

Wilson v. State Farm

Court Rules That Insurer Did Not Act in “Bad Faith” by Delaying Payment of a Settlement Pending Determination of Medicare’s Conditional Payment Amount

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In the case of *Wilson v. State Farm Mutual Automobile Insurance Company*, No. 3:10-CV-256-H, 2011 WL 2378190 (W.D. Ky., June 15, 2011), the United States District Court for the Western District of Kentucky ruled that an insurance carrier did *not* act in “bad faith” by delaying payment of a settlement pending its determination of Medicare’s reimbursable conditional payment amount.

In *Wilson*, the plaintiff filed an uninsured motorist claim which the insurer agreed to settle for the policy limits. However, the insurer delayed tendering payment until after it obtained Medicare’s reimbursable conditional payment amount. The plaintiff sued the insurer claiming that the insurer’s delay in paying the settlement violated Kentucky’s bad faith law. For the reasons more fully discussed below, the court found that the insurer’s actions did *not* constitute bad faith under Kentucky law.

The author breaks down the *Wilson v. State Farm* decision in greater detail as follows:

Factual Background

The plaintiff, Steven Wilson, was a passenger in a SUV which was involved in a motor vehicle accident. As a result of this accident, the plaintiff sustained bodily injuries for which Medicare paid some of his accident related medical bills.

As the driver of the other vehicle was uninsured, the plaintiff filed an uninsured motorist claim against the defendant insurer, State Farm. The insurer agreed to settle the claim for the policy limits (\$50,000).

In relation thereto, the insurer attempted to determine Medicare’s conditional payment amount and sought the plaintiff’s cooperation in addressing this issue with Medicare. The plaintiff refused and instead demanded that the insurer tender the full policy limits into an escrow account from which Medicare’s conditional payment amount would be payable. The plaintiff further advised that he would agree to hold the insurer harmless with respect to any potential claim asserted by Medicare.

In response, the insurer proposed an alternative plan consisting of naming Medicare as a payee on the settlement check. The plaintiff rejected this proposal. The insurer ultimately elected to delay payment of the settlement until after it obtained Medicare’s reimbursable conditional payment amount.

Plaintiff Sues the Insurer for “Bad Faith”

While the parties were waiting to obtain the applicable conditional payment amount from Medicare, the plaintiff sued the insurer for “bad faith” under Kentucky law.

The plaintiff argued that the insurer’s failure to ten-

der payment violated KRS 304.12-230(6). Under this statute, an insurer could be deemed to act in bad faith when it does not attempt “*in good faith to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear.*”¹

In addition, the plaintiff based its action on KRS 304.12-235 which provides that “[*a*]ll claims arising under the terms of any contract of insurance shall be paid to the named insured person or health (sic) care provider not more than thirty (30) days from the date upon which notice and proof of claim, in the substance and form required by the terms of the policy, are furnished the insurer.”²

By way of note, two months after the plaintiff filed his lawsuit, the insurer obtained Medicare’s conditional payment amount and then issued payment via separate checks to the plaintiff and Medicare the following day after it had received this information.

Both parties then filed motions for summary judgment asking the court to rule in their favor as a matter of law.

How Did the Court Rule?

The court ruled that the insurer did *not* act in “bad faith” by delaying payment of the policy proceeds pending its determination of Medicare’s reimbursable conditional payment amount.

In reaching its decision, the court first noted that for an insurer to have acted in bad faith under Kentucky law it must “(1) have an obligation to pay the claim at issue; (2) not have a reasonable basis for failing to pay the claim; and (3) know that it lacked a reasonable basis to delay payment or act in reckless disregard to the existence of that basis.”³

In *Wilson*, the major point of dispute between the parties related to the second factor – that is, whether or not the insurer had a “reasonable basis” to have delayed payment of the settlement.

On this point, the court referenced specific Kentucky

case law decisions indicating that “mere delay of payment alone” did not constitute bad faith, and that an insurer did not act in bad faith if the basis for the delay in payment was “fairly debatable as to either the law or the facts.”⁴ The court also noted authority under Kentucky law suggesting that actions constituting bad faith generally involve “outrageous conduct” meeting certain evidentiary standards warranting punitive damages.⁵

The court then looked to the Medicare Secondary Payer Statute (MSP)⁶ and noted that under the MSP an insurer could be deemed ultimately liable for repayment of Medicare’s conditional payment amount. In light of this potential liability, the court found the insurer’s actions to be “responsible.” The court stated:

It appears that Plaintiff has the primary responsibility to repay Medicare. 42 C.F.R. § 411.24(h). However, State Farm is absolutely liable to Medicare should Plaintiff not satisfy the Medicare lien from his settlement funds. 42 C.F.R. § 411.24(i)(1) (stating “If Medicare is not reimbursed ..., the primary payer must reimburse Medicare even though it has already reimbursed the beneficiary or other party.”).

Moreover, State Farm may have an obligation to protect Medicare’s lien under the Medicare Secondary Payer Act and its corresponding regulations. *See* 42 U.S.C. §1395y (b)(2) and 42 CFR § 411.24(i)(1). For State Farm to consider these obligations seems responsible.⁷

The court also found that the insurer had “sound reasons” to determine Medicare’s conditional payment amount and to take “reasonable precautions to protect itself from overpayment.”⁸ In addition, the court commented that it “was certainly reasonable” for the insurer to have proposed naming Medicare as a co-payee on the check.⁹

The plaintiff argued that the insurer acted “in pure self interest and that such overriding self interest coupled with the delayed settlement payment could constitute bad faith.”

General Considerations

The court, however, rejected this argument finding as follows:

The Court concludes ... that to comply with federal law and to protect its own legitimate interest against overpayment is reasonable and certainly is not in bad faith. Defendant did not delay payment in order to pay less or harass Plaintiff (citation omitted). While it may serve Defendant's self interest to comply with federal law, such action was not bad faith, especially when Plaintiff apparently refused to cooperate with Defendant's attempts to pay the claim more quickly. These undisputed facts cannot constitute bad faith on State Farm's part.¹⁰

The plaintiff also asserted a separate claim for interest under KRS 304.12-235. This statute permits the assessment of interest on the value of a settlement "[i]f an insurer fails to make a good faith attempt to settle a claim within the time prescribed" and reasonable attorney's fees "[i]f an insurer fails to settle a claim within the time prescribed ... and the delay was without reasonable foundation."¹¹

In response, the insurer argued that since it had tendered payment to the plaintiff and Medicare the day after it finally obtained Medicare's conditional payment amount, it acted within the statutory guidelines.

The court agreed with the insurer. In rejecting the plaintiff's claim, the court stated:

State Farm's delay in payment does not constitute bad faith, and, in fact, its multiple attempts to speed settlement suggest just the opposite. Defendant had a 'reasonable foundation' to delay settlement by seeking assurances concerning the amount and payment of the lien.¹²

Based on the foregoing analysis, the court denied the plaintiff's motion for summary judgment finding that the insurer's actions did not constitute bad faith under Kentucky law.

From a practical standpoint, *Wilson* demonstrates the importance of addressing the conditional payment issue as part of the underlying claim in order to ascertain (as best as possible under Medicare's current process) the potential conditional payment reimbursement amount. Since obtaining this information can take some time, the parties should consider starting this process sooner, rather than later, in the claims process. Along these lines, a certain degree of cooperation and coordination between the parties would seem to be in order, especially in light of the fact that multiple parties are at risk under the MSP.

In this regard, an important consideration surfaces relating to what many view as a significant deficiency with Medicare's current conditional payment process—the parties' inability to obtain Medicare's final and reimbursable conditional payment amount *before* claim settlement.

Under the current process, the reimbursable conditional payment amount generally cannot be obtained from the Centers for Medicare and Medicaid Services (CMS) until *after* the claim is settled and a copy of the executed settlement agreement is sent to the applicable CMS contractor. The inability to obtain Medicare's reimbursable conditional payment amount prior to settlement places the primary payer in a precarious position.

On the one hand, the primary payer could ultimately be held liable for reimbursing Medicare's conditional payment claim (including the prospect of double damages), but it is unable to determine the reimbursable amount until *after* the case is settled and it could take several months before this figure is received. These concerns have only been heightened in the aftermath of the recent decision of *Haro v. Sebelius*, No. CV 09-134 TUC DCB, 2011 WL 2040219 (D. Ariz., May 9, 2011) which can be interpreted as placing the primary payer further behind the eight ball in this regard.¹³

On the other hand, while efforts are made to obtain

the reimbursable conditional payment amount, the primary payer may face potential liability for bad faith or other penalties if it does not tender payment of the settlement in a timely manner.

This larger dilemma is currently the subject of reform efforts in Congress. In particular, one of the proposals contained in the *Strengthening Medicare and Repaying Taxpayers Act of 2011 (SMART Act) (H.R. 1063)* recently introduced in Congress would change this process. Under the SMART Act, the parties would be able to obtain Medicare's reimbursable conditional payment amount *prior* to a settlement, judgment, award or other payment. This proposal has generated considerable interest and support in the industry as it would provide an orderly and timely method for the parties to determine their repayment obligations *prior* to claim settlement.

For a more detailed discussion of this issue, and to

learn more about the reform proposals contained in the SMART Act, the reader may wish to review the author's article as contained in NuQuest/Bridge Pointe's *Settlement News, March 2011 Edition* which can be obtained at <http://www.nqbp.com/sites/default/files/March2011SettlementNews.pdf>.

Conclusion

In certain regards, the court's ruling in *Wilson* represents an important victory for primary payers in terms of protecting against (or at least mitigating) potential liability under the MSP. While this case will undoubtedly be viewed favorably in primary payer quarters, it is important for the reader to remember that legal counsel should be consulted to determine the potential applicability or non-applicability of this decision in regard to his/her particular jurisdiction or specific claim.

About the Author

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End Notes

¹ *Wilson*, 2011 WL 2378190, at *1.

² *Id.*

³ *Wilson*, 2011 WL 2378190, at *2, citing *Wittmer v. Jones*, 864 S.W.2d 885, 890 (Ky.1993) (quoting *Fed. Kemper Ins. Co. v. Hornback*, Ky., 711 S.W.2d 844, 846-47 (Ky.1986)).

- ⁴ *Wilson*, 2011 WL 2378190, at *2, citing *Motorist Mut. Ins. Co. v. Glass*, 996 S.W.2d 437, 452 (Ky.1997) and *Empire Fire & Marine Ins. Co. v. Simpsonville Wrecker Serv. Inc.*, 880 S.W.2d 886, 890 (Ky.Ct.App.1994).
- ⁵ *Wilson*, 2011 WL 2378190, at *2, citing *Wittmer*, 864 S.W.2d at 890 quoting Restatement (Second Torts), Sec. 909 (2)(1979).
- ⁶ The Medicare Secondary Payer Statute (MSP) is codified at 42 U.S.C. § 1395y, et. seq. In addition, pertinent MSP provisions are contained in Subparts B, C and D of Title 42 of the Code of Federal Regulations (42 C.F.R. §§ 411.20 through 411.50, et. seq.)
- ⁷ *Wilson*, 2011 WL 2378190, at *2. In addition, it should be noted that Medicare may seek *double damages* against primary payers. *See e.g.*, 42 U.S.C. § 1395(y)(b)(2)(B)(iii) and 42 C.F.R. § 411.24(c)(2).
- ⁸ *Wilson*, 2011 WL 2378190, at *2.
- ⁹ *Id.* In support of this proposition the court cited *Lewis v. Allstate Ins. Co.*, No. 09–05–225–CV, 2006 WL 665790 (Tex. App. March 16, 2006) and *Wall v. Leavitt*, Civ. No. S–05–2553 FCD GGH, 2008 WL 4737164, at *8 (E.D.Ca. Oct. 29, 2008). *But see*, *Zaleppa v. Seiwel*, 9 A.3d 632, 639 (Pa.Super.Ct.2010) and *Tomlinson v. Landers*, No. 3:07 –CV-1180-J-TEM, 2009 WL 1117399 (D. M.D. FL April 24, 2009).
- ¹⁰ *Wilson*, 2011 WL 2378190, at *3.
- ¹¹ *Id.*
- ¹² *Id.*
- ¹³ In *Haro*, the court essentially ruled that certain CMS conditional payment collection practices were improper and violated specific statutory and regulatory provisions. Through this decision, the court also limited potential liability for plaintiff counsel in specific circumstances which has caused increased concerns for primary payers given that they could ultimately be held liable for reimbursing Medicare per 42 C.F.R. § 411.24.