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A SURVEY OF BAD FAITH LAW IN THE SOUTH

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A SURVEY OF BAD FAITH LAW IN THE SOUTH

BY

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I. Alabama

A. Origin of the Duty

1. Statutory Basis

- a. There is no statutory basis for an insured to bring a bad faith claim under Alabama law. *N.C. Mut. Life Ins. Co. v. Holley*, 533 So. 2d 497, 508 (Ala. 1987).

2. Common Law Cause of Action

- a. Alabama courts recognize a common law cause of action for bad faith. See *Fed. Ins. Co. v. Travelers Cas. & Sur. Co., et al.*, 843 So. 2d 140 (Ala. 2002); *Chavers v. Nat. Sec. Fire & Cas. Co.*, 405 So. 2d 1, 7 (Ala. 1981).
- b. In order to recover for a claim for bad faith failure to settle, the insurer must have no lawful basis to refuse the claim and actual knowledge of this fact, or the insurer has intentionally failed to determine whether or not there was a lawful basis for the refusal. *Chavers*, 405 So. 2d at 7.
- c. In *National Security Fire & Casualty Company v. Bowen*, 417 So. 2d 179, 183 (Ala. 1982), the Alabama Supreme Court stated that there are five requirements for plaintiff to satisfy its burden in a bad faith case:
 - i. An insurance contract between the parties and a breach thereof by the insurer;
 - ii. An intentional refusal to pay the insured's claim;
 - iii. The absence of any reasonably legitimate or arguable reason for the refusal;
 - iv. The insurer's actual knowledge of the absence of a legitimate or arguable reason; and
 - v. If the intentional failure to determine the existence of a reasonable basis is relied upon, the plaintiff must prove the insurer's intentional failure to determine whether there is a legitimate or arguable reason to pay.

B. Third-Party Actions

1. Because there is no statutory basis for an insured to bring a bad faith claim under Alabama law, a third party cannot bring a statutory bad faith claim.

C. Applicability to Sureties and Fidelity Insurers

1. Alabama courts have not directly addressed the issue of bad faith in the context of suretyship. However, courts have analyzed a surety's actions under the elements of bad faith when discussing whether the tort of bad faith should apply to a surety.
2. In *Elmore v. Morrison Assurance Co.*, 502 So. 2d 378 (Ala. 1987), a surety brought an action against the principal and its indemnitors on a performance bond. The trial court instructed the jury to award damages to the surety in the amount that is paid in good faith on behalf of the principal.
3. In *Hightower & Company v. United States Fidelity & Guaranty Company*, 527 So. 2d 698 (Ala. 1988), a surety brought an indemnification action against its principal on payment and performance bonds. The principal counterclaimed, alleging that the surety had breached its duty of good faith. The issue of the application of bad faith to sureties went unresolved, as the appellate court found that the trial court's decision to grant the surety's motion for summary judgment was premature.
4. In *Knutilla v. Auto-Owners Insurance Company*, 578 So. 2d 1359 (Ala. Civ. App. 1991), the purchasers of time-share units brought a claim against a statutory surety bond for bad faith refusal to pay their claim. The court found that the claim was debatable, and a lawful basis for denial existed. Therefore, the court found that there was no basis for a bad faith action. However, the court refrained from directly addressing the issue of whether a bad faith action can be brought against the surety, as it was unnecessary to make such a determination under the facts of the case.

D. Damages

1. Punitive Damages
 - a. Punitive damages are recoverable for the tort of bad faith under Alabama law. See *Intercontinental Life. Ins. Co. v. Lindblom*, 598 So. 2d 886, 890 (Ala. 1992).
2. Attorneys' Fees
 - a. Attorneys' fees are only recoverable under Alabama law if provided for by statute. No statutory attorneys' fees are provided for under Alabama law.

3. Consequential Damages
 - a. Consequential damages, such as economic loss, are recoverable for bad faith claims under Alabama law. *Chavers*, 405 So. 2d at 7; *Gulf Atl. Life Ins. Co. v. Barnes*, 405 So. 2d 916, 925 (Ala. 1981).
 4. Emotional Distress
 - a. Alabama courts have recognized emotional distress damages arising out of bad faith claims against insurers. *Chavers*, 405 So. 2d at 7.
- E. Statute of Limitations
1. The statute of limitations for bad faith claims under Alabama law is two years. Ala. Code Ann. § 6-2-38(1).
 2. A claim of bad faith accrues at the time the party bringing the action knew facts that would put a reasonable person on notice of the possible bad faith. *Alfa Mut. Ins. Co. v. Smith*, 540 So. 2d 691 (Ala. 1988).

II. Arkansas

- A. Origin of the Duty
1. Statutory Basis
 - a. A limited private cause of action is available under Arkansas Code Annotated § 23-79-208(a)(1) if an insurer fails to pay losses within the time specified in the policy after demand is made.
 - b. The Arkansas Unfair Trade Practices Act does not provide a private cause of action for violation of its terms. A.C.A. § 23-66-201, *et seq.*
 2. Common Law Cause of Action
 - a. Arkansas courts recognize a common law cause of action for bad faith. *See, e.g., Findley v. Time Ins. Co.*, 573 S.W.2d 908, 909 (Ark. 1978).
 - b. A common law cause of action for bad faith requires affirmative conduct, without a good faith defense; the conduct must be dishonest, malicious or oppressive, and performed in order to escape liability under an insurance policy. *Reynolds v. Shelter Mut. Ins. Co.*, 852 S.W.2d 799, 801 (Ark. 1993).
 - c. The tort of bad faith does not arise from the mere denial of a claim; rather, there must have been affirmative misconduct on the part of the

insurer. See *Columbia Nat'l Ins. Co. v. Freeman*, 64 S.W.3d 720 (Ark. 2002).

B. Third-Party Actions

1. Arkansas Code Annotated § 23-79-208(a)(1) has not been applied to third-party claims.
2. Arkansas common law recognizes a third-party claim on the tort of bad faith for the negligent failure of an insurer to settle a third-party claim within policy limits. *R.J. "Bob" Jones Excavating Contractor, Inc. v. Fireman's Ins. Co.*, 920 S.W.2d 483, 487 (Ark. 1996).

C. Applicability to Sureties and Fidelity Insurers

1. *Johnson v. Safeco Insurance Company of America*, 576 S.W.2d 220 (Ark. 1979), involved allegations of bad faith against a surety. The *Johnson* court found that no allegations of bad faith were made in the matter, since failure to properly investigate does not constitute bad faith under Arkansas law. In dicta, the court distinguished sureties from insurers. The court noted that a surety is put in an untenable position if it is held to the standard set forth and applied to insurers. The court reasoned that the volunteer doctrine creates a "Catch-22" that the surety cannot escape: "If a surety should pay a claim when there is no liability on the part of its principal, it is treated as a volunteer and cannot recover the payment from the principal." However, the issue of whether an action for bad faith can be brought against a surety was never directly decided by the court.
2. The issue of the viability of a bad faith action against a surety was again avoided in *R.J. "Bob" Jones Excavating Contractor, Inc.* In that case, a subcontractor brought suit against a general contractor's surety under a payment bond for bad faith. The court found that the surety was justified in its failure to pay the subcontractor since there was a genuine issue as to the principal's liability. The court questioned whether the tort of bad faith applies to a surety. However, the court did not decide the issue, because the tort was not proven under the circumstances of the case.

D. Damages

1. Punitive Damages
 - a. An insured can recover punitive damages from an insurer if the insurer's conduct is dishonest, malicious or oppressive. *Viking Ins. Co. of Wis. v. Jester*, 836 S.W.2d 371 (1992).

- b. An insurer who has failed to pay an insured in violation of Arkansas Code Annotated § 23-79-208(a)(1) shall be liable for the amount of the loss, in addition to 12% damages upon the amount of the loss.
- 2. Attorneys' Fees
 - a. Reasonable attorneys' fees are available for violations of section 23-79-208(a)(1).
 - b. Arkansas courts have not addressed whether attorneys' fees are available under a common law bad faith claim.
- 3. Consequential Damages
 - a. Consequential damages have been allowed pursuant to a common law bad faith claim.
- 4. Emotional Distress
 - a. A plaintiff was able to recover for emotional distress damages in *Southern Farm Bureau Casualty Insurance Company v. Allen*, 934 S.W.2d 527 (1996).
- E. Statute of Limitations
 - 1. There is a three-year statute of limitations for common law bad faith claims. Ark. Code Ann. § 16-56-105.
 - 2. The statute of limitations for actions brought under section 23-79-208(a)(1) is two years. Ark. Code Ann. § 16-56-108.

III. Florida

- A. Origin of the Duty
 - 1. Statutory Basis
 - a. A first-party insured can bring a bad faith action under Florida Statute § 624.155 after the insured provides the Florida Department of Financial Services and the insurer with 60 days written notice of the violation.
 - 2. Common Law Cause of Action
 - a. There is a common law cause of action for third parties under Florida law, but not first parties. See *Talat Enter., Inc. v. Aetna Cas. & Sur. Co.*, 753 So. 2d 1278, 1281 (Fla. 2000).

B. Third-Party Actions

1. Florida Statute § 624.155(b)(1) provides for a third-party bad faith cause of action in the event of an excess judgment. See *Dadeland Depot, Inc. v. St. Paul Fire & Marine Ins. Co.*, 945 So. 2d 1216, 1224 (Fla. 2006); *State Farm Fire & Cas. Co. v. Zebrowski*, 706 So. 2d 275 (Fla. 1997).

C. Applicability to Sureties and Fidelity Insurers

1. The Florida legislature has amended the bad faith statute to exempt contract sureties. Fla. Stat. Ann. § 624.155. However, this statute is only prospective from its effective date of June 14, 2005.
2. In *Dadeland Depot, Inc.*, the Florida Supreme Court was asked to determine whether a surety was liable under F.S.A. 624.155 for bad faith refusal to settle with an obligee under a performance bond. The court determined that a surety is an insurer under section 624.03. Next, the court determined that an obligee falls under the definition of an “insured” for purposes of section 624.155(1)(b)(1). Accordingly, the court held that the obligee of a surety contract qualifies as an “insured” and is therefore entitled to sue its surety for bad faith refusal to settle claims pursuant to section 624.155(1)(b)(1) of the Florida Statutes (1999).

D. Damages

1. Punitive Damages
 - a. Florida Statute § 624.155(5) provides for punitive damages in bad faith causes of action.
2. Attorneys’ Fees
 - a. Florida Statute § 624.155(4) specifically provides for attorneys’ fees upon adverse adjudication at trial or upon appeal.
 - b. Attorneys’ fees are recoverable under Florida Statute § 627.428 for common law third-party bad faith actions.
3. Consequential Damages
 - a. Consequential damages are recoverable for bad faith causes of action under Florida law. See *Nichols v. State Farm Mut.*, 851 So. 2d 742, 752 (Fla. App. 2003).

4. Emotional Distress

- a. The only situation in which an insured can recover emotional distress damages is if it is bringing an action against a health insurer for bad faith failure to settle. See *Time Ins. Co. v. Burger*, 712 So. 2d 389 (Fla. 1998); *Talet Enter., Inc.*, 753 So. 2d at 1281.

E. Statute of Limitations

1. The statute of limitations for an action founded on statutorily imposed liability is four years. Fla. Stat. Ann. § 95.11(f).
2. A claim for bad faith failure to settle accrues only after an insured has proven liability in his or her underlying contractual claim. See *Lane v. Provident Life & Acc. Ins. Co.*, 71 F. Supp. 2d 1255 (S.D. Fla. 1999).

IV. Louisiana

A. Origin of the Duty

1. Statutory Basis

- a. Louisiana law, like that of the vast majority of states, recognizes the inherent obligation on parties to a contract to deal in good faith. The Louisiana Civil Code codifies the obligation to act in good faith incumbent upon all parties at La. C.C. arts. 1759 and 1983. See *Lambert v. Md. Cas. Co.*, 418 So. 2d 553 (La. 1982).
- b. La. R.S. 22:1220(A) provides: “An insurer . . . owes to his insured a duty of good faith and fair dealing. The insurer has an affirmative duty to adjust claims fairly and promptly and to make a reasonable effort to settle claims with the insured or the claimant, or both.”
- c. La. R.S. 22:658(A)(1) provides: “All insurers issuing any type of contract . . . shall pay the amount of any claim due any insured within thirty days after receipt of satisfactory proofs of loss from the insured or any party in interest. . . .”

2. Common Law Cause of Action

- a. Louisiana does not recognize a common law cause of action for bad faith.

B. Third-Party Actions

1. La. R.S. 22:1220(B) permits a third-party claimant to bring a bad faith action against an insurer for knowingly misrepresenting facts or policy provisions

regarding insurance coverage; failing to pay a settlement within 30 days of a written settlement agreement; failing to pay the amount of any claim due any person insured by the contract within sixty days after receipt of satisfactory proof of loss; or misleading a claimant on prescription or the statute of limitations. Prior to the 1990 enactment of section 1220, no duty was owed to third parties.

2. La. R.S. 22:658 requires insurers to pay the amount of any third-party property damage claim and of any reasonable medical expenses claim within 30 days after written agreement of settlement of the claim from any third-party claimant. Further, an insurer must make a written offer to settle any property damage claim, including a third-party claim, within 30 days after receipt of satisfactory proofs of loss of that claim.
3. In *Great Southwest Insurance Company v. CNA Insurance Company*, 557 So. 2d 966 (La. 1990), an excess carrier recovered against a primary carrier for failure to settle within policy limits, causing a loss to the excess insurer.

C. Applicability to Sureties and Fidelity Insurers

1. In *Bankston v. Loranger Milk Plant, Inc.*, 17 So. 2d 332 (La. 1944), the Louisiana Supreme Court discussed the penalties allowable under the predecessor statutes to sections 22:658 and 22:1220, denying recovery of fees and penalties against a surety. According to the *Bankston* court, those provisions applied only to bonds given in connection with a **fiduciary relationship**. A relationship of creditor/debtor, which was present in *Bankston*, did not warrant the imposition of penalties against the surety. Attorneys' fees were, however, properly assessed against the surety for its failure to show good cause for delay in settlement.
2. In *National Bank of Commerce of New Orleans v. Fidelity & Casualty Company*, 312 F. Supp. 71 (E.D.L.A. 1970), *aff'd* 437 F.2d 96 (5th Cir. 1971), the U.S. District Court for the Eastern District of Louisiana, applying Louisiana law, determined that the penalty provisions of La. R.S. 22:658 may be applicable to a fidelity insurer issuing a blanket banker's bond. The court refused to assess penalties under the statutes, but only because the insurer's actions were not deemed arbitrary or capricious, as defined by that provision. A very similar analysis was employed by the court in *Hudson v. Maryland Casualty Company*, 260 So. 2d 805 (La. App. 2 Cir. 1972).
3. The Fifth Circuit Court of Appeals, applying Louisiana law, engaged in the same analysis in *Howard, Weil, Labouisse, Friedrichs, Inc. v. Insurance Company of North America*, 557 F.2d 1055 (5th Cir. 1977), but clarified its previous commentary by stating that an insurer issuing a broker's blanket bond would be susceptible to the penalty provisions of La. R.S. 22:658 for arbitrary or capricious refusal to pay a claim to the principal.

4. In *Austin v. Parker*, 672 F.2d 508 (5th Cir. 1982), the Fifth Circuit found that section 22:658 applies to surety contracts, since surety bonds are considered insurance contracts under La. R.S. 22:6(8).
5. In *Metro Builders Hardware, Inc. v. Burko Construction, Inc.*, 633 So. 2d 838 (La. App. 4 Cir. 1994), a material man sought recovery from a surety on a Public Works Act bond. Concerning the plaintiff's claims for penalties and delay in payment under section 22:658, the court distinguished *Austin* by citing the Public Works Act. According to the *Burko* court, bonds issued under the Public Works act are not subject to the penalty provisions of La. R.S. 22:658 or La. R.S. 22:1220.
6. In *Hershell Corporation v. Fireman's Fund Insurance Company*, 743 So. 2d 698 (La. App. 3 Cir. 1999), a subcontractor sought to recover from a Private Works Act surety for a lien placed on the project. The court noted that both La. R.S. 22:658 and La. R.S. 22:1220 provide for attorneys' fees and penalties, but both provisions require an adequate proof of loss. Because there was no adequate proof of loss, the court denied recovery under these sections.

D. Damages

1. Punitive Damages

- a. La. R.S. 22:658 provides a penalty for a breach of some duties. The penalty is 50% damages on the amount found to be due from the insurer to the insured, or \$1,000.00, whichever is greater.
- b. La. R.S. 22:1220 provides for a penalty of an amount not exceeding twice the damages actually sustained as a result of breach of the insurer's duty, or \$5,000.00, whichever is greater.

2. Attorneys' Fees

- a. Attorneys' fees are not allowed in Louisiana except where authorized by statute or contract. *Wallace v. State Farm Mut. Auto. Ins. Co.*, 821 So. 2d 704, 709 (La. App. 2 Cir. 2002).
- b. Attorneys' fees are not provided for under La. R.S. 22:1220 or La. R.S. 22:658.

3. Consequential Damages

- a. La. R.S. 22:1220 states that both claimants and insureds are entitled to recover any general or special damages incurred as a result of the insurer's breach of an enumerated duty under that statute.

4. Emotional Distress

- a. A claimant or insured can recover for emotional distress (general damages) for breach of a duty under La. R.S. 22:1220.

E. Statute of Limitations

1. There is a one-year prescriptive period for torts in Louisiana. La. Civ. Code Ann. art. 3492.
2. There is a ten-year prescriptive period for breach of contract actions. La. Civ. Code Ann. art. 3499. Some courts have found that the prescriptive period for an insurer's breach of its statutory duties is ten years. *See Hebert v. Hill*, 37,208 (La. App. 2 Cir. 5/14/03), 855 So. 2d 768, 770; *We Sell Used Cars, Inc. v. United Nat'l Ins. Co.*, 30,671 (La. App. 2 Cir. 6/24/98), 715 So. 2d 656.

V. Mississippi

A. Origin of the Duty

1. Statutory Basis

- a. Section 75-1-203 of the Mississippi Code Annotated provides: "Every contract or duty within this code imposes an obligation of good faith in its performance or enforcement." This duty applies to insurance contracts. *See Lippincott v. Miss. Bureau of Narcotics*, 858 So. 2d 465 (Miss. App. 2003).

2. Common Law Cause of Action

- a. Mississippi recognizes a common law cause of action for bad faith. The cause of action is one for intentional tort. *See Universal Life Ins. Co. v. Veasley*, 610 So. 2d 290, 295 (Miss. 1992).

B. Third-Party Actions

1. Mississippi statutory law does not specifically set forth a third-party cause of action for bad faith. However, third parties can bring a common law cause of action against an insurer for bad faith.

C. Applicability to Sureties and Fidelity Insurers

1. In *Sentinel Industrial Contracting Corporation v. Kimmins Industrial Service Corporation*, 743 So. 2d 954 (Miss. 1999), a subcontractor sued the general contractor's surety alleging, inter alia, breach of contract and bad faith failure to pay the amounts due on the payment bond. The subcontractor argued on appeal that the trial court erred in refusing to instruct the jury on its claim against the surety for bad faith, alleging that sufficient evidence was presented "for the jury to determine that the surety acted with gross negligence or malice in failing to independently investigate and pay [the subcontractor's] claims." The court found that, where there is a legitimate dispute as to the amount owed, Mississippi Courts have held that a denial of a punitive damages instruction was proper. The court found that the parties were involved in a legitimate dispute as to the amount of damages owed under the subcontract. Further, the court found that the surety did not act with malice or gross negligence. As a result, the court found that the trial court had properly refused to grant the subcontractor's requested punitive damages instruction.
2. In *First United Financial Corporation v. United States Fidelity & Guaranty Company*, 96 F.3d 135 (5th Cir. Miss), a financial institution brought suit against its fidelity insurer to recover for losses resulting from the dishonest or fraudulent acts of its employees. The court held that the fidelity insurer did not breach its duty of good faith in failing to fully investigate the insured's claim, since the claims asserted in the insured's proof of loss were abandoned.
3. In *McQueen Contracting, Inc. v. Fidelity & Deposit of Maryland*, 871 F.2d 32 (5th Cir. 1989), a subcontractor sued to recover under a payment and performance bond issued by the general contractor's surety. In addition to compensatory damages, the subcontractor sought punitive damages based on the surety's bad faith in failing to pay under the bonds. The court found that the surety had a reasonably arguable basis for denying the subcontractor's claim. Therefore, the court denied the subcontractor's claim for punitive damages.

D. Damages

1. Punitive Damages

- a. Mississippi recognizes the assessment of punitive damages in bad faith cases. See *Sentinel Industrial Contracting Corp.*, 743 So. 2d at 972.
- b. Punitive damages are only appropriate in the context of a denial of an insurance claim if the insurer acted with malice, gross negligence, or reckless disregard for the insured's rights. *Gordon v. Nat'l States Ins. Co.*, 851 So. 2d 363, 366 (Miss 2003).
- c. In order to submit a claim for punitive damages against an insurer to a jury, the trial court must determine that there are jury issues with regard to whether (1) the insurer lacked an arguable or legitimate basis for denying the claim, and (2) the insurer committed a wilful or malicious wrong, or acted with gross and reckless disregard for the insured's rights. *State Farm Mut. Auto Ins. Co. v. Grimes*, 722 So. 2d 637, 641 (Miss. 1998).

2. Attorneys' Fees

- a. Attorneys' fees are recoverable when punitive damages are not available. For example, "an award of attorney fees would be appropriate as extra-contractual damages where a claim or defense was raised for purposes of harassment or delay or a party acted to unreasonably protract the proceedings." *Garner v. Hickman*, 733 So. 2d 191, 198 (Miss. 1999).
- b. Attorneys' fees may be awarded when an insurer is without an arguable basis to deny a claim, even though the insured is not awarded punitive damages. *Allstate Ins. Co. v. McGory*, 697 So. 2d 1171, 1179 (Miss. 1997).

3. Consequential Damages

- a. A plaintiff may recover consequential damages that were reasonably foreseeable at the time the contract was made and established at trial. *Wright v. Stevens*, 445 So. 2d 791, 835 (Miss. 1984).

4. Emotional Distress

- a. Damages for mental anguish may be awarded when such distress was reasonably foreseeable by the insurer at the time of the wrongdoing. *Veasley*, 610 So. 2d at 295.

E. Statute of Limitations

- 1. A common law cause of action for bad faith has a three-year statute of limitations. Miss. Code Ann. § 15-1-49.

VI. Tennessee

A. Origin of the Duty

1. Statutory Basis

- a. A bad faith claim can be asserted under the Tennessee Consumer Protection Act of 1977. Tenn. Code Ann. § 47-18-101, *et seq.*
- b. An insured also has a cause of action against its insurer for bad faith breach of an insurance contract under section 56-7-105 of the Tennessee Code Annotated. To recover under this section, the insured must show that the failure to pay inflicted additional expense, loss or injury upon the insured. See *Ray v. Shelter Ins. Cos.*, No. 01A01-9208-CV-00324, 1993 WL 15151 (Tenn. App. Jan. 27, 1993).

2. Common Law Cause of Action

- a. Tennessee courts do not recognize a common law cause of action for bad faith. See *Persian Galleries, Inc. v. Transcontinental, Ins. Co.*, 38 F.3d 253, 259 (6th Cir. 1994); *Chandler v. Prudential Ins. Co.*, 715 S.W.2d 615 (Tenn. Ct. App. 1986).

B. Third-Party Actions

1. A third party can bring an action for bad faith under the Tennessee Consumer Protection Act.
2. A third party cannot recover for an insurer's bad faith breach of contract.

C. Applicability to Sureties and Fidelity Insurers

1. Section 56-7-105 of the Tennessee Code Annotated specifically provides for a cause of action against the issuer of a "fidelity bond" for bad faith failure to pay promptly.
2. Although it is clear that section 56-7-105 applies to fidelity insurers, the issue of whether the section applies to a surety has not yet been decided. In *Curlee v. State Auto. Mut. Ins. Co.*, No. M2002-01627-COA-R3-CV, 2003 WL 22098037 (Tenn. App. Sept. 11, 2003), a property owner sued a permit bond surety for failing to pay a judgment against the principal under section 56-7-105. However, the court determined that the property owner had no contractual privity with the surety. Accordingly, the property owner's suit was dismissed upon that basis.

D. Damages

1. Punitive Damages
 - a. Punitive damages are available, but only in the most egregious of cases. See *Hodges v. Toof*, 833 S.W.2d 896 (Tenn. 1992).
 - b. An insured can recover punitive damages against an insurer for bad faith breach of an insurance contract. Tenn. Code Ann. § 56-7-105. Such damages cannot exceed 25% of the insured's loss and interest.
2. Attorneys' Fees
 - a. Attorneys' fees are recoverable at the trier of fact's discretion. Tenn. Code Ann. § 56-7-105(a).

3. Consequential Damages

- a. Tennessee Code Annotated § 56-7-105 provides for consequential damages for expense, loss or injury above and beyond the amount of the underlying loss.

4. Emotional Distress

- a. Emotional distress damages are recoverable for bad faith claims under Tennessee law. However, such damages are only awarded where conduct has been outrageous or extreme. *Dunn v. Moto Photo, Inc.*, 828 S.W.2d 747, 752 (Tenn. App. 1991); *Holt v. Am. Progressive Life Ins. Co.*, 731 S.W.2d 923 (Tenn. Ct. App. 1987).

E. Statute of Limitations

1. There is a one-year statute of limitations for personal tort actions under section 56-7-105. Tenn. Code Ann. § 28-3-104.
2. There is a three-year statute of limitations for civil actions based upon the alleged violation of a state statute creating liability for personal services rendered if there is no other time provided for by statute. Tenn. Code Ann. § 28-3-105.

VII. Texas

A. Origin of the Duty

1. Statutory Basis

- a. Chapters 541 and 542 of the Texas Insurance Code provide a private cause of action for unfair or deceptive acts or trade practices and unfair claim settlement practices.
- i. Section 541.151(1) of the Texas Insurance Code authorizes a private cause of action for damages against a “person engaging in an act or practices which is defined by [the Insurance Code] to be . . . an unfair or deceptive trade practice in the business of insurance.”

- ii. Section 541.060 provides that an insurer has engaged in unfair or deceptive acts or practices if the insurer misrepresents a material fact or policy provision relating to coverage; fails to attempt to effectuate a prompt, fair and equitable settlement; fails to provide a policy holder with the basis of the insurer's denial of a claim; fails to affirm or deny coverage or submit a reservation of rights to a policyholder; or fails to investigate a claim.
 - iii. Under § 542.056, an insurer is bound to notify a claimant in writing of the acceptance or rejection of a claim within 15 days from the time the insurer has received documentation constituting an adequate proof of loss. The insurer must then notify the insured of acceptance or rejection of the claim within 30 days from the submission of the proof of loss. The insurer must state the reasons for rejecting a claim. If the insurer is unable to accept or reject the claim within the specified time frame, the insurer can notify the insured of its need for more time, but must accept or reject the claim within 45 days of such notification.
- b. Section 17.50(a)(4) of the Texas Business & Commercial Code, also referred to as the Deceptive Trade Practices Act ("DTPA"), provides a consumer the right to maintain an action where a person's act or practice is false, deceptive, unfair or misleading in violation of Chapter 541 of the Texas Insurance Code.

2. Common Law Cause of Action

- a. In Texas, the tort of bad faith arises from the common law duty to perform every contract with "care, skill, reasonable expedience and faithfulness." *Aranda v. Ins. Co. of N. Am.*, 748 S.W.2d 210, 212 (Tex. 1988).
- b. An insurer's duty to deal fairly and in good faith with insureds in the processing and payment of claims "arises out of the special trust relationship between the insured and the insurer." *Aranda*, 748 S.W.2d at 212.
- c. In order to maintain a successful bad faith claim, the insured must show: (1) that the insurer either denied or delayed payment of the claim and (2) that the insurer know or should have known that it was reasonably clear that the claim was covered. *Kondos v. Allstate Tex.*

Lloyds, No. Civ.A 1:03-CV-1440, 2005 WL 1004720, at *11 (E.D. Tex. Apr. 25, 2005).

B. Third-Party Actions

1. Texas law does not recognize the tort of bad faith in third-party actions against insurers. *Universal Life Ins. v. Giles*, 950 S.W.2d 48, 54 (Tex. 1997); *Westcott Holdings, Inc. v. Monitor Liab. Managers, Inc.*, No. Civ.A. H-05-1945, 2005 WL 2206196 (S.D. Tex. Sept. 12, 2005).
2. A third party lacks standing under chapter 541 to sue the insurer directly. *Allstate Ins. Co. v. Watson*, 876 S.W.2d 145, 150 (Tex. 1994).

C. Applicability to Sureties and Fidelity Insurers

1. In *Tacon Mechanical Contractors, Inc. v. Aetna Casualty & Surety*, 65 F.3d 486, 488 (5th Cir. 1995), the Fifth Circuit Court of Appeals stated that there is no common law duty of good faith and fair dealing between a surety and an obligee.
2. In *Great American Insurance Company v. North Austin Municipal Utility District No. 1*, 908 S.W.2d 415 (Tex. 1995), the Texas Supreme Court held that there is no common law duty of good faith and fair dealing between a surety and bond obligee. Therefore, a surety could not be held liable for alleged delay in making payment under bonds. The Texas Supreme Court also found that the section of the Texas Insurance Code creating a private cause of action for injuries caused by practices declared to be “unfair or deceptive” does not apply to commercial sureties.
3. The Texas Supreme Court has also held that a surety does not owe a common law duty of good faith to its principal. *Associated Indem. Corp. v. Cat Contracting, Inc.*, 964 S.W.2d 276, 282 (Tex. 1998).
4. Texas state and federal courts have applied a duty of good faith and fair dealing to fidelity insurers. See, e.g., *Amarco Petroleum, Inc. v. Tex. Pac. Indem. Co.*, 889 S.W.2d 695 (Tex. App. 1994); *First Tex. Sav. Ass’n v. Reliance Ins. Co.*, 950 F.2d 1171, 1178-79 (5th Cir. 1992).

D. Damages

1. Punitive Damages

- a. If an insurer knowingly committed an unfair or deceptive act or practice, the trier of fact may award an amount not to exceed three times the amount of actual damages. Tex. Ins. Code § 541.152(b).
- b. If an insurer delays payment of a claim past the statutorily mandated period, the insurer must pay damages in the amount of the claim, in addition to 18% interest per year. Tex. Ins. Code § 542.060(a).
- c. Exemplary damages for common law causes of action are also recoverable under Texas Civil Practice and Remedies Code § 41.003(a) when the insured proves by clear and convincing evidence that its harm results from the insurer's fraud, malice, or gross negligence. The amount of exemplary damages may not exceed the greater of (1) two times the amount of economic damages, plus an amount equal to any non-economic damages found by the jury and not exceeding \$750,000; or (2) \$200,000. However, no limitations apply if the insurer's conduct is a knowing and intentional commission of a felony. Tex. Civ. Prac. & Rem. Code § 41.008(b).

2. Attorneys' Fees

- a. Attorneys' fees are not awarded unless permitted by statute or by contract between the parties. *Travelers Indem. Co. of Conn. v. Mayfield*, 923 S.W.2d 590, 593 (Tex. 1996).
- b. "A person may recover reasonable attorneys' fees from an individual or corporation, in addition to the amount of a valid claim and costs, if the claim is for . . . an oral or written contract." Tex. Civ. Prac. & Rem. Code § 38.001(8).
- c. Reasonable and necessary attorneys' fees are available under sections 541.152 and 542.060 of the Texas Insurance Code.

3. Consequential Damages

- a. If an insured can establish that the insurer breached its duty of good faith and fair dealing, the insured is entitled to recover all damages

proximately caused by the insurer's actions. *Chitsey v. Nat'l Lloyds Ins. Co.*, 738 S.W.2d 641, 643 (Tex. 1987).

4. Emotional Distress
 - a. Emotional distress damages are recoverable if the insurer's actions were committed knowingly. Tex. Ins. Code § 541.152(b); *State Farm Life Ins. Co. v. Beaston*, 907 S.W.2d 430, 436 (Tex. 1995).
- E. Statute of Limitations
1. There is a two-year statute of limitations for common law claims. Tex. Civ. Prac. & Rem. Code § 16.003(a).
 2. The limitations period begins to run on a first-party claim when an insurer denies coverage. *Murray v. San Jacinto Agency, Inc.*, 800 S.W.2d 826, 829 (Tex. 1990).
 3. A DTPA action must be brought within two years of the false, misleading or deceptive act or practice, or within two years after the consumer discovered or should have discovered it. If the defendant caused the plaintiff to delay institution of the action, the limitations period can be extended up to 180 days.