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**Responding to Policy Limits Demands – Best Practices**

## I. Introduction

For Plaintiffs' attorneys, a policy limit demand can prove a very valuable tool. Oftentimes, they feel like a setup – and they might be. After all, depending upon the circumstances, the failure to accept a policy limit demand may leave an insurance carrier with bad faith exposure, if a judgment in excess of policy limits is later rendered against the insured. The policy limit demand presents various issues and complications, and one thing is certain – the demand should not be ignored.

This presentation provides information concerning the issues faced by insurers and defense counsel when presented with a policy limits demand by the plaintiff. The presentation will cover the timing of the demand and address the differences in responding when in a time-limit jurisdiction versus a jurisdiction that does not have specific time limits. The presentation will cover the duty to settle generally and provide an overview of the requirements of reasonableness and promptness, and whether coverage issues may influence a decision to reject a policy limits demand. The presentation will delve into the factors that should be considered in responding to a policy limits demand, and finally provide some best practices and tips for practitioners to use when responding to such demands.

## II. The Duty to Settle

Each insurance company contains an implied covenant of good faith and fair dealing, which obligates the insurer to accept reasonable settlement demands in order to avoid exposing an insured to liability in excess of available insurance. When this duty is breached, bad faith exposure may exist. Key to this analysis, though, is the fact that the settlement offer is reasonable.

### a. Reasonable settlement

Whether a duty to accept a demand exists depends upon the reasonableness of the settlement demand. Although courts have articulated it in slightly different fashions, most often a reasonable settlement demand will be one where an ordinarily prudent insurer would accept the demand, considering the terms of the policy and the insured's potential exposure to a judgment in excess of policy limits. *E.g.*, *OneBeacon Ins. Co. v. T. Wade Welch & Assoc.*, 841 F.3d 669 (5th Cir. 2016) (insurers liable for failing to settle within policy limits if the claim is within the scope of coverage, demand was within policy limits, and the demand was such that an ordinarily prudent insurer would accept); *Dorroh*

*v. Deerbrook Ins. Co.*, 223 F. Supp. 3d 1081 (E.D. Cal. 2016) (an insurer cannot be held liable for bad faith when a reasonable offer within policy limits was not made).

If a policy limit demand will resolve less than all claims pending against the insured, the insurer may not be liable for negligence or bad faith. *E.g.*, *Linthicum v. Mendakota Ins. Co.*, 687 Fed. Appx. 854 (11th Cir. 2017). When multiple insureds are at issue, the insurer may be held liable for bad faith if it 1) fails to make its best efforts to settle claims against al the insureds or 2) fails to settle claims against one, after it knows it cannot settle claims against both.

Therefore, in evaluating whether the demand is reasonable, the insurer must consider the insured – but depending on the jurisdiction, can also consider its own interests.

**b. Consideration of coverage defenses**

A conflict arises in every construction defect matter, whereby some (if not a majority) of the damages sought by plaintiffs will not be recoverable under the terms of the policy. The issue that arises in the context of a policy limit demand is whether an insurance carrier can consider its own coverage defenses and potential liability, when considering the reasonableness of the plaintiff's offer. Some courts have held that an insurer might not breach its obligations of good faith when there are questions as to whether policy exclusions will apply to bar the claim. *Redding v. ProSight Specialty Mgmt Co., Inc.*, 90 F. Supp. 3d 1109 (D. Mon. 2015).

In some jurisdictions, insurers may not be able to consider policy defenses without the threat of being exposed to bad faith. *See Johansen v. California State Auto Assn. Inter-Ins. Bureau*, 15 Cal. 3d 9, 538 P.2d 744 (Cal. 1975) (noting that "in deciding whether or not to compromise the claim, the insurer must conduct itself as though it alone were liable for the entire amount of the judgment.") In these instances, the inherent conflict between settling and paying for noncovered damages, and delaying payment but risk being exposed to bad faith, may be resolved by an insurer reserving its rights to seek reimbursement for the noncovered portions of a settlement. First, the insurer must timely reserve that right via express communication with the insured, must notify the insured of its intent to accept the demand, and must offer the insured an opportunity to assume its own defense in the event that the insured does not agree with the insurer's proposed course of action.

In sum, the factors that an adjuster should consider are:

1. The total potential recovery from the plaintiff
2. The potential liability of the insured
3. The potential liability of other defendants
4. The probability that the ultimate judgement could exceed the amount of the offer
    1) Which takes into account:
        1) The strengths and weaknesses of the witnesses and experts on both sides
        2) Results from similar litigation
        3) Jury pool
        4) Jurisdiction
        5) Plaintiff's attorney vs. defense attorney
            1) Reputation
            2) Experience
            3) Capabilities

4) Trial experience

5. Coverage under the policy
    1) Which takes into account the jurisdiction, in order to determine if it is best to investigate the potential for coverage, or pay the settlement immediately while reserving the right to recover noncovered amounts
6. Whether an adverse verdict could cause financial harm to the insured and/or cause harm to their business reputation
7. The insured's desire to settle or try the case

## III. <u>Time to Respond</u>

In many states, the amount of time insurers has to respond to a plaintiff's policy limit demand is determined by the time limit the plaintiff chooses to allow. If the plaintiff provides a reasonable amount of time for the insurer to respond, then the insurer's failure to respond within that time limit can be considered an act of bad faith.

### a. Jurisdictional examples

In some jurisdictions, the plaintiff can set its own time limit for the insurer to respond to its policy limit demand. *Graciano v. Mercury Gen. Corp.*, 231 Cal. App. 4th 414, 434, 179 Cal. Rptr. 3d 717, 732-33 (2014). However, to serve as a basis for wrongful refusal to settle, that proposed time limit must be reasonable. *Id.* (citing *Martin v. Hartford Acc. & Indem. Co*. (1964) 228 Cal.App.2d 178, 185 [39 Cal.Rptr. 342]). Circumstances, as we know, weigh heavily on whether a time limit will be deemed "reasonable." For example, under certain circumstances, even a limit of one week does not preclude a finding of bad faith on the part of the insurer. *Id*. (citing *Critz v. Farmers Ins. Grp.*, 230 Cal. App. 2d 788, 798 (1964)). Or, if both damages and the insured's liability are certain, and damages are obviously going to exceed the policy limits, a court will be more willing to accept a shorter time limit as reasonable. *See Jenkins v. All Nation Ins. Co.*, No. 86-4124, 1988 U.S. App. LEXIS 21665, at *7-8 (9th Cir. June 29, 1988); See *Grumbling v. Medallion Ins. Co*., 392 F. Supp. 717, 721 (D. Ore. 1975).

Other jurisdictions have established minimum amounts of time in which an insurer has to respond. *See, e.g.*, Ga. Code Ann. § 9-11-67.1(a)(1) (requiring that the time period within which any type of settlement offer must be accepted cannot be less than 30 days from receipt of the offer or policy limit demand); Mo. Code Ann. § 537.058 (a time limited demand for personal injury, bodily injury, or wrongful death claims, must be no less than 90 days).

## IV. Failure to respond

The insurer's conduct and the jurisdiction where the suit is pending is key to determining whether an insurer will be liable for an excess judgment under all circumstances, or rather, only when bad faith is shown. In Florida, for example, although negligence is a relevant factor, an excess judgment will not be held against the insurer absent bad faith. *See, e.g.*, *Stalley v. Allstate Ins. Co.*, 183 F. Supp. 3d 1209 (M.D. Fla. 2016). In Georgia, on the other hand, insurers may be held liable for excess judgments in the absence of bad faith, so long as the refusal to settle was both wrongful and the proximate cause of the excess judgment. *See, e.g.*, *Camacho v. Nationwide Mut. Ins. Co.*, 188 F. Supp. 3d 1331 (N.D. Ga. 2016).

## V. Ok, what do we do?

As indicated above, the reasonableness of a policy limits demand (or any other settlement offer or demand) depends upon the facts known to the insurer at the time, and the facts readily ascertainable to the insurer with investigation. Therefore, if a policy limit demand is presented early on in litigation, and the insurer does not have enough information to evaluate the demand thoroughly, the insurer can respond in writing:

- First, carefully select the author of the response
    - In some jurisdictions, if a response is authored by coverage counsel, you may risk waiver of the attorney-client privilege between the insurance company and coverage counsel
- Acknowledging receipt of the offer
- Acknowledging an understand of the offer of terms
- Explain the facts or documentation needed to evaluate the claim
- Request whichever documents may be in plaintiff's possession to assist in this investigation; and
- Request an extension to respond
    - Be sure to request an extension that does not give the impression that the adjuster is acting with undue need for delay, as this might help give color to a claim that the carrier was not acting in good faith. Rather, request enough time to reasonably gather documents, and be sure to comply with the extension requested. Be sure to have confirmation in writing, if a plaintiff is not willing to extend the time to respond.
- Reserve rights if and when coverage is at issue