No. 35763 – *Thomas D. Loudin and Alice M. Loudin v. National Liability & Fire Insurance Company, Jack Sergent, D.L. Thompson and Consolidated Claim Service, Inc.*

FILED
October 24, 2011
RORY L. PERRY II, CLERK
SUPREME COURT OF APPEALS
OF WEST VIRGINIA

Benjamin, Justice, dissenting:

In a radical departure from our jurisprudence and wholly without support from other courts, the majority opinion creates a duty of good faith and fair dealing in the absence of an underlying contractual duty. In doing so, the majority opinion places insurance companies in the impossible position of owing a duty of good faith and fair dealing to two potentially antagonistic parties at the same time. For these reasons, I am compelled to dissent.

The majority bases its opinion solely on the fact that Thomas Loudin was the purchaser of the insurance policy in this case. This analysis is superficial and incomplete. An insurance policy contains both first-party and third-party coverages. This case involves a liability insurance provision which is third-party coverage.[1]

---

[1]The liability portion of the insurance policy at issue provides, in part, as follows:

> **SECTION II - LIABILITY COVERAGE**
>
> **A. Coverage**
>
> We will pay all sums an "insured" legally must pay as damages because of "bodily injury" or "property damage" to which this insurance applies, caused by an "accident" and resulting from the ownership, maintenance or use of a covered "auto".

Authorities have explained the distinction between first-party and third-party coverages as follows:

> An insurance policy may contain both first party property and third party liability coverages, and these coverages differ in their focus. "First-party coverage" pertains to loss or damage sustained by an insured to its property, and under such a policy, the insured receives the proceeds when the damage occurs. If the insurer's duty to defend and pay runs to a third-party claimant who is paid according to a judgment or settlement against the insured, then the insurance is classified as "third-party insurance."
>
> Once an occurrence or accident has happened and the third party has been injured by the insured's conduct, liability coverage becomes implicated.

---

* * * *

> We have the right and duty to defend any "insured" against a "suit" asking for such damages or a "covered pollution cost or expense". However, we have no duty to defend any "insured" against a "suit" seeking damages for "bodily injury" or "property damage" or a "covered pollution cost or expense" to which this insurance does not apply. We may investigate and settle any claim or "suit" as we consider appropriate. Our duty to defend or settle ends when the Liability Coverage Limit of Insurance has been exhausted by payment of judgments or settlements.
>
> **1. Who Is An Insured**
>
> The following are "insureds".
>
> **a.** You for any covered "auto".
> **b.** Anyone else while using with your permission a covered "auto" you own, hire or borrow[.]

46 C.J.S. *Insurance* § 1239, in part, (2007) (footnotes omitted). Commentators further have indicated that

> In many insurance contexts, ranging from principles of causation to the varied post-loss duties addressed here, courts recognize the conceptual and practical differences between "first-party" and "third-party" insurance.
>
> "First-party" insurance is a contract between the insurer and the insured to protect the insured from its own actual losses and expenses. Property insurance, fidelity insurance, and medical/health insurance are all examples of first-party insurance.
>
> "Third-party" insurance is a contract to protect the insured from losses resulting from actual or potential liability to a third party. This protection may involve defending the insured from suit, paying or settling a claim against the insured, or a combination of both. Liability insurance is third-party insurance.

Couch On Insurance3d § 198:3 (2005) (footnotes omitted).

The courts of other jurisdictions uniformly recognize that liability insurance constitutes third-party coverage. *See e.g., Sibothan v. Neubert,* 168 S.W.2d 981, 983 (Mo. Ct. App. 1943) ("third party coverage . . . is . . . insurance against the liability of the insured for injury which has been sustained by some third person through negligence in the operation of the automobile"); *U. S. Fidelity and Guaranty Co. v. Nationwide Mut. Ins. Co.,* 110 Ohio App. 363, 163 N.E.2d 46, 54 (Ohio Ct. App. 1959 (same); *Hartford Acc. & Indem. v. Aetna Cas.,* 164 Ariz. 286, 792 P.2d 749, 752 n. 1 (1990) ("Third party coverage comes into play

when an insurance carrier contracts to compensate its insured for liability to third parties. First party coverage involves liability policies which directly benefit the insured."); *Kromer v. Reliance Ins. Co.,* 450 Pa.Super. 631, 677 A.2d 1224, 1230 n. 3 (1996) ("A liability policy is commonly known and referred to as a [sic] third party coverage. There are three parties, the insurance company, the insured and the claimant. . . . [I]f the insured is liable for whatever is claimed, the insurance company will pay on behalf of the insured to the claimant the damages sought up to the liability limits" (citation omitted)); *Lynch ex rel. Lynch v. Am. Family Mut.,* 626 N.W.2d 182, 188 (Minn. 2001) ("[l]iability insurance is third-party coverage, meaning that it pays for damage the insured is legally obligated to pay another person, a third party, for bodily injury"); *American Family Mut. Ins. Co. v. Petersen,* 679 N.W.2d 571, 581 (Iowa 2004) ("Liability coverage involves third-party coverage and exists as a form of indemnification to protect the insured from paying for damages the insured causes to others."); *Black v. Allstate Ins. Co.,* 100 P.3d 1163, 1168 (Utah 2004) ("first-party coverage[] . . . refers to an insurance agreement where the insurer agrees to pay claims submitted to it by the insured for losses suffered by the insured, and third-party coverage[] . . . refers to an agreement wherein the insurer contracts to defend the insured against claims made by third parties against the insured and to pay any resulting liability up to the specified dollar limit." (Internal quotation marks and citation omitted)).

Liability coverage involves three parties: the insurance company, the insured,

and the claimant. The insured is the party whom the insurer agrees to defend and indemnify in a suit brought by the third-party claimant. The third-party claimant is the injured person who asserts a claim against the insured for damages allegedly caused by the insured's conduct. The insured under the liability coverage in this case is William Loudin who was a permissive user of the covered automobile. Thomas Loudin sued William Loudin for bodily injuries allegedly caused by William Loudin's negligence. The insurer, National, provided a defense to William Loudin and paid a settlement on his behalf to Thomas Loudin per the terms of the liability coverage. It is evident then that even though Thomas Loudin is the policyholder, he is not a first-party insured but rather a third-party claimant in this case.

The fact that Thomas Loudin is a third-party claimant is further supported by the legislative rules of the Insurance Commissioner. According to 114 CSR § 14-2.3,

> "First-party claimant" or "Insured" means an individual, corporation, association, or partnership or other legal entity asserting a right to payment under an insurance policy or insurance contract arising out of the occurrence of the contingency or loss covered by such policy or contract.

On the other hand,

> "Third-party claimant" means any individual, corporation, association, partnership or other legal entity asserting a claim against any individual, corporation, association, partnership or other legal entity under an insurance policy or insurance contract of an insurer.

114 CSR § 14-2.8. The majority wrongly indicates that Thomas Loudin falls within the

above definition of a first-party claimant. He does not. Thomas Loudin did not assert a right to payment under the insurance policy arising out of the occurrence of the contingency or loss covered by the policy. Instead, he asserted a claim against William Loudin who had liability coverage under the National policy. It is only through William Loudin that Thomas Loudin is able to collect under his insurance policy. This places Thomas Loudin squarely within the definition of a third-party claimant.

My conclusion that Thomas Loudin is a third-party claimant under the facts of this case is supported by every other court that has addressed this specific issue. For example, in the case of *Gillette v. Estate of Gillette,* 163 Ohio App.3d 426, 837 N.E.2d 1283 (2005), Joseph M. Gillette wrecked his minivan resulting in an injury to his wife. At the time of the accident, Mr. Gillette's minivan was covered by a policy issued by Nationwide. The declarations page of the policy named Joseph as the only named insured. Although, Mrs. Gillette was not the named insured, as the spouse of the named insured, she was an insured under the policy. After Mrs. Gillette rejected Nationwide's settlement offer, she filed a complaint against Nationwide, asserting bad faith on the part of the insurer for refusing to pay the full amount of insurance proceeds owed to her under the policy. She also asserted a negligence claim against her husband for causing the accident in which she was injured. The issue on appeal was whether a third-party claimant who is also an insured may bring a claim for bad faith against an insurer. In deciding this issue, the court in Gillette reasoned

as follows:

> From this antagonistic position, the insured spouse did not seek benefits based upon a duty the insurer owed directly to her. Rather, the insured spouse sought benefits based upon the duty the insurer owed to the coinsured to pay for damages for which the coinsured was liable. Although the insured spouse might ultimately benefit from a claim under her coinsured's liability coverage, that benefit flowed from the insurer's compliance with the duty owed to the coinsured, not any duty owed to the insured spouse. Accordingly, because the insurer did not owe any contractual duty to the insured spouse to pay her liability benefits, the insurer did not owe any overlying duty of good faith in handling the insured spouse's claims for liability benefits.

Gillette, 837 N.E.2d at 1288. The court in *Gillette* concluded,

> although [Mrs. Gillette] is an insured under the Nationwide policy, where she seeks liability coverage for the negligence of the named insured - her husband - she stands in the shoes of a third party claimant who is not owed any contractual duty by the insurer. Thus, we conclude that [Mrs. Gillette] is barred from asserting a claim for bad faith for Nationwide's delay in paying her benefits pursuant to the "Auto Liability" section of the policy.

837 N.E.2d at 1289. *See also, Wilson v. Wilson,* 121 N.C.App. 662, 468 S.E.2d 495 (1996); *Rumley v. Allstate Indemnity Co.,* 924 S.W.2d 448 (Tex. App. 1996); *Smith v. Allstate Ins. Co.,* 202 F.Supp.2d 1061 (D.Ariz. 2002). The reasoning in these cases also applies where the third-party claimant was a named insured under the subject insurance policy as in the instant case. *See Herrig v. Herrig,* 844 P.2d 487 (Wyo. 1992); *Sperry v. Sperry,* 990 P.2d 381 (Utah 1999).

Despite the majority's assertions to the contrary, the reasoning in *Gillette* and its progeny is applicable to the instant case. Thomas Loudin did not seek benefits based upon a duty that National owed directly to him. Instead, Thomas Loudin sought benefits based upon the duty that National owed to William Loudin as the insured permissive user to pay damages for which William Loudin was liable. The benefit to Thomas Loudin flowed from National's compliance with the duty owed to William Loudin, not any duty owed under the liability coverage to Thomas Loudin. Therefore, because National did not owe any contractual duty to Thomas Loudin under the liability coverage, National did not owe any underlying duty of good faith and fair dealing in handling Thomas Loudin's claim for liability benefits.

Further, in addition to my concern with the majority's incorrect application of legal precedent, I am also troubled by the practical effects of the majority opinion. Unfortunately, the majority opinion creates a real conflict of interest for insurance companies in cases like this one. According to the majority, insurers now owe a duty of good faith and fair dealing to two potentially antagonistic parties in a liability dispute. First, the insurer has a duty of good faith and fair dealing to the permissive user under its policy. *See Shamblin v. Nationwide Mut. Ins. Co.,* 183 W. Va. 585, 396 S.E.2d 766 (1990) (recognizing an insurer's duty to attempt in good faith to negotiate a settlement with an injured third party and to accord interests and rights of the insured at least as great a respect as its own);

Charles v. State Farm Mut. Auto. Ins. Co., 192 W. Va. 293, 298, 452 S.E.2d 384, 389 (1994) (explaining that "[a]lthough [the permissive user of the covered auto] was not the original purchaser of the insurance, he was nonetheless an 'insured' under the policy and is, therefore, entitled to the protections of the *Shamblin* doctrine"). According to the majority, if an insurer allegedly fails to exercise good faith in procuring a settlement with a third-party policyholder claimant, *both* the permissive user and the third-party policyholder claimant can pursue a bad faith claim against the insurer. In addition, if the insurer rolls over in its defense and indemnification of the permissive user in favor of the policyholder claimant, the policyholder claimant can maintain a first-party bad faith action against the insurer on the basis that the insurer wrongly failed to defend the permissive user, causing an increase in the policyholder's experience rating and resulting in future higher premiums to the policyholder.

In sum, the majority has taken the unprecedented step of creating a duty of good faith in the absence of an underlying contractual obligation. This novel free-floating duty places insurance companies in the untenable position of owing a duty of good faith and fair dealing to two potentially antagonistic parties at the same time. Finally, it increases exponentially the potential number of bad faith claims against insurers arising from their handling of liability claims where the policyholder is also a third-party claimant. For these reasons, I respectfully dissent.