

## Delaware Supreme Court Determines Timing of Action for Bad Faith Failure to Settle Third-Party Claim

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On March 4, 2016, the Delaware Supreme Court ruled that an action for an insurer's bad faith failure to settle a third-party claim accrues only after a judgment against the policyholder for an amount exceeding the policy limits becomes final and non-appealable. The case is captioned *Connolly v. State Farm Mutual Auto Insurance Company*, No. 426, 2015. In this matter of first-impression for the court, it joined the majority of authorities to have considered the issue.

### FACTS

In an underlying personal injury action, State Farm Mutual Automobile Insurance Company insured Ronald Brown at the time his vehicle rear-ended a vehicle driven by Christina Connolly. Brown's State Farm policy provided bodily injury limits of \$100,000 per person and up to \$300,000 per occurrence. Connolly sued Brown for personal injuries, and offered to resolve her claims for \$35,000. State Farm rejected Connolly's settlement offer and the case proceeded to trial where the jury awarded Connolly more than \$224,000 on her claims, which rose to more than \$333,000 with interest and costs. State Farm did not appeal the excess judgment. State Farm paid Connolly approximately \$152,000, but left Brown responsible for the remainder of the judgment. Brown assigned his bad faith claim to Connolly, who then filed a lawsuit against State Farm for bad faith related to its refusal to settle within policy limits and neglecting to appeal the excess judgment.

The trial court dismissed Connolly's bad faith lawsuit, citing that it was time-barred by the three year statute of limitations under 10 *Del. C. § 8106*. According to the trial court, the bad faith claim accrued at the time State Farm breached its insurance contract (*i.e.*, when it refused Connolly's settlement offer). The Delaware Supreme Court agreed that section 8106 supplied the appropriate statute of limitations, but held that it did not begin to run until the excess verdict became final and non-appealable, a date well-within three years of Connolly's bad faith lawsuit.

### ANALYSIS

A duty of good faith and fair dealing is implied in every contract. In the context of an insurance policy, the implied covenants obligate an insurer to settle claims within policy limits where recovery in excess of those limits is substantially likely according to the Delaware Supreme Court. With this context in mind, the court weighed several public policy considerations:

1. reducing the possibility of a conflict of interest between the insurer and insured by avoiding early pursuit of a bad faith claim while the parties should be working together on a defense of the underlying bodily injury claim,
2. protecting the insurer from bad faith claims for failing to settle even the most frivolous claims, and
3. avoiding wasting judicial and party resources over premature bad faith claims that may turn out to be unnecessary if there is not an excess judgment.

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Lastly, the court analogized the indemnification obligations of insurance policies to the indemnification of officers and directors under the Delaware General Corporate Law, which does not accrue until the underlying action is resolved with certainty.

## FINDINGS

As such, the date an excess judgment becomes final and non-appealable is the bright line trigger for a bad faith lawsuit in Delaware. Of course, not every excess verdict will constitute bad faith failure to settle. For example, many factors must be considered before determining whether there is a "substantial likelihood" of an excess judgment or whether the underlying claim is "frivolous." The Delaware Supreme Court reserves to the insurer the freedom to judge these factors when considering offers to settle within policy limits. However, insurers are cautioned to exercise this freedom carefully as the tenor of the court's ruling in *Connelly* evidences a preference for protecting policy-holders from excess judgments.

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