

# EXTRA! EXTRA!

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# FLORIDA DISTRICT COURT HOLDS THAT INSURER DID NOT ACT IN BAD FAITH BY AGREEING TO SETTLEMENT THAT EXHAUSTED POLICY LIMITS, BUT ONLY RELEASED ONE OF TWO INSUREDS

A Florida District Court recently held that a CGL insurer did not act in bad faith by agreeing to a settlement that exhausted its policy limits, but only released claims against one of its two insureds. See *Shin Crest PTE, Ltd. v. AIU Ins. Co.*, 2009 WL 804671 (M.D. Fla. March 26, 2009). In 2001, Doreen Blair was rendered a paraplegic when she fell off an outdoor chair manufactured by Shin Crest and sold by Sam's Club. Blair filed suit against Sam's Club, alleging that the chair was defective, but did not name Shin Crest in the suit. Sam's Club sought defense and indemnification from AIU Insurance Company ("AIU"), which had issued to Shin Crest a CGL policy with a \$2 million policy limit, naming Sam's Club as an additional insured. AIU retained an attorney to represent Sam's Club, and assigned an adjuster to assist in the investigation and defense of the suit.

The judge ordered Blair and Sam's Club to participate in mediation, and requested that Shin Crest attend the mediation even though it was not a party. Sam's Club attorneys felt that they had very strong liability defenses, but recognized the potential that a sympathetic jury would nonetheless find in Blair's favor and award her between \$4 and \$8 million. Accordingly, they assigned a settlement value on the case between \$1 and \$1.5 million. Similarly, AIU's adjuster determined that \$1 million was a fair settlement value. Shin Crest's position was always that the chair was not defective, but it nonetheless agreed with Sam's Club's settlement valuation. At no point did Shin Crest ever offer to contribute to settlement.

At the mediation, Blair's counsel expressed that his litigation strategy was to get as much money as possible from Sam's Club and then sue Shin Crest. Blair's initial demand was \$20 million for the release of Sam's Club only, and the AIU adjuster (who had settlement authority up to \$1 million) responded with an annuity settlement offer valued

at approximately \$625,000 for the release of both Sam's Club and Shin Crest. Blair's counsel later discussed possibly decreasing her demand to \$5 or \$6 million, but would not agree to release both Sam's Club and Shin Crest. The AIU adjuster never offered its \$1 million authority and instead ended the mediation.

Blair and Sam's Club continued to negotiate after the mediation, with Blair's counsel ultimately offering to settle the suit for AIU's remaining policy limit, but only for the release of Sam's Club. AIU considered the settlement offer, and noted that if it rejected the offer and the case went to trial resulting in a judgment in excess of the policy limit, it could potentially be liable for the entire judgment. AIU again asked whether Blair would consider a settlement for the release of both Sam's Club and Shin Crest, but Blair was adamant that she would not consider such a settlement. Therefore, AIU determined that this was the best settlement offer it could get, and accepted the offer.

A month after the settlement between Blair and Sam's Club was finalized, Blair filed suit against Shin Crest. Because its policy limits had been exhausted, AIU would not provide Shin Crest with a defense. More than two years later, Shin Crest and Blair entered into a stipulated judgment for \$12 million, but Blair agreed not to attempt to collect the judgment if Shin Crest pursued a bad faith claim against AIU.

Shin Crest then filed suit, alleging that AIU acted in bad faith by failing to offer its policy limits at the mediation for the release of both Sam's Club and Shin Crest. The Florida District Court recognized the nuances of settlement negotiations and noted that liability was reasonably contested, there was valid evidence in support of no liability, and Shin Crest's position was always that the chair was not defective. Therefore, the court held that, because AIU followed a reasonable and rational settlement negotiation strategy, it did not act in bad faith by failing to offer its policy limits at the mediation.

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## DECISION WORTH NOTING...



In *Shawnee Lodging, Inc. v. Certain Underwriters at Lloyd's*, London, 2009 WL 921131 (10th Cir. April 7, 2009), a hotel owner submitted a claim to its property insurer for hail damage to its roof. Although the insurer forwarded a number of payments pursuant to the policy, the parties could not agree on the ultimate value of the claim. The insured filed suit for breach of contract and bad faith, and the district court granted summary judgment in favor of the insurer.

On appeal, the insured argued that the district court erred in granting summary judgment because there were genuine issues of material fact in dispute. Specifically, the insured argued that the district court had, in effect, evaluated the credibility of its expert. The Tenth Circuit held that the district court had not erred in granting summary judgment on either the breach of contract or the bad faith claims. The court ruled that the district court had *not* assessed the credibility of the insured's expert witness, but rather had concluded, correctly, that his conclusory deposition testimony was insufficient to raise a genuine issue of material fact.

# TENTH CIRCUIT RULES THAT DISTRICT COURT'S LEGAL ERROR IN APPLYING STRICTER STANDARD FOR FIRST-PARTY BAD FAITH TO THIRD-PARTY BAD FAITH CLAIMS CONSTITUTED REVERSIBLE ERROR

On March 19, 2009, the United States Court of Appeals for the Tenth Circuit held that the district court committed reversible error by applying Colorado's more stringent first-party bad faith standard, rather than its third-party standard, to a third-party claim. In *Trout v. Nationwide Mut. Ins. Co.*, 2009 WL 721551 (10th Cir. March 19, 2009), Stephanie Trout was a passenger in the back seat of a car that hit a tree. Trout suffered severe injuries, and filed suit against the driver and the owner of the car, alleging that the driver had consumed alcohol prior to the accident. Trout also alleged that the daughter of the car's owner had given permission to the driver despite knowing that he had consumed alcohol. Trout's attorney had a conference call with the driver's attorneys, and inquired as to whether the driver's insurance company, Nationwide, "is going to offer the \$100,000 you say is the limit of coverage for him for this accident." The next day, one of the driver's attorneys wrote to the Nationwide claim representative, passing along the inquiry concerning policy limits, but also stating that Trout's attorney had made it clear in the telephone conference that his inquiry did not constitute a demand to settle the case.

Eventually, Nationwide offered its \$100,000 policy limits, subject to six conditions: 1) a release of Trout's claims against the driver, the owner's daughter, and their respective parents; 2) Trout's agreement to defend, hold harmless, and indemnify the driver, the owner's daughter, and their respective parents in any action brought by a third party; 3) Trout's warranty regarding the assignment of her claim; 4) a dismissal of the lawsuit with prejudice; 5) a waiver of subrogation rights by Trout's medical insurance provider; and 6) a waiver of subrogation by any underinsured motorist insurance carrier. Trout rejected Nationwide's offer, stating that she did not accept the "improperly conditioned" offer and would pursue the matter against the driver because of Nationwide's "bad faith posture."

At trial, Trout was awarded \$640,000 in damages, plus pre- and post-judgment interest and costs. A restitution judgment was also entered in a criminal action against the driver in the amount of \$170,138, to be paid to Trout's medical provider. After entry of judgment, Nationwide tendered its policy limits of \$100,000. The driver did not have sufficient assets to satisfy the remainder of the judgment, and assigned all rights to pursue Nationwide to Trout.

Trout filed suit against Nationwide, arguing that Nationwide's offer to pay its policy limits subject to the six conditions was wrongful and made in bad faith. Trout argued that, at the time Nationwide made the conditional offer, it knew that: 1) Trout's injuries were catastrophic; 2) any verdict in Trout's favor would likely

be in excess of the \$100,000 limit; and 3) the driver faced personal liability for the amount of any judgment in excess of the policy limits. Nationwide moved for summary judgment, arguing that it never had the opportunity to settle for the policy limits because Trout never actually made a policy limits demand. The district court granted Nationwide's motion. In so doing, the district court applied Colorado's first-party bad faith standard, which requires a showing that the insurer "acted both unreasonably and with knowledge or reckless disregard of its unreasonableness." The court went on to find that, even if Trout had raised an issue of fact as to whether Nationwide acted unreasonably by imposing conditions on its offer of the policy limit, she had wholly failed to present argument or evidence as to whether

See *Tenth Circuit* on page 4

## DECISION WORTH NOTING...



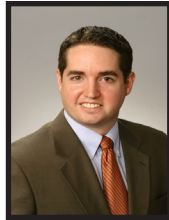
A federal district court refused to grant summary judgment in favor of an automobile insurer relating to its termination of no-fault medical benefits. In *Johnson v. Auto-Owners Ins. Co.*, 2009 WL 762109 (D. N.D. March 19, 2009), the insureds (a mother and her adult daughter) were involved in three separate automobile accidents over the course of several months. After each respective accident, the insureds submitted claims seeking no-fault benefits for medical treatment of their accident-related injuries. The insurer initially accepted their claims and paid the benefits, including chiropractic treatment and massage therapy. Eventually, the insurer arranged for the insureds to undergo independent medical exams ("IMEs") to determine whether further treatment was warranted. Following the IMEs, the insurer ultimately discontinued benefits for both insureds.

The insureds filed suit, alleging that the insurer had wrongfully failed to pay reasonable no-fault benefits, and that the insurer had acted in bad faith. The insurer moved for summary judgment, contending that it had produced an "inordinate amount" of evidence showing that the insureds' claims for continued medical treatment were properly handled and lawfully denied. The court denied the insurer's motion, ruling that the necessity of medical services and the reasonableness of the charges for those services are questions of fact, and that even the "inordinate amount" of evidence presented by the insurer could not satisfy the necessary factual inquiry. In addition, the court declined to award the insurer summary judgment on the issue of whether it had acted in bad faith. Again, the court held that the issue of whether the insurer acted in bad faith was a question of fact, and a number of fact issues remained. The court explained that, although the insurer is permitted to require IMEs under North Dakota law, the court was not aware of any North Dakota decisions holding that an insurer's termination of benefits after an IME is reasonable in all circumstances as a matter of law.

Nationwide did so either knowingly or recklessly.

On appeal, the court held that the matter involved not a first-party claim for bad faith, but a third-party claim for bad faith, because the allegation was that Nationwide acted in bad faith towards a third party rather than towards its policy insured. In the third party context, the court explained, an insured's claim is based on general principles of negligence and requires proof that the insurer acted "unreasonably under the circumstances." The second element of a first-party bad faith claim, that the insurer did so either knowingly or with reckless disregard, is not an element of

a third-party bad faith claim. Because the district court relied, at least in part, on this distinct element of a first-party bad faith claim in granting summary judgment in favor of Nationwide, the Tenth Circuit held that the error was not harmless. Accordingly, the judgment was reversed and remanded.



Prepared by Thomas G. Drennan, an associate in our Chicago office.

## DECISION WORTH NOTING...



The United States Court of Appeals for the Seventh Circuit recently addressed bad faith allegations in connection with the refusal to pay benefits under several life insurance policies. *Malone v. Reliastar Life Ins. Co.*, 558 F.3d 683 (7th Cir. March 12, 2009), involved three life insurance policies obtained by the same individual from two separate insurance companies. That individual apparently disappeared in 1998, and his beneficiaries filed claims for death benefits in 2003. The insurers initially refused to pay the benefits due to the requirement that, under Indiana law, seven years must pass before the common law presumption of death takes effect. When the beneficiaries submitted renewed death claims in 2005, the insurers again refused to pay benefits, citing evidence they had obtained suggesting that the individual was either still alive or had not died at the time of his disappearance. In the ensuing lawsuit, the beneficiaries asserted that the insurers had breached the insurance contract by failing to pay death benefits, and had acted in bad faith by making unfounded refusals to pay benefits and deceiving the beneficiaries. The trial court granted summary judgment for the insurers on the bad faith claims. The breach of contract claims proceeded to trial, after which the jury returned a verdict for the defendants.

On appeal, the court held that errors in both the jury instructions and the special verdict form prejudiced the trial's outcome. Those mistakes, the court ruled, had prevented the jury from considering one of the two ways in which the beneficiaries could prove death: namely, the common law presumption of death. Therefore, the court reversed and remanded on the breach of contract issue.

With respect to the bad faith claims, and the corresponding requests for punitive damages, the court upheld the granting of summary judgment for the insurers. The court explained that an insurer's duty of good faith extends beyond decisions to pay or deny benefits. However, evidence of bad faith in refusing to pay benefits or causing unfounded delays must demonstrate "a state of mind reflecting dishonest purpose, moral obliquity, furtive design, or ill will." After reviewing the record, the court concluded that the matter was nothing more than a good faith dispute over coverage, and that the beneficiaries had not demonstrated evidence of bad faith on the part of the insurers sufficient to survive summary judgment.

Shin Crest also alleged that AIU acted in bad faith by exhausting its policy limits in a settlement for Sam's Club, leaving Shin Crest exposed to liability against Blair. Initially, the court recognized that AIU was put in an impossible situation, because if it did not settle for the policy limits, it would face a bad faith suit by Sam's Club for failure to settle, but by offering the policy limits to settle the claim against Sam's Club only, it opened itself up to a bad faith claim by Shin Crest, who was left with no insurance. Accordingly, the court held that AIU did not act in bad faith, because it reasonably attempted

to procure a settlement on behalf of both Sam's Club and Shin Crest, and only agreed to the settlement releasing Sam's Club after it was clear that there was no reasonable possibility to settle globally.



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