BAD FAITH UPDATE:

MASSACHUSETTS

Massachusetts Supreme Judicial Court determines underlying judgment is measure of damages for excess insurer's bad faith.

Rhodes v. AIG Domestic Claims, Inc., 461 MA 486 (2012).

Mass. Gen. Laws. ch. 176D, § 3 (a)-(f) defines what actions by an insurer qualify as unfair or deceptive acts or practices punishable under the Consumer Protection Act. With regard to remedies for such violations, the Massachusetts Supreme Judicial Court (SJC) recently held that the appropriate measure of damages for post-verdict bad faith conduct by an excess insurer was the underlying tort judgment.

The Rhodes v. AIG case presented a "perfect storm" of facts regarding a motor vehicle liability accident. On the afternoon of January 9, 2002, a tree service company was grinding tree stumps near Route 109 in Medway. The company retained a policeman to stop one lane of traffic to protect the safety of its tree service truck and employee. The police officer stopped a Toyota driven by Marcia Rhodes, then age 46 years old. As she was stopped in the roadway, an 18 wheel tractor trailer truck approached from the rear, struck the back of Ms. Rhodes' vehicle, and pushed it off the road and down an embankment. Ms. Rhodes suffered traumatic spinal cord injury and broken ribs and was rendered a paraplegic.

At the time of the accident, the owner of the truck had a $2 million primary automobile liability insurance and a $50 million excess umbrella policy with another insurer.

The truck operator vehicle claimed that prior to the accident he was traveling down a gradual hill at the speed limit of 35 mph when a car "popped out" at an intersecting street and caused him to apply his brake "vigorously." (He was cited criminally for Operating Negligently to Endanger.)

After completing an investigation into the facts and circumstances of the accident, a claims adjuster for the primary insured concluded that the insured was clearly liable for Ms. Rhodes' injuries and that the value of the case was between $5 and $10 million.

Initially, plaintiff's counsel submitted an oral demand for $18.5 million and later a written demand for $16.5 million. The primary insurer tendered the $2 million policy limits to the excess insurer because it determined that the probability of a plaintiff's verdict was 100% and there was no possibility of a comparative negligence reduction. The excess insurer then evaluated the case, and after conducting some jury verdict and settlement research, determined that the average settlement for comparable automobile liability cases

was over $6.6 million and the average verdict was over $9.6 million.

Ms. Rhodes filed suit, discovery propounded and a trial was scheduled for September 7. 2004. The excess insurer and the plaintiff agreed to mediate the case in August. The excess insurer had authority to make an offer of up to $3.75 million to settle the case ($2.0 million from the primary insurer and $1.75 million in new money). At the mediation, the plaintiff made an initial demand of $15.5 million and the excess insurer offered $2.75 million. The plaintiff reduced its demand to $15 million and the excess insurer increased their offer to $3.5 million (but did not extend the full amount of its authority).

At the trial, the defendant stipulated to liability and the case was tried on the issue of damages only. At the close of the evidence, the excess insurer made a $6 million settlement offer. The jury returned a verdict awarding damages of $9.412 million, which, together with statutory interest, totalled $11.3 million.

There were then post-verdict settlement negotiations. The excess insurer filed a notice of appeal and also offered $7 million in settlement. Ultimately, the underlying tort case was settled for $8.965 million, but the plaintiffs preserved their right to file a Chapter 93A/176D bad faith claim against the excess insurer.

At a subsequent bench trial concerning the bad faith claims, each side presented expert testimony concerning the promptness and reasonableness of the settlement offers made by the insureds. However, the trial judge found that the excess insurer willfully and knowingly breached its duty to make a prompt settlement offer once liability was reasonably clear, but also concluded that the failure to do so did not cause the plaintiff to suffer any actual damages because there was no evidence that the plaintiff would have accepted even a timely reasonable settlement offer. With respect to the alleged post-verdict bad faith conduct, the trial judge determined that the excess insurer willfully and knowingly violated its duty to effectuate a prompt and fair settlement and concluded that the $7 million post-judgment settlement offer was "not only unreasonable, but insulting." In connection with the post-judgment claim, however, the trial court did not use the $11.3 million judgment as a measure of damages. Instead, the court concluded that the damages were the loss of use (or loss of interest) between the date the case should have settled (January 2005) and the date it actually settled (June 2005), and this resulted in an award of $448,250.

On appeal, the Massachusetts Appeals Court was asked to determine whether the trial judge properly concluded that the unfair and deceptive conduct before trial did not cause the plaintiff injury, and whether the proper measure of damages for the post-judgment conduct claim should be a multiple of lost interest or the amount of the tort judgment. On the first issue, the Appeals Court, in a divided decision, reversed the conclusion of the trial court and held that a causal link between the unfair settlement practices and injury to the plaintiff was sufficiently established.

On the second issue, the court held that the appropriate measure of damages for the pre-verdict violation should be the loss of use of the funds between the time the excess insurer should have offered settlement and the time it actually did offer settlement. The Appeals Court also awarded loss of use damages for the post-judgment violation. The SJC then accepted the matter for further appellate review.

The SJC held that a plaintiff need not prove that they would have accepted a prompt, reasonable settlement offer, had the insurer made such an offer, to prevail on a bad faith case under Chapter 93A/176D. Instead, the court concluded that the plaintiff need only prove that they suffered a loss, or an adverse consequence, due to the insurer's failure to make a timely, reasonable offer. The plaintiff need not speculate about what they would have done with a hypothetical offer that the insurer might have, but in fact, did not, make on a timely basis.

The SJC also held that the appropriate measure of damages to be awarded to the plaintiff for the post-verdict bad faith conduct was the amount of the underlying tort judgment (or the $11.3 million judgment). The court noted that the Chapter 93A, Section 9(3) contains the following directive concerning multiple damages: "for the purposes of this chapter, the amount of actual damages to be multiplied by the court shall be the amount of the judgment on all claims arising out of the same and underlying transaction or occurrence. . . ." The excess insurer argued that the underlying tort judgment of $11.3 million did not arise out of the same and underlying transaction or occurrence as the Chapter 93A claim. The excess insurer also argued that multiplying the amount of the judgment in the tort action created a "grossly excessive" award of punitive damages. The SJC rejected these arguments and held that the plaintiff was entitled to $22 million (or two times the judgment) for the Chapter 93A claim alone. In so doing, the Court noted that this figure was "an enormous sum" and that the legislature may wish to consider expanding the range of permissible punitive damages to be awarded for knowing or willful violations of the statute to include more than single but less than double damages.

The Rhodes case may have significant implications for bad faith claims in Massachusetts. The decision resulted in a significant bad faith award for the plaintiff. However, the case presented a unique set of factual circumstances and the measure of damages will be the underlying tort judgment only if: (a) there is a willful or knowing violation of Chapter 93A, or a bad faith denial of relief made with knowledge or reason to know such denial violated Chapter 93A; and (b) there is an underlying tort judgment.

Several unanswered questions remain for future review by the SJC, such as precisely what test should apply to determine if liability is "reasonably clear," and whether it is appropriate to punish an insurance company for exercising its right to a non-frivolous appeal in a post-verdict context.

Rhode Island

Rhode Island Supreme Court concludes that Asermely applies to multiple claimants.

Demarco v. Travelers Insurance Company, 26 A.3d 585, (R.I. 2011).

The Rhode Island Supreme Court in DeMarco v. Travelers Insurance Company, 26 A.3d 585 (R.I. 2011) held that the principles set forth in Asermely v. Allstate Ins. Co., 728 A.2d 461 (R.I. 1999) apply in the context of multiple claimants. The Asermely standard mandates that an "insurer has fiduciary duty to engage in timely and meaningful settlement negotiations on behalf of its insured and will assume risk of judgment in amount exceeding policy limits, even in absence of bad faith, unless insured was unwilling to accept third-party's settlement offer." DeMarco v. Travelers Ins. Co., 26 A.3d 585 (R.I. 2011). Prior to DeMarco, it was unclear whether the Asermely rule could or should apply in circumstances where there were two or more claimants.

In DeMarco, two passengers in a vehicle owned by a Virginia transportation corporation were seriously injured when the car veered off the road and struck several utility poles. The passengers were Wayne DeMarco and Paul Woscyna. At the time of the accident, Virginia Transportation had an automobile insurance policy with a liability limit of $1 million.

Following the accident, the passengers, who were each seriously injured and incurred several hundred thousand dollars in medical expenses, separately demanded that the liability insurer pay them the applicable $1 million policy limit. For approximately three years, the insurer attempted to adjust the claims without success. The claimants then filed suit against the insureds and, on the eve of the first trial, the insurer offered its policy limit to be shared by both claimants. The carrier took no position on how any of the money should be divided and, instead, argued that the claimants should decide among themselves how the policy limits would be allocated. All along, the carrier asserted that Asermely could not apply to a multiple claimant situation and that it could not be held liable in excess of the policy limits.

Approximately one month before the first case against Virginia Transportation went to trial, the insurer commenced an interpleader action and filed a motion requesting it be allowed to deposit the policy limits into the registry of the court. The court ruled that the interpleader was not warranted at that time because the insurer had "a considerable interest in the outcome" of the underlying personal injury litigation and the motion seeking leave to deposit the policy proceeds into the registry of the court was denied.

Thereafter, the parties participated in a mediation and the insurer offered $550,000.00 to DeMarco and $450,000.00 to Woscyna. The mediation was unsuccessful.

Shortly before the trial commenced, the insurer again offered DeMarco

$550,000.00 and indicated that the insured was willing to contribute $150,000.00 of its own funds.

At trial, the insurer stipulated to liability and it did not present any witnesses with respect to the damage issues. The jury returned a verdict in favor of DeMarco in the amount of $2,053,795.00 which, together with interest, resulted in a total judgment of $2,801,939.07.

After the trial, the insurer entered into partial settlements with the claimants and paid $450,000.00 to Woscyna and $550,000.00 to DeMarco. DeMarco reserved his rights to assert any and all claims against the insurer and the insureds assigned DeMarco any and all claims that they had against the insurer and defense counsel.

DeMarco then commenced an action against the insurer and defense counsel seeking to hold the insurer liable for the entire $2.8 million judgment pursuant to the Asermely doctrine. He claimed the insurer was liable for the entire amount of the judgment and that, pursuant to Rhode Island General Laws, §27-7-2.2 (the so-called "rejected settlement offer statute"), the insurer was required to pay all interest due on the judgment in the personal injury action (including both pre- and post-judgment interest). He also alleged bad faith and breach of fiduciary duty. The parties then filed cross-motions for summary judgment and the trial judge entered partial summary judgment in favor of DeMarco and against the insurer. She held that the Asermely rule applied to cases in which multiple claimants sought limited insurance policies. The trial judge held that the insurer was liable for the entire amount of the judgment. She concluded that the insurer failed to present any evidence showing that plaintiff's offer to settle for $1 million was not reasonable or that it did not have adequate time to investigate the offer. She also held that the insurer was liable under §27-7-2.2 for both pre- and post-judgment interest. The Court noted that the insurer did not attempt to negotiate any of the claims until days before the trial.

On appeal, the Rhode Island Supreme Court held that "the principles underlying this Court's opinion in Asermely apply to cases involving multiple claimants that exceed the policy limits; but it is further our opinion that it is incumbent upon us to explicate the applicability of Asermely principle's in multiple claimant context." According to the DeMarco Court, under the Asermely doctrine "even if bad faith cannot be shown, an insurer will still be exposed to potential liability for the amount of a judgment that exceeds policy limits, unless the insurer can show that the insured was unwilling to accept a plaintiff's settlement offer."

In its decision, the Court acknowledged that it had not previously indicated whether the Asermely rule is one of strict liability or a negligence standard. However, it observed that in previous decisions it had referred to a "reasonableness standard" articulated in Asermely.

It is noteworthy that the DeMarco Court cited favorably to the First Circuit's opinion in Peckham v. Continental

Casualty Insurance Co., 895 F.2d 830 (1st Cir. 1990), wherein the Federal Court discussed the "thorny problem" of excess limits in cases. In Peckham, the Federal Court noted that

> the insurer's goal should be to try to affect settlement of all or some of the multiple claims so as to relieve its insured of so much of his potential liability as is reasonably possible, considering the paucity of the policy limits. So long as it acts in good faith, the insurer is not held to standards of omniscience or perfection, it has leeway to use, and should consistently employee, its honest business the judgment. The carrier, in fine, "will not be held to prophesy."

The DeMarco case also cited favorably to the Fifth Circuit decision entitled, Liberty Mutual Insurance Co. v. Davis, 412 F.2nd 475 (Fifth Cir 1969). The Court there held that it is a question for the jury to decide and the jury should be instructed to consider:

> bearing in mind the existence of multiple claims and the insured's exposure to heavy damages, did the insurer act in good faith in managing the proceeds in a manner reasonably calculated to protect the insured by minimizing his total liability? In many cases, efforts to achieve an overall agreement, even though entailing a refusal to settle immediately with one or more parties, will accord with the insurer's duty. In other cases, use of the whole fund to cancel out a single claim will best serve to minimize the defendant's liability.

The Rhode Island Supreme Court suggested that the standards set forth in Peckham and Davis constitute the most sensible and jurisprudentially sound way to approach the complex issues involved in multiple claimant cases where the available proceeds are decidedly finite. The Court held that insurers have an affirmative duty to engage in timely and meaningful settlement negotiations and to make and consider offers of settlement consistent with an insurer's fiduciary duty to protect its insured from excess liability.

In DeMarco, the Court remanded the case for further proceedings to determine whether the insurer acted reasonably. This issue could not properly be resolved on Motions for Summary Judgment. The Court suggested that the issue of whether the insurer should be liable for the excess judgment should be tried to the jury along with the bad faith claim. (One of the issues to be considered on remand was whether the insured was willing to have the policy limits paid to the plaintiff).

The Court also considered the applicability of the rejected settlement offer statute, §27-7-2.2. Again, the insurer claimed that it would be unfair and illogical to apply this statute to cases involving multiple claimants and insufficient policy limits. The Court essentially avoided this issue by holding that there was only one plaintiff at issue

in the case and that the statute applied. The Court suggested that the rejected settlement offer statute may apply to the extent that the insurer is "found liable" on remand. (It is not clear why the Court indicated that the insurer's liability for pre and post judgment interest under the statute would be "applied on remand to the extent that the insurer is found liable." After all, the statute appears to impose strict liability for interest in circumstances where an offer within the policy limits is rejected by an insurer).

In summary, it appears that the Rhode Island Supreme Court in DeMarco adopted a "reasonableness" standard for the evaluation of the conduct of insurers in attempting to settle cases involving multiple claimants. The Court held that:

> the insurer has a fiduciary duty to engage in timely and meaningful settlement negotiations and a purposeful attempt to bring about settlement of as many claims as possible, such that the insurer will thereby relieve its insured of as much of the insured's potential liability as is reasonably possible given the policy limits in the surrounding circumstances. . . . The insurer must exercise its best professional judgment throughout the process, always keeping in mind the best interest of the insured and the necessity of minimizing its insured's possible eventual direct liability. To show that an insurer has violated its fiduciary duty, the claimant need not demonstrate that the insurer acted in bad faith but only that the insurer did not act reasonably and in its insured's best interests in light of the surrounding circumstances.

The DeMarco Court suggested that the question of whether an insurer has met its duty in a multiple claimant's case will involve a "comprehensive factual analysis" that takes into account the circumstances of the case including the number of claimants, the relevant extent of the damages suffered by each claimant, the time at which the extent of those damages were made known to the insurer, the amount of the claimants' settlement demands, the wishes of the insured, the timing and nature of the insurer's attempts at negotiating a settlement, the perceived likelihood of litigation being commenced by a particular claimant, and the relevant willingness of the various claimants to settle. This inquiry necessarily involves an inquiry with respect to the facts and circumstances of the claim and the insurer's conduct. As a result, it is unlikely that the question of whether an insurer should be liable for an excess judgment can be resolved by motion. Instead, this fact specific inquiry will result in a jury trial.

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