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INSURER REQUIRED TO PAY $22 MM FOR UNTIMELY SETTLEMENT OFFER

What You Need to Know

An insurer that fails to settle a case in which liability is reasonably clear may be liable for up to three times the amount of any judgment that enters against its insured, rather than a multiple of the amount attributable to the loss of use of the judgment proceeds.

The Massachusetts Supreme Judicial Court has held that an insurer that knowingly and unreasonably delayed offering to settle a claim against its insured, thereby forcing the matter trial, must pay $22 MM to the claimant based on the underlying award against its insured. The decision, Rhodes v. AIG Domestic Claims, Inc., significantly increases an insurer's potential exposure where liability against its insured has become reasonably clear and insurer does not settle pre-trial.

In Massachusetts, an insurer has a statutory duty to make prompt, fair, and equitable settlement of claims in which liability has become reasonably clear. If an insurer fails to do so, the affected party - including a third-party that has asserted a claim against the insured - may bring an action against the insurer for bad-faith settlement practices and recover damages. If the insurer's violation of its statutory duty is found to be willful or knowing, then the aggrieved party is entitled to recover at least double, and up to treble, damages. Until Rhodes was decided, it generally was believed that the damages in such a situation was limited to the value of the loss of use of the settlement funds between the time a settlement offer should have been made and the time a reasonable settlement offer was made.

In Rhodes, a woman was paralyzed when her automobile was struck by a truck. She, her husband, and her daughter brought a tort action against, among others, the company for which the truck driver was performing services at the time of the accident. The company's primary and excess insurers quickly determined that liability against its insured was likely, and estimated that the value of the case was between $5 MM and $10 MM. Nevertheless, the excess carrier waited four months, until the eve of trial, before making an offer of $3.5 MM. The plaintiffs rejected the offer, and went to trial. The jury awarded the plaintiffs $9.5 MM, which with pre-trial interest resulted in a judgment in the amount of approximately $11 MM.

The excess insurer, through its insured, appealed the verdict, arguing the verdict was excessive. The plaintiffs responded with a suit against the excess insurer under M.G.L. c. 93A, alleging the insurer had failed to effectuate a prompt and equitable settlement of the plaintiffs' underlying tort claims. Several months after the jury verdict, the excess carrier settled the plaintiffs' underlying tort claims for $8.965 MM. However, as part of the settlement, the plaintiffs retained the right to pursue their bad faith settlement practices claim.

After a trial on the bad faith settlement practices claim, the trial judge determined that the excess insurer had violated its duty to effectuate a prompt, fair, and equitable settlement (a) when it waited four months before offering $3.5 MM pre-trial, and (b) when it waited five months before settling the claim for $8.965 MM post-trial. For damages, the trial judge awarded $448,250, which the judge determined was the lost interest on the $8.965 MM settlement during the five month delay. The trial judge then doubled that award because he found the excess insurer's bad faith settlement practices to have been willful or knowing.

The Supreme Judicial Court reversed trial judge's ruling on the damages award. Relying on a 1989 amendment to the Massachusetts Unfair Business Practices Act, the Court determined that where an insurer willfully or knowingly fails to effectuate a prompt, fair, and equitable settlement, thereby forcing the claim to trial, the damages to be multiplied is the amount of the underlying judgment. Thus, because the underlying judgment was approximately $11 MM, the excess insurer was liable to the plaintiffs in the sum of approximately $22 MM.

In a footnote, the Court limited its holding to situations in which the violation was willful or knowing, and a judgment has entered against the insured. The Court distinguished situations in which the violation was not willful or knowing, or where the underlying case settles prior to trial. In those instances, the traditional loss of use damages calculation continues to apply.

Rhodes is important because it exposes insurers to the risk of significant damages if the insurer allows a claim against its insured to go to trial. If the insured tries the case and is found liable, and the insurer later is found to have willfully or knowingly failed to effectuate a prompt, fair, and equitable settlement, then the insurer, separate and apart from having to pay the underlying judgment on behalf of its insured, will be directly liable for two or three times the underlying judgment. If, however, the insurer settles the case before trial, then the insurer will be responsible only for the loss of use of the settlement amount. This rule will encourage insurers to settle claims prior to the entry of judgment. Somewhat perversely, Rhodes also may encourage plaintiffs with strong claims, who believe that the insurer has willfully or knowingly failed to effectuate a prompt, fair, and equitable settlement, to refuse to settle prior to trial – even if the insurer subsequently has made a fair and equitable settlement offer. A plaintiff in such a situation may conclude that the possibility of recovering, in additional to its damages against the defendant, a multiple of those damages against the defendant's insurer more than justifies the risk of trial.

*This client advisory was written by **Kurt B. Fliegauf**. If you wish to inquire further about our real estate or litigation/insurance practices, please contact Michael or your attorney at **Conn Kavanaugh Rosenthal Peisch & Ford, LLP**.*

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