Fiduciary in Settlement and The American Law Institute's Principles of Liability Insurance Law

Refusing the Shackles of "Reasonable" Summary Judgments

by
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I. AN INTRODUCTION TO FIDUCIARIES IN SETTLEMENT.

A fiduciary acts on behalf of another party with powers delegated to the fiduciary by that other party, or delegated to the fiduciary by third parties on behalf of the other party.[2] In most cases in most courts, liability insurers' duties with respect to reasonable settlement demands and offers is governed by a fiduciary standard of extracontractual or "bad faith" liability, even though in many cases that standard may not be expressly labeled as "fiduciary". The purpose of this article is to explore the long-term results of that standard and to compare them to the short-term and long-term results likely to follow from switching to an alternative standard of simply making "reasonable settlement decisions".

As will be developed in this article, since a "reasonableness" standard unaccompanied by fiducia-

1. The author is grateful for the editorial comments of John DiMugno, Esquire and Professor Jay Feinman of Rutgers Law School. This article which has benefitted from their suggestions is in the end the complete responsibility of the author as to any inaccuracies as well as for any thoughts or observations with which the reader might not agree.

2. *See generally* Tamar Frankel, Fiduciary Law (Oxford U. Press 2011).

ry obligations already prevails in one kind of insurance bad faith or extracontractual liability situation, i.e., in first-party cases, there is a danger inherent in changing to that short-hand standard in third-party or liability insurance cases. Lawyers and judges who may not be familiar with the different criteria employed to assess reasonableness in these two categories of insurance might naturally turn to established first-party bad faith cases. In first-party bad faith cases, a simple reasonableness standard of extracontractual liability has determined the outcomes. This stands in marked contrast to third-party bad faith cases involving verdicts and judgments in excess of the liability insurance policy limits of a policy issued by a liability insurance company. Where the liability insurance company's settlement conduct arguably caused or contributed to causing the excess amount over its policy limits, then the liability insurance company is exposed to extracontractual liability by its alleged conduct for causing the excess amount over its liability policy limit. In such a third-party bad faith case, the excess amount is a sum for which the policyholder would otherwise be responsible and for which there is no counterpart in first-party insurance situations.

Simple reasonableness is the standard governing the extracontractual liability of first-party[3] insurance companies in all or mostly all jurisdictions when claims are presented that first-party insurance companies acted in "bad faith" in negotiating settlement of a particular claim:

> The legal standard governing an insurer's settlement conduct is one of reasonableness. D. Wall, *Litigation and Prevention of Insurer Bad Faith* § 9.03 (1985).[4]

The test of reasonableness employed in first-party bad faith disputes allows insurers to avoid a jury trial by convincing a judge that the insurer had a "fairly or debatable reason" for denying policy benefits. "This is the clear majority view of the question."[5]

In *third*-party[6] bad faith cases, in contrast, most courts turn to a different standard to measure liability insurers' extracontractual liability for their settlement decisions. The liability insurer's duties concerning reasonable settlement offers is evaluated in the context of the fiduciary responsibilities the insurer assumes in exercising its contractual right under the liability policy to control the defense and settlement of claims against the insured. The predominant legal standard governing a liability insurance company's settlement of claims against its policyholders and other insureds is the standard of liability of a fiduciary, although not always articulated as such. The fiduciary standard in third-party bad faith failure to settle cases has important practical consequences: Liability insurers cannot obtain summary judgment and avoid a jury trial on the reasonableness of their decision to refuse to settle.

II. PRACTICAL CONSIDERATIONS.

It should not take a Holmes to know it, although Holmes himself said it, that "[t]he life of the law has not been logic — it has been experience."[7] Insurance companies' fear of jury trials in insurance bad faith cases is legendary. The experience of insurance companies with jury verdicts in bad faith cases makes insurance companies reluctant to try bad faith cases. Their well-known preference is to settle insurance bad faith cases rather than take them to trial.

The insurance companies have another preference, perhaps less publicized, for obtaining summary

3. "First-party insurance" is obtained by an insured to protect itself, herself or himself against its, her or his own losses. Examples include fire insurance, theft coverage, and property insurance. *See also* Jay M. Feinman, Delay, Deny, Defend Ch. 9, "*Hurricane Katrina and Other Insurance Catastrophes*" (Portfolio / Penguin Books 2010); Eugene Anderson, Jordan S. Stanzler & Lorelie S. Masters, Insurance Coverage Litigation (Aspen Law & Business Second Edition and 2013 updates).

4. *Cruz v. American Utd. Ins. Co.,* 580 So. 2d 311, 312 (Fla. 3d DCA 1991).

5. 2 Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 9:3 (Thomson Reuters West Third Edition and 2013 Supplement). In addition, *see* John K. DiMugno, Steven Plitt & Dennis J. Wall, CAT Claims: Insurance Coverage For Natural and Man-Made Disasters § 2:12, "*Claims Handling Practices Issues: The Common Law of Good Faith and Fair Dealing, Acts, and Regulations Generally*" (Thomson Reuters West, November, 2013 Edition).

6. "Third-party insurance" is liability insurance. It involves three parties, hence the name: A policyholder or other insured; a liability insurance company, and an injured claimant. In order to trigger liability insurance coverage, in general terms the injured claimant presents a claim against the insured on the ground that the insured is liable for the injured party's losses.

7. O.W. Holmes, Jr., The Common Law 1 (1881).

judgments. For that reason, insurance companies tend to embrace the "reasonableness" standard of extracontractual liability.

Cognitively, at first glance it may appear that a "reasonableness" standard of extracontractual liability for settlement decisions would be feared by insurance companies. Theoretically, more cases would be decided by a jury because trial judges would seemingly be reluctant to grant summary judgments which eliminate the necessity of a trial and so the need for a jury.

There is a clear need for research and statistics on the question. There is just not enough hard information as distinct from personal experience to bring to bear on it. However, either we all face the same lack of hard data, or there is once again an "information asymmetry" or "asymmetric information"[8] at work in the insurance arena and insurance companies know that reasonableness results in more summary judgments than it does in jury trials in cases of alleged bad faith in settlement.

My own experience over the past 35 years of insurance bad faith litigation is that Courts enter many more summary judgments in first-party bad faith cases than Courts enter in third-party bad faith cases. This is partly explained, no doubt, by the unique requirements in first-party bad faith cases including such things as compliance with conditions precedent including Civil Remedy Notices in various jurisdictions.[9] My own unique experience is also partly explained by the fact that I practice in Florida which has unique requirements even more so than other jurisdictions in first-party bad faith cases, increasing the likelihood that claims of first-party insurance bad faith can result in summary judgments.

Those factors, however, do not explain why in many cases, many trial judges grant summary judgments on *reasonableness* as a matter of *law* in *first-party bad faith cases.*[10]

This article is based, then, on the expectation born of experience that insurance companies prefer a reasonableness standard of extracontractual liability in all cases if possible, in large part because they are more likely to obtain a favorable summary judgment ruling in trial courts applying that standard than in trial courts applying other standards to measure the insurance companies' settlement conduct. In the *liability* insurance context, the standard would involve something like a duty to make reasonable settlement decisions. Such a change in the liability context has been proposed by some.[11]

For example, the American Law Institute's Principles of the Law of Liability Insurance Project offers the following pending proposal for a standard to determine extracontractual or "bad faith" liability in third-party bad faith failure-to-settle cases:

§ 27. The Liability Insurer's Duty to Make Reasonable Settlement Decisions

Unless otherwise stated in a policy issued to a large commercial policyholder:

> (1)When a liability insurer has the authority to settle a claim brought against the insured, or when the authority to settle a claim rests with the insured but the insurer's prior consent is required for any settlement to be payable by the insurer, the insurer has a duty to the insured to

8. "The idea of 'asymmetric information' or 'unbalanced information,' [describes situations] in which one side of an economic exchange has significantly greater information available to it than another side of the same exchange ...." 2 Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 9:5, "*The Question of Bad Faith -- Presence or Absence of Fault,*" n. 17 (Thomson Reuters West Third Edition and 2013 Supplement).

9. *See* 2 *id.,* § 9:21, "*Common Law and Statutory Regulation of Civil Remedy Notice to Act in Good Faith*".

10. *See* 2 *id.,* § 11:17, "*Fairly or Reasonably Debatable Claims*". The recent expansion of a "fairly or reasonably debatable claims defense" in third-party bad faith cases, largely via dicta to date, has been explored elsewhere. It is likely to be an area of even greater commentary in the future, particularly if a reasonableness standard is adopted for measuring a liability insurer's settlement conduct. *E.g.,* 2 *id.,* § 5:16, "Fairly or Reasonably Debatable Claim" Defense in Third-Party Bad Faith Cases; Case Comment, "Bad Faith/Defenses/ Insurance Company Can Seek Declaratory Judgment on Coverage and Not Be in Bad Faith/ *In Dicta, Sixth Circuit Takes Kentucky Law Where It Has Not Gone Before/Philadelphia Indemnity Insurance Co. v. Youth Alive, Inc.*" 35 Ins. Lit. Rptr. 629 (November 18, 2013).

11. Some of these proposals are discussed, but by no means advocated, in Dennis J. Wall, "The Era of Initiating Settlement Negotiations: What is a Liability Insurance Company to Do?" 32 Ins. Lit. Rptr. 1 (Feb. 2, 2010).

make reasonable settlement decisions. The duty to make reasonable settlement decisions is owed only with respect to claims that expose the insured to liability in excess of the policy limits.

(2)A reasonable settlement decision is one that would be made by a reasonable person that bears the sole financial responsibility for the full amount of the potential judgment and the costs of defending the claim.

(3)An insurer's duty to make reasonable settlement decisions includes a duty to accept reasonable settlement demands made by claimants, subject to the following limitation: the amount, if any, that an insurer is obligated by this duty to contribute to a settlement is never greater than policy limits.

(4)An insurer's duty to make reasonable settlement decisions includes the duty to contribute its policy limits to a reasonable settlement of a covered claim if that settlement exceeds those policy limits.[12]

In contrast, third party cases applying the fiduciary standard are complicated and there are too many issues to adjudicate as not being genuine issues of material fact, for trial courts to grant motions for summary judgment in third-party bad faith cases. Cases in which trial judges do not grant motions for summary judgment are on their way to a jury determination of those issues unless those cases are settled before they go before a jury.

And that is what happens in practice. *Third-party bad faith* cases measured by fiduciary standards of settlement do *not* result in summary judgments very often. Far more often, these cases are on track for a jury determination of the issues unless those cases are settled before they go before a jury, and so the experience of these cases is that they are settled rather than tried. Changing from the prevailing fiduciary standard of extracontractual liability to a "reasonableness" standard similar at least in name to the standard followed in the vast majority of first-party bad faith cases, will cause a number of summary judgment motions to be filed on behalf of insurance companies arguing that this is the same "reasonableness" standard by the same name which ought therefore to govern third-party bad faith failure-to-settle cases in the same way.

III. THE LAW BEHIND THE EXPERIENCE OF FIDUCIARY IN SETTLEMENT.

"Bad faith" lawsuits against liability insurance companies after an excess judgment or settlement, and after the liability insurance company failed to settle the claims, are a unique type of litigation. In the vast majority of bad faith failure to settle cases against liability insurers, courts assess the reasonableness of the insurer's settlement decision in light of the insurer's fiduciary duties.[13]

This settled majority view of the thing is also the

12. Council Draft No. 4 (Pending as of this writing), § 27, Principles of the Law of Liability Insurance (© 2013 by the American Law Institute, Council Draft -- not approved, September 20, 2013). In the immediately preceding draft of this provision, Council Draft No. 3 (© 2012 by the American Law Institute -- not approved), the section most closely corresponding to Section 27 which has just been quoted in the text, was numbered 35 and the provision was stated somewhat differently. The ALI Principles Project is still at work, but the draft provision quoted in the text is the pending language as of this writing.

13. *E.g., Reddick v. Allstate New Jersey Ins. Co.,* 2011 WL 6339688 *7 (D.N.J. December 16, 2011)(distinguishing liability insurer's settlement conduct under New Jersey law, from alleged conduct in case at bar), *app. dismissed* (*unreported*) (3d Cir. June 14, 2012); *OK Lumber Co v Providence Wash. Ins. Co*., 759 P.2d 523, 525 (Alaska 1988); *Cotton States Mut. Ins. Co. v. Brightman*, 276 Ga. 683, 685, 580 S.E.2d 519, 521 (2003); *Fireman's Fund Ins. Co. v Continental Ins. Co.*, 308 Md. 315, 519 A.2d 202, 204 (1987); *Farris v. United States Fid. & Guar. Co.*, 284 Or. 453, 587 P.2d 1015, 1019 n. 2 (1978); *Birth Center v. St. Paul Cos.*, 567 Pa. 386, 787 A.2d 376, 388 & n.17 (2001); *Myers v Ambassador Ins. Co.,* 146 Vt. 552, 508 A.2d 689, 691 (1986); *Allied Processors, Inc. v. Western Nat'l Ins. Co.,* 246 Wis. 2d 1034, 629 N.W.2d 329, 333 (Ct. App. 2001), *review denied,* 247 Wis. 2d 1034, 635 N.W.2d 782 (2001); *see, e.g., Santacruz v United Pac Ins. Co.,* 650 F. Supp. 32, 34 (D. Nev. 1986); *Farmers Grp., Inc. v Trimble*, 691 P.2d 1138, 1141–42 (Colo. 1984) (en banc); *Berges v. Infinity Ins. Co.*, 896 So. 2d 665, 668, 669 (Fla. 2004); *Campbell v. State Farm Mut. Auto. Ins. Co.*, 840 P.2d 130, 140 (Utah Ct. App.), cert. denied, 853 P.2d 897 (Utah 1992); Tank v State Farm Fire & Cas. Co., 105 Wash. 2d 381, 715 P.2d 1133, 1136 (1986) (en banc); *cf. State Farm Fire & Cas. Co. v Superior Ct*., 216 Cal. App. 3d 1222, 1226, 265 Cal. Rptr. 372, 374 (Cal. 4th DCA, Div. 1, 1989)("The relationship between an insurer and an insured is *akin* to a fiduciary relationship." [Emphasis added.]).

only proper view of the thing, it is submitted. The fiduciary view is the only view which results both in adjudications of liability insurers' extracontractual liability exposure for the exercise of their settlement duties, and also at the same time remains internally consistent as a legal doctrine. In the absence of stated reasons for applying a lesser standard than a fiduciary standard of extracontractual liability to liability insurance companies in failure-to-settle cases, the fiduciary standard should govern. It will help to understand the reasons behind the courts' application of the fiduciary standard, in addition to helping determine the outcome of actual cases of this kind, to explore the legal principles which are applicable to all fiduciaries.[14]

A. Fiduciary Relation.

A fiduciary relationship fits the liability insurance relationship between the liability or third-party insurance company and its policyholder in ways in which it just does not fit the relationship which a first-party insurance company shares with its policyholder. A *fiduciary* relationship is one in which one party, the fiduciary, exercises delegated power in order to act solely on behalf of another party. It is a relation in which the fiduciary acts in the place and solely for the benefit of the other party.[15] Second, it is a relation in which the fiduciary acts by exercising power delegated to the fiduciary by the other party or by a third party.[16] The fundamental problem which attracts the attention of the courts to fiduciary relationships is the abuse of power by fiduciaries.[17]

Any fiduciary is required to act solely for the benefit of the other party.[18] A fiduciary may not act for its own interests at the expense of the interests of the other party. The judicial shorthand to describe these standards of conduct is to describe their collective features as the fiduciary duty of good faith.[19]

In the case of the liability insurer, its relationship with its insureds has both of these characteristics of a fiduciary relation with regard to the settlement of covered or arguably covered claims against the

14. Fiduciary law has something important in common with the law of insurer bad faith. Courts have expanded the reach of both bodies of law to an increasingly wider range of situations in an increasingly greater number of cases. Unlike the law of insurer bad faith, which has produced and continues to produce many comments from many people, the law governing fiduciary relationships has caused a total of some four books which have treated fiduciary law as a separate area of law worthy of its own separate study. *See, e.g.,* Frankel, Fiduciary Law, 71 Cal. L. Rev. 795, 796 & n.9 (1983), noting the production of three books on the subject as of 1983. Professor Frankel's own recent book on the topic makes a fourth. Insurance practitioners and academics alike would all benefit from reading Professor Frankel's seminal book: Tamar Frankel, Fiduciary Law (Oxford U. Press 2011).

Professor Frankel presents compelling arguments useful to practitioners and potentially enlightening to academics, starting from the proposition that changing societal relationships compel recognition by the courts and legal scholars of a unified body of fiduciary law. She points out that fiduciary law deals with the broader issues of abuse of delegated power and not simply with particular situations in which delegated power may be abused. The situations may vary, but the principles of fiduciary law applicable to all these situations are the same. Frankel, Fiduciary Law, *supra,* at 220-22 (also pointing out that fiduciary rules also adjust based on their application to new situations).

15. *E.g.*, *Donovan v Fitzsimmons,* 90 F.R.D. 583, 586 (N.D. Ill 1981); *Groob v. Keybank*, ¶¶16, 25, 2006-Ohio-1189, 108 Ohio St. 3d 348, 351 ¶ 16, 353 ¶ 25, _843 N.E.2d 1170, 1173 ¶ 16, 1175 ¶ 25 (Ohio 2006); *see, e.g.*, *Pitts v. Jackson Nat'l Life Ins. Co.*, 352 S.C. 319, 330, 574 S.E.2d 502, 507 (S.C. Ct. App. 2002); 1 Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 3:32, "*Legal Bases of Liability in Settlement—First Element: Fiduciary Relation*" (Thomson Reuters West Third Edition and 2013 Supplement).

16. Frankel, Fiduciary Law, 71 Cal L. Rev. 795, 809 (1983). *See, e.g.*, *DiSalvatore v. Aetna Cas. & Sur. Co*, 624 F. Supp. 541, 543, 544 (D.N.J. 1986) (predicting that New Jersey could adopt tort view of malicious first-party extracontractual liability on basis of disparate bargaining powers of first-party insurer vis-a-vis first-party insured; recognizing that a first-party insurer ordinarily is not a fiduciary).

17. *E.g.*, Rochester Radiology Assoc's, P.A. v. Aetna Life Ins. Co., 616 F. Supp. 985, 989 (W.D.N.Y. 1985); *see, e.g.*, Phillips Chem. Co v. Morgan, 440 So. 2d 1292, 1294 (Fla. 3d DCA 1983), review denied sub nom Gamble v. Phillips Chem. Co, 450 So. 2d 486 (Fla. 1984) (employee liable to employer for amounts improperly received in undisclosed compensation, i.e., kickbacks, by virtue of employee's "blatant disregard of the most elemental fiduciary duties owed an employer"); Crabb v. National Indem. Co., 87 S.D. 222, 205 N.W.2d 633, 637 (1973) (liability insurer violated fiduciary duties concerning settlement "by not giving 'equal consideration' to the interests of the insured").

18. *E.g.*, *Burgess Mining & Constr. Corp. v Lees*, 440 So. 2d 321, 334 (Ala. 1983); *Canion v Texas Cycle Supply, Inc.,* 537 S.W.2d 510, 513 (Tex. Civ. App. 1976).

19. *See, e.g.*, *Burgess Mining & Constr. Corp. v Lees*, 440 So. 2d 321, 334 (Ala. 1983); *Georgia Cas. Co. v Mann*, 242 Ky. 447, 46 S.W.2d 777, 780 (1932) ("The agent is always under the duty to exercise the utmost good faith toward his principal."); *Meinhard v Salmon*, 249 N.Y. 458, 164 N.E. 545, 546, 547–48 (1928).

insured. First, it is a relationship in which the fiduciary, the liability insurer, acts in the place and solely for the benefit of the other party, the insured. Most courts have held, in one expression or another which leads to the same result, that a liability insurer must act regarding settlement opportunities as it would act if it had no policy limits applicable to the claim. In doing so, the courts have applied a fiduciary standard of settlement conduct to liability insurers regarding settlement of claims against the insured.[20]

Second, it is a relation in which the liability insurer acts by exercising settlement power delegated to it by someone else, the named insured. The delegated power is the exclusive power to settle claims against all persons and entities insured under the liability policy.[21] The potential for abuse of fiduciary power was and remains obvious. Most courts have accordingly held that the measure of a liability insurer's settlement conduct is whether it meets the standard of care of a reasonable person with respect to the handling of her, his, or its own business. Courts which have measured liability insurers' settlement conduct by this standard have thus both expressly held that the settlement relationship between liability insurer and insured is a fiduciary one, and they have also applied fiduciary standards but without a short-hand label or new "rule".[22]

B. Fiduciary Duties

In broad terms, courts have dealt with abuses of fiduciary relationships by imposing fiduciary duties which are actionable if they are breached. These universally imposed duties include duties of:

1. Loyalty;

2. Prohibition of or restrictions on self-dealing, and

3. Information.[23]

In 1928, then-Chief Judge Cardozo of the New York Court of Appeals summarized the *duty of the finest loyalty* in the following terms, which have since repeated many times by many courts and many commentators:

> Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions.... Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd.[24]

Similarly, the courts have also imposed a "duty of loyalty" from a liability insurer to its insured with respect to settlement negotiations on behalf of the insured. The liability insurer undertakes the exercise of the insured's rights of investigating, evaluating, and negotiating settlement of claims against the insured because of the liability insurance policy. Accordingly, the courts have required not only that an

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20. *E.g.*, *Combined Investigative Serv's v Scottsdale Ins. Co.,* 165 Wis. 2d 262, 477 N.W.2d 82, 85 (1991); *see, e.g.*, *Vencill v Continental Cas. Co.*, 433 F. Supp. 1371, 1377 (S.D. W. Va. 1977) (applying West Virginia law regarding a practical "'trusteeship'" in such a case); *Beck v Farmers Ins. Exch.*, 701 P.2d 795, 799 (Utah 1985).

21. *E.g.*, *Merrett v. Liberty Mut. Ins. Co.,* 2013 WL 1245860 *2 (M.D. Fla. March 27, 2013); *Allstate Ins. Co. v Reserve Ins. Co.*, 116 N.H. 806, 373 A.2d 339, 341 (1976); *see, e.g.*, *Johansen v California State Auto. Ass'n Inter-Ins. Bureau*, 15 Cal. 3d 9, 18, 538 P.2d 744, 750, 123 Cal. Rptr. 288, 294 (1975); *Auto Mut. Indem. Co. v Shaw*, 134 Fla. 815, 184 So. 852, 859 (1938).

22. *E.g.*, *Continental Ins. Co. v Bayless & Roberts, Inc.*, 608 P.2d 281, 287, 293 (Alaska 1980); *Kranzush v Badger State Mut. Cas. Co.*, 103 Wis. 2d 56, 307 N.W.2d 256, 259, 265 (1981); *see Bowers v Camden Fire Ins. Ass'n*, 51 N.J. 62, 237 A.2d 857, 861, 865–66 (1968).

23. *See, e.g., Food Lion v. Capital Cities/ABC, Inc.*, 951 F. Supp. 1224, 1227 (M.D.N.C. 1996), in which the United States District Court discussed the features of a fiduciary "duty of loyalty in the employment context" under both North Carolina and South Carolina law; Tamar Frankel, Fiduciary Law 106-07 (Oxford U. Press 2011). In the liability insurance context in particular, *see* 1 Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 3:33. "*Legal Bases of Liability in Settlement—Second Element: Fiduciary Fault*" (Thomson Reuters West Third Edition and 2013 Supplement).

investigation of the claim actually be made, but that the liability insurer's investigation must also be reasonable and adequate.[25] The liability insurer's *evaluations* will generally be held to be adequate only if the evaluations are objectively based on the factors of both liability and damages to which the claim exposes the insured.[26] Settlement *negotiations* follow, generally, and in most jurisdictions with the liability insurer not only responding to demands but also initiating settlement negotiations, all in ways reasonably calculated to avoid exposing the insured to liability for sums beyond the policy limits.

A second judicially imposed "duty" in the use of fiduciary powers is to require the fiduciary to ordinarily refrain from self-dealing, i.e., requiring the fiduciary not to deal for itself when it acts in the place of the other party.[27]

For this reason, settlement arrangements by liability insurers are almost always held to be unreasonable unless the insured is given a release from the claim.[28]

A third and final "duty" imposed by the courts on the use of fiduciary power, is the fiduciary's duty to keep the other party informed about matters in which the fiduciary is acting on behalf of the other party.[29] Otherwise, the fiduciary "might steal a march on his comrade under cover of the darkness, and then hold the captured ground."[30] This is exactly the same concern which has caused courts to impose a duty on liability insurers to inform their insureds concerning the negotiations of settlement of claims against the insureds.[31]

The insured or other principal in a relationship with a fiduciary does not have to prove actual reliance on the fiduciary's superior expertise in exercising the delegated power.[32] The existence of the fiduciary's superior expertise is one of the main reasons a fiduciary was chosen to act for the other party in the first place.[33] For example, risk management skills are now a clearly recognized responsibility of financial fiduciaries.[34] The courts therefore require the fiduciary to employ the fiduciary's own expertise of a fiduciary in the exercise of powers which are given up by the other party, or which are given up by others for the benefit of the other party.[35] This is the identical standard of extracontractual liability by which the

24. *Meinhard v Salmon,* 249 N.Y. 458, 164 N.E. 545, 546 (1928). *See, e.g., Prudential Ins. Co. of Am. v Sipula*, 776 F.2d 157, 165–66 (7th Cir. 1985) (discussing fiduciary's duty of loyalty in case arising under Illinois law; corporate directors' liability for their alleged "failure to monitor liability creating activities"); In re *Citigroup Inc. Shareholder Derivative Litigation*, 964 A.2d 106, 122 (Del. Ch. 2009) (same issue of corporate directors' liability, under Delaware law); *Sherman v. Ryan*, 392 Ill. App. 3d 712, 728–29, 911 N.E.2d 378, 394–95, 331 Ill. Dec. 557, 573–74 (1st DCA, 3d Div., 2009)(corporate directors' fiduciary duty of loyalty in context of corporate exposure), *app. denied*, 234 Ill. 2d 552, 920 N.E.2d 1081 (2009).

25. *E.g.*, *Rova Farms Resort, Inc. v Investors Ins. Co. of Am.*, 65 N.J. 474, 323 A.2d 495, 503–04 (1974); *Warren v. American Family Mut. Ins. Co.,* 122 Wis. 2d 381, 361 N.W.2d 724, 727 (Wis. Ct. App. 1984).

26. *E.g.*, *Bennett v Conrady,* 180 Kan. 485, 305 P.2d 823, 826 (1957); *United States Fid. & Guar. Co. v. United States Sports Specialty Ass'n,* 270 P.3d 464, 470-71 ¶ 20 (Utah 2012); *see Warren v American Family Mut. Ins. Co.*, 122 Wis. 2d 381, 361 N.W.2d 724, 727 (Wis. Ct. App. 1984).

27. *E.g., Phillips Chem. Co. v. Morgan*, 440 So. 2d 1292, 1294 (Fla.3d DCA 1983), *review denied sub nom Gamble v Phillips Chem. Co.*, 450 So. 2d 486 (Fla. 1984) (employee/agent is prohibited from dealing for own benefit in employer/master's business); *Canion v Texas Cycle Supply, Inc.*, 537 S.W.2d 510, 513 (Tex. Civ. App. 1976) (corporate officers and directors cannot take a corporate business opportunity and make it their own).

28. "The object of settlement is the avoidance of potential liability for higher sums. Under no circumstances can a liability insurer take a release from a third party without also insisting upon that protection for its insured." 1 Dennis J. Wall, Litigation and Prevention of Insurer Bad Faith § 3:20 (Thomson Reuters West Third Edition and 2013 Supplement).

29. *E.g.*, *Meinhard v Salmon*, 249 N.Y. 458, 164 N.E. 545, 547–48 (1928) partners/coadventurers); *Stone v Davis*, 66 Ohio St. 2d 74, 419 N.E.2d 1094, 1098 (Ohio 1981), *cert. denied*, 454 U.S. 1081 (1981) (bank which extends mortgage loan and gives advice to loan customer on mortgage insurance "is under a duty to fairly disclose to the customer the mechanics of procuring such insurance."); *see, e.g.*, *Buccino v Continental Assur. Co.*, 578 F. Supp. 1518, 1521–22 (S.D.N.Y. 1983); *King Mountain Condo. Ass'n v Gundlach*, 425 So. 2d 569, 571–72 (Fla. 4th DCA 1982).

30. *Meinhard v Salmon*, 249 N.Y. 458, 164 N.E. 545, 547 (1928) (Cardozo, CJ).

31. *E.g.*, *Boston Old Colony Ins. Co. v Gutierrez*, 386 So. 2d 783, 785 (Fla. 1980), *cert. denied*, 450 U.S. 922 (1981); *Ranger County Mut. Ins. Co. v Guin*, 704 S.W.2d 813, 820 (Tex. Ct. App. 1985), *aff'd*, 723 S.W.2d 656 (Tex. 1987); *Warren v American Family Mut. Ins. Co.*, 122 Wis. 2d 381, 361 N.W.2d 724, 727 (Wis. Ct. App. 1984).

32. *See, e.g.*, *Burgess Mining & Constr. Corp. v Lees*, 440 So. 2d 321, 334 (Ala. 1983); *Stone v Davis,* 66 Ohio St. 2d 74, 419 N.E.2d 1094, 1097–98, *cert. denied*, 454 U.S. 1081 (1981).

courts measure the settlement conduct of liability insurers. A decision not to settle "must be a realistic one when tested by the necessarily assumed expertise of the company."[36] For this reason, no case has been found in which any insured ever had to prove actual reliance on the settlement conduct of the liability insurer.

In truth, comparison of liability insurers negotiating settlement of claims against their policyholders and other insureds, with other kinds of fiduciaries, is not a comparison of twins. Fiduciary law in general has been plagued with confusion due to unarticulated premises and unexplained analogies between different fiduciaries with differing potentials for abuse of their particular fiduciary powers.[37] The liability insurer is a fiduciary in its own right.

IV. CONCLUSION

Changing the long-established fiduciary standard of liability insurers' extracontractual liability for their settlement conduct to a reasonableness measure, not only changes the law but disproportionately favors underperforming liability insurance companies in the process. The courts' focus should remain where the courts have always placed their focus: on the liability insurer's settlement conduct in particular cases. The standard of extracontractual liability is objective. It requires comparing the particular liability insurer's actual conduct in the given case, with the presumed actions not simply of a hypothetical reasonable liability insurer, but of a liability insurer charged with acting with due diligence in the management of its own affairs, i.e., the settlement of claims against itself, in that same case.

In sum, the law of liability insurer bad faith and unfair dealing in settlement is governed by a fiduciary standard. Fiduciary doctrines not only provide policyholders and other insureds with an established mechanism for remedying abuses of delegated settlement powers. They also provide liability insurers with established rules, which are the best possible protection against the imposition of unwarranted extensions of extracontractual liability by the courts.

33. *See Minnesota Timber Producers Ass'ns v American Mut. Ins. Co.,* 766 F.2d 1261, 1267 (8th Cir. 1985), *cert. denied,* 474 U.S. 1059 (1986) (Minnesota law). *Cf. McAdams v. Massachusetts Mut. Life Ins. Co.*, 391 F.3d 287, 303 (1st Cir. 2004): "Under Massachusetts law, the question of whether one party owes fiduciary duties to another is a question of fact…. Key factors in this fact-specific inquiry include one party's lack of sophistication relative to another on the relevant issues, and whether one party has granted another party a great deal of discretion."

34. Dennis J. Wall, "Risk Management a Recognized Responsibility of Financial Fiduciaries" (February 23, 2009, "Insurance Claims Issues" web log at www.insuranceclaimsissues.typepad.com, Categories: Fiduciary Duty, Risk Management).

35. *See* Tamar Frankel, Fiduciary Law 171 (Oxford U. Press 2011)("Fiduciaries should possess and use the expert skills they purport to possess").

36. *Bowers v Camden Fire Ins. Ass'n*, 51 N.J. 62, 237 A.2d 857, 861 (1968). *Accord Continental Ins. Co. v Bayless & Roberts, Inc.*, 608 P.2d 281, 293 (Alaska 1980); *Kranzush v Badger State Mut. Cas. Co.*, 103 Wis. 2d 56, 307 N.W.2d 256, 259 (1981); *see Continental Cas. Co. v United States Fid. & Guar. Co,* 516 F. Supp. 384, 387, 390 (N.D. Cal 1981) (applying California law to effect that the test is whether a prudent *carrier* without limits would have accepted particular settlement demand or demands).

37. *See King Mountain Condo. Ass'n v Gundlach*, 425 So. 2d 569, 571 (Fla. 4th DCA 1982).