (1st Cir. 2005) (noting that "a potential conflict of interest . . . may be such as to warrant refusing to let an insurer intervene in the underlying action"); *Borgard v. Integrated Nat'l Life Ins. Co.*, 954 S.W.2d 532, 535 (Mo. Ct. App. 1997) (indemnity claim from insured does not create sufficient interest for insurer to intervene in underlying case); *Cromer v. Sefton*, 471 N.E.2d 700, 704 (Ind. Ct. App. 1984) (holding that an insurer may not intervene to litigate coverage issues).

100. *Huber & Krahulik*, *supra* note 4, at 41, 46.

101. This is exactly the sort of "remedy" the courts used in the cases cited by the *Bad Faith Coverage Litigation* authors. See *E. Air Lines, Inc. v. U.S. Aviation Underwriters, Inc.*, 716 So. 2d 340 (Fla. Dist. Ct. App. 1998) (denying the insurer's motion to compel); *Rhone-Poulenc Rorer, Inc. v. Home Indem. Co.*, 32 F.3d 851 (3d Cir. 1994) (same); *Remington Arms Co. v. Liberty Mut. Ins. Co.*, 142 F.R.D. 408 (D. Del. 1992) (same).

102. *Waste Mgmt., Inc. v. Int'l Surplus Lines Ins. Co.*, 579 N.E.2d 322, 327-28 (Ill. 1991).

103. *Cal. Physicians' Serv. v. Superior Court*, 12 Cal. Rptr. 2d 95, 98-100 (Ct. App. 1992).

Therefore, although courts may arrive at different results on what documents may or may not be discoverable, there is no authority supporting the *Bad Faith Coverage Litigation* authors' assertion that a bad faith or continuing bad faith cause of action can arise from insurers' requests for documents.

D. *Use of the Same Adjuster to Handle the Underlying Claim and the Coverage Action*

The authors of *Bad Faith Coverage Litigation* also assert that an insurer can be held liable for bad faith by using the same adjuster or claims handler to handle both the underlying claim and the coverage claim.¹⁰⁴ As with the other conduct that *Bad Faith Coverage Litigation* discusses, the authors cite no case law to support the argument that the use of one adjuster to handle both the underlying claim and the coverage action can be a basis for a bad faith action.¹⁰⁵ In fact, the opposite is true. Courts have rejected insureds' attempts to bring bad faith actions against their insurers for failure to assign separate adjusters.¹⁰⁶

The California Court of Appeal addressed the issue of multiple adjusters in the context of a discovery dispute in *State Farm Fire & Casualty Co. v. Superior Court (Durant)*.¹⁰⁷ In *Durant*, the insureds were sued by individuals who purchased the insureds' home, claiming damages for defects in the foundation. The insureds tendered the defense of the claim to State Farm Fire & Casualty under their homeowners' policy, and State Farm agreed to provide a defense subject to a reservation of rights.¹⁰⁸ Because the insurer's reservation of rights created a conflict situation between the insureds and the insurer, the insureds retained independent *Cumis* counsel, and the

104. Huber & Krahulik, *supra* note 4, at 46–47.

105. *Id.* at 46–48. The authors of *Bad Faith Coverage Litigation* seem to imply that state unfair claims settlement practices acts require the use of multiple adjusters. See Huber & Krahulik, *supra* note 4, at 47–48. This is incorrect. The statutes cited in the article do not support that proposition. See, e.g., GA. CODE ANN. §§ 33-6-30 to -37 (2001); IND. CODE §§ 27-4-1-1 to -19 (2003) (neither the statutes nor cases citing the statutes state or even imply that an insurer has an obligation to use multiple adjusters or risk bad faith liability). Further, the authors also rely upon a section of a treatise that they admit was omitted from later editions of that same treatise: CLINTON E. MILLER, HOW INSURANCE COMPANIES SETTLE CASES §§ 311–311.2 (13th rev. ed. 2001). See Huber & Krahulik, *supra* note 4, at 48, n.75 (noting that “[i]n a subsequent edition, these particular sections in the Miller treatise have been revised and largely omitted”).

106. See *Aetna Cas. & Sur. Co. v. Mitchell Bros., Inc.*, 814 So. 2d 191, 198 (Ala. 2001) (insurer did not act in bad faith where its personnel were involved in both the coverage dispute and defense of a claim against its insured and the insurer disclosed settlement information to a party adverse to the insured); *Employers Ins. of Wausau v. Albert D. Seeno Constr. Co.*, 945 F.2d 284, 286 (9th Cir. 1991) (rejecting the insured's argument that “where the carrier reserves its right to assert a coverage defense, it must use different people on the liability side and the coverage side, without exchange of information between them”).

107. 265 Cal. Rptr. 372 (Ct. App. 1989).

108. *Id.* at 373.

insurer agreed to pay the defense fees.¹⁰⁹ The insurer simultaneously retained its own counsel for its declaratory judgment action against the insureds and assigned a single adjuster to handle the insureds' claim as well as the declaratory judgment coverage action.¹¹⁰ Throughout the adjuster's interaction with the insureds' counsel, the adjuster consistently informed counsel that State Farm did not believe that there was coverage.¹¹¹

In the declaratory action, the insureds sought production of all documents in the adjuster's files, claiming that the adjuster acted as their agent regarding the underlying claim. The insureds asserted that they should be permitted to see the contents of his files, including any communications between the adjuster and State Farm's coverage counsel. The court rejected the insureds' argument that the insurance company should be required to assign separate adjusters or face waiver of the attorney-client privilege with its coverage counsel.¹¹²

The *Durant* court stated that although "[t]he relationship between an insurer and an insured is akin to a fiduciary relationship . . . [.] the protection afforded by that relationship is not unlimited."¹¹³ Additionally, it found that "the insurer has no duty to totally disregard its own interests when they conflict with the insured's interests."¹¹⁴ As further support for its decision, the court pointed out that, particularly in situations where coverage is at issue, it should be obvious to the insured that the "adjuster's loyalties are divided and the insured and his counsel cannot reasonably expect that he represents only the interest of the insured."¹¹⁵ Thus, the holding in *Durant* makes it clear that an insurer should not be liable for bad faith for using one adjuster to handle the underlying claim and the coverage action.

E. Multiple, Unsubstantiated Defenses

Finally, the authors of *Bad Faith Coverage Litigation* assert that an insurer may be liable for bad faith where, for example, it pleads a number of boilerplate affirmative defenses in its answer to an insured's complaint.¹¹⁶ Notably, the only relevant cited case involved a set of facts where the court found that the insurer had not acted in bad faith by asserting affirmative

109. *Id.* The term "Cumis counsel" derives from *San Diego Federal Credit Union v. Cumis Insurance Society, Inc.*, 208 Cal. Rptr. 494 (Ct. App. 1984), where the court held that when an insurer issues a reservation of rights on a coverage issue that could be affected by the handling of the underlying case, there is a conflict of interest between the insurer and the insured. *Id.* at 506. In those situations, the insurer must provide, at its expense, independent counsel to the insured. *Id.* The court's holding in *Cumis* has been codified in CAL. CIV. CODE § 2860.

110. *State Farm*, 265 Cal. Rptr. at 373.

111. *Id.* at 373-74.

112. *Id.* at 375-76.

113. *Id.* at 374 (internal citations omitted).

114. *Id.*

115. *Id.* at 375.

116. Huber & Krahulik, *supra* note 4, at 49.

defenses.¹¹⁷ Further, contrary to prior arguments where there was little or no authority, a number of courts have considered and almost uniformly rejected bad faith claims that rely upon the alleged impropriety of the insurer's tactics during coverage litigation. Simply put, an insurer's choices regarding what pleadings it will file (including answers, dispositive motions, and counterclaims) and what positions it will take (such as asserting affirmative defenses or objecting to or serving discovery) are not open to scrutiny and cannot form the basis of bad faith liability.¹¹⁸

As indicated, courts have considered and almost universally determined that insurers should decide (without the threat of a bad faith action) the specific tactical approach to take in any given set of circumstances. The Federal Rules of Civil Procedure provide rules for proceeding with litigation as well as remedies in cases where alleged violations occur. It is not necessary to add an extra layer of protection in the form of possible bad faith liability for insureds that are engaged in coverage litigation with their insurers.

Further, like other litigants, an insurer's coverage litigation pleadings must meet the applicable pleading standards. If they do not, the insured can move to strike the pleadings, seek sanctions, or pursue whatever remedies the applicable rules allow. Like other litigants, the insurer may raise defenses that turn out to be unupportable after conducting discovery. An insurer should not be subject to the threat of bad faith liability simply because the insurer seeks to defend itself in the coverage litigation.¹¹⁹

CONCLUSION

Twenty-three years ago, the California Supreme Court in *White v. Western Title Insurance Co.* held that an insurer's settlement conduct after the

117. *Chowdhury v. LMI Ins. Co.*, No. CIV. A. 94-6223, 1996 WL 53804 (E.D. Pa. Feb. 8, 1996).

118. *See, e.g., Timberlake Constr. Co. v. U.S. Fid. & Guar. Co.*, 71 F.3d 335, 339-40 (10th Cir. 1995) (holding that trial court erred in allowing insurer's litigation conduct into evidence, including (1) a letter from insurer's counsel to its adjuster, (2) the insurer's counterclaim against the insured, and (3) the insurer's motion to join a third party to the coverage litigation); *Palmer by Diacon v. Farmers Ins. Co. Exch.*, 861 P.2d 895, 909 (Mont. 1993) (holding that evidence of insurer's litigation conduct, in the form of reports from counsel, should not have been admitted); *Sims v. Travelers Ins. Co.*, 16 P.3d 468, 471 (Okla. Civ. App. 2000) (holding that evidence regarding insurers' deposition scheduling, rejection of request for mediation, and filing of motion to dismiss were irrelevant to insured's bad faith claim); *Parsons v. Allstate Ins. Co.*, No. 03CA2051, 2006 WL 3437561, at *9 (Colo. Ct. App. Nov. 30, 2006) (holding that insurer counsel's refusal to be deposed, filing of answer denying coverage, and other litigation conduct was inadmissible).

119. *See Reserve Life Ins. Co. v. Ayers*, 115 S.E.2d 477, 479 (Ga. Ct. App. 1960) (noting that when determining whether an insurer has acted in bad faith, "[t]he issue is whether or not the insurance company frivolously or by unfounded reason refused to pay a just claim, and not whether the insurance company is defending the case in bad faith") (internal citations omitted).

commencement of coverage litigation could be used as evidence of bad faith. As discussed, the *White* holding and the efforts to expand *White* are contrary to the foundational principles of bad faith law. Simply put, the choices that an insurer makes in coverage litigation do not relate to or arise out of the insurer-insured relationship. Policyholders can resolve adequately their grievances by using the Federal Rules of Civil Procedure and the ethical rules governing the conduct of attorneys. Moreover, allowing policyholders to use insurers' conduct during coverage litigation to show bad faith would hold insurers to a more stringent standard of litigation conduct than noninsurers. Courts in numerous jurisdictions have already recognized these problems and have refused to apply a different litigation standard to insurers.

Attempts by some courts subsequent to *White* to distinguish settlement conduct from other types of insurers' conduct in coverage litigation are ineffective. The efforts to maintain this distinction likely grew from an inability or a reluctance to eliminate the *White* holding completely. Litigants routinely make settlement offers after litigation commences. Noninsurer litigants are able to decide freely when and how much to offer without the threat of bad faith liability. Failing to afford insurers the same right is unreasonable and unduly prejudicial and inevitably results in insurers being held to a higher standard of litigation conduct.

Although the so-called doctrine of continuing bad faith is in decline, the authors of this article call for its total fall. The decisions by a minority of courts that have expanded continuing bad faith or otherwise allowed the admission of insurers' settlement conduct during coverage litigation have most often failed to consider the principles underlying bad faith law. However, the majority of courts that have at least partially considered the application of these principles have laid the groundwork for future courts to correct this unfounded legal anomaly. Accordingly, courts should adopt an absolute prohibition precluding a policyholder from using an insurer's conduct during the course of coverage litigation as a basis for bad faith or continuing bad faith.