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Commonwealth of Kentucky

Court of Appeals

NO. 2018-CA-000475-MR

WILLIAM GERALD WATSON — APPELLANT

v.

APPEAL FROM MCCRACKEN CIRCUIT COURT
HONORABLE WILLIAM A. KITCHEN, III, JUDGE
ACTION NO. 09-CI-01400

UNITED STATES LIABILITY INSURANCE COMPANY — APPELLEE

OPINION
REVERSING AND REMANDING

** ** ** ** **

BEFORE: JONES, KRAMER, AND K. THOMPSON, JUDGES.

KRAMER, JUDGE: This dram shop case has a long and convoluted history, having been initiated in 2009 by Appellant William Gerald Watson, who had been severely injured in an automobile accident in 2008. It is before the Court, however, on a narrow issue involving the accrual date for statute of limitation purposes of a bad faith claim against a third-party insurer brought pursuant to the

Unfair Claims Settlement Practices Act (UCSPA), KRS[1] 304.12-230. Given the convoluted history and the fact that it is before us on a narrow issue, we will not belabor portions of the factual and procedural background that are not relevant for the disposition of this appeal. Our focus, therefore, is singularly toward reaching a decision as to when the alleged bad faith claim accrued, and more to the point – as argued by Watson – what date the underlying claim was settled.

Procedurally relevant, in February of 2012, Watson sought to amend his complaint to assert a third-party bad faith claim against Appellee United States Liability Insurance Company ("USLI"), which provided coverage to an underlying defendant, Pure Country, LLC. In his tendered amended complaint, Watson alleged that during the on-going dram shop litigation – before his claims against Pure Country ultimately settled – USLI had acted in violation of UCSPA. The circuit court denied Watson leave to amend his complaint. However, over five years later on August 9, 2017,[2] Watson moved to amend his second amended complaint; this time he was granted leave to do so on August 11, 2017.

Thereafter, in a November 14, 2017 order, the circuit court granted a CR[3] 12.02(f) motion from USLI and consequently dismissed Watson's claim

[1] Kentucky Revised Statute.

[2] Litigation continued against some of the non-settling parties at this time.

[3] Kentucky Rule of Civil Procedure.

purely on limitations grounds – to the extent that his claim encompassed alleged bad faith conduct from USLI that occurred on or predated August 9, 2012 (*e.g.*, five years prior to the date Watson moved to amend his complaint to add a bad faith claim against USLI).[4] Second, in a February 26, 2018 order, the circuit court granted a CR 56 motion from USLI and dismissed what remained of Watson's claim. It did so for two reasons: (1) limitations grounds, after reconsidering the issue of when Watson's bad faith claim against USLI had accrued, and determining it had actually accrued no later than June 30, 2012 (the date USLI represented that Watson and Pure Country had settled "in principle"); and (2) Watson's inability to prove USLI had engaged in any actionable bad faith conduct between June 30, 2012, and the month Watson executed the settlement agreement and was paid the settlement amount, December 2012.

[4] The UCSPA does not provide any specific time or statute of limitations for which claims falling under its purview must be asserted. However, in *State Farm Mut. Auto. Ins. Co. v. Reeder*, 763 S.W.2d 116 (Ky. 1988), it was held that a violation of the UCSPA could, when read together with KRS 446.070, create a private cause of action in favor of a claimant who is injured by the violation. Accordingly, the applicable statute of limitations for such a claim is KRS 413.120, which provides in relevant part:

> The following actions shall be commenced within five years after the cause of action accrued:
> . . .
> (2) an action upon a liability created by statute, when no other time is fixed by the statute creating a liability.

As such, the applicable statute of limitations for an UCSPA claim is five years from when the cause of action accrued.

Now on appeal, the dispositive issue presented is when Watson's bad faith claim accrued. USLI maintains that Watson's claim accrued no later than June 30, 2012, when an offer of settlement was conveyed to Watson from USLI. Watson, on the other hand, argues that his claim should have been deemed asserted as of February 2012 (when he moved for leave to amend his complaint a second time to assert his bad faith claim against USLI) or on April 17, 2012 (the date the circuit court denied him leave to do so). Alternatively, Watson argues his bad faith claim did not accrue until December 2012,[5] when he executed the agreement that settled his claims against Pure Country and was paid the settlement amount.

Because we agree that Watson's claim did not accrue until December 2012, we reverse.

Turning to our analysis, we begin with Watson's argument that the circuit court erred in denying him leave to assert his bad faith claim on or before April 17, 2012, while his underlying dram shop claim against Pure Country was still being litigated. Watson's argument is founded upon his allegation that USLI had engaged in bad faith settlement *conduct* prior to that date. And, claiming the circuit court erred in denying his motion on the basis that his claim was *unripe* at

[5] There is no dispute that Watson executed the settlement agreement and was paid the settlement amount during this month, but the record does not reflect the exact date.

that time,[6] he notes that in *Wittmer v. Jones*, 864 S.W.2d 885, 891 (Ky. 1993), the Kentucky Supreme Court stated: "While *we see no impediment* to joinder of the claims in a single action, at trial the underlying negligence claim should first be adjudicated. Only then should the direct action against the insurer be presented." (Emphasis added). Watson reasons that if the Court in *Wittmer* saw "no impediment" to allowing the joinder of a third-party bad faith claim against an insurer before the insurer's obligation to pay the underlying claim against its insured was established or deemed uncontested, then there was no "impediment" to his claim going forward, either.

However, the *Wittmer* Court merely stated that an underlying negligence claim against an insured must be adjudicated before a third-party claim of bad faith against an insurer may proceed. *Wittmer* never addressed the issue of when a third-party bad faith claim accrues for limitations purposes.

With respect to most torts, *conduct standing alone* is not the typical starting point of the applicable limitations period; rather, the earliest starting point is the date a claimant is able to demonstrate the complained-of conduct caused a

[6] "Ripeness" was one of two bases the circuit court cited for denying Watson's motion for leave to amend his complaint a *second* time to assert his bad faith claim against USLI. The circuit court's other basis was delay. The circuit court explained that because discovery had not yet been directed to the matter of USLI's alleged bad faith and because Watson's motion sought to add new claims against new parties, it was "practically assured that the amendment would result in a continuance of the trial" (which was set to begin approximately four months from when the order was entered).

non-speculative injury. As explained in *Saylor v. Hall*, 497 S.W.2d 218, 225 (Ky. 1973), "[r]ecovery is not possible until a cause of action exists. A cause of action does not exist until the conduct causes injury that produces loss or damage." Thus, where the *existence* of an injury is speculative until the final resolution of some other claim or litigation, the injury cannot exist – and the applicable statute of limitations therefore cannot run – until that other claim or litigation is finally resolved. *See Vandertoll v. Commonwealth*, 110 S.W.3d 789, 796 (Ky. 2003) ("The statute of limitations begins to run from the time when a complete cause of action accrues . . . . Where a party's right depends upon the happening of a certain event in the future, the cause of action accrues and the statute begins to run *only* from the time when the event happens.") (Quoting *Forwood v. City of Louisville*, 283 Ky. 208, 140 S.W.2d 1048, 1051 (1940)).

For example, because an essential element of *malicious prosecution* is the favorable termination of underlying criminal proceedings, a claim of malicious prosecution cannot accrue for limitations purposes until there is a favorable termination of underlying criminal proceedings. *See Dunn v. Felty*, 226 S.W.3d 68, 73 (Ky. 2007). Similarly, regarding legal malpractice claims based on "litigation negligence," our Supreme Court has held "that the injury becomes definite and non-speculative when the underlying case is final" and non-appealable. *Pedigo v. Breen*, 169 S.W.3d 831, 833 (Ky. 2004). The premise

underlying this rule of finality is that there is a theoretical possibility that the injured party may be "fully restored" by virtue of the appeals process "to the position that he occupied before the negligent act or omission." *Doe v. Golden & Walters, PLLC*, 173 S.W.3d 260, 272 (Ky. App. 2005). "In other words, because professional negligence may or may not cause an actual injury, until the final adverse outcome in an *underlying* case happens, a plaintiff has no right to bring an action because there are no certain damages." *Saalwaechter v. Carroll*, 525 S.W.3d 100, 106 (Ky. App. 2017).

The same holds true in the context of third-party claims of bad faith. Only an *injured* third-party claimant may sue an insurer for violating UCSPA.[7] And, the existence of any actionable injury likewise depends upon the final resolution of another claim. As explained in *Pryor v. Colony Ins.*, 414 S.W.3d 424, 432-33 (Ky. App. 2013),

> In *N.Y. Indem. Co. v. Ewen*, 221 Ky. 114, 298 S.W. 182, 185 (1927), the highest Court in Kentucky recognized "that the injured person must *first* establish his claim against the wrongdoer in his action for negligence and thereafter be assured of the fruits of his victory by being permitted to collect from the indemnity company." Hence, the general rule declared in this seminal case is that a complainant must first establish liability *before* seeking indemnity from an insurer in an action based on

[7] As indicated in *Reeder*, 763 S.W.2d at 117-18, a violation of the UCSPA is only actionable when read together with KRS 446.070, which provides: "A person *injured* by the violation of any statute may recover from the offender such damages as he sustained by reason of the violation, although a penalty or forfeiture is imposed for such violation." (Emphasis added).

the insured's negligence. *Id*. The prohibition of direct actions against insurers until liability has been established has remained the law in Kentucky. *See State Auto. Mut. Ins. Co. v. Empire Fire & Marine Ins. Co.*, 808 S.W.2d 805, 808 (Ky. 1991); *Cuppy v. General Accident Fire and Life Assur. Co.*, 378 S.W.2d 629, 632 (Ky. 1964); *Chambers v. Ideal Pure Milk Co.*, 245 S.W.2d 589, 591 (Ky. 1952); and *Ford v. Ratliff*, 183 S.W.3d 199, 203 (Ky. App. 2006).

. . . .

[A]n insurance company's violation of the UCSPA creates a private cause of action both for the named insured and for those who have claims against the named insured, and the same standards govern both types of cases. *Motorists Mut. Ins. Co. v. Glass*, 996 S.W.2d 437, 452 (Ky.1997). *But a third-party claimant may only sue the insurance company under USCPA when coverage is not contested or already established*. *Knotts v. Zurich Ins. Co.*, 197 S.W.3d 512, 516 (Ky. 2006). And, as stated by Chief Justice Robert Stephens in his concurring opinion in *Curry v. Fireman's Fund Ins. Co.*, 784 S.W.2d 176, 178 (Ky. 1989):

> An insured does not avail himself of this cause of action by merely alleging bad faith due to an insurance company's disputing or delaying payment on a claim. An insured must prove that the insurer is obligated to pay under the policy, that the insurer lacks a reasonable basis for denying the claim, and that the insurer either knew there was no reasonable basis to deny the claim or acted with reckless disregard for whether such a basis existed. An insurer's refusal to pay on a claim, alone, should not be sufficient to trigger the firing of this new tort.

(Emphasis added).

In short, third-party claims against insurers generally cannot be maintained, and thus cannot accrue, until *after*: (1) a judgment fixing liability against the insured has been entered; or (2) the insured becomes legally obligated to pay pursuant to terms of the insurance contract. *See Kentucky Hosp. Ass'n Tr. v. Chicago Ins. Co.*, 978 S.W.2d 754, 755-56 (Ky. App. 1998); *see also Martin Cnty. Coal Corp. v. Universal Underwriters Ins. Co.*, 792 F.Supp.2d 958, 961 (E.D. Ky. 2011) (explaining that there are only two conceivable bases for holding an insurer liable for its insured's liabilities: Either a judgment; or a contractual agreement between the parties that the insurer would pay for its "insured's voluntary settlements no matter whether the insured could have actually have been held liable.").

And, third-party *bad faith* claims against insurers asserted under the purview of UCSPA are no exception to this general rule. *See Davidson v. Am. Freightways, Inc.*, 25 S.W.3d 94, 100 (Ky. 2000), explaining:

> The gravamen of the UCSPA is that an insurance company is required to deal in good faith with a claimant, whether an insured or a third-party, with respect to a claim which the insurance company is *contractually obligated* to pay. Absent a contractual obligation, there simply is no bad faith cause of action, either at common law or by statute.

See also Kentucky Nat. Ins. Co. v. Shaffer, 155 S.W.3d 738, 742 (Ky. App. 2004) ("[T]here being no contractual obligation to pay under the present policy, we

conclude as a matter of law that Mrs. Shaffer could not maintain an action for bad faith against Kentucky National.").

Indeed, this was exactly what was held when the issue was squarely presented and addressed in *Simpson v. Travelers Ins. Cos.*, 812 S.W.2d 510 (Ky. App. 1991). There, a plaintiff prevailed in an automobile negligence action on May 6, 1987; during the pendency of the appeal, the defendant and its insurer made various settlement offers which the plaintiff declined; the verdict was affirmed and ultimately became final after the appellate court issued its mandate on September 29, 1988; and the insurer's motion for leave to pay its policy limits plus interest on the full judgment into the court was sustained on March 28, 1989. *Id*. at 511. Considering this timeline, it was held that the plaintiff's ensuing third-party bad faith claim against the defendant's insurer "accrued at some time after finality on September 29, 1988," because the insurer "had no obligation to pay prior to finality."[8] *Id*. at 512. This, even though much of the insurer's alleged bad faith conduct underlying the plaintiff's claim occurred prior to the date of finality. *Id*. at 511 (explaining the substance of the plaintiff's claim was that the insurer "unfairly failed to pay off the judgment against its insured," and that the plaintiff attempted

[8] Here, the essence of Watson's claim is that USLI should have settled with him earlier than it did; whereas in *Simpson*, the plaintiff's third-party bad faith claim was that the insurer had "unfairly failed to pay off the judgment against its insured." *Id*. at 511.

to support his claim by tying in what he deemed to be inadequate settlement offers made by the insurer prior to the appellate court's mandate).

With these guiding principles in mind, it is evident that Watson's third-party bad faith claim against USLI was unripe when the circuit court denied him leave to assert it on April 17, 2012. At that time, there was neither a judgment fixing liability against USLI's insured, nor an executed settlement resolving Watson's claim.

Likewise, Watson's claim could not have accrued on June 30, 2012. USLI contends this was the applicable accrual date because it was the date its insured emailed a settlement agreement to Watson's counsel. USLI further emphasizes: (1) the settlement agreement was the product of negotiations between its insured and Watson; (2) Watson indicated on or about that date that he planned to execute the settlement agreement; (3) the settlement agreement was eventually executed by Watson without further negotiation; (4) between the date its insured emailed the settlement agreement to Watson and the date Watson eventually executed it, no further litigation took place; and (5) the only reason the settlement agreement was not executed on June 30, 2012, was that Watson required more time to resolve the finalization and payment of various medical liens.

But, USLI is merely describing an *offer* of settlement that was made by its insured on June 30, 2012. And, it is disingenuous for USLI to argue that its

insured's June 30, 2012 *offer* of settlement caused Watson's third-party bad faith claim to accrue. On page twelve of its appellate brief, over the course of explaining that neither February 2012 (when Watson moved for leave to amend) nor April 17, 2012 (when his motion was denied) were the appropriate accrual dates of Watson's third-party bad faith claim, USLI pointed out:

> USLI's obligations under the policy would not be triggered unless and until Pure Country, its insured, became *legally obligated to pay damages to Watson*. This had not happened at the time of Watson's February 2012 motion for leave to amend. And because USLI had not yet become *legally obligated* to *pay damages to Watson*, Watson's bad faith claim against USLI was not yet ripe.

(Emphasis added).

In other words, for purposes of arguing against February or April of 2012 being the potential accrual dates of Watson's third-party bad faith claim, USLI itself recognized that Watson's claim could not have accrued because USLI was not, during those months, "legally obligated to pay damages to Watson." And, the same holds true for June 30, 2012 – the date Pure Country emailed its settlement *offer* to Watson. Settlements are contracts; and like any other contract, they require not only an *offer*, but also *acceptance* and *consideration* before they become legal obligations. *See Cantrell Supply, Inc. v. Liberty Mut. Ins. Co.*, 94 S.W.3d 381, 384 (Ky. App. 2002) (explaining settlement agreements are binding contracts and are subject to the rules of contract law.). Indeed, USLI only paid

Watson the settlement amount when Watson executed the proffered settlement agreement – not before.

This, in turn, leads to why Watson's third-party bad faith claim against USLI accrued in December 2012. That month, Watson *accepted* Pure Country's offer of settlement by executing the settlement agreement; and USLI then paid Watson the *consideration*, thereby forming a binding contract – a *legal obligation*. Thus, when Watson asserted his third-party bad faith claim against USLI on August 9, 2017, his claim was within the allotted five-year limitations period and was therefore timely.

With that said, what remains is the circuit court's summary determination set forth in its February 28, 2018 order that Watson failed to adduce evidence supporting *part* of his claim – namely, evidence demonstrating that USLI engaged in bad faith settlement conduct between June 30, 2012 and December 2012.[9] We are unaware of and have not been directed to any authority that permits a third-party claim of bad faith, split in this fashion, to be considered final and

[9] Throughout much of its brief, USLI focuses upon evidence relating to the circumstances of Watson's underlying dram shop claim against Pure Country and appears to insinuate that Watson's third-party bad faith claim against it is untenable because liability in that separate matter was, in its view, reasonably debatable. But, Watson's *proof* of USLI's alleged bad faith conduct, or his proof regarding whether Pure Country's dram shop liability was reasonably debatable, were not the bases of the circuit court's CR 12.02(f) order of dismissal; its order was based entirely upon limitations. Watson's proof was only the basis of the circuit court's CR 56 dismissal and only to the extent of his proof that demonstrated USLI engaged in bad faith conduct on or after June 30, 2012.

appealable. Therefore, we will not review it. *See Tax Ease Lien Investments 1, LLC v. Brown*, 340 S.W.3d 99, 102 (Ky. App. 2011) (explaining final judgments must adjudicate an entire claim, not just part of a claim).

Accordingly, we REVERSE and REMAND for further proceedings not inconsistent with this opinion.[10]

ALL CONCUR.

BRIEF FOR APPELLANT:	BRIEF FOR APPELLEE:
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[10] An additional argument Watson raised on appeal is whether he was allowed an adequate period of discovery prior to the dismissal of his claims. In light of our decision, we need not address this point.