No. 96536-6

(Washington Court of Appeals No. 76479-9-I)

SUPREME COURT OF THE STATE OF WASHINGTON

ZURICH AMERICAN INSURANCE COMPANY,
a foreign insurer doing business in Washington State,

Appellant.

v.

JOGINGER SINGH DBA AP TRANSPORT,

Respondent.

APPELLANT'S PETITION FOR REVIEW

Jaquelyn A. Beatty, WSBA #17567
Karr Tuttle Campbell
701 Fifth Avenue, Suite 3300
Seattle, WA 98104
(206) 223-1313
Attorneys for Respondent
Zurich American Insurance Company

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I. IDENTITY OF RESPONDENT AND COURT OF APPEALS DECISION

Zurich American Insurance Company ("ZAIC") seeks review of the decision terminating review in *Joginder Singh dba AP Transport v. Zurich American Insurance Company,* 2018 Wash. App. LEXIS 1937, filed by Division I of the Court of Appeals on August 13, 2018 (the "Opinion") as an unpublished decision. On October 17, 2018, Division I filed its Order Granting Motion to Publish the Opinion. (The Opinion and Order Granting Motion to Publish are attached as Appendix A.) This case is linked and this petition is related to *Sykes v. Singh,* No. 76009-2-I.[1]

II. ISSUES PRESENTED FOR REVIEW

Accidents giving rise to multiple suits and potential claims, and for which an insured has insufficient insurance, are not uncommon. Other states have adopted specific rules for insurers and parties to follow. Currently, Washington does not have such a rule. This case demonstrates the need for guidance that is consistent with Washington's principles that insurance contracts are to be enforced as written, and that bad faith cannot be based on obligations that are not part of the parties' agreement. This petition raises the following issues:

1. Whether insurers that settle suits presenting excess exposure to their insureds for the limit of their policies, and thereby satisfy the

[1] "CP" references pertain to the record in this action, Court of Appeals No. 76479-9-I, unless designated as "CP ___ (No. 76009-2-I)."

policy's obligation to pay indemnity, must defend a new lawsuit filed sixteen months later?

2. Whether a claim of bad faith can be founded upon an insurer's payment of policy limits in settlement of a covered claim for which the insured is liable and which claim, if not settled, will expose the insured to a substantial uninsured judgment?

3. Whether presumed damages should be awarded at the same time as actual damages? If so, what is being presumed?

4. Whether emotional distress damages are the type of damages that should be available for the unintentional tort of insurance bad faith that does not involve physical injury?

Petitioner seeks review under RAP 13.4(b)(1), 13.4(b)(2), and 13.4(b)(4).

III. STATEMENT OF THE CASE

On July 20, 2011, two commercial trucks collided. The ensuing chain collision affected many vehicles and resulted in the death of Rachel Beckwith. ZAIC's insured, Joginder Singh d/b/a AP Transport ("Singh"), owned one of the trucks, driven by employee Richard Noble. The indemnity limit of Singh's policy was $1 million. Under Singh's policy: "We [ZAIC] have the right and duty to defend any insured against a 'suit' asking for such damages .... However, we have no duty to defend any insured against a 'suit' ... to which this insurance does not apply." The policy also gave ZAIC discretion in the investigation and settlement of claims and suits: "We may investigate and settle any claim or 'suit' as we

consider appropriate." "Suit" is a "civil proceeding."[2] Gilliardi Logging & Construction owned the other truck, driven by employee Mullins.

Three months after the accident, The Estate of Rachel Beckwith and Rachel's parents sued Singh, Noble, Gilliardi, and Mullins. ("*Beckwith*"). ZAIC defended Singh and Noble. The following July, the Washington State Patrol concluded the collision was caused by Singh's driver Noble. In March 2013, two months before trial, ZAIC paid Singh's policy limit to settle *Beckwith.* Had *Beckwith* not settled and gone to trial, Singh faced a multi-million-dollar judgment and bankruptcy.[3] The only other suit pending at the time was one by Farmers for $25,150.32.[4] Other claimants had submitted documentation of damages totaling $76,510.89.[5] Brian Sykes was not among them.[6] After receiving notice that policy limits were

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[2] Ex. 201, p. 76 and 87.

[3] Defense counsel determined the wrongful death claim had a value that "significantly exceeds the combined value of all other personal injury claims," and that the $3 million insurance available ($1 million for Singh and $2 million for Gilliardi) was "arguably not enough insurance to fully compensate the Beckwith Estate and Rachel's parents for the death and consortium claims in that lawsuit by itself." CP 195 (No. 76009-2-I). One *Beckwith* lawyers, Max Meyers, testified *Beckwith* was worth $15 million for Singh alone, and "my advice to [his clients] at that time was we were not going to take anything less than full limits." RP 383-386 (12/13/2016).

[4] Ex. 243, p. 6.

[5] Ex. 215, p. 3-12; Ex. 217; Ex. 219; Ex. 220; Ex. 221, p. 1-3, 6-8; Ex. 222, p. 2; Ex. 223, p. 5; Ex. 225; Ex. 228; Ex. 233, p. 4; CP 183-185; CP 233, p. 5; CP 479-527.

[6] Sykes had submitted a letter of representation but no documentation of injuries and damages, Ex. 212. Such information was requested by defense counsel. Ex. 214, p. 2.

exhausted, Farmers dismissed its case and the other claimants withdrew. ZAIC continued to pay for Singh's defense during this period.[7]

Sixteen months later, Brian Sykes sued Singh and Noble. The only information ZAIC had about Sykes' injuries, until the *Sykes* case later settled, was that he: "Had a bloody hand. Relatively minor injuries."[8] *See also* CP 99 (No. 76009-2-I) (July 2012 police investigation report): "Sykes sustained an injury to his finger and his shoulders and back were sore." After defense counsel corresponded with Sykes and other potential claimants two months after the accident, and asked for "any documentation supporting your claim,"[9] Sykes supplied only a letter of representation.[10]

Singh tendered the *Sykes* suit to ZAIC. ZAIC informed Singh that ZAIC had no duty to defend because Singh's policy was exhausted. Per the terms of the policy, ZAIC's duty to defend terminated when the policy limit was paid to settle *Beckwith*. Ex. 287. "Our duty to defend or settle ends when the Liability Coverage Limit of Insurance has been exhausted by payment of judgments or settlements...." Ex. 201, p. 76. Singh and Sykes settled and obtained court approval of their $250,000 settlement. (*See* linked appeal no. 76009-2-I.)

Meanwhile Singh filed this case against ZAIC for breach of contract, bad faith, negligence, and CPA and IFCA violations, based on

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[7] CP 631-632.

[8] Reported by defense counsel in CP 399.

[9] Ex. 214.

[10] Ex. 212.

ZAIC's failure to defend the *Sykes* case. The jury found ZAIC in bad faith and, as instructed, awarded the Sykes/Singh settlement amount plus Singh's purported attorney's fees from that case.[11] The jury also awarded emotional distress damages.[12] ZAIC prevailed on Singh's IFCA and CPA claims.[13] The trial court entered judgment on the jury's verdict. Division I affirmed.

This case should have been,[14] and should now be, decided as a matter of law.

IV. ARGUMENT WHY REVIEW SHOULD BE ACCEPTED

A. This Court should grant review because insurers that pay the policy limit to settle suits that pose excess exposure to their insureds, should not have to defend a new lawsuit filed sixteen months later—as plainly stated in the policy.

1. Division I did not enforce Singh's policy as written.

Insurers cannot speculate about suits that might be brought in the future. They should not be required to predict if a claimant will sue. Insurers have no duty to solicit claims and encourage lawsuits. Insurers

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[11] CP 2512; CP 3164-65. The only evidence regarding the amount of these fees came from Singh's son, Harmit, who testified his father "incurred" fees of approximately $36,000. RP 505 (12/14/2016).

[12] CP 3165. The only evidence of Singh's emotional distress came from Singh's son, Harmit, who said his father went to the hospital for stomach trouble but "they could find nothing." RP 509-510 (12/14/2016).

[13] CP 3166-67.

[14] Before answering, ZAIC moved to dismiss Singh's complaint pursuant to CR 12(b)(6). ZAIC later moved for summary judgment, for judgment as a matter of law, and renewed that motion after the jury rendered its verdict. CP 124-125. CP 730-755; 127-729; 1253-1260. CP 1286-1288.

have the duty to defend suits actually brought, and their conduct in settling those suits should not be judged sixteen months after the fact. Singh's policy plainly states that ZAIC's duty to defend terminates when the policy limit is paid to settle a case.

Beckwith presented a multi-million-dollar uninsured exposure to Singh and Noble. Trial was two months away. ZAIC had the contractual duty to defend, and the contractual right—and good faith obligation—to settle *Beckwith,* eliminating the most serious risk Singh and Noble faced. ZAIC also acted in accordance with Washington law requiring that insurers settle policy limit cases when it is possible to do so.

WAC 284.30.330 (6) and (12) require insurers to settle when liability is "reasonably clear." Singh's liability for Rachel Beckwith's death was absolutely clear. Washington case law insists that insurers meet policy limit demands to avoid exposing their insureds to excess exposure, and themselves to bad faith. Of all the claims and potential claims arising from the July 2011 collision, the *Beckwith* lawsuit presented by far the most serious exposure to Singh and Noble.

As long ago as 1974 this Court held in *Hamilton v. State Farm Ins. Co.*, 83 Wn. 2d 787, 523 P.2d 193 (1974) that an insurer's refusal to compromise a claim within policy limits when reasonable analysis indicates finding liability against the insured in excess of policy limits is a negligent or bad faith performance of an insurer's duty. *See also First State Ins. Co. v. Kemper Nat'l. Ins. Co.,* 94 Wn. App. 602, 612, 971 P.2d 953 (1999): "[A]n insurance company undertaking to defend its insured may be liable

to the insured for failing to make a good faith attempt to settle." In *Miller v. Kenny,* 180 Wn.App. 772, 325 P.3d 278 (2014), Safeco was found liable for bad faith. "Miller's major theme was that Safeco could have protected Kenny from exposure to an excess judgment by promoting a policy limits settlement much earlier." As a matter of law, ZAIC's payment of Singh's policy limit to settle *Beckwith* was reasonable under the circumstances and in accord with the insurance contract's terms and Washington law.

Beckwith did not involve a situation in which ZAIC "attempted to circumvent its duty to defend by making an early escape from the litigation." Opinion at 9. After receiving what he confirmed was a policy limit demand in January 2013,[15] defense counsel offered Singh's policy limit on February 4, 2013 after consulting with Singh.[16] The *Beckwith* plaintiffs agreed to accept the limit on February 27, 2013, after getting Gilliardi's $2 million-dollar commitment.[17] ZAIC paid the policy limit on March 7, 2013.[18] Trial was set for May 20. Defense counsel informed everyone else, including Sykes that "Mr. Singh had very limited commercial liability insurance of $1 million, and facing the prospect of a

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[15] Ex. 249 p. 1-4.

[16] Exs. 252; 299 p. 222 and 228 (defense counsel invoices describing discussions with Singh and his son about "damages exposure" and "policy limit settlement offer strategy." Also, as early as March 2012, ZAIC and defense counsel determined the greatest exposure facing Singh and Noble was the *Beckwith* suit. Defense counsel recommended that Singh's limits be reserved for that purpose. Singh agreed. CP 187-188.

[17] Exs. 255-258.

[18] Ex. 265.

jury trial schedule for May 20, 2013 in the Rachel Beckwith Estate's wrongful death case, we have reached a settlement ... for the full policy limit of $1 million. This settlement fully exhausts (depletes) my client's insurance coverage.... Unfortunately, there simply was not enough insurance to compensate all claims that arose from the accident."[19] There is no evidence ZAIC tried to make "an early escape."

Moreover, when *Beckwith* settled, ZAIC did not abandon Singh. Farmers' suit was pending and numerous other claimants were demanding payment. ZAIC continued to pay for Singh's defense until Farmers dismissed its action and the other claimants withdrew upon proof that Singh's limits were exhausted.[20] Singh himself paid the WA DOT claim.[21]

ZAIC had fully performed under Singh's insurance policy by the time Sykes filed his case sixteen months later. Per the express terms of the contract, ZAIC had no further duty to Singh.

Interpretation of an insurance policy is a question of law. *Woo v. Fireman's Fund Ins. Co.,* 161 Wn.2d 43, 52, 164 P.3d 454 (2007). "If the language is clear, the court must enforce the policy as written...." *Quadrant Corp. v. Am. States Ins. Co.,* 154 Wn.2d 165, 171, 110 P.3d 733 (2005).

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[19] Ex. 263.

[20] Exs. 271, 273, 276, 288; RP 141-144 (12/16/2016).

[21] WA DOT refused to withdraw its claim for $2,512.73 and threatened to revoke Singh's commercial driver's license. Singh agreed to pay that claim in installments after *Beckwith* settled. ZAIC paid defense counsel to negotiate this for Singh. Ex. 288, p. 4-7; RP 130-136 (12/16/2016).

This Court held in *Weyerhaueser Co. v. Commercial Union Ins. Co.,* 142 Wn. 2d 654, 692, 15 P.3d 115 (2000) that an "insurer's duty to defend ceases once its policy has been exhausted by payments made" for an insured's liability. Division II said in *Ross v. Frank B. Hall,* 73 Wn. App. 630, 638, 870 P.2d 1007 (1994): "Thus it logically follows that if the policy limits were exhausted, the assured would be accountable for any loss, damages, costs, fees, expenses and/or claims exceeding the policy limit." Division III said in *Perez Trucking v. Ryder Truck,* 76 Wn. App. 223, 233-34, 886 P.2d 196 (1994) that primary insurers had the duty to defend "until judgment or settlement." Singh purchased a $1 million dollar insurance policy, the minimum required for commercial truckers,[22] which said that when the limit was paid in judgment or settlement, ZAIC's duty to defend ended.

In this case Division I expanded an insurer's duty to defend, limited in the policy to a "suit" defined as a "civil proceeding," to an inchoate claim that might never materialize. "The insurer of a truck driver who caused a multi-vehicle freeway accident settled the largest claim for policy limits and then refused to defend its insured from a smaller [Sykes] claim," Opinion at 1. The court also said "Zurich did not independently investigate the potential value of that claim [Sykes] in relation to the Beckwith claim...." Opinion at 9. First, that is not true. ZAIC had information that Sykes "had

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[22] Federal Motor Carrier Safety Regulations, 49 CFR part 387, subpart A, Section 387.9 (73 FR 769406 Dec. 2008).

a bloody hand. Relatively minor injuries."[23] "Sykes sustained an injury to his finger and his shoulders and back were sore."[24] Second, an insurer has no duty to solicit claims. *Smith v. Premier Alliance Co.*, 48 Cal. Rptr. 2d 461, 466 (Ct. App. 1995); *Allstate Ins. Co. v. Russell,* 788 N.Y.S. 2d 401, 402 (N.Y. App. Div. 2004). Third, stating that ZAIC had a duty to defend Sykes' potential claim, before he filed suit, contradicts what Division II said in *United Servs. Auto. Ass'n v. Speed,* 179 Wn.App. 184, 194, 317 P.3d 532 (2014): "[W]hether a claim triggers a duty to defend *is a question of law*.... Most Washington cases recite[] that the insurer's duty to defend is triggered when a complaint is filed against the insured..... The cases reference a 'complaint' because most standard policies require the insurer to defend only a 'suit' against the insured." Singh's policy required ZAIC to defend "suits," defined as a "civil proceeding," which is not a letter of representation from a lawyer who says his client will be making a claim and then disappears for almost three years.

Division I's opinion leaves insurers in Washington in limbo. Do insurers settle policy limit cases promptly and remove their insureds from the most serious exposures they face? Do insurers reject policy limit demands in excess exposure cases because someone else might come along later and sue their insureds? Are insurers required to defend all suits that arise from a single accident even though the policy limit is needed to settle

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[23] Reported by defense counsel. CP 399.

[24] CP 99 (No. 76009-2-I) (July 2012 police investigation report).

the most serious claim? Must an insurer wait until the statute of limitations has run before settling any suit—even if it means the first filed suit goes to trial and results in a judgment exceeding the insured's policy limit? And what about the unfavorable impacts to insurer and insured alike by requiring that an insurer defend a lawsuit when it has no obligation or ability—because limits are exhausted—to settle or pay a judgment in the case?

2. **This Court should adopt the "First to Settle Rule."**

Division I said: "[T]here is no bright line absolutely excusing an insurer from its duty to defend once coverage is exhausted...." Opinion at 8. There should be a bright line rule: If the coverage is exhausted in payment of a covered claim that, if settled for the policy limit in exchange for a complete release of the insured in a clear excess exposure situation, and the policy so provides, an insurer has no continuing duty to defend.

The "first to settle rule" reflects the majority position. Richmond, Douglas R., "Too Many Claimants or Insureds and Too Little Money: Insurers' Good Faith Dilemmas," 44 TORT & INS. L.J 871 (Spring/Summer 2009) (Appendix B.) The rule "recognizes that insurers should be able to selectively settle with any or several of multiple claimants, even though these settlements deplete or exhaust the policy limits, without incurring bad faith liability in connection with any of the remaining claims." *Id.* at p. 8 of 30. As this commentator explains, the first to settle rule promotes efficiency and allows insurers the best opportunity to protect their insureds. "Indeed, to require an insurer to await the reduction of multiple claims to

judgment before paying them has the unfortunate effect of encouraging litigation and increasing the likelihood of insureds incurring liability beyond their limits." *Id.* at p. 9 of 30. The rule is not boundless—it requires that each settlement an insurer pays be reasonable—but at the time *Beckwith* was resolved, paying Singh's limit to obtain a complete release for Singh and Noble was eminently reasonable. ZAIC protected them from their largest exposure.

B. This Court should grant review because a claim of bad faith cannot rest on terms that do not exist in the insurance contract.

Division I and Singh focused their bad faith analyses on ZAIC's settlement of *Beckwith*. "If the insurer acted in bad faith when negotiating a settlement that exhausted the policy limits the insurer cannot then use the exhaustion of policy limits as the basis for denying defense coverage.... At trial Singh presented evidence that Zurich placed its own interest above his when it settled the Beckwith claim." Opinion at 9.

Bad faith requires that an insurer's conduct be "unreasonable, frivolous, or unfounded." *Overton v. Consol. Ins. Co.,* 145 Wn.2d 417, 424, 38 P.3d 322 (2002). Settling *Beckwith* when given the opportunity protected Singh and Noble, eliminating what was certain to be a substantial judgment exceeding a million dollars, if the case went to trial. Settling *Beckwith* for limits also had the desired effect of discouraging other litigation. Farmers and all other claimants withdrew. The fact that Sykes filed suit sixteen months later does not alter the circumstances that existed

when ZAIC settled *Beckwith*. And ZAIC's conduct must be evaluated under those circumstances, not future ones.

The Opinion places new and unreasonable burdens on insurers in ways that contradict existing law and express contract terms. Insurers should not be required to think of "creative ways," Opinion at 3, to avoid exhausting a policy limit when a demand has been made for that limit by the estate of a sympathetic 9-year old decedent and her parents. What happens if those creative ways backfire, and a settlement opportunity is lost? *See Miller v. Kenny, supra.*

ZAIC had no obligation to accept Singh's proposal to contribute $1000 of his own funds towards the *Beckwith* settlement to preserve a defense for future lawsuits. Opinion at 9-11. Does Division I mean that as long as Singh could contribute in some small way to a settlement, he could avoid exhausting his policy and extend ZAIC's obligation to pay defense costs indefinitely? The insurance contract did not give Singh that option.

The duty of good faith does not require that an insurer accept changes to a policy after the policy is issued. "The duty of good faith does not extend to obligate a party to accept a material change in the terms of its contract ... [n]or does it inject substantive terms into the parties' contract. Rather, it requires only that the parties perform in good faith the obligations imposed by their agreement." *Badgett v. Sec. State Bank*, 116 Wn. 2d 563, 807 P.2d 356 (1991). *Viking Ins. Co. of Wisc. V. Hill*, 57 Wn. App. 341, 349-50, 787 P.2d 1385 (1990) does not hold otherwise. There, the insurer did not actually pay its limit in a settlement or judgment and obtain a release.

Instead, it paid the limit into the court registry, allegedly with the insured's permission, and terminated its defense. The court expressly stated it was not against public policy for insurers to provide in their policies that if limits are exhausted the duty to defend terminates. At issue was whether Viking's unilateral payment to the registry of the court without a settlement agreement and before entry of judgment was in good faith.

Division I said: "If Zurich had held back a mere $1000 in coverage as Roessler proposed, it is speculative to assume that one of the other potential claimants would have gone to the trouble of suing Singh in order to get it." Opinion @ 11. No speculation is required because Farmers had already taken the "trouble" to sue Singh. Farmers' suit for $25,150.32 was pending when *Beckwith* settled; defense counsel had received another $76,510.89 in claim documentation and those parties were demanding satisfaction; and DOT was insisting on its $2,512.73. More problematic—for Singh—would have been defense counsel's inability to truthfully tell Farmers and the others that Singh's insurance was gone. Once they learned *Beckwith* settled for $1 million, but Singh's policy was not exhausted, they would have demanded the rest and asked if Singh had other assets.

The Opinion also suggests ZAIC should have asked defense counsel, who knew nothing about Alaska National's "holdback" agreement when he offered Singh's policy limit after consulting with his client, to negotiate one for Singh, and that ZAIC's failure to do so supports Singh's bad faith claim: "The *Beckwith* claimants had agreed to a $100,000 holdback from the $2 million policy limits contributed by Alaska National,

Gilliardi's insurer, so it is reasonable to infer that they would have accepted a similar arrangement with Zurich." Opinion at 10. Considering the communications between defense counsel and the *Beckwith* plaintiffs about Singh's exposure, that is wild speculation.

Division I's notion of reasonable inference is unsustainable as a basis for bad faith, and here there is no reliable, competent evidence to support it. Bad faith cannot be based on speculation and conjecture. It must be proven by a preponderance of evidence and have a solid foundation in fact. There was no testimony whatsoever that the Luvera Firm and Max Meyers, who valued the case against Singh alone at $15 million, would have accepted anything less than Singh's full policy limit to settle their wrongful death case where, for Singh, liability was undisputed. What is reasonable to infer is that if Singh had other assets, the *Beckwith* lawyers, with resources of their own, would have pursued those assets.

Singh and Gilliardi were not similarly situated, so it is purely speculative that ZAIC could have gotten a holdback agreement from the *Beckwith* plaintiffs. Gillardi had twice as much insurance and far less liability risk. The trial court in *Sykes* valued it at zero, as did Division I in *Sykes v. Singh,* No. 76009-2-I. Anyone suing Gilliardi could not rely on the police report that implicated Singh as the sole at-fault party, and would have had to incur the expense, as the *Beckwith* plaintiffs did, to hire experts.[25]

[25] CP 137-138; 202-203; 1074. Ex. 230 p. 1, and Ex. 231.

C. This Court should grant review because the Opinion impermissibly allows insureds in bad faith cases to recover presumed *and* actual damages, including damages for emotional distress.

1. If there is proof of actual damages, what is being "presumed"? Both should not be recoverable.

The trial court instructed the jury that it if it found ZAIC acted in bad faith harm was presumed, damages were presumed, and it "shall award $250,000"—the settlement amount deemed reasonable in the *Sykes* case—as "economic" damages for each of Singh's claims. At the same time, Division I said it was not error for the trial court to exclude the settlement agreement, which would have allowed ZAIC to show the jury that Singh's economic obligation under the agreement was only $10,000. Opinion 12-13. Division I also said it was not error for the jury to award actual damages as well—Singh's defense costs in *Sykes* and something for Singh's alleged emotional distress; and any other "actual damages that were reasonably foreseeable." CP 2513.

This Court adopted a presumption of harm in *Safeco v. Butler,* 118 Wn.2d 383, 823 P.2d 499 (1992). In *Besel v. Viking Ins. Co.*, 146 Wn. 2d 730, 738-39, 49 P.3d 887 (2002), this Court decided the amount of a stipulated judgment or settlement between the insured and a claimant, if deemed reasonable in a different proceeding, was the "proper measure of damages" for the presumed harm found in *Butler.* Before *Butler,* this Court recognized presumed damages only in First Amendment cases. *Stephanie Rasor v. Retail Credit Company,* 87 Wn.2d 516, 554 P.2d 1041 (1976).

The United States Supreme Court also has recognized, in cases involving important personal rights (free speech and due process), that in limited instances of those cases, it may be appropriate to presume harm and award presumed damages. *See Carey v. Piphus* 435 U.S. 247, 255-56 (1978) (due process) and *Gertz v. Robert Welch, Inc.,* 418 U.S. 323, 349-350 (1974) (defamation). But even then, the Supreme Court has rejected presuming harm and damages in all instances of defamation and due process violations, reserving presumptions for extreme situations. At present, Washington insureds seek presumed damages in nearly all cases alleging bad faith, and dissatisfied with that, are also asking for and, as here, recovering actual damages.

In *Memphis Community School Dist. v. Stachura*, 477 U.S. 299 (1986) (and there are many other cases in accord), the Supreme Court articulated two relevant characteristics of presumed damages, which Washington has not yet done. Presumed damages are intended as a "substitute" for "ordinary" damages proved in the usual way. They are not a "supplement." Second, they are intended to "approximate the harm" suffered by the plaintiff when the harm is deemed difficult to establish. But a plaintiff does not get both kinds of damages. "Presumed damages are a *substitute* for ordinary compensatory damages, not a *supplement* for an award that fully compensates the alleged injury." *Memphis v. Strachura, Id.* at 310-311. In *Klinger v. Nebraska Dept. of Correctional Services*, 902 F. Supp. 1036, 1042 (D. Neb 1995) (overruled on other grounds, 107 F.3d 609 (8th Cir. 1997)), the court said: "[W]hen one is dealing with the normal

type of case where damages are readily measurable, presumed damages are not appropriate." Prior Washington law is in accord. *See Stephanie Rasor v. Retail Credit Company, supra,* where this Court distinguished cases in which presumed damages are permitted (First Amendment cases), and decided that claimants under the Fair Credit Reporting Act, while they do not get presumed damages, could still show actual damages.

Even this case shows the tort of bad faith is amenable to proof of actual harm and actual damages. Singh's defense costs in *Sykes*, and emotional distress (if otherwise permissible for the non-intentional tort of bad faith), were subject to (albeit inadequate) proof, and the jury awarded specific compensation for them. *Rasor* itself implicitly recognized it is presumed damages or actual damages, not both. Also like the U.S. Supreme Court has done, *Rasor* limited the use of presumptions to certain kinds of cases such as those involving constitutional rights. To the extent Washington continues to allow presumed damages for insurance bad faith, not every bad faith case merits imposing them.

2. **This Court has been cautious about allowing emotional distress damages and has not approved them for insurance bad faith.**

This Court's most recent statement on the availability of emotional distress damages is this: "When emotional distress is the sole damage resulting from negligent acts, our court is cautious in awarding damages."

Schmidt v. Coogan, 181 Wn. 2d 661, 676, 335 P.23d 425 (2014).[26] This Court further observed:

> The dissent argues that we should analogize legal malpractice claims against attorneys to insurance bad faith cases in order to determine the recoverability of emotional distress damages. *Id.* This argument places the cart before the horse in that we have never before addressed the availability of emotional distress damages for insurance bad faith, and the dissent cites only one case[27] asserting without analysis that emotional distress damages are recoverable for insurance bad faith. ....

Other decisions reveal this Court's reluctance to expand the availability of emotional distress damages. This Court said in *Washington State Physicians Ins. Exch. & Ass'n v. Fisons Corp.,* 122 Wn.2d 299, 858 P.2d 1054 (1993): "Generally, in cases where emotional distress is not a consequence of physical injury, or caused by intentional conduct, Washington courts have been cautious about extending a right to recovery...." *See also White River Estates v. Hiltbruner,* 134 Wn.2d 761, 953 P.2d 796 (1998) (emotional distress is an element of damages only for

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[26] Emotional distress damages are also not recoverable for breach of contract, *Gaglidari v. Denny's Rests., Inc.*, 117 Wn. 2d 426, 446-48, 815 P.2d. 1362 (1991); nor under the Consumer Protection Act, *see Leingang v. Pierce Co. Med. Bureau, Inc.*, 131 Wn. 2d 133, 157-58 (1997); nor under IFCA, *see Schreib v. American Family Mut. Ins. Co.*, 129 F. Supp. 3d 1129, 1141 (W.D. Wash. 2015).

[27] That case was *Anderson v. State Farm Mut. Ins. Co.,* 101 Wn. App. 323, 333, 2 P.3d 1029 (2000), *rev. denied,* 142 Wn.2d 1017 (2001), and this Court was correct. *Anderson* allowed an award of emotional distress damages in a bad faith case, without analysis.

intentional torts). Bad faith is not an intentional tort,[28] and ZAIC did not physically injure Singh. Emotional distress damages are currently being allowed in insurance bad faith cases, without analysis, by the courts in this state. This Court should accept review to determine whether emotional distress damages are available in these circumstances.

V. CONCLUSION

Division I refused to apply a bright line rule in excess exposure situations when there is inadequate insurance. No one disputes that *Beckwith,* if it had gone to trial would have resulted in a large excess judgment against Singh. Singh's policy expressly provided that ZAIC's duty to defend terminated when the limit was paid to settle the *Beckwith* suit, at which time *Sykes* existed as an inchoate claim at best. ZAIC urges the adoption of a rule in Washington, consistent with the majority "first to settle" rule and the policy language at issue in this case, that relieves insurers from the duty to defend other litigation once they pay the policy limit in judgment or settlement a covered suit that, if not resolved, would leave their insureds with significant uninsured exposure. ZAIC also urges the Court to rule that if presumed damages are to be awarded, they are a substitute for actual damages when the latter cannot be proven, not a substitute for them. Finally, because bad faith is not an intentional tort and does not physically injure, consistent with Washington jurisprudence, ZAIC asks the Court to disallow emotional distress damages in bad faith cases.

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[28] *Sharbono v. Universal Underwriters Ins. Co.*, 139 Wn.App. 383, 410–11, 161 P.3d 406 (2007).

Respectfully submitted this 16th day of November 2018.

KARR TUTTLE CAMPBELL

By: */s/ Jacquelyn A. Beatty*
Jacquelyn A. Beatty, WSBA No. 17567
Attorney for Petitioner Zurich American Insurance Company

CERTIFICATE OF SERVICE

The undersigned certifies that on November 16th, 2018, I caused to be served the foregoing document to:

George Mix Mix Sanders Thompson, PLLC 1420 5th Ave., Ste 2200 Seattle, WA 98101-1346 george@mixanders.com	☐ Via U.S. Mail ☐ Via Hand Delivery ☒ Via Electronic Mail ☐ Via Overnight Mail ☒ CM/ECF via court's website

I declare under penalty of perjury under the laws of the state of Washington on November 16, 2018, at Seattle, Washington.

/s/ Kay M. Sagawinia
Kay M. Sagawinia

APPENDIX A

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

JOGINDER SINGH dba AP TRANSPORT, Respondent, v. ZURICH AMERICAN INSURANCE COMPANY, a foreign insurer doing business in Washington State, Appellant.	No. 76479-9-I DIVISION ONE UNPUBLISHED OPINION FILED: August 13, 2018

BECKER, J. — The insurer of a truck driver who caused a multi-vehicle freeway accident settled the largest claim for policy limits and then refused to defend its insured from a smaller claim. The insurer appeals from a jury verdict on a claim of bad faith. We affirm the judgment on the verdict.[1]

FACTS

The case arose from a 16-vehicle traffic accident on July 20, 2011. A chain reaction was precipitated when an employee of respondent Joginder Singh, driving Singh's semitruck, approached congested traffic ahead of him in the right lane without slowing down. He swerved into the adjacent lane and

[1] This case is linked to Zurich American Insurance Co. v. Sykes, No. 76009-2-I.

collided with a logging truck owned by Gilliardi Logging and Construction Inc. The momentum of the collision caused the trucks and their cargo to crash into other vehicles. One, a truck driven by Bryan Sykes, was flipped onto its side. Another was occupied by nine-year-old Nancy Beckwith, who died as a result of the impact.

Beckwith's family and estate filed a wrongful death complaint against Singh and Gilliardi and secured a trial date in 2013. The Beckwith claimants made clear early on that they saw the value of their claim as exceeding the combined policy limits of Singh and Gilliardi and they were not interested in global mediation with other claimants.

Singh was insured by appellant Zurich American Insurance Company with a limit of $1 million in coverage for liability. The insurance policy set forth Zurich's duty to defend Singh. It also stated, "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."

Zurich retained attorney Ken Roessler to defend Singh. Roessler contacted other potential claimants asking for information about their claims. He received a letter of representation from Sykes' attorney stating that Sykes was injured. Although the letter did not specify the details of Sykes' damages, it said he "makes claim for said injuries" and stated that his wife and daughters were tendering loss of consortium claims. Farmers Insurance Company, having paid claims to its own insureds, filed a subrogation suit for $25,150.32.

Roessler recognized that it was in Singh's interest to remove his exposure to the Beckwith claim by offering to settle for $1 million. At the same time, he recognized that under the Zurich policy, a settlement that exhausted Singh's policy limits would leave Singh undefended if other significant claims emerged later. Roessler testified that he was trying to think of "creative ways" to get the Beckwith claim settled while still maintaining a defense for Singh to continue "shooing away" the other claims.[2] In January 2013, Roessler asked Zurich to allow Singh to contribute $1,000 toward the $1 million that would be offered to settle the Beckwith claim. He wrote, "Mr. Singh understandably wants to keep some indemnity money left on the Zurich policy so he can continue to get a legal defense, while he would still be effectively tendering his 'policy limit' to the Beckwith Estate plaintiffs and maximizing his chances for negotiating settlement with them and avoiding the significant excess exposure that the Beckwith Estate wrongful death claim represents."[3]

Zurich declined Roessler's proposal and instructed Roessler to offer to settle the Beckwith claim for the full $1 million policy limit in March 2013. Roessler did so, and the offer was accepted. Zurich wrote to Singh quoting the policy and explaining that the policy "does not require Zurich to allow you to pay a portion of the settlement so as to not exhaust your limits of liability."[4]

At the same time, the Beckwith plaintiffs accepted a policy limits settlement of $2 million from Gilliardi, who was covered by Alaska National

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[2] Clerk's Papers at 631-32.
[3] Clerk's Papers at 1091-92.
[4] Clerk's Papers at 37-38.

Insurance. Under the terms of the settlement, Gilliardi held back $100,000 until the expiration of the statute of limitations. This arrangement allowed Gilliardi to maintain some degree of coverage and to have a defense in the event another claimant came forward.

Farmers withdrew its subrogation suit upon learning that Singh's policy limits had been exhausted. For a number of months, Zurich continued to pay Roessler to fend off the other claims.[5]

The statute of limitations expired in July 2014. Shortly before that, Sykes filed a complaint. Singh tendered the complaint to Zurich. On August 1, 2014, Zurich informed Singh that because his policy limits had been exhausted, the company had no further duty to defend and would not defend him. "Since Zurich can take no further action, it will be up to you to handle this matter personally."[6]

Singh retained private counsel and settled with Sykes for $250,000 on May 11, 2016. The trial court determined this was a reasonable settlement after holding hearings on September 16 and 23, 2016. Meanwhile, Singh proceeded with a lawsuit against Zurich for bad faith, breach of contract, negligence, and violations of the Insurance Fair Conduct Act (IFCA) and the Consumer Protection Act (CPA). The case went to trial in December 2016.

The jury found that

- Zurich breached the insurance policy, causing economic damages of $286,000. This included $250,000, the amount of his settlement with

[5] Clerk's Papers at 631-62.
[6] Clerk's Papers at 48-49.

Sykes that constituted presumed damages for Zurich's bad faith, and $36,000 in damages for the legal fees he incurred defending Sykes' suit;

- Zurich was negligent, causing the same $286,000 in economic damages;
- Zurich failed to act in good faith, causing the same $286,000 in economic damages plus $5,000 in emotional distress damages;
- Zurich violated the IFCA, but the violation did not cause damage; and
- Zurich did not violate the CPA.

The trial court entered judgment on the verdict of $291,000.00 plus interest and awarded Singh $293,710.23 in attorney fees and costs. Zurich appeals.

ANALYSIS

Evidence of Bad Faith

This was an excess exposure case involving multiple claimants. Given the damage caused by the accident, Singh's liabilities were certain to exceed his $1 million policy limit. Due to the large number of potential claimants, Singh's potential defense costs were high. These costs were Zurich's responsibility as long as Zurich was obligated to provide a defense for Singh. Singh alleged that Zurich, favoring its own interest over his, exhausted the policy limit in the Beckwith settlement so that it could refuse to defend him from other claimants and save on the costs of defense. This decision, according to Singh, unfairly left him exposed to substantial defense costs when Sykes sued him.

In four separate motions, Zurich asked the trial court to rule that its decision to exhaust the policy limits in the Beckwith settlement was in good faith as a matter of law. Zurich appeals the denial of all four motions. As Zurich summarizes its position, there was no need for a trial because after the limits were exhausted, Zurich had an unambiguous contractual right to terminate Singh's defense:

> ZAIC's exercise of its contractual right to terminate its defense upon policy exhaustion cannot be a basis for bad faith or for any other theory of liability. The duty of good faith and fair dealing safeguards both parties' rights to receive the benefits of the agreement *actually* made. The duty may not be used to create new rights or obligations not otherwise provided for in the parties' contract. An insurer's duty to consider an insured's interests equally with its own does not require the insurer to submerge its own interests, or surrender its contractual rights.
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> . . . Material facts are not in dispute. ZAIC defended and settled Singh's largest exposure by far. There is no dispute the amount paid to settle *Beckwith* was justified, and no dispute Singh needed protection from the significant personal exposure *Beckwith* presented. Singh's policy unambiguously terminated ZAIC's duty to defend when his policy exhausted. When *Sykes* was filed sixteen months later, ZAIC simply had no duty to defend.[7]

Whether an insurer acted in bad faith is typically a question of fact. Smith v. Safeco Ins. Co., 150 Wn.2d 478, 485, 78 P.3d 1274 (2003). Zurich could prevail as a matter of law only if there were no disputed material facts pertaining to the reasonableness of its conduct under the circumstances. Smith, 150 Wn.2d at 484. Review is de novo. Smith, 150 Wn.2d at 483.

Zurich argues that Singh's bad faith claim impermissibly expanded Zurich's obligations under the insurance contract, citing Badgett v. Sec. State

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[7] Brief of Appellant at 4.

Bank, 116 Wn.2d 563, 569, 807 P.2d 356 (1991) ("The duty of good faith does not extend to obligate a party to accept a material change in the terms of its contract.") The insurance contract stated that Zurich had the right to investigate and settle any claim as it deemed appropriate. Zurich reasons that its conduct could not have been in bad faith because the contract contained no provision limiting its right to exhaust policy limits with the Beckwith settlement.

Zurich cites Tyler v. Grange Insurance Association, 3 Wn. App. 167, 172, 473 P.2d 193 (1970), where this court held that the "typical liability insurance policy . . . gives the company control over the defense of the claim and control over the decision concerning opportunities of settlement within policy coverage." Tyler, 3 Wn. App. at 172. However, an insurer's right of control over settlement is not without limits. The insurer must "give consideration to the interests of the insured, when negotiating a settlement." Tyler, 3 Wn. App. at 172. An insurer "cannot put its financial interest before the interest of its insured; for an insurer to do so is to act in bad faith." Mut. of Enumclaw Ins. Co. v. T&G Constr., Inc., 165 Wn.2d 255, 269, 199 P.3d 376 (2008). Rather, an insurer must give equal consideration to the insured's interests. Safeco Ins. Co. of Am. v. Butler, 118 Wn.2d 383, 389, 823 P.2d 499 (1992). "The insurer is not free to proceed through negotiation and defense stages of litigation safeguarding only its own interests and neglecting those of its insureds." Weber v. Biddle, 4 Wn. App. 519, 525, 483 P.2d 155 (1971).

Zurich contends that insurers are entitled to rely on contractual language to cap their exposure and they are not required to defend every lawsuit, despite

the benefits that might bring to the insured. Zurich cites Weyerhaeuser Co. v. Commercial Union Insurance Co., 142 Wn.2d 654, 692, 15 P.3d 115 (2000), and Perez Trucking, Inc. v. Ryder Truck Rental, Inc., 76 Wn. App. 223, 233, 886 P.2d 196 (1994). In Weyerhaeuser, the court stated that "the underlying insurer's duty to defend ceases once its policy has been exhausted by payments made for this purpose." Weyerhaeuser and Perez Trucking involve the contractual allocation of defense responsibilities between two different insurers. Because they do not involve a claim of bad faith, they do not control the issue here.

"The insurer's duty to defend the insured is one of the main benefits of the insurance contract." Butler, 118 Wn.2d at 392. "The duty to defend is broader than the duty to indemnify because it is antecedent to and independent of the duty to indemnify." Viking Ins. Co. of Wisc. v. Hill, 57 Wn. App. 341, 346-47, 787 P.2d 1385 (1990). "Thus, while the policy may specifically provide for termination of the duty to defend upon payment of the policy limits, public policy requires the insurer to act in good faith in the interest of the insured." Viking, 57 Wn. App. at 349. A breach of the duty of good faith results in a cause of action "which arises from the contract *and* the fiduciary relationship." Butler, 118 Wn.2d at 393 (emphasis added). Courts "cannot focus solely on the contract aspect of that relationship." Butler, 118 Wn.2d at 394.

We conclude there is no bright-line rule absolutely excusing an insurer from its duty to defend once coverage is exhausted in an excess exposure case involving multiple claimants. The existence of bad faith "requires us to set aside traditional rules regarding harm and contract damages because insurance

contracts are different." Kirk v. Mt. Airy Ins. Co., 134 Wn.2d 558, 562, 951 P.2d 1124 (1998). If the insurer acted in bad faith when negotiating a settlement that exhausted the policy limits, the insurer cannot then use the exhaustion of policy limits as the basis for denying defense coverage. Even when the contractual language is unambiguous, there may still be a valid concern that the insurer has attempted to circumvent its duty to defend by making an early escape from the litigation. Pareti v. Sentry Indem. Co., 536 So. 2d 417, 423 (La. 1988).

At trial, Singh presented evidence that Zurich placed its own interest above his when it settled the Beckwith claim. The evidence included testimony by a witness, Gerald Hartmann, who had nearly 40 years of experience working for another insurance company, primarily with high-end casualty claims. A core portion of his testimony was that Zurich should have explored the option of a holdback when negotiating the Beckwith settlement. Hartmann's review of Zurich's files convinced him that the reason Zurich rejected Roessler's proposal of a $1,000 contribution by Singh for the Beckwith settlement was to avoid having to create a reserve for defense costs for non-Beckwith claims.

Hartmann testified that he was familiar with generally accepted standards for the investigation of claims and the negotiation of settlements in Washington. In his opinion, Zurich did not conduct an adequate investigation of the non-Beckwith claims. In particular, although Zurich knew Sykes intended to make a claim, Zurich did not independently investigate the potential value of that claim in relation to the value of the Beckwith claim and instead hastened to offer the entire limits to satisfy the Beckwith claimants. Hartman testified that even though

the Beckwith claim by itself was clearly worth more than the limits, it was reasonable to expect the Beckwith claimants to settle "somewhat south of the policy limits," RP 317, knowing there were other claims and other people Zurich had to consider. He said that rejecting Roessler's proposal did not comply with generally accepted claims handling standards. He testified that insurers are bound to use good faith when exercising a policy right to terminate the duty of defense when the limits have been exhausted by a judgment or settlement, and in his opinion Zurich's use of that clause in its policy was not in good faith.

Roessler testified that Zurich's rejection of his $1,000 contributions was not in Singh's best interest. "That's a tough question, but I would have to say no. That's the reason that we recommended that Zurich go for it. . . . So them saying no, I can't say that that served the best interests of my client."[8] Roessler, Zurich's claims supervisor Tonya Truitt, and Zurich's claim manager Robert Reynolds, all struggled to provide an explanation for why Zurich declined Singh's offer to contribute $1,000 to the Beckwith settlement. The Beckwith claimants had agreed to a $100,000 holdback from the $2 million policy limits contributed by Alaska National, Gilliardi's insurer, so it is reasonable to infer that they would have accepted a similar arrangement with Zurich.

Zurich's claims file included an e-mail from Truitt to Roessler requesting an updated matrix of the claimants and their damages so that Zurich could obtain a current picture of its exposure for Singh's potential liability to non-Beckwith claimants. Truitt's e-mail was sent days before Zurich settled with Beckwith.

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[8] Report of Proceedings (Dec. 15, 2016) at 52.

Singh argued this information was unnecessary to Zurich's evaluation of the Beckwith claim and was sought by Zurich only to determine what defense costs it could expect if the settlement did not completely exhaust Singh's policy limits.

The evidence described above supports Singh's theory that Zurich could have negotiated a settlement of the Beckwith claim that did not leave him undefended if other claimants like Sykes came forward later. It is sufficient to support the jury's finding that Zurich failed to act in good faith.

Zurich argues that holding back a small amount of coverage would not have made a difference. Like any other tort, a bad faith claim requires damages proximately caused by a breach of duty. Smith, 150 Wn.2d at 485. Zurich contends that if other potential claimants knew that Singh still had $1,000 in coverage left after the Beckwith settlement, they would have come forward and demanded it, exhausting the limits before Sykes filed his lawsuit. Thus, Zurich argues that Singh cannot show proximate cause. The argument is unconvincing. Gilliardi held back $100,000 in coverage, yet was sued by no one except the Beckwith parties. If Zurich had held back a mere $1,000 in coverage as Roessler proposed, it is speculative to assume that one of the other potential claimants would have gone to the trouble of suing Singh in order to get it. In fact, the continuing defense paid for by Zurich up to the point of the Sykes suit did have the effect of "shooing off" other potential claimants and arguably would have discouraged Sykes as well.

When the evidence is viewed in the light most favorable to Singh, it raises a question of material fact as to whether Zurich considered Singh's interest

equally with its own when negotiating the Beckwith settlement and, if not, whether its failure to do so damaged Singh. We conclude the trial court did not err in refusing Zurich's various requests to rule that Zurich acted in good faith as a matter of law.

We now turn to other errors alleged by Zurich.

Admissibility of the Covenant Not To Execute

Zurich contends that the trial court erred by excluding evidence of the stipulated covenant between Singh and Sykes. The covenant not to execute was part of the parties' settlement agreement. Under the covenant, Singh was personally liable to Sykes for $10,000 of the $250,000 settlement. Sykes' recovery of the remaining $240,000 was limited to Singh's proceeds from his bad faith action against Zurich.

In a motion in limine, Zurich moved to have the covenant admitted on the grounds that it rebutted the $250,000 in presumptive damages by showing that Singh was personally liable for only $10,000. A trial court's rulings on motions in limine are reviewed for abuse of discretion. Gammon v. Clark Equip. Co., 38 Wn. App. 274, 286, 686 P.2d 1102 (1984), aff'd, 104 Wn.2d 613, 707 P.2d 685 (1985).

When an insurer denies coverage in bad faith, a reasonable settlement between the insured and injured party is the presumed measure of damages. Besel v. Viking Ins. Co. of Wis., 146 Wn.2d 730, 738, 49 P.3d 887 (2002). Under Besel, the measure of presumptive damages is the total settlement, not the amount for which an insured is personally liable. A covenant not to execute does

not mean the insured was not harmed. Besel, 146 Wn.2d at 737. The trial court correctly ruled that under Besel, the damages of $250,000 were presumed; the covenant was not admissible to support an argument that the damages were only $10,000.

Zurich argues that the settlement was relevant to show collusion between Singh and Sykes. The trial court correctly ruled that Zurich had already litigated that issue and lost. At the earlier reasonableness hearing, the court found no evidence of collusion or bad faith in reaching the settlement.

Privileged Attorney-Client Communications

Zurich moved in limine for in camera review and admission of communications between Singh and his attorney, Roessler. The trial court denied this motion on the basis of the attorney-client privilege. Zurich contends that Singh waived the privilege.

Zurich's claim is rooted in Singh's answer to an interrogatory in which he claimed he was surprised when Zurich settled the Beckwith claim for full policy limits without notifying or consulting him:

> Zurich's decision to offer my full policy limits came as a shock to me because Zurich knew I was facing additional claims and because the decision was made without consultation, notification, or even advising me that Zurich had received something that it considered a policy limits demand . . . .
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> . . . Zurich did not even attempt settlement negotiations with the Beckwith plaintiffs. Rather, it promptly decided to tender my full policy limits to the Beckwith plaintiffs without seeking input (or even informing) either me or my attorney of its decision.

Singh submitted the interrogatory answer on July 27, 2016. Zurich claims the credibility of the answer was undermined by an e-mail Roessler sent to Singh on

September 13, 2013. The e-mail was inadvertently disclosed in Hartmann's expert report. According to Zurich, Singh's interrogatory answer falsely implied that before the Beckwith settlement, he did not know what was being done in his defense and no one informed him that settling with Beckwith for the full policy limits could eliminate Zurich's duty to defend him from future claims. Zurich's motion sought to admit the e-mail at trial to show that Singh *was* informed about the pros and cons of the Beckwith settlement.

The trial court ruled that the communications were privileged "and may not be introduced or discussed in front of the jury unless Mr. Singh opens the door to these communications." Because Zurich does not identify any point in the trial where the trial court was asked to revisit the issue and rule that the door had been opened, Zurich has not preserved the alleged error as a ground for reversal. Instead, Zurich asks that if this case is remanded for a new trial, it should be with instructions to put the privileged e-mail before the jury and allow Zurich to obtain discovery of related communications between Singh and Roessler. Because we are not remanding for a new trial, there is no need to address this issue.

Motion To Exclude Expert Testimony

Zurich moved in limine to exclude Hartmann's testimony on the ground that it would "add little probative evidence," that it would "usurp the Court's role of instructing the jury about applicable law," and that Hartmann's opinions amounted to incorrect legal opinions. Zurich contends the trial court erred by denying the motion.

Trial courts "are afforded wide discretion and trial court expert opinion decisions will not be disturbed on appeal absent an abuse of such discretion." Johnston-Forbes v. Matsunaga, 181 Wn.2d 346, 352, 333 P.3d 388 (2014). Zurich contends the admission of Hartmann's opinions should be reviewed de novo because they misrepresented Washington law and the language of Singh's policy. We see nothing in Hartmann's testimony that calls for de novo review.

Zurich cites the rule that expert testimony must have a factual basis. Davidson v. Mun. of Metro. Seattle, 43 Wn. App. 569, 578, 719 P.2d 569, review denied, 106 Wn.2d 1009 (1986). In Davidson, the expert witness reached his opinion by assuming facts conflicting with eyewitness testimony and drawing inferences from facts not in evidence. Davidson, 43 Wn. App. at 575. Unlike the expert in Davidson, Hartmann did not base his opinion on unsupported facts. Hartmann was qualified to discuss industry practice by his 40 years of experience working on high damage insurance claims. An expert may be qualified to testify by experience alone. Taylor v. Bell, 185 Wn. App. 270, 285, 340 P.3d 951 (2014), review denied, 183 Wn.2d 1012 (2015).

In Hartmann's opinion, when Zurich settled the Beckwith claim in a way that left Singh on his own to defend against Sykes, Zurich was putting its own interest ahead of Singh's. Zurich could have accepted Roessler's proposal to let Singh contribute $1,000 to the Beckwith settlement or could have considered a holdback like the one the Beckwith claimants agreed to with Gilliardi. Hartmann's review of the claims file and other documents convinced him that Zurich decided to pay full policy limits with the intention of cutting off its responsibility to cover

Singh's defense costs. The trial court did not abuse its discretion in allowing Hartmann to state this opinion. Zurich was able to cross-examine Hartmann and to present a different expert witness, David Mandt, who disagreed with virtually everything Hartmann said.

In a related argument pertaining to the negligence claim, Zurich contends Hartmann did not specify the standard of care in the insurance industry, and the trial court erred by not providing a standard of care in the negligence instructions.

In highly technical or specialized cases like medical and legal malpractice, a plaintiff is ordinarily required to present expert testimony setting forth an industry specific standard of care. See, e.g., Geer v. Tonnon, 137 Wn. App. 838, 851, 155 P.3d 163 (2007), review denied, 162 Wn.2d 1018 (2008). Zurich does not argue that an insurance company's duty to defend is so technical that it is beyond the knowledge of the ordinary person. Hartmann testified in terms of generally accepted claims handling standards. His testimony was helpful to explain why an insurance company must use care when conducting settlement negotiations in an excess exposure situation with multiple claimants. He placed Zurich's alleged negligence in the context of state regulations that generally define an insurance company's obligations when communicating with the insured and when investigating and settling a claim.

The jury was given pattern instructions defining negligence and stating that the standard of care is ordinary care. Zurich did not object to these instructions or propose anything additional. We find no error in the presentation of the negligence claim.

Jury Question

Zurich argues that the trial court erred in its answer to a question from the jury. The question was whether jurors "all have to agree on the *specifics* of the contract breach or do we all have to agree simply that the contract was breached even if we believe that the contract was breached for different reasons?" The court responded that "ten jurors must agree upon the answer to any question on the special verdict form."

On appeal, Zurich argues that the court should have identified how Zurich breached the contract. As there is no indication in the record that Zurich objected to the court's response at the time, the argument is waived. Millies v. LandAmerica Transnation, 185 Wn.2d 302, 310, 372 P.3d 111 (2016).

Presumption of Damages

The trial court instructed the jury to award $250,000—the amount of Singh's settlement with Singh—if it found that Zurich breached its duty of good faith. Zurich argues that instructing the jury to award presumed damages violated its due process rights. Zurich contends that the jury should be responsible for determining damages as is done in other cases.

It is well settled that a settlement including a covenant not to execute will serve as the measure of damages in a bad faith case if the amount of the settlement has been determined to be reasonable. It is not unconstitutional to have a judge rather than a jury make that determination Bird, 175 Wn.2d at 767-68. Zurich has not meaningfully distinguished the present case from Bird.

Following Bird and its predecessors, we conclude the jury was properly instructed to award $250,000 if it found Zurich breached its duty of good faith.

Emotional Distress Damages

The jury awarded Singh $5,000 for emotional distress. Zurich contends that emotional distress damages may not be awarded in an insurance bad faith action.

The Supreme Court affirmed a jury award of emotional distress damages for an insurer's bad faith in Coventry Associates v. American States Insurance Co., 136 Wn.2d 269, 284, 961 P.2d 933 (1998). This court similarly affirmed awards of emotional distress damages in Anderson v. State Farm Mutual Insurance Co., 101 Wn. App. 323, 333, 2 P.3d 1029 (2000), review denied, 142 Wn.2d 1017 (2001), and in Miller v. Kenny, 180 Wn. App. 772, 802, 325 P.3d 278 (2014). We reasoned that because bad faith is a tort, a plaintiff is not limited to economic damages. Anderson, 101 Wn. App. at 333.

Zurich contends that these cases must give way to the Supreme Court's more recent decision in Schmidt v. Coogan, 181 Wn.2d 661, 676, 335 P.3d 424 (2014). Schmidt was an appeal from a plaintiff's verdict in a legal malpractice case. The malpractice occurred when the defendant failed to file an amended complaint before the expiration of the statute of limitations. Schmidt, 181 Wn.2d at 663. The defendant was found liable, but the trial court held that emotional distress damages were not available. Schmidt, 181 Wn.2d at 664. The majority affirmed the trial court's ruling, holding that foreseeable damages for emotional distress were available in legal malpractice if the conduct was particularly

egregious or the representation was of a sensitive or personal nature, and the facts of the case did not meet these criteria. Schmidt, 181 Wn.2d at 674. A dissent argued that emotional distress damages should be made available in a legal malpractice action by analogy to bad faith cases like Coventry, Anderson, and Miller. Schmidt, 181 Wn.2d at 688-89 (Stephens, J., dissenting). Because those three cases "simply say that insurance bad faith is a tort" without further analysis and because "attorney malpractice differs considerably from insurer bad faith," the majority did not endorse the analogy. Schmidt, 181 Wn.2d at 676. However, the court did not hold that emotional distress damages are categorically unavailable in insurance bad faith claims. The court simply concluded, "The analogy between insurance bad faith and attorney malpractice must await a fuller exploration than either the dissent or the parties have offered." Schmidt, 181 Wn.2d at 677.

Since Schmidt, this court has again affirmed an award of emotional distress damages in a bad faith case. Mut. of Enumclaw Ins. Co. v. Myong Suk Day, 197 Wn. App. 753, 769, 393 P.3d 786, review denied, 188 Wn.2d 1016 (2017). Following Myong Suk Day as well as Coventry, Anderson, and Miller, we affirm the award of emotional distress damages.

Attorney Fees

The trial court found that Singh was entitled to an award of attorney fees under Olympic Steamship Co. v. Centennial Insurance Co., 117 Wn.2d 37, 811 P.2d 673 (1991). Zurich assigns error to this ruling.

An award of attorney fees "is required in any legal action where the insurer compels the insured to assume the burden of legal action, to obtain the full benefit of his insurance contract." Olympic Steamship, 117 Wn.2d at 53. Entitlement to an award of fees under Olympic Steamship arises when an insurer wrongfully denies coverage, as distinguished from the situation where coverage is conceded but the claim fails or recovery is diminished on its factual merits. Greengo v. Pub. Emps. Mut. Ins. Co., 135 Wn.2d 799, 817, 959 P.2d 657 (1998).

Olympic Steamship does not apply if the only dispute is over the value of a claim. Dayton v. Farmers Ins. Grp., 124 Wn.2d 277, 280, 876 P.2d 896 (1994). Zurich contends Olympic Steamship also does not apply where, as here, the insurance company accepted coverage and paid the full policy limit. But because Zurich also has a duty to defend, paying the full policy limit is not equivalent to providing the full benefit of the insurance contract. We conclude the trial court properly awarded fees under Olympic Steamship. See Unigard Ins. Co. v. Mut. of Enumclaw Ins. Co., 160 Wn. App. 912, 928, 250 P.3d 121 (2011) (Olympic Steamship fees awarded because insurer refused in bad faith to defend its insured).

Zurich contends the court awarded an excessive amount. This court reviews the amount of an attorney fee award for abuse of discretion. Miller, 180 Wn. App. at 820. "Courts must take an *active* role in assessing the reasonableness of fee awards, rather than treating cost decisions as a litigation afterthought. Courts should not simply accept unquestioningly fee affidavits from

counsel." Mahler v. Szucs, 135 Wn.2d 398, 434-35, 957 P.2d 632, 966 P.2d 305 (1998).

Singh's attorney's affidavit claimed 792 hours devoted to the case by five attorneys, a law clerk, and a paralegal. The hourly rates for the attorneys ranged from $445.00 for lead counsel to $225.00 per hour for a first-year associate. With the addition of time spent responding to Zurich's supplemental briefing, the fee claim was for a total of $294,954.50. Singh requested a multiplier of 2.0 for high quality work and the contingent nature of the fee. He asked for an award of costs amounting to $17,792.63.

Zurich objected generally that the claimed fees showed overstaffing, duplicated effort, unproductive time spent on unsuccessful claims and on unfiled motions, and unreasonable hourly rates. Zurich objected to the request for a multiplier and opposed awarding costs. After having the opportunity to review billing records, Zurich filed a supplemental brief with more detailed objections and suggestions for where reductions could be made.

In response to Zurich's objections, the court made reductions totaling $19,019.00 and found the remaining $275,935.50 to be reasonable. The court awarded $17,774.73 in costs.[9] The court did not grant a multiplier.

On appeal, Zurich contends this is a case like Berryman v. Metcalf, 177 Wn. App. 644, 659, 312 P.3d 745 (2013), review denied, 179 Wn.2d 1026 (2014). It is not. In Berryman, the trial court awarded fees exactly as claimed by

[9] Clerk's Papers at 3476-77 (Order Granting Plaintiff's Motion for Attorney Fees and Costs).

the plaintiff, including a multiplier, and rubber-stamped the plaintiff's proposed findings without addressing the defendant's detailed objections. The fee award was nearly $292,000 for a short trial de novo of a minor soft tissue injury case. There was "no indication that the trial judge actively and independently confronted the questions of what was a reasonable fee." Berryman, 177 Wn. App. at 658. Here, it is evident from the record that the court thoughtfully considered Zurich's objections and made appropriate reductions for duplicative and unproductive work.

Zurich faults the trial court's findings for not specifically addressing the reasonableness of Singh's hourly rates, block billing, unsuccessful claims which Singh failed to segregate when he could have, and "unsubstantiated expenses."[10] The record supports the trial court's finding that the hourly rates charged, ranging from $225 to $445, were reasonable. Singh's attorney provided a declaration stating his qualifications. He attached a survey of the hourly rates of plaintiff lawyers, showing that his hourly rate was within the range. He showed that his rate had been found reasonable in other cases.

Zurich claimed that Singh listed 183.2 hours in block billing, but Zurich did not provide the court with specific examples. Zurich argued that the court should deduct $39,492 for overstaffing because, like in Berryman, two attorneys attended the trial. But Zurich's argument did not take into consideration the greater complexity of a bad faith case. Zurich unreasonably identified any entry

[10] Brief of Appellant at 74.

where more than one attorney worked on an issue as an example of overstaffing or duplicative work.

Singh presented the time records of counsel in a lengthy table identifying the specific work performed, the hours spent, and the rate charged. These records satisfied the concerns identified in Berryman and gave the court a meaningful basis for evaluating the reasonableness of the time spent by Singh's attorneys. The court reduced the attorney fees by $8,000 for duplicative work and $360 for the cost of a law clerk to attend a four-hour mediation. These adjustments were within the court's broad discretion.

Zurich argued below for a reduction in hours to account for the fact that the jury found no CPA violation and no damages for the IFCA violation. Singh's billing records identified $2,646 for work done on those claims, and the trial court reduced the award by that amount. The trial court did not abuse its discretion by refusing Zurich's request for a more substantial reduction for these relatively insignificant claims, for which segregation would be difficult because they were closely related to the overarching claim of bad faith.

Zurich argues that the trial court should have reduced the award for time spent on Singh's breach of contract claim, which Zurich contends should be deemed unsuccessful even though the jury found that Zurich breached its contract with Singh. The basis of this argument is the trial court's decision to instruct the jury on breach of contract separately from breach of the duty of good faith. The trial court summarized its rulings on the issues pertaining to the jury

instructions in an order.[11] In the order, the court stated that Singh had "no viable cause of action for breach of contract *other* than his claim for a bad faith breach of contract." Zurich reasons that there is no such thing as a bad faith breach of contract in Washington because bad faith sounds in tort, and therefore Singh's attorneys wasted their time preparing and arguing their breach of contract theory. This argument lacks merit. The trial court was not ruling that there is only a tort cause of action. The trial court's order on jury instructions simply recognized that the breach of contract claim could not succeed unless there was a finding of bad faith on the part of Zurich and cited Kirk in support of its ruling.[12]

Zurich contends Singh failed to document his itemized list of costs. Singh provided records and invoices substantiating most of the items. It was not an abuse of discretion for the court to accept the list as support for the remaining undocumented items, which were for such things as court costs, production of trial exhibits, and copying.

We conclude the court gave an appropriate level of scrutiny to the claim for attorney fees and Zurich's objections to it, as required by Mahler and Berryman.

Olympic Steamship fees are available to parties prevailing on appeal. Leingang v. Pierce County Med. Bureau, Inc., 131 Wn.2d 133, 148, 930 P.2d 288

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[11] Clerk's Papers at 2459-62 (Order on Jury Instructions), Dec. 20, 2016.

[12] See also Report of Proceedings (Dec. 20, 2016) at 288 (in response to Zurich's objection to the breach of contract instruction, court stated, "I do believe that a breach of the implied duty of good faith in a contract is a contract-based claim".)

(1997). Singh is entitled to an award of appellate fees and expenses subject to compliance with RAP 18.1(d).

We affirm the judgment on the verdict and the award of attorney fees and costs.

Becker, J.

WE CONCUR:

Trickey, J

Cuppelwick, C.J.

FILED
10/17/2018
Court of Appeals
Division I
State of Washington

IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON
DIVISION ONE

JOGINDER SINGH dba AP TRANSPORT, Respondent, v. ZURICH AMERICAN INSURANCE COMPANY, a foreign insurer doing business in Washington State, Appellant.	No. 76479-9-I ORDER GRANTING MOTION TO PUBLISH

Respondent Joginder Singh d/b/a AP Transport has filed a motion to publish the opinion filed on August 13, 2018. Appellant Zurich American Insurance Company has filed an answer to the motion. The court has taken the matter under consideration and has determined that the motion should be granted.

Now, therefore, it is hereby

ORDERED that the unpublished opinion filed on August 13, 2018, shall be published and printed in the Washington Appellate Reports.

FOR THE COURT:

Becker, J.

APPENDIX B

TOO MANY CLAIMANTS OR INSUREDS AND TOO LITTLE MONEY: INSURERS' GOOD FAITH DILEMMAS

Spring/Summer, 2009

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44 Tort & Ins. L.J. 871

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Author: Douglas R. Richmond

Douglas R. Richmond is Senior Vice President in the Global Professions Practice of Aon Risk Services in Chicago. The opinions expressed in this article are solely those of the author.

Text

I. INTRODUCTION

Assume that you are a claims professional for a personal lines insurer assigned a case in which your insured, who appears to have been driving under the influence of alcohol, crossed a highway center line and struck another vehicle head on. The collision seriously injured the three people in the other vehicle. Your insured's automobile policy provides liability limits of $ 25,000 per person and $ 50,000 per occurrence. Your insured has no assets beyond his insurance policy. You communicate with lawyers for two of the people injured, and each agrees to accept $ 16,666.66 to settle their clients' claims against your insured in exchange for a full release. The lawyer for the third claimant, however, demands the full $ 25,000 per person limit for her client. In an effort to protect the insured as best you can under the circumstances, you settle with the first two claimants, and tell the lawyer for the third that you will gladly pay her client the remaining third of the per occurrence limits in exchange for your insured's full release. Instead, the third claimant sues your insured and obtains a judgment far in excess of the total policy limits. Does your company face extracontractual liability because of your settlement strategy? The answer is "perhaps," although it plainly should be "no," as this article will explain.

Alternatively, assume that your insured loans his car to a friend, who, while driving drunk and speeding, strikes and kills a pedestrian. The driver is insured under the owner's automobile policy by virtue of his permissive use of the vehicle. You quickly recognize the seriousness of the loss and offer to settle with the insured's surviving spouse on behalf of both insureds for the policy's $ 100,000 per person liability limit. The spouse agrees to accept $ 100,000 with respect to her claims against the owner, but refuses to release the driver. When you insist that any settlement must include both insureds, the spouse sues the owner and the driver for wrongful death and obtains multimillion dollar judgments against them. The owner files for bankruptcy and the bankruptcy trustee assigns his bad faith claim to the spouse, who pursues your company for the full amount of the judgment against the owner. You were doing your best to protect both insureds against excess liability. Is your company exposed to extracontractual liability as a result of your insistence on a global settlement? The answer is "perhaps," [1] as this article will again explain.

Part II outlines liability insurers' duty of good faith and fair dealing in settlement. Part III discusses traditional approaches to resolving cases involving multiple claimants and inadequate policy limits, including examinations of interpleader, the first to judgment rule, the pro rata rule, and the first to settle rule. It then examines leading bad faith cases involving multiple claimants and recommends a good faith approach for insurers attempting to resolve

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[1] *Compare* Strauss v. Farmers Ins. Exch., 31 Cal. Rptr. 2d 811, 813 15 (Ct. App. 1994) (indicating that this scenario would not support a bad faith claim), *with* Contreras v. U.S. Sec. Ins. Co., 927 So. 2d 16, 20 22 (Fla. Dist. Ct. App. 2006) (recognizing possibility of bad faith on these facts).

multiple claims in cases with inadequate policy limits. Part IV addresses insurers' duty of good faith and fair dealing in cases involving multiple insureds, as compared to multiple claimants. It also recommends steps that insurers may take to reduce the risk of bad faith liability when attempting to settle such cases.

II. GOOD FAITH AND SETTLEMENT

It is widely known that the law implies a duty of good faith and fair dealing in all insurance policies, and that an insurer's breach of this duty is generally actionable in tort. These are two sides of the same coin; an insurer's duty to act in good faith and its liability for bad faith refer to the same obligation. [2] In insurance as elsewhere, though, "good faith" and "bad faith" are somewhat elusive concepts. [3] Essentially, the duty of good faith and fair dealing requires that neither party to a contract do anything to injure the other party's right to receive the benefits of their agreement. [4] An insurance company is therefore guilty of bad faith if it subordinates an insured's financial interests to its own in handling a claim or suit. [5] Indeed, bad faith liability cannot lie absent such subordination, because insurers are clearly permitted to consider their own interests equally with those of their insureds. [6]

An insurer found to have committed bad faith faces liability beyond its policy limits. [7] Most jurisdictions require some level of intentional wrongdoing by an insurance company for extracontractual liability to attach, [8] while others allow

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[2] *Brown v. Patel*, 157 P.3d 117, 121 n.5 (Okla. 2007); *Mut. of Enumclaw Ins. Co. v. Dan Paulson Constr., Inc.*, 169 P.3d 1, 8 n.11 (Wash. 2007).

[3] ROBERT H. JERRY II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW 176 77 (4th ed. 2007).

[4] *Jackson v. Am. Equity Ins. Co.*, 90 P.3d 136, 142 (Alaska 2004) (quoting *Guin v. Ha*, 591 P.2d 1281 (Alaska 1979)); *Wilson v. 21st Century Ins. Co.*, 171 P.3d 1082, 1086 87 (Cal. 2007) (quoting ***Frommoethelydo v. Fire Ins. Exch., 721 P.2d 41 (Cal. 1986)).***

[5] *See* JERRY & RICHMOND, *supra* note 3, at 179 80.

[6] *Wade v. EMCASCO Ins. Co.*, 483 F.3d 657, 666 (10th Cir. 2007) (quoting *Bollinger v. Nuss*, 449 P.2d 502, 510 (Kan. 1969)); *Acosta v. Phoenix Indem. Ins. Co.*, 153 P.3d 401, 404 (Ariz. Ct. App. 2007); Jordan v. Allstate Ins. Co., 56 Cal. Rptr. 3d 312, 318 (Ct. App. 2007) (quoting ***Frommoethelydo v. Fire Ins. Exch., 721 P.2d 41 (Cal. 1986));*** *Sharbono v. Universal Underwriters Ins. Co.*, 161 P.3d 406, 411 (Wash. Ct. App. 2007).

[7] In addition to compensatory damages beyond its policy limits, an insurer may, on the right facts, face punitive damages.*See, e.g.*, *Goddard v. Farmers Ins. Co.*, 179 P.3d 645, 670 71 (Or. 2008) (affirming punitive damage award in third party bad faith case).

[8] *See, e.g.*, *Royal Indem. Co. v. King*, 532 F. Supp. 2d 404, 414 (D. Conn. 2008) ("'Bad faith means more than mere negligence; it involves a dishonest purpose.' ") (quoting *De La Concha of Hartford, Inc. v. Aetna Life Ins. Co.*, 849 A.2d 382 (Conn. 2004)); *Unum Life Ins. Co. of Am. v. Edwards*, 210 S.W.3d 84, 87 (Ark. 2005) (stating that bad faith requires "'dishonest, malicious or oppressive conduct carried out with a state of mind characterized by hatred, ill will, or a spirit of revenge'") (quoting *State Auto Prop. & Cas. Ins. Co. v. Swaim*, 991 S.W.2d 555 (Ark. 1999)); *Allstate Ins. Co. v. Fields*, 885 N.E.2d 728, 732 (Ind. Ct. App. 2008) (stating that bad faith requires "'conscious wrongdoing'" by insurer, i.e., "'evidence of state of mind reflecting dishonest purpose, moral obliquity, furtive design, or ill will'") (quoting *Lumbermens Mut. Cas. Co. v. Combs*, 873 N.E.2d 692, 714 (Ind. Ct. App. 2007)); *Rinehart v. Shelter Gen. Ins. Co.*, 261 S.W.3d 583, 591 (Mo. Ct. App. 2008) (requiring evidence that insurer intentionally disregarded insured's financial interests in hope of escaping full policy obligations) (quoting *Zumwalt v. Utils. Ins. Co.*, 228 S.W.2d 750, 754 (Mo. 1950)); *Sloan v. State Farm Mut. Auto. Ins. Co.*, 85 P.3d 230, 237 (N.M. 2004) (mandating "dishonest judgment" by an insurer for third party bad faith liability); *Lavaud v. Country Wide Ins. Co.*, 815 N.Y.S.2d 680, 681 (N.Y. App. Div. 2006) (requiring "gross disregard" of insured's interests for bad faith liability); *Badillo v. Mid Century Ins. Co.*, 121 P.3d 1080, 1094 (Okla. 2005) (requiring more than mere negligence for bad faith, but less than recklessness required for punitive damages); *Zappile v. Amex Assur. Co.*, 928 A.2d 251, 254 (Pa. Super. Ct. 2007) ("Further, mere negligence or bad judgment is not enough; bad faith imports a dishonest purpose and means a breach of [the duty of good faith and fair dealing] through some motive of self interest or ill will."); *Johnson v. Tenn. Farmers Mut. Ins. Co.*, 205 S.W.3d 365, 370 (Tenn. 2006) (stating that mere negligence is not sufficient and that bad faith requires "an insurer's disregard or demonstrable indifference toward the interests of its insured").

insureds or their assignees to recover extra contractual damages for an insurer's simple negligence. [9] Still other states allow recovery on both bad faith and negligence theories, each turning on the proof of different elements. [10] However defined, explained, or measured, extracontractual liability is a significant economic threat to insurers. [11]

As a general rule, an insurer's duty of good faith and fair dealing flows only to its insured. [12] Insofar as liability insurance goes, most bad faith claims arise out of an insurer's failure to settle a covered claim or suit against its insured within its policy limits despite the opportunity to do so, followed by a judgment against the insured exceeding those limits. [13] The allegation here, of course, is that the insurer's failure to settle within its policy limits was unreasonable and thus in bad faith, and that it accordingly should be liable for the full amount of the judgment. [14] But the prevalence of such claims does not mean that the duty of good faith and fair dealing assumes that settlement is always the preferred means of protecting policyholders' interests. [15] To the contrary, insurers are generally free to litigate or settle at their discretion without risking liability for judgments exceeding their policy limits, [16] so long as the chance of a defense verdict or verdict within policy limits is "real and substantial" and the decision to litigate is made honestly. [17] Insurers may also decline to settle free from the fear of extracontractual liability if the plaintiff is unwilling to grant the insured a full release in exchange for a policy limits payment. [18] Extracontractual

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[9] *See, e.g.,* Cotton States Mut. Ins. Co. v. Brightman, 580 S.E.2d 519, 521 (Ga. 2003); McKinley v. Guar. Nat'l Ins. Co., 159 P.3d 884, 888 (Idaho 2007); Hein v. Acuity, 731 N.W.2d 231, 235 (S.D. 2007).

[10] *See, e.g.,* ***Mut. Assur., Inc. v. Schulte, 970 So. 2d 292, 296 (Ala. 2007)*** (noting differences in elements of causes of action).

[11] *See, e.g.,* Charles Emerick, *Allstate Appeals $ 16M Verdict, Questions Bad Faith Claims,* MO. LAW. WEEKLY, Nov. 3, 2008, at 5 (reporting on $ 16 million bad faith verdict in Missouri and insurer's attempt to overturn it on appeal); Laurie Mason, *Insurer to Pay $ 20M in DUI Crash,* BUCKS COUNTY COURIER TIMES, June 29, 2007 (reporting $ 20 million bad faith verdict based on insurer's refusal to settle within policy limits); Natalie White, *Insurer Held Liable for Refusing to Pay Claim for Lawyer's Diabetes,* LAW. USA, Apr. 24, 2006, at 10 (detailing $ 4.7 million verdict in Ohio first party bad faith case); *Insurer Told to Pay $ 36M for Not Honoring Policy,* NAT'L L.J., Feb. 27, 2006, at 17 (reporting Mississippi verdict in first party bad faith case); *$ 55.2M Award to Firm Insurer Failed to Defend,* NAT'L L.J., Dec. 26, 2005, at 19 (reporting Minnesota third party bad faith verdict); *Bad Faith Claim Nets $ 10 Million,* MO. LAW. WEEKLY, Aug. 29, 2005, at 9 (reporting $ 10 million California third party bad faith verdict).

[12] Goodson v. Am. Standard Ins. Co. of Wis., 89 P.3d 409, 415 (Colo. 2004); Carford v. Empire Fire & Marine Ins. Co., 891 A.2d 55, 57 59 (Conn. App. Ct. 2006); Benchmark Ins. Co. v. Atchison, 138 P.3d 1279, 1284 (Kan. Ct. App. 2006); Charleston Dry Cleaners & Laundry, Inc. v. Zurich Am. Ins. Co., 586 S.E.2d 586, 588 (S.C. 2003).

[13] Most jurisdictions require a settlement demand or offer within policy limits as a prerequisite to bad faith liability premised on a failure to settle.*See, e.g.,* Chandler v. Am. Fire & Cas. Co., 879 N.E.2d 396, 400 (Ill. App. Ct. 2007); Mid Continent Ins. Co. v. Liberty Mut. Ins. Co., 236 S.W.3d 765, 776 (Tex. 2007).

[14] An insurer may be unable to resolve a case within policy limits through no fault of its own. For a bad faith case in which an insurer acquitted itself admirably, see*Maldonado v. First Liberty Insurance Co., 546 F. Supp. 2d 1347 (S.D. Fla. 2008)* (exonerating insurer).

[15] Dairyland Ins. Co. v. Herman, 954 P.2d 56, 61 (N.M. 1997).

[16] Eskind v. Marcel, 951 So. 2d 289, 293 (La. Ct. App. 2006); *see, e.g.,* Christian Builders, Inc. v. Cincinnati Ins. Co., 501 F. Supp. 2d 1224, 1229 40 (D. Minn. 2007) (finding no bad faith where insurer did not settle and plaintiff won excess judgment).

[17] Walt v. Ohio Cas. Ins. Co., 513 F. Supp. 2d 287, 296 (E.D. Pa. 2007); *see also* Johnson v. Am. Family Mut. Ins. Co., 674 N.W.2d 88, 90 91 (Iowa 2004) (discussing insurer's ability to reject demand within policy limits it believes it to be unreasonable and instead try case); Anglo Am. Ins. Co. v. Molin, 670 A.2d 194, 197 98 (Pa. Commw. Ct. 1995) (stating that an insurer "may reject a settlement offer and insist on litigation if it has a bona fide belief that it has a good possibility of succeeding on the merits").

[18] Trinity Universal Ins. Co. v. Bleeker, 966 S.W.2d 489, 491 (Tex. 1998).

liability arising out of the litigate or settle calculus requires bad faith by the insurer; that is, it requires that the insurer's decision be unreasonable. [19]

In deciding whether an insurer acted unreasonably and thus in bad faith in declining to settle within policy limits, courts must consider the insurer's conduct in light of the circumstances existing when the decision was made. [20] Hindsight has no place in this analysis. Courts typically weigh such factors as (1) the insured's probable liability; (2) the policy limits; (3) the extent of the claimant's damages; (4) the adequacy of the insurer's investigation; (5) the quality of the defense provided by the insurer; (6) whether the insurer heeded defense counsel's advice concerning settlement; (7) whether the insurer heeded its own adjusters' advice concerning settlement; (8) the insurer's willingness to engage in settlement negotiations; (9) whether the insured made any misrepresentations that may have misled the insurer with respect to settlement negotiations; (10) the openness of the communications between the insurer and insured; (11) whether the insurer kept the insured informed about settlement negotiations; and (12) any other conduct by the insurer reflecting greater concern for its financial interests than for its insured's financial risk. [21] Not every factor will apply or be material in every case. Different courts may assign different weights to different factors. [22] Courts should also consider additional factors negating an insurer's alleged bad faith. [23]

Regardless of the factors to be weighed when scrutinizing an insurer's failure to settle, courts generally afford insurers' settlement decisions less deference when there is a substantial likelihood of a verdict exceeding the policy limits. [24] As a result, insurers are presented with difficult problems in most cases with excess verdict potential. [25]

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[19] *See* Kransco v. Am. Empire Surplus Lines Ins. Co., 2 P.3d 1, 9 (Cal. 2000); Doe v. S.C. Med. Malpractice Liab. Underwriting Ass'n, 557 S.E.2d 670, 674 (S.C. 2001).

[20] Century Sur. Co. v. Polisso, 43 Cal. Rptr. 3d 468, 487 (Ct. App. 2006) ("We evaluate the reasonableness of the insurer's actions and decision to deny benefits as of the time they were made rather than with the benefit of hindsight."); Glenn v. Fleming, 799 P.2d 79, 85 (Kan. 1990) ("The conduct of the insurer must not be viewed through hindsight. Instead, the offer and the strength of the plaintiff's case must be viewed as they fairly appeared to the insurer and its agents and attorneys at the time the offer was refused."); Fletcher v. Anderson, 3 P.3d 558, 566 (Kan. Ct. App. 2000) (quoting Associated Wholesale Grocers, Inc. v. Americold Corp., 934 P.2d 65 (Kan. 1997)); Gainsco Ins. Co. v. Amoco Prod. Co., 53 P.3d 1051, 1058 (Wyo. 2002) (stating that an insurer's good faith must be measured at the time of the plaintiff's settlement offer) (quoting W. Cas. & Sur. Co. v. Fowler, 390 P.2d 602, 606 (Wyo. 1964)).

[21] These factors are compiled from the following cases: Truck Ins. Exch. v. Bishara, 916 P.2d 1275, 1279 80 (Idaho 1996); O'Neill v. Gallant Ins. Co., 769 N.E.2d 100, 106 09 (Ill. App. Ct. 2002); Smith v. Audubon Ins. Co., 679 So. 2d 372, 377 (La. 1996); Smith v. Gen. Accident Ins. Co., 697 N.E.2d 168, 170 71 (N.Y. 1998); and Smith v. Safeco Ins. Co., 50 P.3d 277, 281 (Wash. Ct. App. 2002).

[22] *Compare* McKinley v. Guar. Nat'l Ins. Co., 159 P.3d 884, 888 (Idaho 2007) (assigning primary weight to the insurer's communications with the insured, with a special focus on settlement aspects, and amount of the financial risk to which each party will be exposed if settlement is refused), *with* Eskind v. Marcel, 951 So. 2d 289, 293 (La. Ct. App. 2006) (considering probability of insured's liability, extent of the claimant's damages, policy limits, adequacy of the insurer's investigation, and openness of the communications between insurer and insured).

[23] McKinley, 159 P.3d at 888 (quoting Bishara, 916 P.2d at 1280).

[24] *See* Princeton Ins. Co. v. Qureshi, 882 A.2d 993, 997 (N.J. Super. Ct. App. Div. 2005) (quoting Rova Farms Resort, Inc. v. Inv. Ins. Co. of Am., 323 A.2d 495 (N.J. 1974)); Dairyland Ins. Co. v. Herman, 954 P.2d 56, 61 (N.M. 1997); Johnson v. Tenn. Farmers Mut. Ins. Co., 205 S.W.3d 365, 370 (Tenn. 2006).

[25] A good argument can be made that insurers' settlement decisions in cases where ***multiple claims*** will plainly outstrip the total policy limits ought to be granted substantial deference. As a rule, judicial deference to an insurer's settlement discretion lessens when there is a substantial likelihood of a recovery exceeding policy limits because of the inherent conflict of interest in this situation. The insurer may be willing to risk litigation to avoid paying its full policy limits, while the insured wishes to avoid litigation for fear of an excess judgment. Herman, 954 P.2d at 61. In most cases with multiple claimants, however, there is no similar conflict. The insurer knows that its policy limits are certain to be consumed, and it seeks only to protect its policyholder as

These problems are "complicated logarithmically when ***multiple claims*** exist, each likely to outstrip the coverage." [26] The same is true where multiple insureds are involved and the insurer's policy limits are inadequate to fully indemnify them all. [27]

III. THE PROBLEM OF MULTIPLE CLAIMANTS

Insurers have no duty to pay more than the applicable liability limits of their policies to settle claims or suits against their insureds. [28] The obvious problem for an insurer in a case with multiple claimants is how to divide a limited pool of money among them. The insurer's exhaustion of its policy limits through settlements with one or more claimants, but fewer than all, potentially exposes the policyholder to uninsured liability to the remaining claimants. Most insurers feel obligated to protect their policyholders against uninsured liability if possible, so leaving some claims unresolved is an unappealing option. Insurers further recognize that if the policyholder is exposed to uninsured liability for the remaining claims, that will almost certainly lead to bad faith litigation. [29] Plaintiffs' lawyers in these cases commonly look for ways to set up bad faith claims, recognizing that their clients will not be made whole from the existing policy limits or insureds' personal resources. [30]

A. *The Incomplete Solution of Interpleader*

At the outset, it would seem that an insurer facing ***multiple claims*** outstripping its coverage should easily be able to avoid potential bad faith liability by filing an interpleader action. Interpleader permits a party holding money to which there are competing claims to deposit the money into court, and allow the rival claimants to litigate their rights to it before the court. This is a two step process. In the first phase of an interpleader action, the court determines whether the requirements for interpleader have been met; in the second phase, the claimants litigate among themselves over the division of the interpleaded funds. [31] In the second phase, the claimants must establish their rights to a portion of the proceeds. [32] If the court determines that interpleader is appropriate and the insurer pays its funds into court, the insurer's indemnity obligation to its insured is fully satisfied. [33]

From a liability insurer's perspective, however, interpleader is often an incomplete solution. First, the claimants remain free to proceed against the insured despite the pending interpleader action, and interpleading its policy limits

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best it can in exhausting its limits. The reason for limiting the deference normally afforded the insurer's settlement decision has therefore disappeared. The obvious counter argument is that even in a serious multiple claimant case, an insurer may be tempted to low ball individual claimants in an effort to save some of its policy limits. *See, e.g.,* *Rinehart v. Shelter Gen. Ins. Co., 261 S.W.3d 583, 595 96 (Mo. Ct. App. 2008)* (describing this alleged scenario). Fortunately, such cases are rare.

[26] *Peckham v. Cont'l Cas. Ins. Co., 895 F.2d 830, 835 (1st Cir. 1990).*

[27] *See* Deborah M. Minkoff & Michael A. Hamilton, *Can a Good Faith Settlement Terminate a Right to a Defense?,* FOR THE DEF., May 2000, at 8, 11.

[28] *See* *Cent. Ill. Pub. Serv. Co. v. Agric. Ins. Co., 880 N.E.2d 1172, 1181 (Ill. App. Ct. 2008); Am. Physicians Assur. Corp. v. Schmidt, 187 S.W.3d 313, 318 (Ky. 2006); Tex. Farmers Ins. Co. v. Soriano, 881 S.W.2d 315, 316 (Tex. 1994).*

[29] 1 ALLAN D. WINDT, INSURANCE CLAIMS & DISPUTES § 5:8, at 5 49 (5th ed. 2007) ("Since it can settle with one claimant, but not with all of them, the company will always confront the spectre of an excess judgment, regardless of what it does.").

[30] Jeanne H. Unger, ***Inadequate Limits*** of Coverage: Avoiding Bad Faith When There Are ***Multiple Claims*** and ***Inadequate Limits*** 4 (2008) (unpublished paper on file with the author).

[31] *State Farm Fire & Cas. Co. v. Pietak, 109 Cal. Rptr. 2d 256, 264 (Ct. App. 2001); Am west Sur. Ins. Co. v. Stamatiou, 996 S.W.2d 708, 712 (Mo. Ct. App. 1999); Farmers Ins. Co. of Wash. v. Romas, 947 P.2d 754, 758 (Wash. Ct. App. 1997).*

[32] *Wills v. Nat'l Auto. Ins., 926 So. 2d 771, 773 (La. Ct. App. 2006).*

[33] *See Amwest Sur. Ins. Co., 996 S.W.2d at 712.*

probably will not relieve the insurer of its duty to defend. [34] As a result, an insurer cannot interplead all the third parties potentially having claims against its insured and be certain of discharging its own obligations. [35] Second, interpleader does not work a complete release of the insured. [36] An insurer may be able to obtain its insured's complete release through negotiations after posting the full limits of its coverage for multiple claimants to divide, the claimants on their own may agree or offer to release the insured upon distribution of the interpleaded funds, [37] or the interpleader court may require parties to release the insured as a condition of receiving their shares of the stake, [38] but merely filing an interpleader action and paying the policy limits into court does not accomplish that goal.

An insurer that files an interpleader action in a case where ***multiple claims*** are likely to exceed its policy limits cannot reasonably be accused of bad faith for doing so, [39] as *Lehto v. Allstate Insurance Co.* [40] illustrates. In *Lehto,* Allstate insured Israel Carbajal under an auto policy with liability limits of $ 25,000 per person and $ 50,000 per accident. Israel's teenage son, Raul, caused an accident in which five people were injured, with Lehto hurt the worst. The Carbajals had no assets from which to satisfy a judgment other than their insurance policy. Allstate filed an interpleader action to divide its policy limits among the claimants. [41] Lehto then sued the Carbajals. Lehto refused to release the Carbajals from liability for the $ 25,000 per person policy limits, and Allstate refused to pay him without a release. [42] While all the claimants, including Lehto, eventually agreed on how to apportion the policy limits, the court presiding over the interpleader action required them to release the Carbajals as a condition of obtaining their shares. [43] Lehto refused those terms. After twists and turns spanning several years, the Carbajals and Lehto entered into a $ 2.63 5 million stipulated judgment, coupled with a covenant not to execute and an assignment of the Carbajals' bad faith claims against Allstate. [44] Lehto then sued Allstate for bad faith. He won a multimillion dollar judgment at trial and Allstate appealed.

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[34] *Emcasco Ins. Co. v. Davis, 753 F. Supp. 1458, 1461 (W.D. Ark. 1990)* (finding that duty to defend continues after insurer interpleads policy); Gov't Employees Ins. Co. v. Lao, No. CV054008736, 2005 WL 3594057, at *2 (Conn. Super. Ct. Nov. 29, 2005) (same); *Cont'l Ins. Co. v. Burr, 706 A.2d 499, 502 (Del. 1998)* (same); *Am. Standard Ins. Co. v. Basbagill, 775 N.E.2d 255, 259 62 (Ill. App. Ct. 2002)* (same); *Romas, 947 P.2d at 758 59* (same). *But see Carolina Cas. Ins. Co. v. Estate of Studer, 555 F. Supp. 2d 972, 978 80 (S.D. Ind. 2008)* (paying policy limits into court with understanding and intent that they will be fully distributed discharges duty to defend under Illinois and Indiana law upon entry of judgment in the interpleader action).

[35] JERRY & RICHMOND,*supra* note 3, at 735.

[36] Claycomb v. Vision Ins. Group, Civ. Action No. 03 *CI 01135, 2006 WL 1045438,* at *1 (Ky. Ct. App. Mar. 31, 2006).

[37] *See, e.g.,* Farm Family Cas. Ins. Co. v. Noble, No. Civ.A. 1471 K, 2001 WL 765460, at *1 (Del. Ch. June 26, 2001).

[38] *But see Oak Cas. Ins. Co. v. Lechliter, 524 S.E.2d 704, 711 12 (W. Va. 1999)* (finding that trial court could not require claimants to release insured as a condition of receiving interpleaded funds).

[39] *See, e.g.,* ***Mahan v. Am. Standard Ins. Co., 862 N.E.2d 669, 677 (Ind. Ct. App. 2007);*** *Skinner v. John Deere Ins. Co., 998 P.2d 1219, 1223 (Okla. 2000).*

[40] *36 Cal. Rptr. 2d 814 (Ct. App. 1994).*

[41] *Id. at 815.*

[42] *Id. at 816.*

[43] *Id.*

[44] *Id. at 816 17.*

One of the issues on appeal was whether Allstate had committed bad faith by filing the interpleader action. [45] The *Lehto* court rejected this argument. Allstate had filed the interpleader action to apportion its policy proceeds among competing claimants, just as the procedure was intended. [46] While filing the interpleader action would not have absolved Allstate of liability had it refused in bad faith to offer its policy limits to the competing claimants, that was not what happened, and "the filing of the interpleader, standing alone, [could not] itself constitute an act of bad faith." [47]

Retreating, the plaintiff argued that the interpleader action itself constituted bad faith because Allstate filed it to reduce its defense costs. [48] The court also rejected this argument. Allstate had used interpleader exactly as it was intended and, indeed, it had the desired result in terms of fairly apportioning the policy limits. The fact that it simultaneously lowered All state's defense costs did not transform it into an act of bad faith. [49]

On the other hand, *McNally v. Nationwide Insurance Co.* [50] suggests that an insurer may commit bad faith if it does not file an interpleader action where doing so allegedly would have induced a claimant to accept the policy limits in satisfaction of its loss, rather than pursuing full recovery from the insured. [51] Or, twisting the issue slightly, under *McNally* an insurer commits bad faith if, by failing to file an interpleader action, it induces litigation against the insured. [52] Either way, this theory is flawed for at least three reasons.

First, this theory is sound only if the insurer's actions are judged in the bright light of hindsight. This offends basic bad faith doctrine, which requires that an insurer's conduct be scrutinized "in light of the circumstances existing at the time." [53] Second, but in relation to the first point, this theory requires insurers to speculate about opposing parties' potential conduct based on incomplete, unknown, or perhaps unknowable, information. *McNally* implies that insurers can somehow predict whether a claimant will sue rather than negotiate, even where the claimant has not threatened immediate litigation. Of course, the fact that an insurer makes a mistake in formulating or executing settlement strategy is not sufficient to impose bad faith liability even applying a negligence standard. "Mistake is not negligence; the duty of good faith does not make the insurance company an insurer against the uncertainties inherent in the settlement process." [54] Third, this approach discourages insurers from reasonably attempting to settle competing claims within their policy limits, which is often more advantageous to insureds.

B. *Traditional Approaches in Multiple Claimant Cases*

Apart from interpleader, courts employ three principal rules for resolving ***multiple claims*** exceeding an insured's policy limits. These are (1) the first to judgment rule; (2) the pro rata rule; and (3) the first to settle rule.

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[45] *Id. at 818.*

[46] *Id.*

[47] *Id.*

[48] *Id. at 819.*

[49] *Id. at 819 20.*

[50] *815 F.2d 254 (3d Cir. 1987).*

[51] *Id. at 262 63.*

[52] *Id. at 263.*

[53] *Commercial Union Ins. Co. v. Liberty Mut. Ins. Co., 393 N.W.2d 161, 166 (Mich. 1986).*

[54] *Steele v. Hartford Fire Ins. Co., 788 F.2d 441, 447 (7th Cir. 1986).*

Under the first to judgment rule, those claimants who first obtain judgments against the insured receive priority in payment from insurance proceeds. [55] The first to judgment rule chalks the lanes for a race to the courthouse by the injured parties, although it is now outdated and disfavored. [56] The widespread recognition of third party bad faith and the length of time between filing and judgment common to modern litigation have combined to erase the first to judgment rule. [57]

The pro rata rule applies where several claims are combined in one lawsuit and the insurer's liability limits are inadequate to pay the full amount deserved by each of the claimants. [58] Applying the pro rata rule, the insurance policy proceeds are distributed on a pro rata basis in accordance with the amount of damages suffered by each claimant. [59] An individual claimant's maximum apportioned recovery is capped at the per person liability limits of the policy. [60] The claimants cannot agree among themselves to apportion the policy proceeds differently. [61] This is an essentially equitable approach. Obviously, the pro rata rule depends on a court or jury assessing the claimants' damages; although generally accepted in cases where damages are set, the rule is not determinative where an insurer is presented with ***multiple claims*** before suit is filed or the insured's liability is established in litigation. [62] To the extent that insurance claim representatives attempt to settle ***multiple claims*** on a pro rata basis before a suit is filed, that approach may be validly chosen for its ease or perceived fairness, but the law does not rigidly compel it.

Finally, there is the first to settle rule, which reflects the majority position. The first to settle rule enters play where the insurer has settled with some but not all claimants, and the settlements that have been achieved have either completely or nearly exhausted the policy limits. Despite its name, the rule does not require than an insurer settle with the first claimant who offers to settle within policy limits. [63] Rather, the first to settle rule recognizes that insurers should be able to selectively settle with any or several of multiple claimants, even though these settlements deplete or exhaust the policy limits, without incurring bad faith liability in connection with any of the remaining claims. [64] This is true even if only some potential claimants are known at the time of settlement; an insurer has no

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[55] Douglas R. Richmond,*An Overview of Insurance Bad Faith Law and Litigation,* 25 SETON HALL L. REV. 74, 92 93 (1994).

[56] *Id. at 93.*

[57] *Id.*

[58] *Christlieb v. Luten, 633 S.W.2d 139, 140 (Mo. Ct. App. 1982); Allstate Ins. Co. v. Ostenson, 713 P.2d 733, 735 (Wash. 1986); Wondrowitz v. Swenson, 392 N.W.2d 449, 451 52 (Wis. Ct. App. 1986).*

[59] *Christlieb, 633 S.W.2d at 140; Ostenson, 713 P.2d at 735; Wondrowitz, 392 N.W.2d at 452.*

[60] *See, e.g., Ostenson, 713 P.2d at 735.*

[61] *Balz v. Heritage Mut. Ins. Co., 720 N.W.2d 704, 715 (Wis. Ct. App. 2006).*

[62] *See Babcock v. Liedigk, 497 N.W.2d 590, 593 94 (Mich. Ct. App. 1993)* (denying pro rata distribution where claims had not yet been reduced to judgment).

[63] ***Williams v. Infinity Ins. Co., 745 So. 2d 573, 576 (Fla. Dist. Ct. App. 1999).***

[64] *See, e.g., Cont'l Cas. Ins. Co. v. Peckham, 895 F.2d 830, 835 (1st Cir. 1990)* (applying Massachusetts law); *Voccio v. Reliance Ins. Cos., 703 F.2d 1, 2 4 (1st Cir. 1983)* (applying Rhode Island law); *Elliott Co. v. Liberty Mut. Ins. Co., 434 F. Supp. 2d 483, 499 (N.D. Ohio 2006)* (interpreting Connecticut, Delaware, New York, Ohio and Pennsylvania law); *TIG Ins. Co. v. Smart Sch., 401 F. Supp. 2d 1334, 1359 51 (S.D. Fla. 2005)* (applying Florida law); *Gen. Sec. Nat'l Ins. Co. v. Marsh, 303 F. Supp. 2d 1321, 1325 26 (M.D. Fla. 2004)* (same); ***Farinas v. Fla. Farm Bureau Gen. Ins. Co., 850 So. 2d 555, 561 (Fla. Dist. Ct. App. 2003);*** *Miller v. Ga. Interlocal Risk Mgmt. Agency, 501 S.E.2d 589, 590 91 (Ga. Ct. App. 1998); Allstate Ins. Co. v. Evans, 409 S.E.2d 273, 274 (Ga. Ct. App. 1991); Levier v. Koppenheffer, 879 P.2d 40, 45 (Kan. Ct. App. 1994); Oliver v. Imperial Fire & Cas. Ins. Co., 983 So. 2d 172, 175 (La. Ct. App. 2008); Pieno v. Bailey, 815 So. 2d 188, 190 (La. Ct. App. 2002); Babcock, 497 N.W.2d at 593 94; Goughan v. Rutgers Cas. Co., 570 A.2d 501, 503 (N.J. Super. Ct. Law Div. 1989); Allstate Ins. Co. v. Russell, 788 N.Y.S.2d 401, 402 (N.Y. App. Div. 2004); STV Group, Inc. v. Am. Cont'l Props., Inc., 650 N.Y.S.2d 204, 205 (N.Y.*

duty to solicit or consolidate claims. [65] Some courts go so far as to suggest that insurers must attempt to settle as many claims as possible within policy limits. [66]

Because the first to settle rule does not require the reduction of ***multiple claims*** to judgment, it promotes efficiency and allows insurers the best opportunity to protect their insureds. Indeed, to require an insurer to await the reduction of ***multiple claims*** to judgment before paying them has the unfortunate effect of encouraging litigation and increasing the likelihood of insureds incurring liability beyond their policy limits. [67]

The First Circuit thoughtfully related the first to settle rule to insurers' duty of good faith and fair dealing in *Continental Casualty Insurance Co. v. Peckham.* [68] As the *Peckham* court explained, an insurer's goal in a multiple claimant case should be to try to settle all or some of the claims so as to relieve the insured of as much potential liability as is reasonably possible given the paucity of the policy limits. [69] So long as the insurer attempting to resolve ***multiple claims*** acts in good faith, it is entitled to exercise its "honest business judgment." [70] The fact that the insured ultimately incurs liability beyond its policy limits does not mean the insurer is obligated to indemnify the insured against that liability. An insurer honestly attempting to settle ***multiple claims*** to inadequate policy limits is not required to make perfect judgments in the process, or to be omniscient. "The carrier, in fine, 'will not be held to prophesy.'" [71] Furthermore, while claimants in such cases are not obligated to ease the insurer's bind, nor can they "insist upon any punctilio in the insurer's observance, or not, of its obligations toward its insured." [72] Courts should not allow claimants to play cat and mouse games with the insurer. [73]

Naturally, and as *Peckham* indicates, the first to settle rule is not boundless. The individual settlements that the insurer strikes must be reasonable. [74] For example, an insurer could not unilaterally decide to pay a single claimant a disproportionate share of the policy limits because the claimant was somehow subjectively favored, or the lawyer for that claimant was exceptionally aggressive.

Although the first to settle rule theoretically aids insurers, it has not stemmed the tide of multiple claimant bad faith cases. We now turn to some of those decisions.

C. *Bad Faith in the Multiple Claimant Context*

Brown v. United States Fidelity & Guaranty Co. [75] is dated, but it remains a key case on bad faith in the multiple claimant realm. There, Marion Brown was insured under a USF&G auto policy with liability limits of $ 10,000 per

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App. Div. 1996); Tex. Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 315 (Tex. 1994); Carter v. State Farm Mut. Auto. Ins. Co., 33 S.W.3d 369, 372 73 (Tex. App. 2000).

[65] Smith v. Premier Alliance Ins. Co., 48 Cal. Rptr. 2d 461, 466 (Ct. App. 1995); Russell, 788 N.Y.S.2d at 402.

[66] See, e.g., ***Farinas, 850 So. 2d at 561.***

[67] See Evans, 409 S.E.2d at 274.

[68] 895 F.2d 830 (1st Cir. 1990).

[69] Id. at 835 (footnote omitted).

[70] *Id.*

[71] *Id.* (quoting Murach v. Mass. Bonding & Ins. Co., 158 N.E.2d 338 (Mass. 1959)).

[72] *Id.*

[73] *Id.*

[74] ***Farinas v. Fla. Farm Bureau Gen. Ins. Co., 850 So. 2d 555, 561 (Fla. Dist. Ct. App. 2003).***

[75] ***314 F.2d 675 (2d Cir. 1963).***

person and $ 20,000 per accident. Her son, Allen, was driving her car in New York City when he struck a taxicab, injuring the taxi driver, Morris Ruby, and his passengers, Joan O'Dwyer and Anthony Sacco. Allen's passenger, David Borowiak, was also injured. USF&G settled with Ruby for $ 8,000 and Borowiak for $ 6,000, leaving O'Dwyer and Sacco to split $ 6,000. They instead sued the Browns, with O'Dwyer obtaining a $ 25,000 judgment and Sacco a $ 20,000 judgment. They then sued to collect the excess $ 39,000 from USF&G on the theory that it had negotiated Borowiak's settlement in bad faith, exposing the Browns to uninsured liability. [76]

As it turned out, Borowiak and Allen Brown had been out drinking together in the hours leading up to the accident. Accordingly, Borowiak was the only injured party who might be found to be comparatively at fault for the accident. [77] O'Dwyer and Sacco were injured worse than he was. [78] Moreover, USF&G had negotiated dishonestly. Fitzgibbons, the USF&G claims superintendent negotiating with O'Dwyer and Sacco's lawyer, had insisted on a global settlement with the four claimants splitting the $ 20,000 policy limits. [79] The plaintiffs' lawyer agreed to this plan if Fitzgibbons could persuade Ruby and Borowiak to go along because the Browns were not persons of means and would be unable to satisfy any judgment exceeding their policy limits. While that offer was pending, however, USF&G secretly settled with Borowiak. [80]

The bad faith case went to trial and the district court dismissed the plaintiffs' case at the close of the evidence. [81] The Second Circuit reversed and remanded, reasoning that the case should have been submitted to the jury. In doing so, the court in *Brown* did not focus on any particular act of misconduct alleged against USF&G, but instead based its decision on the totality of the circumstances. [82]

The court noted that this case was different from a typical bad faith case, in which the insurer is accused of bad faith for obstinately refusing to settle despite receiving an offer within its policy limits. [83] Here, the insurer had settled two of the four claims against its insureds, but was being sued for bad faith for its overeager settlement. [84] The difference, however, was not dispositive. [85] "In either case, the issue to be adjudicated [is] whether the insurer's conduct reveal[ed] a bad faith disregard of the assured's financial interest." [86]

Brown seemingly heralds a comparative seriousness rule in multiple claimant cases. In other words, when evaluating which claims to settle or how much to pay, insurers must favor the most seriously injured claimants. Of course, the case would stand for nothing of the sort indeed, the decision would not even exist had USF&G kept its promise to the plaintiffs' lawyer to divide the policy proceeds equally among the four claimants. But assuming that the case does favor comparative seriousness analysis, of what consequence is it? Do not insurers routinely factor in the seriousness of competing claimants' injuries when negotiating the settlement of ***multiple claims***?

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[76] ***Id. at 676.***

[77] *Id.*

[78] *See* id. at 681.

[79] *Id.*

[80] *Id.*

[81] ***Id. at 680.***

[82] *See* id. at 682.

[83] ***Id. at 681.***

[84] ***Id. at 682.***

[85] *Id.*

[86] *Id.*

As a practical matter, in many cases insurers do account for the relative seriousness of multiple claimants' alleged injuries when negotiating individual settlements. That is an easy task where the injuries are disparate, as where one claimant is comatose and another broke a leg. In other cases, it is a fair approach. There are many cases, however, in which all claimants are seriously injured, or in which it is impossible for an insurer to reasonably distinguish the seriousness of the respective injuries. In other cases, claimants suffering apparently lesser injuries may in fact have greater potential damages because of the nature of their injuries or occupations. A wrongful death claim may not be as valuable as a claim by a catastrophically injured victim. Thus, the comparative seriousness of claimants' alleged injuries should never be the sole basis for judging the reasonableness of an insurer's settlement decisions. At most, it is in some cases one factor to be considered when scrutinizing an insurer's conduct.

In *Farmers Insurance Exchange v. Schropp,* [87] a vehicle driven by Farmers' insured, Sohl, struck a vehicle in which Schropp was a passenger. Schropp was seriously injured, spending over thirty days in intensive care and incurring medical bills exceeding $ 26,000. Sohl, who was killed in the accident, had policy limits of $ 25,000 per person and $ 50,000 per accident. In addition to Schropp, there were four other claimants with far less at stake. [88] Unfortunately, when Schropp demanded $ 25,000 to settle, Farmers strung him out and never meaningfully responded. [89] The company made no settlement offers to any of the other claimants, either. Roughly eight months after the accident, Farmers filed a declaratory judgment action, alleging that it was in doubt as to whom it should pay any part of its $ 50,000 per accident policy limits; asking the court to determine the competing claimants' rights; and seeking a release of all further liability. Farmers paid its $ 50,000 per accident limits into court at the same time. [90]

Schropp, who was named as a defendant in the declaratory judgment action, counter claimed against Farmers and cross claimed against Sohl's estate, which was also named as a defendant in the action. Schropp and Sohl's estate stipulated to a $ 110,000 judgment. [91] A jury determined that Farmers had acted in bad faith and returned a verdict consistent with the consent judgment. [92] Farmers appealed to the Kansas Supreme Court.

The supreme court noted that Farmers had investigated the accident promptly and determined its liability. [93] Farmers knew that Schropp's injuries were serious and that his medical expenses alone exceeded its per person policy limit. [94] It also knew that all of the other claimants' damages were in the range of $ 4,000 to $ 5,000 and that its insured's negligence had caused the accident. [95] All but one of the claimants were represented by counsel who were known to Farmers, and the one who was not was a minor whose parents were available for consultation. [96] Under these circumstances:

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[87] *567 P.2d 1359 (Kan. 1977).*

[88] *Id. at 1367.*

[89] *See* id. at 1363.

[90] *Id. at 1363 64.*

[91] *Id. at 1365.*

[92] *Id.*

[93] *Id. at 1367.*

[94] *Id.*

[95] *Id.*

[96] *Id.*

> Farmers could well have notified all of the potential claimants involved that the value of the claims would doubtless exceed policy limits, and invite them or their attorneys to participate jointly in efforts to reach agreement as to the disposition of the available funds. Alternatively, Farmers could have attempted to settle claims within the policy limits as they were presented. Or as a third alternative, Farmers could have promptly and in good faith commenced an interpleader action, and paid its policy limits into court. . . . *The first of these alternatives is preferable, where the claimants are readily available, and such a procedure may avoid litigation.* Farmers pursued none of these alternatives. [97]

The court concluded that there was substantial evidence to support the jury's finding that Farmers had acted negligently or in bad faith in handling Schropp's claim. [98] The court also rejected Farmer's defense that it had no duty to act in good faith because Schropp's estate was insolvent and thus could not be harmed by the entry of an excess judgment. [99] The supreme court affirmed the trial court judgment with the exception of one portion that reflected duplicative damages.

Schropp is generally understood to stand for the principle that in a multiple claimant case where the insurer knows all claimants and their representatives, the duty of good faith ought to compel it to attempt to facilitate a global resolution of the competing claims before settling with individual claimants or filing an interpleader action. [100] Regardless of whether an insurer is duty bound to take that approach, it represents sound advice. *Schropp* does not otherwise alter the first to settle rule, which the Kansas Supreme Court had adopted six years earlier. [101]

Texas Farmers Insurance Co. v. Soriano [102] arose out of an accident in which Richard Soriano crashed head on into a car driven by Carlos Medina. Medina's wife was killed, as was Adolfo Lopez, a teenage passenger in Soriano's car. Medina was severely injured and his two children were also hurt. Soriano was drunk, speeding, and recklessly attempting to pass another vehicle at the time of the accident. He had only minimal insurance coverage with Farmers; his policy provided liability limits of $ 10,000 per person and $ 20,000 per occurrence. [103]

Farmers offered the Medinas the full policy limits of $ 20,000, which they rejected because they wanted to investigate Soriano's personal assets. The Medinas and Lopez's parents then sued Soriano in consolidated cases. Shortly before trial, Farmers settled with the Lopezes for $ 5,000 and offered the remaining $ 15,000 to the Medinas. The Medinas rejected this offer and demanded the full policy limits of $ 20,000, i.e., the offer they had earlier rejected. [104] They went to trial against Soriano and were awarded just over $ 172,000. Soriano assigned his rights against Farmers to the Medinas in exchange for a covenant not to execute on the judgment. The Medinas then sued Farmers in Soriano's name for gross negligence, negligence, and breach of the duty of good faith and fair dealing. [105] A jury awarded the Medinas over $ 500,000 in compensatory damages and $ 5 million in punitive

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[97] *Id.* (citation omitted) (emphasis added).

[98] *Id.*

[99] *Id. at 1368 69.*

[100] *See, e.g., Voccio v. Reliance Ins. Co., 703 F.2d 1, 3 (1st Cir. 1983)* ("We doubt that a reasonable jury . . . could have found any relevant bad faith here. . . . For one thing, the carrier met together with counsel for both [the claimants] and sought suggestions on how to divide the money a course recommended in *Farmers Insurance Exchange v. Schropp. . . .").*

[101] *Castoreno v. W. Indem. Co., 515 P.2d 789, 795 (Kan. 1973).*

[102] *881 S.W.2d 312 (Tex. 1994).*

[103] *Id. at 313.*

[104] *Id.*

[105] *Id. at 314.*

damages. The Texas Court of Appeals remitted the punitive award to $ 1 million and reformed the judgment with respect to prejudgment interest, but otherwise affirmed the trial court on the basis that "there was some evidence that the Lopez settlement was unreasonable, negligent and made in bad faith." [106] The Texas Supreme Court disagreed, reversing the lower appellate court and rendering judgment for Farmers. [107]

Under the so called *Stowers* doctrine, which is an essential aspect of Texas insurance law, a liability insurer may be liable for negligently failing to settle a claim within its policy limits. [108] For the *Stowers* doctrine to apply, the claim must be within the scope of coverage; there must be a settlement demand within policy limits; and the terms of the demand must be such that an ordinarily prudent insurer would accept it considering the likelihood and degree of the insured's potential exposure to an excess judgment. [109] In this case:

> When Farmers received the Lopez settlement demand of $ 5,000 ($ 5,000 to settle a wrongful death claim), Farmers was required under *Stowers* to exercise reasonable care in responding to that demand. Had Farmers opted not to settle the Lopez wrongful death claim but, in the face of that demand, to renew its offer of the original face amount of the policy to settle the Medinas' claims instead, Farmers would surely face questions about liability under *Stowers* for failing to settle the Lopez wrongful death claim. To be sure, in settling the Lopez claim, Farmers necessarily reduced the amount of insurance available to satisfy the Medinas' claims, but Farmers also reduced Soriano's liability exposure. [110]

The court in *Soriano* concluded that when confronted with a settlement demand in a case in which there are ***multiple claims*** and inadequate policy limits, an insurer may enter into a reasonable settlement with one claimant even though that settlement diminishes or exhausts the proceeds available to satisfy the remaining claims. [111] This approach promotes settlement and encourages claimants to assert their claims promptly. [112]

Once Farmers settled the Lopez claim, it had only $ 15,000 left to settle the Medinas' claims. The Medinas never demanded the full $ 20,000 before the Lopez settlement; their demand was made afterwards. [113] Farmers had no duty to pay more than its policy limits to settle the Medinas' claims. [114] Furthermore, there was no basis for Soriano to argue that it was unreasonable for Farmers to settle the Lopez wrongful death claim for $ 5,000. [115] The alleged fact that the Medinas' claims were more serious than the Lopez claim did not mean that the Lopez settlement was

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[106] *Id.*

[107] *Id. at 318.*

[108] *Id. at 314* (citing *G.A. Stowers Furniture Co. v. Am. Indem. Co., 15 S.W.2d 544, 547 48* (Tex. Comm'n App. 1929)).

[109] *Id.*

[110] *Id.* at 315.

[111] *Id.*

[112] *Id.*

[113] After Farmers offered its full $ 20,000 policy limits to the Medinas but before settling with the Lopezes, the Medinas' lawyer indicated to Farmers' counsel that he would recommend a settlement of $ 20,000 to the Medinas if Farmers would make the offer again. While this indicated that Farmers might have been able to settle the Medinas' claims for $ 20,000 prior to the Lopez settlement, it was not a settlement demand within policy limits and accordingly could not form a basis for*Stowers* liability. *Id.* at 315 16.

[114] *Id.* at 316.

[115] *Id.*

unreasonable. [116] Soriano could not demonstrate that it was unreasonable for Farmers to settle a meritorious wrongful death claim for $ 5,000, especially in light of his potential excess liability on that claim alone. [117]

With respect to Soriano's bad faith claim, the court noted that it had never recognized a cause of action for breach of the duty of good faith and fair dealing in the liability insurance context; it had always restricted this cause of action to first party insurance. [118] In Texas, a first party insurer commits bad faith if (1) it has no reasonable basis for denying or delaying payment of a claim; or (2) it knew or should have known that there was no reasonable basis for denying or delaying payment of as claim. [119] Without holding that accepted Texas bad faith standards applied to third party claims, the court determined that this claim could not succeed in any event because the Medinas did not make their $ 20,000 settlement demand until after Farmers had settled the Lopez wrongful death claim and Farmers was under no obligation to pay the Medinas more than the remaining $ 15,000 policy limits to settle. As a matter of law, Farmers had a reasonable basis for refusing to pay the Medinas more than the $ 15,000 it offered, and it therefore did not breach its duty of good faith and fair dealing by refusing to settle for $ 20,000. [120]

In *Rinehart v. Shelter General Insurance* Co., [121] Michael Rinehart was driving drunk in August 1998 when he struck another vehicle. Rinehart's passenger, Charles Adkins, was seriously injured in the wreck, as were the two people in the other car, Renee Ingram and Kelly Krohn. Rinehart was insured by Shelter under an automobile policy with liability limits of $ 50,000 per person and $ 100,000 per occurrence. Shelter adjuster Charles Nitz assumed responsibility for the loss approximately two weeks after the accident.

In early 1999, Terry Evans, a lawyer representing Ingram and Krohn, wrote Shelter and demanded $ 50,000 for each of his clients to settle. Nitz responded with a letter of his own, stating that Shelter was willing to pay the policy limit of $ 100,000, but that Ingram and Krohn would have to agree with Adkins on how to divide that sum. [122] Evans replied that Shelter's proposal was unacceptable "because Adkins was 'acting in concert' with Rinehart at the time of the accident and, therefore, should not be considered an 'equal player in the division of the $ 100,000.'" [123] Nitz remained firm that Ingram and Krohn would have to share the policy limits with Adkins.

Nitz had communicated with Adkins three times during 1998. Adkins had been friends with Rinehart for many years, and he neither retained a lawyer nor demanded that Shelter settle with him on Rinehart's behalf. In late May or early June 1999, Nitz told Adkins that "there was 'nothing more he could do'" for him. [124] Adkins understood Nitz to mean that Shelter would pay him nothing in compensation for his injuries. Adkins never made a claim against Rinehart for the accident. [125]

On June 17, 1999, Evans again wrote Shelter to offer to settle on behalf of Ingram and Krohn for $ 100,000, i.e., the per occurrence policy limit. Evans' letters stated that the offers would expire on August 19, 1999, and that all offers

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[116] *Id.*

[117] *See id.* & n.4.

[118] *Id.* at 317.

[119] *Id.* (citing *Arnold v. Nat'l County Mut. Fire Ins. Co., 725 S.W.2d 165, 167 (Tex. 1987)).*

[120] *Id.* at 318.

[121] *261 S.W.3d 583 (Mo. Ct. App. 2008).*

[122] *Id. at 588.*

[123] *Id.*

[124] *Id.*

[125] *Id.*

to settle would then be forever withdrawn. [126] Shelter did not inform Rinehart about Evans' June 17 offer letters. [127] On July 6, however, Shelter wrote Rinehart to tell him that it intended to settle with Ingram and Krohn for two thirds of the per occurrence policy limits unless Rinehart objected within twenty days. Rinehart did not object. [128]

On August 3, Shelter sent a letter to Evans offering to settle with Ingram and Krohn for two thirds of the per occurrence policy limits if they would waive any underinsured motorist claims and hospital liens. [129] Evans did not accept the offer and no settlement was reached by the August 16 deadline. Ingram and Krohn then sued Rinehart. Ingram was awarded a judgment of over $ 3.5 million and Krohn received a judgment of over $ 1 million. To avoid garnishment, Rinehart entered into a written agreement with Ingram and Krohn whereby he agreed to sue Shelter for bad faith in failing to settle, with any proceeds of that lawsuit, as well as any annual income he might earn in excess of $ 50,000, going to satisfy their judgments against him. [130]

In September 2003, Rinehart filed his bad faith action. Following a jury trial, he received a judgment for roughly $ 6.25 million in compensatory damages and $ 3 million in punitive damages. [131] Shelter appealed to the Missouri Court of Appeals.

On appeal, Shelter argued that the bad faith and punitive damage claims against it had to fail because there was no evidence that it disregarded Rinehart's financial interests in an effort to avoid paying its policy limits. [132] Rather, Shelter asserted, its objective was to settle with all potential claimants, including Adkins, for $ 100,000, and thus protect Rinehart from any potential personal liability. [133] The problem for Shelter, Rinehart pointed out, was Nitz's communications with Adkins. As the court explained:

> Shelter negotiated with Ingram and Krohn from January through August 1999, but there [was] no indication of negotiations with Adkins during that period. Adkins testified that in late May or early June 1999, [Nitz] said "there was nothing more he could do for [him]." This evidence supports Rinehart's contention that Shelter had no intention of settling with Adkins during 1999 and merely used him as a 'straw man' for purposes of negotiating a settlement with Ingram and Krohn for two thirds of the policy limit. [134]

In summary, Ingram and Krohn sent Shelter clear settlement letters that imposed a deadline for accepting their offers. The only reason that Shelter gave for refusing to settle with them was Adkins' potential claim, but Rinehart presented evidence that Shelter never intended to settle with Adkins. The jury could infer from that evidence that Shelter tried to escape its full contractual obligation to Rinehart by paying only two thirds of its policy limit to Ingram and Krohn. [135]

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[126] *Id. at 589.*

[127] *Id.*

[128] *Id.*

[129] *Id.*

[130] *Id.*

[131] *Id.*

[132] *Id. at 596.*

[133] *Id.*

[134] *Id.*

[135] *Id.*

The court further found that the evidence Rinehart presented on Shelter's bad faith was sufficient to support punitive damages. In light of Shelter's communications with Adkins in May or June 1999, the jury could infer that it demonstrated reckless indifference to Rinehart's financial interests by refusing to settle with Ingram and Krohn for the full policy limits. [136] Shelter also failed to keep Rinehart fully informed about the settlement negotiations. [137] Accordingly, the court affirmed the judgment for Rinehart. [138]

There are some flaws in *Rinehart.* For example, the plaintiff's expert, Allan Windt, testified that Shelter was negligent in failing to advise Rinehart of Evans' early 1999 offers to settle on behalf of Ingram and Krohn for policy limits. [139] An insurer clearly should keep its insured informed of settlement negotiations in any case of potential excess liability, [140] and a failure to communicate is one factor to consider in analyzing an insurer's possible bad faith. [141] Absent some agreement or understanding between Shelter and Rinehart about necessary communication, the company's failure to inform Rinehart of Evans' settlement offers was a mistake. But unless there was evidence that Shelter's lack of communication contributed to the excess verdicts, that lapse was irrelevant. [142] Shelter's *negligent* failure to communicate was necessarily irrelevant in any event because in Missouri, bad faith requires proof that the insurer *intentionally* disregarded its insured's interests in the hope of escaping the full responsibility imposed on it by its policy. [143]

Furthermore, Shelter apparently understood a May 1999 letter sent on behalf of Ingram and Krohn to be an offer to settle for two thirds of the policy limits. [144] In July, Shelter apparently believed that Ingram and Krohn had reiterated their offer to settle on the same terms. [145] Windt testified that Shelter should have accepted either of these offers. [146]

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[136] *Id. at 597.*

[137] *Id.*

[138] *Id. at 598.*

[139] *Id. at 592.*

[140] *Jackson v. Am. Equity Ins. Co., 90 P.3d 136, 142 (Alaska 2004); Allied Processors, Inc. v. W. Nat'l Mut. Ins. Co., 629 N.W.2d 329, 333 (Wis. Ct. App. 2001).*

[141] *McKinley v. Guar. Nat'l Ins. Co., 159 P.3d 884, 889 (Idaho 2007); O'Neill v. Gallant Ins. Co., 769 N.E.2d 100, 107 (Ill. App. Ct. 2002).*

[142] *DeWalt v. Ohio Cas. Ins. Co., 513 F. Supp. 2d 287, 303 (E.D. Pa. 2007)* ("Where an insurer's bad faith conduct consists of a failure to communicate with its insured, the plaintiff cannot maintain a claim unless there is evidence sufficient to allow a jury to conclude that the lack of communication in some way caused the excess verdict."). A plaintiff may call an expert witness to testify that had the insurer communicated a settlement offer to the insured, the insured could have hired independent counsel to write "hammer letters" to the insurer demanding that it settle within its policy limits. *See, e.g., Johnson v. Allstate Ins. Co., 262 S.W.3d 655, 665 (Mo. Ct. App. 2008).* Of course, to offer such testimony, the expert must be prepared to speculate that the insured would have known to engage an attorney to do so, or, if informed by the insurer of the right to consult with independent counsel in a typical "excess letter," that the insured would have affirmatively acted on that information. If the carrier sent the insured an excess letter before the alleged communication lapse and the insured has not engaged personal counsel despite being informed of that right, *see* ***Mahan v. American Standard Insurance Co., 862 N.E.2d 669, 671 (Ind. Ct. App. 2007)*** (quoting a fairly typical excess letter), it is indeed speculative to think that the insured would have done so when informed of a settlement offer. In addition, the expert must further assume that the insured could have afforded personal counsel. That is not necessarily a valid assumption if the insured has no assets apart from her insurance policy.

[143] *Rinehart, 261 S.W.3d at 591* (quoting *Zumwalt v. Utils. Ins. Co., 228 S.W.2d 750, 754 (Mo. 1950)).*

[144] *Id.* at 592.

[145] *Id.*

In retrospect, it is crystal clear that Shelter should have accepted the May offer in light of Evans' June 17 letter demanding $ 50,000 each for Ingram and Krohn. [147] The failure to do so was harmless, however, if in July Evans reiterated Ingram's and Krohn's willingness to settle for two thirds of the per occurrence policy limits, thus giving Shelter a second bite at the apple. If Evans gave such an indication in July, then Shelter's August 3 letter offering to settle for that amount if Ingram and Krohn waived any underinsured motorist claims and hospital liens does not suggest intentional disregard for Rinehart's financial interests, especially since Shelter informed him of its plan and afforded him the opportunity to object. [148]

Both the trial and the appellate courts appear to have been persuaded of Shelter's bad faith by its treatment of Adkins. It is here that Shelter's defense crumbled. While there was nothing wrong with Shelter honestly attempting to dissuade Adkins from making a claim, the fact that Nitz told Adkins there was nothing he could do for him allowed the jury to infer that Nitz knew that Ingram and Krohn were demanding the full policy limits, and that he was gambling with Rinehart's financial future to save Shelter money. Shelter's failure to convey Evans' early settlement offers mixed in here to strengthen the plaintiff's theory that Shelter was unreasonably attempting to save some of its policy limits. This doomed Shelter on appeal, because the standard of review on these points required the appellate court to view the evidence and all resulting inferences in a light most favorable to the plaintiff. [149] Ironically, Shelter probably could have paid its policy limits to Ingram and Krohn, and Adkins never would have sued Rinehart out of friendship.

Whatever its flaws or virtues, the *Rinehart* decision should not be read as a rejection of the first to settle rule. Rather, *Rinehart* illustrates than an insurer seeking refuge in the first to settle rule must act in good faith when trying to settle fewer than all potential claims. If it does not do so, the presence of multiple claimants is no excuse.

D. *Recommendations for Insurers in Multiple Claimant Cases*

As the various decisions on the subject of bad faith in multiple claimant controversies make clear, "there is no one 'right way'" for an insurer to handle such a case. [150] There are, however, several steps that insurers might take to fulfill their duty of good faith and fair dealing, and thereby reduce their potential exposure to extracontractual liability where ***multiple claims*** exceed their policy limits. [151]

First, when an insurer is notified of a multiple claimant loss, it should reasonably and expediently investigate the matter. [152] The insurer should attempt to ascertain the insured's potential liability, identify the claimants, and assess the nature and extent of the claimants' injuries or damages. In some cases this will be simple, in others difficult. The extent and nature of the required investigation will always depend on the facts of the case. Insurers have the right to request that claimants furnish information concerning their injuries and damages, and the fact that this process perhaps delays resolution of some or all claims does not evidence bad faith. [153] This is particularly true where the

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[146] *Id.*

[147] *See id.* at 589 (discussing the June 17 letter).

[148] *See id.* (discussing these communications).

[149] *Id.* at 595 (quoting *BMK Corp. v. Clayton Corp., 226 S.W.3d 179, 188 (Mo. Ct. App. 2007)).*

[150] Unger,*supra* note 30, at 14.

[151] An insurer's failure to follow the steps outlined here does not necessarily evidence bad faith. Insurers are not required to handle claims perfectly. The test for bad faith in this context as elsewhere is whether the insurer subordinated the insured's interests to its own, rather than considering them equally.

[152] Unger,*supra* note 30, at 17.

[153] *See, e.g., DeWalt v. Ohio Cas. Ins. Co., 513 F. Supp. 2d 287, 300 02 (E.D. Pa. 2007)* (involving delay in obtaining medical records).

delay is attributable to gamesmanship, lack of cooperation, or recalcitrance by the claimants or their lawyers. [154] That said, insurers should not insist on receiving what amounts to unnecessary information to backstop objectively simple decisions or judgments. For example, if an insured with policy limits of $ 25,000 per person and $ 50,000 per occurrence allegedly causes an accident in which two people are killed or so badly injured as to be air lifted to a hospital, the insurer should be able to conclude that the insured faces excess liability without reviewing reams of medical records. An insurer's investigation must always be guided by reason.

If an insurer cannot quickly investigate a matter to conclusion, it still should form a plan for its investigation. It should attempt to learn from the claimants how long it will be before they will be able to assess their injuries or damages, and thus allow the insurer to do the same. The insurer may need this information to be able to fairly communicate with everyone involved.

Second, the insurer should communicate with the insured concerning her potential liability as soon as practicable. The insurer should explain its plan for resolving the ***multiple claims*** likely to be asserted against the insured. The insurer should inform the insured of her right to retain personal counsel and of its willingness to accept guidance and advice from her counsel in resolving claims. The insurer should inform her that regardless of her desire for personal counsel, it will be retaining counsel for her. Consistent with this approach, the insurer should appoint defense counsel for the insured as soon as possible.

Third, the insurer should communicate with all claimants to inform them of its policy limits both per person and per occurrence and its willingness to exhaust its limits to achieve a global resolution. [155] The insurer should invite the claimants or their attorneys to participate jointly in an effort to allocate the policy proceeds. [156] This may include convening a mediation or settlement conference, although not necessarily so. The insurer should make clear that the payment of the policy proceeds as voluntarily allocated depends on the claimants fully releasing the insured from all liability. The insurer should set a reasonable time limit for the claimants to accomplish their voluntary allocation. [157] The insurer should also explain that if the claimants cannot reach agreement on the allocation of policy proceeds by the deadline, it will either (1) file an interpleader action; or (2) begin settling individual claims as it deems reasonable.

Fourth, the insurer should keep the insured apprised of the settlement process and its strategy. [158] As the insurer formulates its strategy for settling with individual claimants, it should consult with the insured about that process and possible approaches. It should check with the insured as often as necessary to confirm the insured's agreement with its decisions. To be sure, neither the insured's agreement with the insurer's settlement decisions nor the insurer's obedience of the insured's related instructions necessarily inoculates the insurer against bad faith. [159] By involving its insured in these matters, however, the insurer is fulfilling its responsibility to communicate and allowing the insured the chance to protect her own interests, both of which are compelling evidence of good faith and fair dealing. [160]

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[154] *See, e.g.,* Wade v. EMCASCO Ins. Co., 483 F.3d 657, 671 72 (10th Cir. 2007) (involving medical records in a single claimant case and attempt to set up bad faith suit).

[155] *See* Gen. Sec. Nat'l Ins. Co. v. Marsh, 303 F. Supp. 2d 1321, 1326 (S.D. Fla. 2004) (exonerating insurer of bad faith).

[156] *See* Voccio v. Reliance Ins. Co., 703 F.2d 1, 3 (1st Cir. 1983); Farmers Ins. Exch. v. Schropp, 567 P.2d 1359, 1367 (Kan. 1977); Carter v. State Farm Mut. Auto. Ins. Co., 33 S.W.3d 369, 372 (Tex. App. 2000).

[157] *See* Marsh, 303 F. Supp. 2d at 1326.

[158] *See id.* (crediting insurer for keeping insured informed).

[159] *See, e.g.,* McNally v. Nationwide Ins. Co., 815 F.2d 254, 264 65 (3d Cir. 1987) (discussing insurer's superior expertise when compared to insured's personal counsel).

[160] *See* Voccio, 703 F.2d at 3.

Oddly, some plaintiffs' lawyers lambaste insurers for consulting with their insureds regarding settlement or for honoring insureds' wishes when settling individual claims. The theory seems to be that because standard liability insurance policies vest carriers with the right to defend and settle claims and suits as they see fit, ceding that right in whole or part is unreasonable. This is nonsense on stilts. First, the fact that an insurer has the right to defend or settle as it sees fit does not mean that it must always insist on it. Companies freely opt not to exercise contractual rights. Second, fundamental bad faith doctrine requires insurers to inform insureds of settlement offers within policy limits so that they can act to protect themselves against excess liability. It would stand bad faith law on its head to hold that an insurer that allows an insured to protect herself against excess liability by involving her in settlement decisions thereby breaches its duty of good faith and fair dealing.

Fifth, in the unfortunate event that the claimants cannot reach agreement among themselves, the insurer should settle with individual claimants in a reasonable manner. In doing so, the insurer should attempt to prioritize the claims that pose the greatest threat of personal liability to the insured. [161] Again, the insurer should strive to involve the insured in this process. If the insured and insurer differ in their desired or intended approaches to settlement, the insurer should follow the insured's direction.

As an alternative to this fifth step, one commentator recommends that the insurer pay its policy limits to the insured to distribute as she deems appropriate. [162] After all, the insurer's duty to settle is owed to the insured and in the multiple claimant situation, the insurer is obligated to expend its policy with the insured's best interests in mind. [163] If the insured were to squander the policy limits, the insurer should be insulated against liability to aggrieved claimants because (a) it owed them no duty; and (b) it exercised due care by first attempting to settle all claims. [164] An insurer taking this approach, however, must first satisfy itself that it will not be subject to the law of a state that recognizes direct actions or affords claimants third party beneficiary status, [165] and must further recognize that paying its policy limits to the insured will not terminate or preempt its duty to defend. Insurers may also be reluctant to take this approach because of the loss of control over the negotiation and settlement process. And, of course, the insured may resist this tactic on the ground that the insurer has vastly superior experience and expertise in these matters, and has contracted for the responsibility it is now selfishly seeking to avoid as a means of protecting its interests.

Some additional points bear mention. First, there may be jurisdictions that are so potentially hostile, or cases that are so potentially volatile, that an insurer prefers to simply interplead its policy limits. If an insurer pursues interpleader, it again must recognize that doing so does not necessarily extinguish its duty to defend. Furthermore, in the interpleader petition or complaint, the insurer should request that claimants be required to fully release the insured from all liability to receive shares of the interpleaded funds.

Second, an insurer should diligently attempt to document all communications with its insured. [166] If claims professionals discuss critical matters with insureds in person or by telephone, for example, they should timely confirm those conversations in writing. Insurers should copy insureds on all letters to claimants or their counsel.

Third, the insurer should carefully document all communications with the various claimants and their counsel. If claimants or their lawyers misstate facts in communications, the insurer should attempt to correct their misimpressions.

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[161] This may not be feasible in all cases and it may be of only marginal benefit to an insured who has no assets apart from her insurance policy.

[162] 1 WINDT,*supra* note 29, § 5:8, at 5 50.

[163] *Id.*

[164] *Id.* § 5:8, at 5 51.

[165] *Id.* § 5:8, at 5 50.

[166] *See* Unger, *supra* note 30, at 17.

Finally, the approach outlined here may be derailed by claimants who make early settlement offers with relatively short deadlines for acceptance, or who make offers at any time that are coupled with unreasonably short deadlines. Insurers must be alert to attempts to position them for bad faith claims based on their failure to settle within policy limits. To the extent possible, insurers should promptly respond to all time restricted offers, even if it is only to request additional time to consider the offer. If forced to act on such a claim, an insurer should consider it in isolation; that is, whether the proposed settlement is reasonable based on the merits of the claim and the insured's potential excess liability. [167] An insurer is not required to settle with one of several claimants simply because that claimant made the first demand or offer. [168] If the settlement offer is reasonable in light of the merits of the claims and the insured's potential excess liability, the insurer should accept it, even though acceptance will reduce the amount of money available to settle with other claimants.

IV. THE PROBLEM OF MULTIPLE INSUREDS

In addition to multiple claimant disputes, insurers may confront bad faith allegations arising out of cases in which they insure several defendants under a policy with limits that are inadequate to fully protect all of them. This scenario surfaces where, for example, a single policy names multiple insureds, one defendant is the named insured on a policy and another is insured by virtue of the policy's omnibus clause, or one defendant is endorsed as an additional insured on another defendant's policy. The insurer in such a case owes a duty of good faith and fair dealing to each insured. [169] Problems arise where a plaintiff makes a settlement offer as to one insured that will exhaust or largely deplete the policy limits, thus leaving the remaining insured potentially exposed to personal liability. Moreover, an insurer that exhausts its policy limits in settling on behalf of one insured will likely disclaim a duty to defend the remaining insured based on its policy language, which states that its "duty to defend ends when [its] limit of liability for this coverage has been exhausted by payment of judgments or settlements," [170] or that its duty to defend "ends when [it has] used up the applicable limit of insurance in the payment of judgments or settlements." [171]

The first to settle rule generally applies in multiple insured cases just as it does in multiple claimant cases. [172] Thus, an insurer generally may expend its policy limits to settle on behalf of one insured even if doing so exposes another insured to personal liability. [173] Similarly, an insurer that exhausts its policy limits in settling on behalf of one insured

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[167] *Travelers Indem. Co. v. Citgo Petroleum Corp., 166 F.3d 761, 765 (5th Cir. 1999)* (quoting *Tex. Farmers Ins. Co. v. Soriano, 881 S.W.2d 312 (Tex. 1994)).*

[168] ***Williams v. Infinity Ins. Co., 745 So. 2d 573, 576 (Fla. Dist. Ct. App. 1999).***

[169] Brummett v. Am. Standard Ins. Co. of Wis., No. 04 1114 *JTM, 2005 WL 1683610,* at *12 (D. Kan. July 18, 2005) (applying Kansas law); *Strauss v. Farmers Ins. Exch., 31 Cal. Rptr. 2d 811, 814 (Ct. App. 1994); Contreras v. U.S. Sec. Ins. Co., 927 So. 2d 16, 21 (Fla. Dist. Ct. App. 2006).*

[170] Ins. Servs. Office, Inc., Personal Auto Policy (PP 00 01 06 98), at 2 (1997).

[171] ISO Props., Inc., Commercial General Liability Coverage Form (CG 00 01 12 04), at 1 (2003).

[172] *But see* 1 WINDT, *supra* note 29, § 5:9, at 5 51 (asserting that all insureds must consent to settlement on behalf of one insured that exhausts or seriously depletes policy limits as to others).

[173] *See, e.g., Travelers Indem. Co. v. Citgo Petroleum Corp., 166 F.3d 761, 764 69 (5th Cir. 1999)* (interpreting Texas law); *Elliott Co. v. Liberty Mut. Ins. Co., 434 F. Supp. 2d 483, 499 (N.D. Ohio 2006)* (construing Conneciticut, Delaware, New York, Ohio and Pennsylvania law); *Contreras v. U.S. Sec. Ins. Co., 927 So. 2d 16, 20 22 (Fla. Dist. Ct. App. 2006); Country Mut. Ins. Co. v. Anderson, 628 N.E.2d 499, 503 (Ill. App. Ct. 1993); Millers Mut. Ins. Ass'n of Ill. v. Shell Oil Co., 959 S.W.2d 864, 870 (Mo. Ct. App. 1997); Anglo Am. Ins. Co. v. Molin, 670 A.2d 194, 198 99 (Pa. Commw. Ct. 1995). But see W. Alliance Ins. Co. v. N. Ins. Co. of N.Y., 176 F.3d 825, 828 29 (5th Cir. 1999)* (rejecting insurer's attempt to exhaust policy on claim against insured sued later to avoid duties to additional insured that was originally sued and that had agreed to settlement); *Schwartz v. State Farm Fire & Cas. Co., 106 Cal. Rptr. 2d 523, 529 (Ct. App. 2001)* ("The duty imposed by the covenant of good faith and fair dealing includes the duty not to favor the interest of one of its insureds over the interests of the other.").

may thereafter decline to defend another insured on the basis that its duty to defend ended upon its prior exhaustion. [174] As a Missouri court explained:

> A settlement offer given to only one insured that would exhaust coverage under the . . . policy creates a dilemma for the insurer. An insurer should not be precluded from accepting a reasonable settlement offer for fewer than all insureds. By accepting the offer the insurer would avoid being subjected to liability exceeding the policy limits due to its rejection of a reasonable offer. . . . Further, any settlement would benefit all insureds by decreasing the total amount of liability in the underlying suit. [175]

Again, any settlements that exhaust the policy limits must be reasonable. [176]

Notwithstanding the broad shelter provided by the first to settle rule, cases involving multiple insureds can pose significant challenges for insurers. [177] Some representative cases are discussed below. [178]

A. *Representative Cases Involving Multiple Insureds*

Travelers Indemnity Co. v. Citgo Petroleum Corp. [179] is probably the leading bad faith case in this context. In that case, Travelers issued a business auto policy, a commercial general liability (CGL) policy, and an umbrella policy to Wright Petroleum, a seller of petroleum products. Citgo, which had a franchise agreement with Wright, was named as an additional insured on all three Travelers policies. In due course, a Wright tanker truck hauling gas for Citgo and other customers struck a vehicle driven by Richard Friedrichs. The Wright driver and Friedrichs were killed in the accident, which apparently was caused by the Wright driver running a red light.

Friedrichs' survivors sued Wright and several other defendants in a Texas state court. The plaintiffs did not initially sue Citgo. Travelers assumed Wright's defense and settled the suit for $ 1.5 million, which represented the full liability limits of Wright's business auto and umbrella policies. [180] The accompanying release absolved Wright, the truck driver's estate, and other defendants. The release did not include Citgo, which had not been sued, and which the plaintiffs never mentioned in their settlement offers. Travelers knew, however, that the plaintiffs were insistent on reserving their rights to sue Citgo. [181]

Shortly after settling with Wright, the plaintiffs amended their complaint to name Citgo as a defendant. Citgo demanded that Travelers defend and indemnify it in connection with the amended action, but Travelers refused. Travelers asserted that it owned Citgo no duties because the earlier settlement had fully exhausted the limits of the business auto and umbrella policies, and the CGL policy included an auto exclusion. [182] Travelers then filed a

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[174] *See, e.g.,* Underwriters Guar. Ins. Co. v. Nationwide Mut. Fire Ins. Co., 578 So. 2d 34, 35 36 (Fla. Dist. Ct. App. 1991); Anderson, 628 N.E.2d at 504; Millers Mut., 959 S.W.2d at 872; Molin, 670 A.2d at 198 99.

[175] Millers Mut., 959 S.W.2d at 870 (citations omitted).

[176] Molin, 670 A.2d at 199 n.5.

[177] *See, e.g.,* Princeton Ins. Co. v. Qureshi, 882 A.2d 993 (N.J. Super. Ct. App. Div. 2005) (involving conflicts of interest and excess liability where single policy covered doctor individually and his two businesses).

[178] At least one court has applied the pro rata rule in a multiple insured case.*See, e.g.,* Countryman v. Seymour R II Sch. Dist., 823 S.W.2d 515, 522 23 (Mo. Ct. App. 1992).

[179] 166 F.3d 761 (5th Cir. 1999).

[180] Id. at 763.

[181] *Id.*

[182] Id. at 763 64.

declaratory judgment action seeking a determination that it owed no duties to Citgo. Citgo counter claimed for breach of contract, fraudulent misrepresentation, unfair trade practices, breach of the duty of good faith and fair dealing, and negligence. The district court awarded summary judgment to Travelers and Citgo appealed.

Central to all of Citgo's arguments was its contention that under Texas law, an insurer cannot favor one insured over another when settling litigation. [183] The Fifth Circuit disagreed.

In Texas, again, the *Stowers* doctrine governs insurers' settlement duties. [184] Under *Stowers,* an insurer defending an insured in a lawsuit over a covered claim, if presented with a settlement offer within policy limits, must accept the offer when an ordinarily prudent insurer would do so in light of the insured's likely exposure to an excess judgment. [185] This creates problems, however, where multiple claimants or multiple insureds are involved. As the court observed:

> In such cases, fulfillment of the *Stowers* duty will reduce the funds available to satisfy the claims of other plaintiffs or the defense of other insured parties. However, if insurers are subject to both liability for failure to settle under *Stowers* and liability for disparate treatment of nonsettling insureds, insurers would find the policy limits they carefully bargained for of little utility. Under *Stowers,* they would be obliged to settle up to the limit of a policy or face a lawsuit by the covered insured as to whom the settlement within policy limits was offered. But if they in fact settled, they would leave themselves open to claims by the insureds excluded from the settlement, and any additional recovery would be in excess of the limits they had originally relied on. [186]

The court noted that the Texas Supreme Court had resolved this dilemma in the multiple claimant context in *Texas Farmers Insurance Co. v. Soriano,* [187] and it was obvious that the Fifth Circuit found *Soriano* persuasive. [188] Citgo attempted to distinguish *Soriano* on the basis that an insurer owes a higher duty to its insured than it does to claimants, and that the lesser duty that allows an insurer to choose which claimant to settle with is not effective where multiple insureds are involved. The court rejected this argument because it ignored the fact that the complaining party in *Soriano* was the insured, not a second claimant. [189] Of course, the argument should have failed in any event because insurers generally do not owe a duty of good faith to third party claimants.

Citgo next attempted to argue that under *Soriano,* a court must examine whether a given settlement is proper in light of all potential claims against all insured parties. [190] That was plainly wrong, since the *Soriano* court had made clear that reasonableness in multiclaim settlements is measured by looking at the first settled claim in isolation. [191] Citgo did not contend that Travelers' settlement on Wright's behalf was unreasonable in light of the merits of the plaintiffs' claim against Wright and Wright's potential liability. [192]

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[183] *Id. at 764.*

[184] *Id.* (citing *G.A. Stowers Furniture Co. v. Am. Indem. Co., 15 S.W.2d 544* (Tex. Comm'n App. 1929)).

[185] *See id.* (citing *Am. Physicians Ins. Exch. v. Garcia, 876 S.W.2d 842, 848 49 (Tex. 1994)).*

[186] *Id.*

[187] *881 S.W.2d 312 (Tex. 1994).*

[188] *See Travelers, 166 F.3d at 765 68* (citing and quoting *Soriano* repeatedly).

[189] *Id. at 765.*

[190] *Id.*

[191] *Id.* (citing and quoting *Soriano, 881 S.W.2d at 315 16).*

[192] *Id.*

Desperate to escape the reasoning of *Soriano,* Citgo argued that one of the reasons the Texas Supreme Court decided that case as it did was the belief that recognition of the first to settle rule would encourage settlements. [193] This case was different, Citgo argued.

> Citgo argues that when multiple insured parties rather than multiple claimants are involved, the *Soriano* approach will discourage settlement. This, Citgo asserts, is because the partial settlements obtained . . . do not prevent continued litigation against the exposed co insured, with the plaintiff now bankrolled by the proceeds of the settlement. [194]

The court acknowledged that recognition of the first to settle rule in multiple insured cases might encourage some unfortunate strategic behavior by plaintiffs, but noted that accepting Citgo's position would place insurers in an untenable position. [195] Moreover, the court was unconvinced that Citgo's approach would better serve the legitimate goal of encouraging settlement in multiple insured cases. [196] As the court explained in detail:

> Citgo's position in essence means that fulfilling the *Stowers* duty by exhausting policy limits (or reducing them to a level inadequate for further settlement) triggers potential liability to any other insured that is not included in the settlement. Thus . . . an insurer faced with liability of multiple insured parties that exceed its policy limits would face an excess liability threat regardless of whether it attempted to create a comprehensive settlement or acted as Travelers did here. Allowing the insurer to focus only on the claim before it . . . avoids this dilemma.
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> Moreover. . . . Citgo is asking that settlement holdout power be given to each insured party, regardless of whether or not it has actually been sued. The difficulty with this position is readily apparent when one considers the type of situations in which *Stowers* intersects with multiple insured policies to produce the dilemma seen here. A valid *Stowers* demand in the context of multiple insureds requires that the settlement offer be reasonable and the insured party reasonably fear liability over the policy limit. In other words, for the issue to come up at all there usually has to be an objective possibility that the liability of at least *one* of the insureds would ultimately exceed the policy limits.
>
> It is almost certain, then, that no happy compromise will emerge that can settle the case for *all* of the insureds within the policy limits. [197]

Having rejected Citgo's *Stowers* claim, the court turned to Citgo's argument that Travelers had not acted reasonably as a matter of contract law in settling. In short, Citgo claimed that an insurer owes "an independent contractual duty to act reasonably" when performing the obligations imposed by its policy, and that Travelers breached its duty to Citgo when it settled on behalf of Wright. [198] Citgo further argued that Travelers acted unreasonably by failing to give it notice of its investigation into the Friedrich loss, by not investigating the plaintiffs' intentions with respect to Citgo, and by providing a defense to Wright when Citgo later sued it. [199] The court found none of Citgo's theories persuasive.

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[193] *Id.* at 766.

[194] *Id.* at 766 67.

[195] *Id.* at 767.

[196] *Id.*

[197] *Id.* (footnotes omitted).

[198] *Id.* at 768.

[199] *Id.*

Under Texas law, an insurer has no duty to defend until the insured is served with process and relays that to the insurer. [200] At the time of the Wright settlement, Travelers' only duty ran to Wright, because the plaintiffs had not yet named Citgo as a defendant. Once Travelers' settlement on Wright's behalf exhausted the limits of its business auto and umbrella policies, its duties ended, including any duties owed to Citgo as an additional insured. [201] Because Citgo did not allege that the Wright settlement was unreasonable when viewed in isolation, Travelers' decision to settle constituted a reasonable performance of its contractual obligations as a matter of law. [202]

As for the alleged deficiencies in Travelers' notice and investigation, any errors were harmless. Even if notice had been given and the plaintiffs' intentions in the underlying action had been clear, Travelers still would have exhausted its policy limits before Citgo was ever entitled to seek a defense or indemnity. [203] Providing Wright with defense counsel was similarly harmless, given that Citgo had no rights under the subject policies at that point and there was no evidence that the alleged conflict of interest damaged it in any way. [204]

Finally, the Fifth Circuit agreed that the auto exclusion in Wright's CGL policy barred coverage for Citgo under that policy. The court thus affirmed summary judgment for Travelers. [205]

Not all states follow Texas in terms of triggering insurers' duty to defend. In some states, an insurer's duty to defend may attach before a suit is filed. [206] Would *Citgo* have turned out the same way in one of these jurisdictions, where Travelers could not have put Citgo aside because it was owed no defense? In a word, yes. The value of the plaintiffs' claims exceeded the liability limits of all of Wright's applicable insurance policies; Travelers did not have the ability to fully protect all of its insureds. Citgo had ample assets to satisfy a substantial judgment; it could not realistically hide behind Wright's inadequate coverage. As a practical matter, all Citgo could reasonably expect was that it would have its liability reduced by the amount of the Travelers policies. The credit it would have received for the Wright settlement accomplished that.

Schwartz v. State Farm Fire & Casualty Co. [207] reflects a different view, albeit in a different context. In *Schwartz,* Andrew and Amy Schwartz and Elliot and Linda Weinstein were riding in the Schwartzes' limousine when it was hit by an uninsured motorist. Andrew Schwartz and Elliot Weinstein were injured. The Schwartzes had two policies providing uninsured motorist (UM) coverage: a primary USAA policy with $ 500,000 per person and $ 1 million per accident limits, and a $ 2 million State Farm umbrella policy. Both the Schwartzes and the Weinsteins made UM claims. The Weinsteins agreed to arbitrate their claims before an arbitrator named Kolts, while the Schwartzes agreed to arbitration before a different neutral.

USAA paid its $ 500,000 per person policy limit to the Weinsteins. The Weinsteins then received a $ 1,528,040 million arbitration award from Kolts, which State Farm paid. The Schwartzes did not learn of the arbitration until after State Farm paid the award. [208] USAA then paid the remaining $ 500,000 of its policy limits to the Schwartzes.

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[200] *Id.*

[201] *Id.*

[202] *Id.*

[203] *Id.* at 769.

[204] *Id.*

[205] *Id.* at 772.

[206] JERRY & RICHMOND,*supra* note 3, at 843.

[207] *106 Cal. Rptr. 2d 523 (Ct. App. 2001).*

[208] *Id. at 527.*

Upon being notified that USAA's policy limits were fully exhausted, State Farm paid the Schwartzes the last $ 471,960 of its policy limits. [209]

The Schwartzes sued State Farm on a variety of theories, including bad faith. They alleged that before arbitrating the Weinsteins' claim and paying that award, State Farm knew that the Schwartzes' and Weinsteins' combined claims would exceed all available coverage. [210] Nonetheless, State Farm took no steps to reserve a proportionate share of its policy limits in anticipation of paying their claim, nor did it advise them of the Weinsteins' award or its intention to pay it. [211] State Farm countered that its duty to pay the Weinsteins arose first; that it had no basis on which to interplead the funds and that it had no duty to do so in any event; and that it could not be held liable for bad faith because it had not withheld any benefits due, but instead paid its policy limits in full. [212] The trial court granted State Farm summary judgment and the Schwartzes appealed.

The *Schwartz* court reversed and remanded. "The duty of good faith and fair dealing includes the duty not to favor the interest of one of its insureds over the interests of the other," the court began. [213] State Farm clearly had no duty to pay the Schwartzes when it paid the Weinsteins, because the USAA policy was not yet exhausted. It did not follow, however, that State Farm had no duty to treat the Schwartzes fairly. They had made a demand under the State Farm policy by the time State Farm paid the Weinsteins' arbitration award. [214] In short:

> State Farm was placed on notice of the Schwartzes' potential interest in the benefits of their excess policy. The insurer's duty not to favor the interests of one insured over the other necessarily applies to require an excess insurer to consider the interests of *all* of its insureds including its named insured in the limited policy proceeds, whether or not that interest has matured to the point of requiring payment. To conclude otherwise would require insureds to engage in a race to exhaust the available primary insurance, with no right to information from the excess insurer about the amount or status of the competing claim, and with no control over actions of the primary insurer. That would be contrary to the insurer's obligation to "give at least as much consideration to the [insured's] interests as it does to its own." [215]

It seems clear that State Farm should have either interpleaded its policy limits or persuaded the parties to agree on a fair division of them. [216] It is, however, unfair to criticize State Farm for paying the Weinsteins' arbitration award. The arbitrator entered a valid award; State Farm could not refuse to pay it on the basis that it had to save money for the Schwartzes. [217] (Hence the importance of interpleader or a negotiated resolution.) Failing to tell the Schwartzes of the Weinsteins' looming arbitration mattered only if the Schwartzes could have intervened or consolidated their case with the Weinsteins' case. It is also difficult to understand how State Farm could be said to have favored one of its insureds over another in any broader sense. State Farm became adverse to the Weinsteins and the Schwartzes the moment they made their UM claims; that is the nature of all first party insurance and it is clearly true

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[209] *Id.*

[210] *Id.*

[211] *Id.*

[212] *Id.*

[213] *Id. at 529.*

[214] *Id. at 530.*

[215] *Id.* (quoting *Egan v. Mut. of Omaha Ins. Co., 620 P.2d 141 (Cal. 1979)).*

[216] *Id.* at 532 (offering these alternatives).

[217] *But see id.* (faulting State Farm for making this argument on the basis that it could have interpleaded its policy limits or persuaded the Weinsteins and Schwartzes to agree on a division of the policy proceeds).

in the UM context. State Farm was interested in minimizing its payout to both the Weinsteins and the Schwartzes; it favored no one at the expense of anyone else.

One of the Schwartzes' arguments was that State Farm did not advise them that they risked losing their benefits if the Weinsteins arbitrated first. [218] But if the company did that, the Weinsteins could have claimed that it favored the Schwartzes over them. Was State Farm supposed to advise both sets of insureds that under the circumstances they should arbitrate all claims in a single proceeding? No matter how broad an insurer's duty of good faith and fair dealing, it clearly does not include advising insureds on litigation strategy in first party cases.

Long story short, *Schwartz* indicates that an insurer of multiple insureds in a UM or underinsured motorist case with clearly inadequate policy limits has two means of ducking potential bad faith liability: (1) persuading the insureds to agreeably divide the policy limits; or (2) filing an interpleader action. [219] If *Schwartz* has any application to liability insurance, which is uncertain, it exemplifies a minority position. *Schwartz* cannot be read to suggest that a liability insurer with inadequate policy limits should pursue interpleader in a multiple insured case, because interpleader is available only if there are competing *claimants.* That is not the situation in a typical third party multiple insured case.

Insurers may draw bad faith allegations where they insist that any settlement must release all insureds, a plaintiff refuses those terms, and one or more insureds later suffers an excess verdict. Two cases at opposite ends of the spectrum, *Strauss v. Farmers Insurance Exchange* [220] and *Contreras v. U.S. Security Insurance Co.,* [221] highlight the relevant issues.

In *Strauss,* Frank Strauss was injured when his vehicle was struck by a truck driven by Kirk Senseney in the course of his employment by New Wave Pool & Spa. Rodney Fagundes owned New Wave. Farmers insured Fagundes under an automobile policy with liability limits of $ 100,000 per person and $ 300,000 per occurrence. The policy also covered Senseney and New Wave. Senseney had a personal auto policy with $ 50,000 liability limits issued by California Casualty. Strauss's damages exceeded the limits of both policies. When Strauss offered to settle for $ 150,000 (the combined value of the California Casualty and Farmers policies), Farmers declined because the offer did not release either Fagundes or New Wave; Strauss's proposed settlement encompassed only Senseney. Farmers countered by offering its full $ 100,000 per person limit for a release of all three insureds. [222] Strauss refused this offer and a later offer that included a modest contribution from Fagundes. He then settled with California Casualty for $ 50,000, and sued Senseny, Fagundes, and New Wave. He obtained a judgment of $ 563,476 against Senseny and New Wave. Farmers paid Strauss $ 100,000 and a bad faith suit followed. [223] Farmers won summary judgment in the trial court and Strauss appealed.

Strauss argued that Farmers' rejection of his settlement offer constituted bad faith. The appellate court disagreed, stating that an insurer's duty of good faith and fair dealing extends to all of its insureds. [224] Thus, an insurer may, within the boundaries of good faith, reject a settlement offer that does not include a complete release of all of its insureds. [225] In this case, Farmers' acceptance of Strauss's settlement offer would have exhausted its policy and

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[218] *Id.* at 534.

[219] *Id.*

[220] *31 Cal. Rptr. 2d 811 (Ct. App. 1994).*

[221] *927 So. 2d 16 (Fla. Dist. Ct. App. 2006).*

[222] *Strauss, 31 Cal. Rptr. 2d at 813.*

[223] *Id.*

[224] *Id. at 814.*

[225] *Id.*

thus would have left Fagundes and New Wave without coverage. That would have breached Farmers' duty of good faith to them, the *Strauss* court explained. [226] Inasmuch as Farmers "would have acted in bad faith by accepting the offer, it could not be held in bad faith for refusing it." [227]

As a policy matter, the court noted, Strauss's approach placed Farmers "in a 'Catch 22' situation." [228] Accepting Strauss's reasoning, an insurer in Farmers' position would be liable for either agreeing or refusing to settle. Adopting that approach would discourage settlements and frustrate insureds' reasonable expectations. [229] The court in *Strauss* thus found that the trial court correctly granted summary judgment for Farmers.

In *Contreras,* [230] Arnold Dale was driving a car owned by Deana Dessanti when he struck and killed a pedestrian, Flor Osterman. Dale was drunk and speeding when he hit Osterman. Dessanti had an automobile liability policy with U.S. Security Insurance Co. with liability limits of $ 10,000 per person and $ 20,000 per accident. Dale was insured under that policy with respect to Osterman's death because he was driving Dessanti's car with her permission. Dessanti promptly reported the accident to U.S. Security, which assigned the matter to adjuster Marlene Plasencia.

Osterman's daughter, Carmen Contreras, retained a lawyer, Carlos Velasquez, to represent her mother's estate. Velasquez wrote Plasencia to demand that U.S. Security pay its policy limits within fifteen days. Valenscia responded with a letter tendering the policy limits, along with a release form discharging Dale and Dessanti. [231] Velasquez agreed to accept the policy limits in exchange for releasing Dessanti and U.S. Security, but he would not agree to release Dale because of the gravity of his misconduct. [232] U.S. Security then hired a lawyer, Mike Nuzzo, who wrote Velasquez in an effort to achieve a global settlement. Nuzzo included in that letter the following paragraph:

> Please note that U.S. Security agrees that this case is serious, however, U.S. Security must act in good faith to all of its insureds. Therefore you can understand why U.S. Security cannot enter into a release which operates to fully exonerate one insured while not releasing the second insured. [233]

Contreras refused to settle with Dale and sued both Dale and Dessanti for her mother's wrongful death. That suit resulted in a judgment of more than $ 1 million against Dessanti and Dale. Dessanti filed for bankruptcy before the judgment was entered. The trustee in her bankruptcy case assigned her bad faith claim to Contreras. [234] Contreras sued U.S. Security for bad faith and lost on a motion for directed verdict in the trial court. The trial court was persuaded that U.S. Security owed Dessanti and Dale equal duties of good faith, and it could not enter into a settlement that did not release both insureds. [235] As the trial court perceived the situation:

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[226] *Id.*

[227] *Id.*

[228] *Id.*

[229] *Id. at 815.*

[230] *Contreras v. U.S. Sec. Ins. Co., 927 So. 2d 16 (Fla. Dist. Ct. App. 2006).*

[231] *Id. at 18.*

[232] *Id.*

[233] *Id. at 19* (footnote omitted).

[234] *Id.*

[235] *Id. at 19 20.*

> If they [U.S. Security] agree to it and cut Dale loose, the [p]laintiff simply takes an assignment from Dale. If they don't agree to it and leave Dessanti in, the [p]laintiff simply takes an assignment from Dessanti. The [p]laintiff's protected either way and the insurance company loses either way. . . . It creates an automatic bad faith [case]. [236]

Contreras appealed the trial court's ruling.

On appeal, Contreras framed the issue as "whether an insurer acts in bad faith in refusing to pay a reasonable settlement demand in order to obtain a release of one of its two insureds, where the claimant refuses to settle with the other insured." [237] The appellate court agreed that was the issue because, under Florida law, the gravamen of third party bad faith is whether under all the circumstances an insurer failed to settle a claim within policy limits when given a reasonable opportunity to do so. [238]

U.S. Security owed both Dale and Dessanti a duty of good faith and fair dealing. [239] To fulfill its duty to both of them, U.S. Security attempted to obtain releases for both with its policy limits offer. Contreras was unwilling to settle with Dale because of the seriousness of his misconduct. Because U.S. Security could not force Contreras to settle with Dale, it did all it could to avoid excess exposure for him. [240] Having fulfilled its obligation to Dale, U.S. Security was obligated to take the steps necessary to protect Dessanti from exposure to a certain excess judgment. That it would have achieved by accepting Contreras' settlement offer. Under the terms of its policy, U.S. Security's duty to defend and indemnify its insureds would have terminated upon the payment of its policy limits. [241] It would have had no obligations to Dale thereafter. [242] Instead, U.S. Security exposed Dessanti to excess liability by insisting on a global release that it had no chance of obtaining.

The court in *Contreras* was unmoved by the trial court's concern that recognizing a bad faith cause of action on these facts would present insurers with "a Hobson's choice." [243] More particularly:

> The argument that U.S. Security, as a matter of law, could not settle the claim only against Dessanti because it would expose itself to a claim of bad faith by Dale is an illusory one. U.S. Security attempted to settle for both Dessanti and Dale and get a complete release for both of them. A release [for both] was unattainable due to Contreras's adamant refusal to settle with Dale. . . . In any event, the focus in a bad faith case is not on the actions of the claimant, but rather on those of the insurer in fulfilling its obligation to the insured. [244]

Accordingly, the court reversed the trial court's judgment for U.S. Security and remanded the case for a new trial.

B. *Recommendations for Insurers in Multiple Insured Cases*

As *Strauss* and *Contreras* contrast and illustrate, insurers face difficult choices in cases where plaintiffs' claims against multiple insureds exceed all available coverage. What then is an insurer to do in such a case?

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[236] *Id. at 20.*

[237] *Id.*

[238] *Id.*

[239] *Id. at 21.*

[240] *Id.*

[241] *Id.*

[242] *See id.* (citing *Underwriters Guar. Ins. Co. v. Nationwide Mut. Fire Ins. Co., 578 So. 2d 34 (Fla. Dist. Ct. App. 1991)).*

[243] *Id.* at 22.

[244] *Id.*

Assuming for illustrative purposes a case in which two insureds face probable excess liability to a single plaintiff, the insurer should first attempt to negotiate a settlement that releases both insureds. This may be impossible in cases like *Contreras,* where one insured's conduct is particularly disturbing, but the effort should be made regardless.

Second, the insurer should communicate with both insureds concerning their potential liability as soon as practicable. The insurer should inform the insureds of their rights to retain personal counsel and of its willingness to accept guidance and strategic advice from their counsel in resolving the matter. The insurer should inform the insureds that regardless of their desire for personal counsel, it will be retaining counsel for them. The insurer should then appoint separate defense counsel for each insured as soon as possible. The insured should not ask a single lawyer to defend both insureds because of the conflicts of interest a joint representation would pose.

Third, if the insurer cannot negotiate a settlement encompassing both insureds, it should negotiate the best settlement possible on behalf of one. This will typically involve the payment of its per person policy limits in exchange for the insured's full release. The identity of this insured will almost certainly be determined by the plaintiff's lawyer, as in *Contreras.* The insurer has no obligation to do more; it fully satisfies its duty of good faith and fair dealing by indemnifying the insured up to the liability limits of its policy, and by defending her prior to the settlement. Assuming standard policy language, the insurer's obligations to its second insured are extinguished by the exhaustion of its policy limits through settlement on behalf of the first insured.

Occasionally, a plaintiff's lawyer will insist on more than just a monetary settlement, such as the insurer's additional agreement to any subsequent consent judgment or assent to an insured entering into a stipulated judgment, the insurer's agreement not to challenge the reasonableness of a subsequent consent judgment, the insurer's promise not to challenge the assignment of a claim or venue in a subsequent bad faith case, and so on. The insurer has absolutely no obligation to do anything of the sort under its policy language, [245] and it cannot be bound to do so by the duty of good faith and fair dealing. [246] Among other things, these requests offend the insurer's right to consider its own interests equally to those of its insureds. The duty of good faith and fair dealing simply does not require an insurer to subordinate its own interests in these ways. [247]

There are two other steps an insurer may wish to consider as means of protecting itself against potential bad faith claims, neither of which are contractually required or compelled by the implied duty of good faith and fair dealing, and both of which have possible negative consequences. First, in a single injury or single death case in which the insurer has low policy limits, such as $ 10,000/$ 20,000 or $ 25,000/$ 50,000, it may wish to consider offering its full per occurrence or per accident policy limits to settle on behalf of both insureds, notwithstanding the fact that only the per person limit applies. The rationale for this maneuver is that the additional settlement funds will be dwarfed by the cost of defending subsequent bad faith litigation brought by the remaining insured or her assignee. In the unlikely event that the plaintiff accepts the offer, the insurer has fully protected both insureds, albeit gratuitously in the case of the second insured. If the plaintiff rejects the offer, the mere fact of the offer will be evidence of the insurer's extreme good faith in any subsequent bad faith litigation.

Second, an insurer that expends its liability limits to settle on behalf of one insured may wish to provide the remaining insured with a defense even though it has no obligation to do so. This perhaps reduces the chance of a

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[245] *See, e.g.,* ISO Props., Inc., Commercial General Liability Coverage Form (CG 00 01 12 04), at 1, 5 8 (2003) (setting forth insuring agreements and supplementary payments provisions); Ins. Servs. Office, Inc., Personal Auto Policy (PP 00 01 06 98), at 2 (1997) (stating insuring agreement and supplementary payments provision of liability coverage); Wash. Surveying & Rating Bureau, Inc., Homeowners 2 Broad Form Washington (HO 00 02 05 06), at 17, 21 22 (2006) (stating personal liability and additional coverages).

[246] *See* *Uno Restaurants, Inc. v. Boston Kenmore Realty Corp., 805 N.E.2d 957, 964 (Mass. 2004)* (explaining that the "covenant [of good faith and fair dealing] may not . . . be invoked to create rights and duties not otherwise provided for in the existing contractual relationship").

[247] This is true regardless of whether such demands are made in a multiple claimant or multiple insured case. Either way, these terms are unreasonable and an insurer has no duty to consider them.

bad faith claim by the remaining insured and is a relatively inexpensive prophylactic measure. It also avoids any claim tied to an alleged breach of the duty to defend on the theory that a severability clause in the policy obligated the insurer to defend the second insured even after exhausting its policy limits on behalf of the first. [248] The fact that such a claim should not succeed does not mean that it cannot be made, and, if it is made, defeating it will cost the insurer something.

Now for the significant negative aspects of the last two alternatives. First, in either instance the insurer is assuming a duty it would not otherwise owe. Of course, even an assumed duty is actionable in breach. Thus, by assuming a duty an insurer is assuming a risk of liability in the event of a misstep in performing that duty. Second, in either instance the insurer is incurring unnecessary expense. Third, in many states the plaintiffs' bad faith bar is tightly knit. If an insurer offers its per occurrence or per accident limits in one case but not another, or provides a gratuitous defense in one case but not another, the plaintiff's bad faith lawyer in the second case will know that and will attempt to exploit the insurer's extraordinary conduct in the first case. The argument will be that by not offering the per accident or per occurrence limits in the second case as it did in the first, or by not defending in the second case as it did in the first, the insurer acted in bad faith the second time around. This attempt at demonization should fail every case is different, and the fact that an insurer opts to elevate its insured's interests far above its own in one case does not mean that it must always do so, or that by not doing so in the later case it has subordinated the insured's interests to its own but it nonetheless merits insurers' attention.

V. CONCLUSION

Cases in which liability insurers are presented with ***multiple claims*** exceeding their policy limits, or in which multiple insureds are exposed to excess liability, pose extremely thorny problems. In the either instance, an insurer must confront the specter of an excess judgment regardless of what it does. In a multiple claimant case, an insurer at least has the option of interpleader, but that is an incomplete solution, and it is no option at all in third party cases involving multiple insureds. Fortunately, many jurisdictions recognize the first to settle rule in both multiple claimant and multiple insured cases, which affords insurers an opportunity to pry themselves from the horns of these dilemmas. But in many states there is no authority on these issues, leaving well meaning insurers to informed speculation about their options. The good faith dilemmas for insurers posed by combinations of too many claimants, too many insureds, and too little money seem certain to endure.

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[248] *See* ISO Props., Inc., Commercial General Liability Coverage Form (CG 00 01 12 04), at 12 (2003) (providing a standard severability clause).

KARR TUTTLE CAMPBELL

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