Rolling the Dice:
Insurer's Bad Faith Failure to Settle within Limits

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"Clearly the obligation to accept a good-faith settlement within the policy limits is the law in Connecticut." *Grand Sheet Metal Products Co. v. Protection Mut. Ins. Co*., 34 Conn. Supp. 46, 49 (Conn. Super. Ct. 1977). Indeed, since the inception of this common law rule in 1933, *see Bartlett v. Travelers' Ins. Co.*, 117 Conn. 147 (1933), the insurer's duty to settle within policy limits has been consistently upheld by Connecticut courts. Yet, for such a "clear" rule, a lack of appellate authority leaves policyholders wondering exactly what conduct by the insurer breaches this obligation.

It's easy to see why the insurer's duty to accept a good-faith settlement offer within policy limits has been the law in Connecticut for the past eighty years. Often times, the insurer has sole discretion over the decision to accept a settlement offer within policy limits. With the insurer controlling the defense of the suit, it may be tempting for the insurer to reject the offer in hopes that litigation will lead to a lesser recovery. This is especially true when the settlement offer is at the high end of policy limits.

However, this impermissible gambling strategy exposes the insured's personal assets to an excess verdict. Accordingly, Connecticut courts insist that the insurer consider the interests of the policyholder in addition to their own in determining whether to accept a settlement offer. *See United Services Auto. Ass'n v. Glens Falls Ins. Co.*, 350 F. Supp. 869, 871 (D. Conn. 1972) (applying Connecticut law). The rationale for this rule was clearly set forth in *The Capitol Fuel Co. Inc. v. New York Cas. Co.*, 16 Conn. Supp. 155 (Conn. C.P. 1949), where the court stated "[i]t is obvious that the defendant preferred to be venturesome and speculate with the outcome of the case in the hope that the verdict would save it a substantial sum. Self interest may have dictated and justified such a course, but due care, diligence and its duty to the plaintiff called for an honest effort to avoid the risk of loss to its assured."

Moreover, breach of the insurer's affirmative obligation to settle within limits carries serious consequences for the insurer, including liability for the entire amount of the judgment against the insured, even in excess of policy limits. *See United Services Auto. Ass'n*, 350 F. Supp. at 871. Despite the widespread acknowledgement of such a rule, policyholders in Connecticut can find themselves at a disadvantage when demanding that their insurer effectuate a settlement within limits due to a lack of appellate authority specifically finding an insurer in bad faith by breaching its obligation to accept a good-faith settlement offer within policy limits. In comparison, many states, including New Jersey and California, for example, have well-developed appellate jurisprudence that sheds light on the insurer's duty to settle.

New Jersey Courts Award Damages for Bad Faith

New Jersey's standard for determining whether an insurer has breached its duty to accept a good-faith settlement offer within policy limits is very similar to that in Connecticut; that is, in deciding whether to settle a claim within policy limits, both parties' interests must be given the same consideration. *Bowers v. Camden Fire Ins. Ass'n*, 51 N.J. 62, 71-72 (1968). Furthermore, the insurer must approach a settlement offer as though there is no policy limit, and decide whether or not to accept the settlement offer on that basis. *Id.*

Unlike Connecticut, New Jersey appellate courts have identified specific instances of an insurer's bad faith in failing to settle a claim within policy limits, and have awarded damages above policy limits in light of the insurer's wrongdoing. For example, in *Rova Farms Resort, Inc. v. Investors Ins. Co. of Am.*, 65 N.J. 474 (1974), the Supreme Court of New Jersey addressed coverage issues concerning a CGL policy issued by Investors Insurance Company to Rova Farms Resort. A man sued Rova Farms after he suffered serious injuries from diving into a lake on its property with low water levels. Investors Insurance offered $12,500 in settlement of the action, well below the policy limits of $50,000, but this offer was not accepted and the jury returned a verdict of $225,000 for the injured swimmer. Following the jury verdict and throughout the appeal process, after which the jury verdict was ultimately upheld, Investors Insurance never increased its offer or otherwise attempted to settle the claim against Rova Farms. Rova Farms successfully sued Investors Insurance for bad faith failure to settle, with the trial court awarding Rova Farms the amount of the excess verdict plus interest.

In further explaining its rationale, which was upheld on appeal, the Supreme Court of New Jersey noted that settlement could have been obtained for $75,000, yet Investors Insurance never increased its initial offer of $12,500, despite the unquestionably grave injuries suffered by the swimmer and repeated urges to settle by the trial judge as well as the counsel assigned to defend the action by Investors Insurance. The insurer argued that it had no duty to offer policy limits without a firm demand for that figure, but the Supreme Court disagreed, stating that "the purpose of this type of insurance is to protect the insured from liability within the limits of the contract, and that, therefore, the courts cannot allow the insurer to frustrate that purpose by a selfish decision as to settlement which exposes the insured to a judgment beyond the specific monetary protection which his premium has purchased." Therefore, despite the lack of a firm offer to settle, the Supreme Court held that the insurer acted in bad faith by failing to affirmatively explore settlement options within policy limits, and held the insurer financially accountable for its wrongdoing.

California's Pro-Policyholder Approach

Like Connecticut, California courts have long held that the insurer has a duty to accept a reasonable settlement offer within policy limits. In fact, in *Grand Sheet Metal Products*, 34 Conn. Supp. at 46, the Connecticut Superior Court imported the tort cause of action for bad faith failure to settle from a California Supreme Court case, *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566 (1973).

California courts have gone beyond merely declaring that an insurer is liable for its "bad faith" failure to settle and have elaborated as to exactly what constitutes this bad faith conduct, stating that an insurer is liable if there is a great risk of recovery beyond policy limits and a prudent insurer would have accepted a settlement offer irrespective of the policy limits. *See Comunale v. Traders & Gen. Ins. Co.*, 50 Cal. 2d 654 (1958); *Crisci v. Security Ins. Co. of New Haven, Conn.*, 66 Cal. 2d 425 (1967). In California, the insurer's duty to settle within policy limits extends even to cases where the insurer may dispute coverage; the courts consider only the probability that the insured will be found liable, without regard to any coverage defenses. *See Rappaport-Scott v. Interinsurance Exch. of Auto. Club*, 53 Cal. Rptr. 3d 245 (Cal. Ct. App. 2007).

Furthermore, as in New Jersey, California courts have actually identified instances where the insurer breached this duty, and held the insurer accountable for its failure to settle by awarding the policyholder damages in excess of policy limits. For example, in *Crisci*, the California Supreme Court found that the insurer should have accepted a $9,000 settlement offer under circumstances where the policy limits were $10,000 and the jury ultimately awarded $101,000. The *Crisci* court found that the insurer did not consider the insured's interests equally to its own, and ordered that the insurer pay the entire judgment, despite the fact that it was ten times the policy limits, as a result of its breach.

Even more noteworthy is a recent decision by the Ninth Circuit stating that not only does the insurer have a duty to settle within policy limits, it may be required to do so even where no demand to settle has been made by a third party. In *Du v. Allstate Ins. Co.*, 681 F.3d 1118 (9th Cir. 2012), the Ninth Circuit, applying California law, stated that the duty to settle within policy limits exists whenever the policyholder's liability is reasonably clear, even in absence of a settlement demand. In an amended ruling just four months later, 697 F.3d 753 (9th Cir. 2012), the Ninth Circuit avoided the issue of whether there is a duty to settle absent a settlement demand, finding instead that the issue need not be reached because the insurer initiated timely settlement offers. However, even the amended decision indicates that California jurisprudence suggests that there may be a duty to settle in absence of a settlement demand. Therefore, the holding in *Du* illustrates the Ninth Circuit's position that an insurer should proactively attempt to settle third party claims in order to avoid putting its insured at risk and exposing itself to bad faith damages.

Conclusion

The rule and rationale for holding insurers liable for failure to settle a claim within policy limits has been repeatedly embraced by the Connecticut Supreme Court. However, the Connecticut appellate courts have not yet held an insurer accountable in bad faith for such misconduct. In the meantime, policyholders and their counsel should continue to demand that their insurers do not unnecessarily expose their assets to an excess verdict. In addition, policyholders and courts alike should look to authority from states such as New Jersey and California, which take similar approaches to the duty to settle, for examples of exactly what type of conduct by the insurer may be in bad faith.

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