INSURER'S FAILURE TO SETTLE

Fact Pattern:

Rosina Crisci owned an apartment building and purchased $10,000 worth of general liability insurance from Security Insurance Company. One of Mrs. Crisci's tenants, June DiMare, was descending an exterior wooden staircase when it gave way, causing her to fall through the opening to her waist and to hang some fifteen feet above the ground for a period of time. Mrs. DiMare suffered physical injuries from the incident, and afterwards experienced a very severe psychosis requiring hospitalization. She sued Crisci seeking $400,000 in damages. Security Insurance Company provided Crisci with a defense and retained an experienced attorney who handled the case with the aid of investigators and a claims manager. The attorney reported that the case was one in which liability was clear, and that the verdict might be very large if the psychosis could be attributed to the incident at the apartment building.

As the case developed, both sides found expert medical testimony to support their positions. The claims manager noted that if the jury believed plaintiffs expert, the damages could reach $150,000. The attorney essentially agreed, though he set the exposure at $100,000. DiMare eventually offered to settle for the $10,000 policy limits. By this time, however, Security was convinced that it could establish through its expert that the psychosis was not caused by the incident.

As a result, Security would offer no more than $3000 to settle the case. DiMare lowered her offer to $9000, and Crisci was willing to contribute $2500 of her own money to a settlement, but Security rejected that offer. The jury returned a verdict of $100,000 for DiMare and $1000 for her husband. The jury returned a verdict of $100,000 for DiMare and $1000 for her husband. Security then paid its $10,000 policy limits.

Mrs. Crisci became essentially destitute as a result of the judgement and her physical and emotional health declined to the point where she attempted suicide. In the action brought by Crisci, the trial court awarded $91,000 plus interests and costs for the excess of the DiMare judgment over the policy limits, and an additional $25,000 for Crisci's emotional distress damages.

Question:

Must an insurer consider both its own interests and the interests of the insured when deciding whether or not to settle a claim?

Rule

In determining whether an insurer has given consideration to the interests of the insured, the test is whether a prudent insurer without policy limits would have accepted the settlement offer.

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Discussion

California has more laws to protect insurance policyholders than any other state in the country. These laws tell insurers what they must, can and cannot do. The insured party is legally entitled to be treated in "good faith" by his or her insurance company and its representatives at all times. This means an insurer must communicate fully and honestly about the policy and about rights and duties relating to a claim. In 1959, the California Legislature enacted the Unfair Insurance Practices Act ("UIPA"), Cal. Ins. Code § 790, et seq., in order to regulate trade practices in the business of insurance by defining and prohibiting unfair or deceptive acts or practices. In 1972, the Legislature enacted § 790.03(h), which prohibits 16 enumerated "unfair claims settlement practices" by insurers, "if knowingly committed or performed with such frequency as to indicate a general business practice."

In every contract, including insurance policies, there is an implied covenant of good faith and fair dealing that neither party will do anything which will injure the right of the other to receive the benefits of the agreement. It is common knowledge that one of the usual methods by which an insured receives protection under a liability insurance policy is by settlement of claims without litigation. The implied obligation of good faith and fair dealing requires the insurer to settle in an appropriate case although the express terms of the policy do not impose the duty, and in determining whether to settle the insurer must give the interests of the insured at least as much consideration as it gives to its own interests. Additionally, when there is great risk of a recovery beyond the policy limits so that the most reasonable manner of disposing of the claim is a settlement which can be made within those limits, a consideration in good faith of the insured's interest requires the insurer to settle the claim.

In determining whether an insurer has given consideration to the interests of the insured, the test is whether a prudent insurer without policy limits would have accepted the settlement offer. When an insurer receives an offer to settle within the policy limits and rejects it, the insurer will be liable in every case for the amount of any final judgment whether or not within the policy limits.

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