INSURANCE COMPANY'S DON'T ASK, DON'T TELL (INSURED'S POLICY LIMITS) RULE MAY BE BAD FAITH

By Richard A. Huver

1. **Introduction**

There is a plethora of case law dealing with an insurance company's potential bad faith liability for failing to settle a claim within an insured's policy limits. One area of the case law pertains to the conflict between the insurance company and their insured when it comes to deciding whether a case should be settled or not. Among these cases are, for example, Comunale v. Traders & General Insurance Co. (1958) 50 Cal.2d 654, 659, wherein the California Supreme Court held that an insurer's failure to accept a reasonable settlement offer within the insured's policy limits can be a breach of the covenant of good faith and fair dealing which is implied in all liability insurance contracts. The Comunale court further held that the implied covenant of good faith and fair dealing obligates the insurer to gives the insured's interests at least as much consideration as its own when evaluating the reasonableness of a settlement demand. Id. at 659. As the court in Gruenberg V Aetna Insurance Co. (1973) 9 Cal.3d 566, noted, the basic effect of the implied covenant is that "neither party will do anything which will injure the right of the other to receive the benefits of the agreement."

Thus, when an insurer receives a policy limits demand, certain obligations are triggered. The carrier must adequately investigate and evaluate the claim. Betts v. Allstate Insurance Co. (1984) 154 Cal.App.3d 688. An insurer's failure to obtain a qualified legal opinion regarding potential settlement of the action may lead to a finding of bad faith liability. Davy v. Public National Insurance Co. (1960) 181 Cal.App.2d 387, 396. In addition, the carrier must properly inform the insured of a policy limits demand and, if there is a potential for an excess verdict, advise the insured "so that he might take steps to protect his own interest." Martin v. Hartford Accident & Indemnity Co. (1964) 228 Cal.App.2d 178, 184.

Coupled with this body of case law is the question of whether the insurance company must initiate settlement negotiations as part of its obligation to act in good faith. Several cases have suggested that the insurer owes a duty to initiate settlement discussions in order to act in good faith. See, e.g., Garner v. American Mutual Liability Insurance Co. (1973) 31 Cal.App.3d 843, 848; Brown v. Guarantee Insurance Co. (1957) 155 Cal.App.2d 679, 689. There is contrary authority which had held that a bad faith claim cannot be based solely upon an insurer's failure to initiate settlement negotiations. Merritt v. Reserve Insurance Co. (1973) 34 Cal.App.3d 858, 877.

Now consider these principles from the perspective of the claimant. In order to trigger an insurer's obligation to consider in good faith a reasonable settlement offer, you need to know one important fact: what is the defendant's insurance coverage? In fact, in our every day practice, one of the first questions you usually ask is: does the potential defendant have insurance? And the second question usually is: how much coverage do they have? Obviously, in order to submit a demand on behalf of your client that will exert any pressure on the insurance company to settle the case, you need to know the defendant's policy limits. Without knowing

what the available limits are, negotiating any resolution (in the dark) may be very risky - or possibly worse.

As those of you who have litigated tort cases also know, finding out what the defendant's insurance policy limits are is often difficult, if not impossible, without first filing a lawsuit and serving the Judicial Council 4.0 series interrogatories. Most insurance companies refuse to disclose their insured's policy limits without a discovery request. Such a pre-litigation request is usually met with the response, "we do not disclose our insured's policy limits without their permission."[1] While this is an accurate reflection of California law, how many insurance companies actually ask their insured for permission? A recent appellate case just might change those percentages.

2. Boicourt v. Amex Assurance Company

In Boicourt v. Amex Assurance Company (2000) 93 Cal.Rptr.2d 763, the plaintiff was a 15-year old passenger in a vehicle being driven by his 16-year old friend. The car overturned and plaintiff suffered catastrophic injuries. Before filing suit, the plaintiff's attorney sent a written request to the adverse adjuster, requesting disclosure of the defendant's policy limits. One month later, the adjuster responded to plaintiff's counsel advising that the company had a "policy not to disclose the amount of the policy limits." Id. at 764.

Plaintiff's counsel made no further request. Four months later, he filed suit. On the same date, plaintiff's counsel again wrote to the adjuster stating that his client would have been willing to settle his case but for the carrier's action in refusing to disclose the policy limits. Five months after suit was filed, Amex offered its policy limits of $100,000. The offer was rejected by plaintiff. No demand was ever submitted by the plaintiff. At trial, the parties stipulated to a judgment of $2.985 million against the adverse driver. Id.

Amex paid its policy limits of $100,000. The adverse driver then assigned his rights against Amex to the plaintiff in exchange for a covenant not to execute on the judgment. The plaintiff filed a bad faith action against Amex, alleging that the carrier's refusal to disclose its policy limits short of litigation was unreasonable, and that this unreasonable conduct resulted in an excess verdict against its insured. Id. at 765.

The trial court dismissed the case on the carrier's summary judgment motion, apparently based upon the belief that because plaintiff had never served a formal settlement offer, there was no conflict between the interests of the insurance company and that of its insured and thus, no bad faith. Id. at 764.

The appellate court reversed. In opening its discussion, the court noted,

> No less an authority on insurance law than John Alan Appleman declared 40 years ago that a liability insurer "is playing with fire"

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[1] Of course, California law requires that the insurer obtain their insured's permission before disclosing the limits. Insurance Code §791.13(a).

> when it refuses to disclose policy limits. Such a refusal "cuts off the possibility of receiving an offer within the policy limits" by the company's "refusal to open the door to reasonable negotiations."

Id. at 763.

The court then defined the issue as follows:

> The present case involves another insurer who, at least allegedly, played with fire in refusing to disclose policy limits....the insurer's sin here was a blanket refusal to contact the insured to see if he wanted the policy limits disclosed....The insurer's refusal to disclose (or in California, the refusal to give the insured the option of disclosing) policy limits may have foreclosed a possible settlement of the underlying claim within those limits.

Id. at 764.

The court then looked outside California, where numerous jurisdictions have held that bad faith liability may be predicated on the refusal of an insurer to disclose their insured's policy limits. For example, in Powell v. Prudential Property & Casualty (Fla.App. 199) 584 So.2d 12, 14, the Florida court held that "liability may be predicated on a refusal to disclose policy limits." In Pennsylvania, the court has held that:

> An insurance company would violate its obligation to an insured to act in good faith if it did not reveal the existence of low policy limits when such a revelation would serve to protect the insured from a judgment far above the policy limits.

Szarmack v. Welch (1972) 220 Pa.Super. 407, 289 A.2d 149, 153. Courts in Illinois, South Dakota, and New York have espoused similar holdings.

But why would the non-disclosure of low policy limits be in bad faith? After all, the carrier did ultimately offer the $100,000 policy limits without any contrary demand. The court reflected on a nearly 50 year old Supreme Court decision, which held "that 'knowledge of low policy limits' could benefit defendants (that is, policyholders) because that knowledge would tend 'to discourage a seriously injured plaintiff from holding out for a settlement commensurate with the extent of the injuries.'" Superior Insurance Co. v. Superior Court (1951) 37 Cal.2d 749, 755.

In order to reach its holding, the Boicourt court also distinguished dicta in a case mentioned above, Merritt v. Reserve Insurance Co. (1973) 34 Cal.App.3d 858. In Merritt, the court had stated that a bad faith claim could "only" arise if a formal settlement offer within policy limits was rejected, and the plaintiff received an excess judgment. Boicourt distinguished Merritt by noting that there had never been any overtures of settlement at any time before a judgment had been entered, and that the Merritt court was not faced with an insurer who had rejected an overture or "suggestion" for settlement. Boicourt v. Amex Insurance Co., supra, 93

Cal.Rptr.2d at 766-767. The court thus reasoned that Merritt's use of the word "only" was not just dicta, but "improvident." Id. at 767.

In fact, Boicourt held that a conflict of interest could indeed exist between the insurer and the insured, even without a formal demand.

> First, there is the conflict between the insured's peace of mind and the elephantine lethargy endemic to many large organizations, certain including many insurance companies. To wit, an insurance company must obtain the insured's written permission before policy limits may be disclosed. [Citations omitted] If an insurer has a blanket rule against ever contacting its insureds regarding requests for disclosure, there is a marginal savings in time and paperwork on any given file. . . . to the degree that such a rule may have the real world effect of "foreclosing" the possibility of a quick settlement within policy limits, the insured has lost out.
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> Second, there is the negotiating advantage an insurer gains for itself (and not for its insured) when it forces a claimant to make any settlement offer either (a) without benefit of knowledge of policy limits or (b) only after incurring the expense of filing litigation and sending out some initial discovery.

Id. at 767-768.

The court went on to catalog the realities of the plaintiff tort lawyer's practice when it noted:

> One might think that the expense of filing a complaint and sending out a simple interrogatory would mean that the choice to which the insurer puts the claimant is a negligible one. But that is not exactly so. Not every plaintiffs' lawyer is able to take every case to trial. The economics of plaintiffs' work places a premium on being able to settle cases as early in the process as possible.

Id. at 768.

While early resolution of cases works to the advantage of the insured, often being "spared the extra months" of "stomach-churning uncertainty characteristic of all litigation," the court noted that insurers have a conflicting interest. Namely, insurers:

> . . . usually benefit from the additional time value of any money eventually used to settle, as well as the additional economic pressure that the passage of time puts on the plaintiff's attorney who, if paid by contingency, must work for free until settlement or collectible judgment. Insurers also know that plaintiffs have the ability to bring only so many of their cases to trial, and know that,

> over the course of a large number of claims, putting plaintiffs' lawyers as a group to the choice of filing suit before they can find out the policy limits may "finesse" . . . a few settlements below policy limits.

Id.

The court was careful to note that its opinion was not holding "as a matter of law" that a carrier is necessarily liable if it refuses to disclose the insured's policy limits. The court also noted that questions of liability and damages must be addressed in order to determine whether the carriers' conduct was unreasonable or not. Finally, the opinion did not address the issue of whether a carrier must pro-actively attempt to settle a case, avoiding the above-mentioned contradictory holdings of Garner, Brown and Merritt. Id. at 769.

3. **Conclusion**.

Consideration of the Boicourt opinion in your every day practice could prove to be beneficial. Much like the plaintiff there, an early written request for a defendant's policy limits (followed, perhaps with confirmation that the insured's permission was actually requested and withheld) may allow you to have an insurer thinking about possible bad faith liability down the road. Besides, it's not in your client's best interests for you to incur substantial costs on a case if the defendant only has minimal insurance limits. It will be interesting to see how the Boicourt case ultimately turns out following the reversal of the summary judgment ruling in favor of the insurer.