The Era of Initiating Settlement Negotiations: What Is a Liability Insurance Company to Do?

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What do the Cases Say? *Whether there is ever such a duty, and if so, when, depends upon some background. What follows is an analysis of research compiled by Dennis J. Wall and published online and in print, in "Litigation and Prevention of Insurer Bad Faith" (Second Edition Shepard's/McGraw-Hill, 2009 Supplement West Publishing Company), particularly Section 3:13.*

Since the generally accepted standard for measuring the settlement conduct of a liability insurer is whether the ordinary and prudent liability insurer without policy limits would settle for a given sum, liability insurers have long been under a duty to make reasonable offers in response to the settlement demands of third parties.[1] A reasonable offer is one based on an objective assessment of liability and damages. It does not include other facts, such as how much reinsurance the liability insurer has for its own protection,[2] whether or in what amount the insured purchased excess insurance[3] unless the demand is in excess of the limits of the primary liability insurer considering whether to offer its own limits,[4] or the

1. *See, e.g.*, Continental Casualty Co v United States Fidelity & Guar Co, 516 F Supp 384, 390 & n7 (ND Cal 1981) (applying California law); Vencill v Continental Casualty Co, 433 F Supp 1371, 1374 & n5, 1375 & nn6 & 7, 1374 & n5, 1375 & nn6 & 7 (SD W Va 1977) (applying West Virginia law). "An insurer may ignore a frivolous offer." Mowry v Badger State Mut Casualty Co, 129 Wis 2d 496, 385 NW2d 171, 185 (1986).

naked desire to "'*try to negotiate some savings on our limits*.'"[5]

Thus, the participants' more-or-less contemporaneous remarks on this comparison may well be admitted in evidence in a later bad faith case. For example, the remarks of three different trial judges at three pretrial conferences in the same case, that the insurance company should settle that case within the company's policy limits, were at issue in *Birth Center v. St. Paul Companies, Inc.*[6] Another remark made by one of the trial judges was also at issue in the later bad faith case. The other remark at issue was that particular trial judge's observation during "a final pretrial conference" in the underlying case *that the insurance company in question was breaching its fiduciary responsibility to its insureds and that there was a clear indication of bad faith.*[7]

The liability insurance company's decision regarding the size and timing of a settlement offer, in response to a particular settlement demand, is a decision which must take into account the honest evaluation of counsel when such advice has been given.[8] Ultimately, the reasonableness of the size of the insurer's offer will also be determined by a comparison with the amount of the verdict rendered or judgment entered against the insured.[9]

Further, many courts, taking what is clearly the modern view, have held that a liability insurer has an affirmative duty to initiate settlement negotiations when:

1. The probability of liability is high;

2. Likely damages are great; or

3. The insured has an excess liability policy.[10]

Also, if there are other financial holdings which could be exposed before or after the entry of an excess judgment, regardless of whether there has been any demand by the injured third party, the insurer must itself begin settlement negotiations.[11]

Kansas law imposes such a duty, it has been held:

> Kansas imposes, under certain circumstances, a duty upon an insurer to initiate settlement negotiations even without an offer to settle

2. *E.g.*, American Fidelity & Casualty Co v Greyhound Corp, 258 F2d 709, 712 (5th Cir 1958) (applying Florida law); Zumwalt v Utilities Ins Co, 360 Mo 362, 228 SW2d 750, 754-55 (1950).

3. Vencill v Continental Casualty Co, 433 F Supp 1371, 1377-78 (SD W Va 1977) (applying West Virginia law); *see* Allstate Indem. Co. v. Oser, 893 So. 2d 675, 677 (Fla. 1st DCA 2005).

4. Continental Casualty Co v United States Fidelity & Guar Co, 516 F Supp 384, 388-89, 391 n8 (ND Cal 1981) (applying California law).

5. Vencill v Continental Casualty Co, 433 F Supp 1371, 1374 (SD W Va 1977)(emphasis by the court).

6. Birth Center v. St. Paul Companies, Inc., 727 A.2d 1144, 1150 (Pa. Super. Ct. 1999) *app. granted & limited*, 560 Pa. 633, 747 A.2d 858 (2000), *& aff'd in pertinent part,* 567 Pa. 386, 787 A.2d 376 (2001), *certain dicta contained in a footnote regarding right to a jury trial disapproved in Mishoe v. Erie Ins. Co*., 573 Pa. 267, 274 n.3, 824 A.2d 1153, 1157 n.3 (2003).

7. Birth Center, 727 A.2d at 1150-51. Finally, the Pennsylvania Superior Court held in the bad faith case that "[t]his evidence was not offered as expert testimony, but [was] only offered as information available to St. Paul when it made its decision not to settle" the underlying case. *Id. at 1167*.

8. *See, e.g.*, Puritan Ins Co v Canadian Universal Ins Co, 775 F2d 76, 77-78, 81 (3d Cir 1985) (Pennsylvania law); State Farm Mut Auto Ins Co v Brewer, 406 F2d 610, 613 (9th Cir 1968) (applying Oregon law); Crabb v National Indem Co, 87 SD 222, 205 NW2d 633, 636-37 (1973).

9. Continental Casualty Co v United States Fidelity & Guar Co, 516 F Supp 384, 391 (ND Cal 1981) (applying California law). The following rulings in the case of U.B. Vehicle Leasing Inc. v. Atlantic Mut. Ins. Co., 2004 WL 503729 *6-*7 (S.D.N.Y. March 12, 2004), will illustrate this rule:

> On the course of the negotiations alone, a reasonable jury could only find that Atlantic acted in good faith. Atlantic moved from $325,000 to $500,000 to $750,000 without any movement from Eakley and Green [the claimants in the underlying liability case], who simply would not negotiate. Surely it was not unreasonable, in light of these undisputed facts, for Atlantic to decline to continue to bid against itself.
>
> Other undisputed facts in the record also show that Atlantic acted reasonably and in good faith. Eakley and Green's demand of $1.6 million was essentially what the jury awarded and was less than the amount of the final judgment; hence, as it turned out, their demand was not much of a compromise. If the final judgment is an accurate measure of what the case was worth, then Eakley and Green should have been willing to compromise for something less to avoid the risk of a low verdict.

being made by the claimant. *Coleman v. Holecek*, 542 F.2d 532, 537 (10th Cir. 1976). Rather than this duty hinging on the existence of a claimant's settlement offer, a Kansas insurer's "duty to settle arises if the carrier would initiate settlement negotiations on its own behalf were its potential liability equal to that of its insured." *Id.*[12]

This duty arises where the liability insurance company would "initiate settlement negotiations" for itself if its own exposure to potential liability was the same as that of its insureds. It is the existence of a *claim* for damages in excess of policy limits that activates this duty, which it was held is a fiduciary duty under Kansas law, and not the existence of an injured claimant's *offer* or *demand* in excess of policy limits.[13] Moreover, Kansas law requires only a *claim*, and does not require a *lawsuit*, for damages in excess of policy limits.[14]

To summarize a canvass of the case law existing on these issues more than two decades ago, the modern view then was that the absence of a third party's settlement demand will not insulate a liability insurer from exposure to liability to pay sums beyond its policy limits as a result of its bad faith and unfair dealing in settlement.[15] To put it another way, the following view has gained increasing numbers of

10. See *Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 3:11 (Second Edition; 2009 Supplement West Publishing Company).* Obversely, where liability is disputed even though damages are great, it has been held that failure to initiate settlement negotiations is not "determinative" of questions of Good Faith and Fair Dealing by the liability insurance company:

> The bottom line is, under the facts of this case, liability is greatly disputed, and settlement negotiations entail strategy regarding the amount to offer and when to make such an offer. This is not a situation in which the insurance company made a de minimus [*sic*] offer. AIU's final offer at mediation was valued at $625,000--a very large sum of money given the fact that there is evidence to support the conclusion that the fall was not caused by the chair and Shin Crest [the policyholder] firmly took that position.
>
> Shin Crest focuses on the fact that Mrs. Blair's injuries were very serious and potential damages could far exceed the policy limits. While this is certainly a factor an insurance company must consider, this factor is not determinative when liability is not clear.

Shin Crest PTE, Ltd. v. AIU Insurance Co., 605 F. Supp. 2d 1234, 1241 (M.D. Fla. 2009). The Court did not seem troubled by considering communications made at a Mediation Conference, which are ordinarily protected from disclosure under Florida law; at least, the Court's opinion does not contain any reference to that consideration. Ultimately, the Federal Court granted the liability insurance company's motion for summary judgment in this Bad Faith case. *Id.* at 1245.

11. *E.g., Goddard v. Farmers Ins. Co., 173 Or. App. 633, 638, 22 P.3d 1224, 1227 (2001)*, *review denied*, 332 Or. 631, 34 P.3d 1178 (2001); *see* City of Hobbs v. Hartford Fire Ins. Co., 162 F.3d 576, 583-84 (10th Cir. 1998)(case of first impression, apparently, under New Mexico law).

In Fulton v. Woodford, 26 Ariz. App. 17, 22, 545 P.2d 979, 984 (Ariz. Ct. App. Div. 1, Dep't B, 1976), the Arizona Court of Appeals wrote a comprehensive treatise on Arizona law on this issue, concluding in pertinent part:

> We therefore hold, in the absence of a demand or request to settle within policy limits or within the limits of the insured's financial ability, plus policy limits, that a conflict of interest would give rise to a duty on behalf of the insurer to give equal consideration to the interest of its insured where there is a high potential of claimant recovery and a high probability that such a recovery will exceed policy limits. It is important to remember that this holding only goes to the issues of when the duty to give equal consideration arises, *not what factors, including failure to initiate settlement, would give rise to a breach of that duty*.

[Emphasis added.]

12. Roberts v. Printup, 422 F.3d 1211, 1215 (10th Cir. 2005).

13. *Id.* at 1215-16.

14. *Id.* at 1216. In the *Roberts* case, the Tenth Circuit reversed a summary judgment for the insurance company, and remanded for further consideration of, among other things, an alleged claim that the liability insurer acted "negligently and/or in bad faith" by allegedly "failing to initiate negotiations for settlement when it was [allegedly] apparent that liability was reasonably clear and damages were in excess of policy limits." *Id.* at 1220.

15. See *Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 3:11 (Second Edition; 2009 Supplement West Publishing Company).*

judicial supporters: The absence of a third party's settlement demand will not insulate a liability insurer from exposure to extracontractual liability, i.e., liability to pay sums beyond its policy limits, as a result of its bad faith and unfair dealing in settlement which can include a failure to initiate settlement negotiations even in the absence of a demand from the injured third party, at least where liability of the insured is clear and damages are great.

That is still the modern view. More than that, it is hard to find any contrary proponent in any judicial decision available today. If not the unanimous view for a very long time, such is the decided majority view and has been the majority view in United States jurisdictions for decades.[16] As a Federal District Court has recently stated, "the duty to accept reasonable settlement offers within policy limits when faced with the significant likelihood of an excess judgment (and potential punitive damage liability for the insured)" is an extension of the duty to defend.[17]

A Florida intermediate appellate court has also explained the view that in at least some situations, a Liability Insurer may have a duty as a matter of law to "initiate settlement negotiations": "Where liability is clear, and injuries so serious that a judgment in excess of the policy limits is likely, an insurer has an affirmative duty to initiate settlement negotiations."[18] This rule of Florida law may have first been pronounced by a Federal Court, nearly forty years ago.[19]

To like effect, where the injured plaintiff does not make a settlement demand within the insured's policy limits:

> The better view is that the insurer has an affirmative duty to explore settlement possibilities.... At most, the absence of a formal request to settle within the policy is merely one factor to be considered in light of the surrounding circumstances, on the issue of good faith.[20]

The burden of proof belongs to the liability insurance company in such a case to show that realistically the injured claimant would not have accepted the settlement offer:

> Any doubt as to the existence of an opportunity to settle within the face amount of the coverage or as to the ability and

16. *E.g.*, Badillo v. Mid Century Insurance Co., 2005 OK 48 ¶¶33-34, 121 P.3d 1080, 1095 ¶¶33-34 (2005)("[A] legally binding, unconditional offer of settlement from the claimant is not a prerequisite to maintaining an action of this type where the insured has been exposed to an excess verdict.... In the circumstances here, insurers could be found to have had an affirmative duty to seize a reasonable opportunity to protect [their] insured from the potential for excess liability and their duty consisted of more than merely playing a passive role in the settlement process."); State Automobile Insurance Co. v. Rowland, 221 Tenn. 421, 432, 427 S.W.2d 30, 34 (1968)("We are asked to hold as a matter of law that an insurance company cannot be held liable for bad faith for failing to settle a case when there is no demand for settlement for an amount of money which is within the limits of coverage afforded by the policy of insurance. We are of the opinion that such is not the law nor should it be."); Alt v. American Family Mutual Insurance Co., 71 Wis. 2d 340, 342, 237 N.W.2d 706, 709 (1976)("We conclude that the trial court erred in holding that a legally binding offer by the claimant is a prerequisite to maintaining an action for bad faith where an insured has been exposed to excess liability.").

17. Rupp v. Transcontinental Ins. Co., 627 F. Supp. 2d 1304, 1324, 2008 WL 4951071 *17 (D. Utah, Nov. 17, 2008)(case involved Utah substantive law).

18. Powell v Prudential Prop & Casualty Ins Co, 584 So 2d 12, 14 (Fla Dist Ct App 1991), review denied, 598 So 2d 77 (Fla 1992). *Accord, Kearney v. Auto-Owners Ins. Co.*, 2009 WL 3363677 *5 (M.D. Fla. October 19, 2009); *Shin Crest PTE, Ltd. v. AIU Insurance Co.*, 605 F. Supp. 2d 1234, 1240-41 (M.D. Fla. 2009); *see Gutierrez v. Yochim*, ___ So. 3d ___, 2009 WL 3787266 *5 (Fla. 2d DCA November 13, 2009)(*citing Powell:* "Under the facts presented, a lack of a formal offer to settle is a factor to be considered in determining whether the insurance company acted in bad faith.").

19. *See* Self v. Allstate Ins. Co., 345 F. Supp. 191, 197 (M.D. Fla. 1972). Under the facts of this case, the Federal Court also held that Allstate acted in Bad Faith because it did not even make a settlement offer in any amount: "This Court has concluded that Allstate is guilty of bad faith in failing to explore the possibility of settling *and in failing to make at least a minimum offer of settlement*." *Id.* [Emphasis added.]

20. Rova Farms Resort, Inc. v. Investors Ins. Co. of Am., 65 N.J. 474, 323 A.2d 495, 505 (1974). West's Keycite display reflects that "overruling" of the *Rova Farms* decision was "recognized" in a Federal case. However, the Federal Court did not refer to *Rova Farms.* Instead, the Federal Court cited to the case in which the Supreme Court of New Jersey adopted a cause of action for Bad Faith in First-Party Cases: *Pickett v. Lloyd's*, 131 N.J. 457, 621 A.2d 445 (1993). The New Jersey Supreme Court's opinion in the Pickett case is carefully and repeatedly written to be in *accord* with *Rova Farms: Id.* at 465, 467, 470, 621 A.2d at 449, 450, 452.

> willingness of the insured to pay any excess required for settlement must be resolved in favor of the insured unless the insurer, by some affirmative evidence, demonstrates that there was not only no realistic possibility of settlement within policy limits, but also that the insured would not have contributed to whatever settlement figure above that sum might have been available.[21]

"Florida law, however, ... treats the unwillingness of a victim to settle as a defense which the insurer must prove."[22] Some jurisdictions follow the Florida view. One explanation of the reason behind this rule of Florida law was given by a Federal Court as follows:

> The recognition of the speculative nature of this kind of testimony is the reason why Florida courts have focused not on the mindset of the injured party but on the conduct of the insurer under the circumstances. That is, rather than trying to conjure the secret intent of the injured party, courts simply ask whether under all the circumstances known to the insurer[,] would reasonable diligence and ordinary care dictate an offer to settle within policy limits. The victim's unwillingness to settle, however, is not completely ignored under Florida law. The unwillingness to settle will become a factor only in the unlikely case where the insurer is able to conclusively prove the unwillingness to settle for the policy limits.[23]

In the recent case of *Barry v. GEICO General Ins. Co.,*[24] this burden was met with evidence that included this testimony of a lawyer as an Expert Witness:

> GEICO presented the testimony of ... a lawyer-expert in insurance bad faith, who opined that GEICO did not act in bad faith. He testified that although GEICO immediately attempted settlement and Stone[, 'the assigned claims adjuster,'] had tried to work with [the widow of the deceased victim,] Capelli, her refusal to communicate with Stone made it clear that she was not intending to settle.... [The lawyer-expert] further stated that the actions of Capelli and her attorney were inconsistent with a willingness to settle. These included Capelli's failure to speak to the insurance company and her attorney's failure to notify the insurance company that he represented Capelli, which indicated to him that this was not a claim which could have been settled.[25]

The result was a jury verdict for the insurance company on the claim of Bad Faith failure to settle. [26] The Florida appellate court explained its affirmance of the Judgment entered by the Trial Court upon the jury verdict:

> Although [the policyholder] Barry is correct that the focus of an insurance bad faith case is not on the motive of the claimant but of the insurer in fulfilling its duty to its insured, *Berges v. Infinity Ins. Co., 896 So. 2d 665, 667 (Fla. 2004)*, that does not mean that all inquiries into prior conduct and motives are irrelevant and prejudicial. In a bad faith case, the insurer has the burden to show that there was no realistic possibility of settlement within the policy limits. *See Powell [v. Prudential Property & Casualty Insurance Co., 584 So. 2d 12, 14 (Fla. 3d DCA 1991)*, *review denied*, 598 So. 2d 77 (Fla. 1992)]. This

21. Rova Farms Resort, Inc. v. Investors Ins. Co. of Am., 65 N.J. 474, 323 A.2d 495, 507 (1974). *Accord*, Powell v. Prudential Prop. & Cas. Ins. Co., 584 So. 2d 12, 14 (Fla. 3d DCA 1991), *review denied*, 598 So. 2d 77 (Fla. 1992).

22. Snowden v. Lumbermens Mut. Cas. Co., 358 F. Supp. 2d 1125, 1128 (N.D. Fla. 2003). *Accord,* Quigley v. Government Employees Ins. Co., 2008 WL 126598 *3 (M.D. Fla. 2008)(in this case, the Federal Court then refused to grant the liability insurance company's motion for a new trial, and denied the liability insurance company's motion for judgment as a matter of law, after a jury found it in Bad Faith under the totality of the circumstances in that case).

23. *Snowden,* 358 F. Supp. 2d at 1129.

24. 938 So. 2d 613 (Fla. 4th DCA 2006).

25. *Id.* at 615-16.

26. *Id.* at 616.

question is decided based upon the totality of the circumstances. *See Berges*. The conduct of Capelli and her attorney would be relevant to the question of whether there was any realistic possibility of settlement. Despite Capelli's testimony at trial that she would have settled the case if GEICO had not made the mistake, her actions and those of her attorney suggested otherwise. The jury could have concluded that the failure of her attorney to notify GEICO of his representation coupled with her refusal to meet with Stone on the settlement, among other incidents, showed that she did not want to settle with GEICO for the policy limits. Thus, GEICO did not inject irrelevant information into the case, and therefore we reject Barry's argument as to the cumulative nature of the errors.[27]

CONCLUSION

The era of initiating settlement negotiations in certain cases in many if not all jurisdictions has been coming for some time. Indeed, it is already here. Whether as an affirmative defense or a part of the claim or cause of action, and whoever may have the burden of proof, in cases involving questions of Good Faith and Fair Dealing it is clear that the absence of a demand to settle from the injured claimant is no longer a valid excuse for not making a settlement offer to protect the insureds of liability insurance companies against claims and lawsuits covered by the liability policy involved.

27. *Id.* at 618.