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A Settlement Offer Above Policy Limits Does Not Trigger an Insurer's Stowers Duty to Act Reasonably.

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INSURANCE—*Stowers* Doctrine—A Settlement Offer Above Policy Limits Does Not Trigger an Insurer's *Stowers* Duty to Act Reasonably.

American Physicians Insurance Exchange v. Garcia, 876 S.W.2d 842 (Tex. 1994).

Between September 1980 and January 1983, Dr. Ramon Garcia prescribed Haldol and Navane to his patient, Gustavo Cardenas.[1] During the treatment period, Dr. Garcia obtained malpractice liability insurance from the Insurance Corporation of America (ICA) and American Physicians Insurance Exchange (APIE).[2] While under Dr. Garcia's care, Mr. Cardenas developed a debilitating brain disease, which ultimately led to his death.[3] In December 1983, Araminta Cardenas, Gustavo's wife, notified Dr. Garcia of her intent to sue for his negligent treatment of her

1. American Physicians Ins. Exch. v. Garcia, 876 S.W.2d 842, 843 (Tex. 1994). Haldol and Navane are common neuroleptic drugs, which can cause tardive dyskinesia, a debilitating brain disease. *See id.* (discussing Cardenases' allegations that Haldol and Navane caused Mr. Cardenas to develop tardive dyskinesia); 3B ROSCOE N. GRAY & LOUISE J. GORDY, ATTORNEY'S TEXTBOOK OF MEDICINE §§ 103.13(1), 103.13(1c) (1986) (listing common neuroleptic, or antipsychotic, drugs and discussing usually irreversible tardive dyskinesia as "[t]he most problematical adverse effect of the neuroleptics").

2. *Garcia*, 876 S.W.2d at 843-44. Pretrial communications revealed much confusion surrounding the available policies and the scope of coverage thereunder. *Id.* at 844. Ross Crossland, the attorney hired by APIE and ICA, initially informed the Cardenases' attorney that the total coverage was $600,000; subsequently, Crossland asserted that the coverage could not exceed $500,000. *Id.* Four separate, consecutive policies covered the relevant periods: in 1980, ICA provided Dr. Garcia with a $100,000 "claims-made" policy; in 1981 and 1982, ICA issued $500,000 "occurrence" policies, one for each year; and in 1983, Dr. Garcia obtained a $500,000 occurrence policy from APIE. *Id.* at 843–44. A claims-made policy ordinarily covers only those claims made within the policy period, whereas an occurrence policy generally covers those claims arising out of, but not necessarily brought within, the policy period. *See* Hartford Fire Ins. Co. v. California, 113 S. Ct. 2891, 2896 (1993) (contrasting claims-made and occurrence insurance policies). The Texas Supreme Court held that, because none of the policies overlapped, they could not be stacked to create coverage exceeding $500,000, the amount of the largest policy. *Garcia*, 876 S.W.2d at 854-55.

3. *See Garcia*, 876 S.W.2d at 843 (discussing Cardenas's affliction with tardive dyskinesia); *Non-Execution Agreements/*Stowers *Duties/Assigning Claims Against Insurers*, TEX. LAW., Jan. 18, 1993, at 6 (discussing malpractice action brought after Gustavo Cardenas's death). Before October 1984, APIE's chairman recognized the difficulty in ascertaining when Cardenas's tardive dyskinesia became apparent and stated that "[i]t will be very difficult to imagine Doctor[ ] Garcia . . . not having to pay something on this case." *Garcia*, 876 S.W.2d at 856 (Hightower, J., dissenting).

husband "from September 1980 'to the present time.'"[4] APIE notified Dr. Garcia of his coverage under its 1983 policy and agreed with ICA to share expenses and any liability associated with the claim.[5] On March 8, 1984, Mrs. Cardenas filed a medical malpractice suit against Dr. Garcia[6] in the 225th District Court of Texas, Bexar County; however, Mrs. Cardenas failed to allege any acts of malpractice within the APIE policy period.[7] The Cardenases' attorney made three separate settlement offers in

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4. *Garcia*, 876 S.W.2d at 844. After learning of the Cardenases' intent to sue, but before the Cardenases filed the original petition, APIE notified Dr. Garcia that it would provide limited coverage for the incident because only one office visit, that of January 18, 1983, occurred within APIE's 1983 policy period. *Id.* Justice Hightower noted the duties ordinarily imposed upon insurers receiving notice of a claim:

> "When an insurer first receives notice of a claim or suit against its insured, the insurer must promptly take one of the following actions:
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> (i) acknowledge receipt of the notice and advise the insured that it will provide coverage;
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> (ii) advise the insured that it will defend the insured subject to a reservation of its right to deny coverage on one or more specified grounds;
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> (iii) deny coverage on the grounds that the claim is either not covered under the policy or that the insured has breached a policy condition; or
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> (iv) rescind the policy if it appears that the policy was procured through fraud, mutual mistake of fact, or the insured's misrepresentation or concealment of material facts in the application."

Id. at 861 (Hightower, J., dissenting) (quoting BARRY R. OSTRAGER & THOMAS R. NEWMAN, HANDBOOK ON INSURANCE COVERAGE DISPUTES § 2.01, at 38 (6th ed. 1993)). Justice Hightower argued that APIE "created a duty to settle . . . where none otherwise would have existed" by providing unconditional coverage for 16 months, by failing to determine whether coverage in fact existed, and by assuming control over Dr. Garcia's defense along with ICA. *Id.* at 866. At trial, an APIE officer admitted that the company denied coverage based solely upon the allegations in the pleadings. *Id.* at 862.

5. *Id.* at 856 (Hightower, J., dissenting). The letter from APIE to ICA reflecting this agreement stated in pertinent part:

> "It is my understanding that we agree to share any settlement or judgment on a pro rata coverage basis. We will share the legal expenses on a 50/50 basis. It is my further understanding that [Ross Crossland's firm] . . . will be filing an Answer on behalf of Dr. Garcia."

Id. (second alteration in original).

6. *Id.* at 843. Mrs. Cardenas filed suit on her own behalf and as guardian of her husband's estate. *Id.*

7. *Id.* at 844. The original petition contained no allegations of Dr. Garcia's malpractice within the period of his coverage under the APIE policy and thus implicated only the ICA policies. *Id.* Although only the last of the Cardenases' six amended petitions facially implicated APIE's policy, APIE continued to provide coverage to Dr. Garcia until five days before trial, when it recognized the absence of policy-invoking allegations in the pleadings. *Id.* at 861 (Hightower, J., dissenting). In the majority opinion, Justice Cornyn stated that APIE's duty to settle could have arisen only upon the filing of the sixth amended petition, which finally included allegations of malpractice within APIE's policy period. *See id.* at 848 (dismissing, as waived, argument that APIE was estopped from denying coverage). *But see id.* at 866 (Hightower, J., dissenting) (insisting that Garcia's cov-

the amounts of $600,000, $1,100,000, and $1,600,000; each offer represented the aggregate amount the attorney believed available under all APIE and ICA policies.[8] APIE made no response, counteroffer, or other attempt to settle and ultimately withdrew coverage from Dr. Garcia five days before trial.[9] Although the Cardenases' sixth amended petition alleged, for the first time, malpractice within the APIE policy period, APIE refused to re-enter the suit.[10] On the day of trial, Dr. Garcia assigned all his potential claims against APIE and ICA to the Cardenases in exchange for a covenant not to execute any forthcoming judgment.[11] After a bench trial, the court awarded the Cardenases $2,235,483 on the malpractice claim.[12]

On August 8, 1985, Mrs. Cardenas, as Dr. Garcia's assignee, sued APIE and ICA[13] in the 45th District Court of Texas, Bexar County, alleging

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erage under APIE policy was conclusively established). The main point of contention between the majority and the dissents in the instant case was not *when* the *Stowers* duty arose, but *whether* it arose at all. *Id.*

8. *Garcia*, 876 S.W.2d at 857-59 (Hightower, J., dissenting). The Cardenases' attorney made the first settlement offer of $600,000 on July 15, 1985 after he received the following letter from Crossland, the attorney retained by APIE and ICA:

> "I have been informed by both companies that due to the difficulty in ascertaining a date of loss for evaluation purposes . . . the companies have elected to pro rate any settlement or adverse jury verdict on an equal basis.
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> My understanding of this arrangement between the two companies is that the total insurance available for settlement or satisfaction of any adverse judgment is therefore $600,000.00."

Id. at 857. On July 26, 1984, the Cardenases' attorney, having become aware of another ICA policy for $500,000, made another settlement offer of $1,100,000. *Id.* at 858. Later that day, the third ICA policy for $500,000 came to the attention of the Cardenases by way of a letter from Crossland; in that letter, Crossland asserted that the policies could not be "stacked" in any manner to exceed $500,000. *Id.* On the day of trial, the Cardenases' attorney made another settlement offer for $1,600,000. *Id.* at 859.

9. *Id.* at 857-58.

10. *See* American Physicians Ins. Exch. v. Cardenas, 717 S.W.2d 707, 708–09 (Tex. App.—San Antonio 1986, writ ref'd n.r.e.) (denying APIE's attempted writ of error appeal because APIE refused to re-enter suit).

11. *Garcia*, 876 S.W.2d at 845.

12. *Id.* The trial court eventually filed findings of fact, which included a determination that Dr. Garcia "'committed continuing acts of negligence in his treatment and care of Gustavo Cardenas from September 19, 1980 to February 1983.'" *Id.* at 860 (Hightower, J., dissenting). This continuing negligence extending throughout the three ICA policies and the APIE policy did not raise the individual indemnity cap in any policy; thus, the coverage for the Cardenases' claim never exceeded $500,000. *Id.* at 854.

13. *Id.* at 845. Prior to trial, ICA paid the Cardenases $2,000,000 for a release from liability in the malpractice and *Stowers* suits. *Id.* The Cardenases also entered into a partial settlement agreement with APIE, whereby APIE paid $500,000 for a six-month continuance and a release from liability for any amount awarded greater than $2,500,000. *Id.*

violations of the *Stowers* doctrine[14] and the duty to defend.[15] The trial court entered judgment on a jury finding that APIE and ICA violated Article 21.21 of the Texas Insurance Code.[16] In affirming the judgment as

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14. *Id.* In Texas, the duty to settle is commonly referred to as the *Stowers* doctrine. *See* G.A. Stowers Furniture Co. v. American Indem. Co., 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved) (imposing duty upon insurer to exercise reasonable care in determining whether to settle third-party claims). The difference between the judgment and the policy limits—the excess judgment—is the center of any *Stowers* claim; *Stowers* shifts the burden of the excess judgment to the insurer when the insurer fails to exercise "that degree of care and diligence which an ordinarily prudent person would exercise in the management of his own business" in controlling settlement decisions. *Id.* In 1987, the Supreme Court of Texas adopted a *Stowers* equivalent for first-party bad faith cases. Arnold v. National County Mut. Fire Ins. Co., 725 S.W.2d 165, 167 (Tex. 1987). Within the first-party context, an insurer breaches the duty of good faith and fair dealing when "there is no reasonable basis for denial of claim or delay in payment or failure on the part of insurer to determine whether there is any reasonable basis for denial or delay." *Id.* This Casenote is concerned with the third-party *Stowers* doctrine and will address the first-party context only by analogy.

15. *Garcia*, 876 S.W.2d at 845. Specifically, the petition alleged that APIE was liable:

(1) In failing to bargain, negotiate and settle the case within the applicable policy limits;
(2) In failing to advise Dr. Garcia of the potential of an excess judgment and exposure beyond the limits of the policy;
(3) In failing to advise Dr. Garcia of settlement offers made and the effect on him if the offers were not accepted;
(4) In failing to act in good faith to bargain, negotiate and effectuate a settlement;
(5) In withdrawing coverage to Dr. Garcia and failing to provide him with a defense;
(6) In breaching their contract of insurance to provide him coverage under the policy and provide him with a defense;
(7) In breaching their fiduciary duty to act in good faith and provide coverage under the policy and a defense to Dr. Garcia;
(8) In not providing coverage and a defense after Plaintiff Cardenas's petition was amended;
(9) In failing to carry on negotiations to settle;
(10) In failing to investigate the facts of the case filed by Cardenas to determine that coverage under the policy existed;
(11) In failing to tender the $500,000.00 as provided in the policy of insurance to Plaintiff to be applied toward the judgment and continuing to refuse to pay under the policy of insurance; and
(12) In abandoning the defense of Dr. Garcia prior to the trial of the case against him.

Id. at 860 n.5 (Hightower, J., dissenting).

16. *Id.* at 846. The jury made a number of findings, including that APIE negligently failed to settle, denied coverage, failed to defend, and acted heedlessly and with reckless disregard of Dr. Garcia's rights in violation of the Texas Insurance Code and the Texas Deceptive Trade Practices-Consumer Protection Act (DTPA). *Id.* at 861 (Hightower, J., dissenting). Justice Cornyn, in the majority opinion, refused to recognize a cause of action under either the Texas Insurance Code or the DTPA for negligent failure to settle a third-party claim. *Id.* at 847. Article 21.21 of the Insurance Code defines "unfair methods of competition and unfair and deceptive acts or practices in the business of insurance." TEX.

modified, the Texas Court of Appeals for the Fourth Judicial District, San Antonio, rejected APIE's argument that a *Stowers* violation cannot exist absent evidence that the claimant would have settled within policy limits.[17] The court noted that a duty to negotiate is implicit in the duty to settle and that the latter duty extends to investigation, preparation for trial, and reasonable attempts to settle.[18] The Supreme Court of Texas granted writ of error[19] and initially affirmed, devoting its entire opinion to the effect of the covenant not to execute.[20] However, the court subsequently granted APIE's motion for rehearing and withdrew and replaced its original opinion.[21] HELD—*Reversed and rendered.* A settlement offer

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INS. CODE ANN. art. 21.21, § 4 (Vernon Supp. 1994). The DTPA incorporates Article 21.21 of the Insurance Code and provides, in pertinent part, a consumer cause of action for "the use or employment by any person of an act or practice in violation of Article 21.21, Texas Insurance Code, as amended, or rules or regulations issued by the State Board of Insurance under Article 21.21, Texas Insurance Code, as amended." TEX. BUS. & COMM. CODE ANN. § 17.50(a)(4) (Vernon 1987). Section 21.21-2 of the Texas Insurance Code specifically addresses claim settlement practices but creates no private cause of action. TEX. INS. CODE ANN. § 21.21-2 (Vernon Supp. 1994).

17. Garcia v. American Physicians Ins. Exch., 812 S.W.2d 25, 33-34 (Tex. App.—San Antonio 1991), *rev'd*, 876 S.W.2d 842 (Tex. 1994).

18. *Id.* at 31–32. APIE also argued that, because Dr. Garcia obtained a covenant not to execute, he was not subject to enforcement of the excess judgment nor did he suffer any damages by it; thus, he was not entitled to indemnification from APIE. *Id.* at 32. The Fourth Court of Appeals disagreed, holding that Dr. Garcia remained legally obligated to pay the excess judgment because the covenant was "merely a contract and not a release." *Id.*

19. American Physicians Ins. Exch. v. Garcia, 35 Tex. Sup. Ct. J. 18 (Tex. 1991) (order granting application for writ of error). APIE's application for writ of error contained six points of error including an assertion that the Fourth Court of Appeals erred in applying the *Stowers* doctrine because APIE never had an opportunity to settle for its policy limits. Application for Writ of Error at 19, American Physicians Ins. Exch. v. Garcia, 876 S.W.2d 842, 849 (Tex. 1994) (No. D-1239).

20. American Physicians Ins. Exch. v. Garcia, 36 Tex. Sup. Ct. J. 406, 406 (Tex. 1992), *withdrawn*, 876 S.W.2d 842 (Tex. 1994). APIE sought rehearing upon the basis that the effect of the covenant not to execute was not presented and that the court failed to consider points of error actually urged. Motion for Rehearing at 4-6, American Physicians Ins. Exch. v. Garcia, 876 S.W.2d 842 (Tex. 1994) (No. D-1239). Numerous amicus briefs addressed the covenant not to execute issue, but APIE asserted that it chose not to raise the issue because it had conceded that the covenant did not extinguish Dr. Garcia's damages. *Id.*

21. *Garcia*, 876 S.W.2d at 843. The court noted that, "[g]iven our disposition of this case, we need not, and do not, decide whether the pretrial non-execution agreement between Garcia and the Cardenases negated all of Garcia's damages under the facts of this case." *Id.* at 843 n.1. The four dissenting justices, led by Justice Hightower, criticized the majority for "ignor[ing] the questions concerning covenants not to execute." *Id.* at 855 (Hightower, J., dissenting). Though this Casenote is limited to the court's treatment of the *Stowers* doctrine, the effect of covenants not to execute in *Stowers* cases is of primary importance. *See id.* (stating that avoided issue of effect of covenants not to execute on

above policy limits does not trigger an insurer's *Stowers* duty to act reasonably.[22]

Liability insurance affords protection from risk of loss when an injured third party asserts a claim against the insured.[23] The typical liability in-

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insured's damages is one of critical significance). At least one post-*Garcia* decision has lamented the majority's failure to decide the issue. *See* State Farm Fire & Casualty Co. v. Gandy, 880 S.W.2d 129, 138 (Tex. App.—Texarkana 1994, writ granted) (interpreting *Garcia*'s silence as acceptance inconsistent with court's previous stance on "Mary Carter" agreements). For an introduction to cases addressing the assignability of claims and covenants not to execute in this context, see Annotation, *Assignability of Insured's Right to Recover Over Against Liability Insurer for Rejection of Settlement Offer*, 12 A.L.R.3D 1158, 1160–65 (1967) (examining incongruent treatment of assignability of bad faith claims).

22. *Garcia*, 876 S.W.2d at 849. Justice Cornyn characterized the suit as solely a *Stowers* suit and held that a *Stowers* breach cannot constitute a violation of either the DTPA or Article 21.21 of the Insurance Code. *Id.* at 847. The court unanimously held that APIE fulfilled its duty to defend Dr. Garcia because APIE continued to help finance his defense until August 13, 1985. *Id.* at 855 (Hightower, J., dissenting). Thus, the remaining issue became whether APIE breached its duty to settle under the *Stowers* doctrine. *Id.* at 848.

23. *See, e.g.*, Cain v. American Policyholders Ins. Co., 183 A. 403, 406-07 (Conn. 1936) (distinguishing liability insurance from other insurance affording protection against insured's own personal injuries); Purcell v. Metropolitan Casualty Ins. Co., 260 S.W.2d 134, 139–40 (Tex. Civ. App.—Fort Worth 1953, no writ) (noting that standard form of liability insurance policy in Texas explicitly precludes recovery for damage to insured or insured's property); American Auto. Ins. Co. v. Cone, 257 S.W. 961, 964–65 (Tex. Civ. App.—Waco 1923, no writ) (prohibiting insured from recovering for personal injuries to body or property under policy insuring against direct loss arising from third-party claims); *see also* Douglas R. Richmond, *Insured's Bad Faith as Shield or Sword: Litigation Relief for Insurers?*, 77 MARQ. L. REV. 41, 42–43 (1993) (asserting personal nature of insurance contracts purchased for "peace of mind, rather than . . . financial gain"). The need for protection against liability and personal loss is evidently quite acute, supporting a two trillion dollar industry nationwide. *See* Willy E. Rice, *Judicial Bias, the Insurance Industry and Consumer Protection: An Empirical Analysis of State Supreme Courts' Bad Faith, Breach-of-Contract, Breach-of-Covenant-of-Good-Faith and Excess-Judgment Decisions, 1900-1991*, 41 CATH. U. L. REV. 325, 327 (1992) (gauging size of American insurance industry). The American insurance industry has long been profitable, and hence, heavily regulated. *See* German Alliance Ins. Co. v. Kansas, 233 U.S. 389, 412 (1914) (recognizing extensive tradition among states in exercising control over insurance business); *see also* McCarran-Ferguson Act, Pub. L. No. 79-15, 59 Stat. 33 (1945) (codified as amended at 15 U.S.C. §§ 1011-1015 (1988)) (responding to United States Supreme Court's determination that business of insurance was "commerce" within Congress's Article I purview); United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533, 552-53 (1944) (declaring business of insurance as commerce subject to congressional regulation). The McCarran-Ferguson Act provides in part:

> (a) The business of insurance, and every person engaged therein, shall be subject to the laws of the several States which relate to the regulation or taxation of such business.
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> (b) No Act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, or which

surance policy imposes upon the insurer a duty to defend,[24] while reserving to the insurer the exclusive right to settle all claims.[25] Most policies permit the insured to settle unilaterally, but only at the insured's expense.[26] In addition, the rights and duties of liability insurers are not

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imposes a fee or tax on such business, unless such Act specifically relates to the business of insurance . . . .

15 U.S.C. § 1012 (1988). Notwithstanding Congress's original restraint, a large-scale federal occupation of the insurance industry may be imminent, as evidenced by bills recently circulated on Capitol Hill. *See, e.g.*, Insurance Competitive Pricing Act of 1993, H.R. 9, 103d Cong., 1st Sess. § 2 (1993) (proposing amendments to McCarran-Ferguson Act that would modify antitrust exemptions pertinent to insurance industry); Federal Insurance Solvency Act of 1993, H.R. 1290, 103d Cong., 1st Sess. §§ 201–07 (1993) (proposing "national standards for the financial condition of insurers in interstate commerce").

24. Brown v. Guarantee Ins. Co., 319 P.2d 69, 75 n.1 (Cal. Ct. App. 1957). The insurer ordinarily must defend even if the claim is "groundless, false or fraudulent." *Id.*; Bollinger v. Nuss, 449 P.2d 502, 507 (Kan. 1969); Tank v. State Farm Fire & Casualty Co., 686 P.2d 1127, 1130 (Wash. Ct. App. 1984), *aff'd in part, rev'd in part*, 715 P.2d 1133 (Wash. 1986); *see* Gray v. Zurich Ins. Co., 419 P.2d 168, 173 (Cal. 1966) (separating duties to indemnify and to defend); *see also* ROBERT E. KEETON, BASIC TEXT ON INSURANCE LAW § 7.8, at 508 & app. at 653-65 (1971) (discussing defense provision in typical liability insurance policy and providing standard policy forms). *See generally* 12 JOHN A. APPELMAN, INSURANCE LAW AND PRACTICE § 7004 (1981) (surveying general effect of insurance policy terms and provisions). For a general discussion of complexities inherent in ascertaining the insurer's duty to defend see Comment, *The Insurer's Duty to Defend Under a Liability Insurance Policy*, 114 U. PA. L. REV. 734, 734–59 (1966).

25. *See* Rector v. Husted, 519 P.2d 634, 640 (Kan. 1974) (considering "standard-type liability policy" reserving right to settle); Short v. Dairyland Ins. Co., 334 N.W.2d 384, 387 (Minn. 1983) (noting that insurer usually acquires control over all negotiations and settlements by terms of contract); *Tank*, 686 P.2d at 1130–31 (describing reservation of settlement control as necessity); *see also* 1A ROWLAND H. LONG, THE LAW OF LIABILITY INSURANCE, § 5A.01, at 3–4 (1994) (assessing insurer's absolute control such that insured may not complain if insurer settles frivolous claim within policy limits). However, when the insured has some special interest in exoneration, as is often the case in malpractice suits, the contract may require the insurer to obtain the insured's consent before settlement. *See* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1172–85 (1990) (analyzing "consent-to-settle" clauses in liability insurance contracts).

26. *See, e.g.*, Eureka Inv. Corp. v. Chicago Title Ins. Co., 530 F. Supp. 1110, 1116 (D.D.C. 1982) (considering clause in title insurance contract precluding claims when insured settles without insurer's consent), *aff'd in part, rev'd in part*, 743 F. 2d 932 (D.C. Cir. 1984); Brassil v. Maryland Casualty Co., 104 N.E. 622, 623–24 (N.Y. 1914) (construing insurance contract provision that forbade insured from settling except at his own cost). The typical "no-action clause" precludes claims against the insurer in the absence of specific compliance with all policy terms in part to protect insurers from collusive, unnecessary, or excessive settlements by insureds. Mayfair Constr. Co. v. Security Ins. Co., 366 N.E.2d 1020, 1024 (Ill. App. Ct. 1977). Insurers who wrongfully deny coverage, defense, or settlement are generally precluded from asserting the no-action clause as an affirmative defense. *Id. See generally* EDWIN W. PATTERSON, ESSENTIALS OF INSURANCE LAW 199 (1935) (explaining typical risk allocation between insurer and insured and detailing doctrines affecting allocation); Thomas B. Alleman, *The Reasonable Thing to Do: The In-*

bound by the "four corners" of the policy alone.[27] The possibility for conflicts of interest arising from third-party claims for damages in excess of policy limits[28] has led courts and legislatures to impose an extra-con-

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surer's Duty to Settle Claims Against Its Insured, 50 UMKC L. REV. 251, 251 (1982) (examining typical automobile liability insurance contract containing prohibition against insured effecting settlement except at own expense).

27. *See* Comunale v. Traders & Gen. Ins. Co., 328 P.2d 198, 200 (Cal. 1958) (implying duty of good faith and fair dealing within insurance contract); *Brassil*, 104 N.E. at 624 (extending insured's rights under liability insurance policy "deeper than the mere surface of the contract"); Hilker v. Western Auto. Ins. Co., 231 N.W. 257, 258 (Wis. 1930) (recognizing "principles of fair dealing which enter into every contract"), *aff'd on reh'g*, 235 N.W. 413 (1931); Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136, 1136 (1954) (exploring myth that all rights and duties can be ascertained within "four corners" of contract); *cf.* MONT. CODE ANN. § 33-18-201 (1993) (defining unfair claim settlement practices within insurance relationship); Klaudt v. Flink, 658 P.2d 1065, 1067 (Mont. 1983) (recognizing cause of action against insurer by third-party claimant). Additionally, any ambiguities in the contract are resolved in favor of the insured. *See Gray*, 419 P.2d at 172 n.7 (asserting "well-established rule" resolving doubts in insured's favor and applying doctrine of reasonable expectation to insurance contract). *See generally* RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. a (1981) (explaining implied obligation of good faith in all contracts); Kerry L. Macintosh, *Gilmore Spoke Too Soon: Contract Rises From the Ashes of the Bad Faith Tort*, 27 LOY. L.A. L. REV. 483, 501–11 (1994) (analyzing notions of contract interpretation that lead to development of extra-contractual duties and remedies).

28. *See* Coleman v. Holecek, 542 F.2d 532, 537 (10th Cir. 1976) (concluding that conflict between insured and insurer arises when third party claims damages which exceed policy limits); Farmers Ins. Exch. v. Schropp, 567 P.2d 1359, 1366 (Kan. 1977) (recognizing conflict of interest arising upon third party's claim for damages in excess of policy limits); *see also* Peavey Co. v. MV ANPA, 971 F.2d 1168, 1175 (5th Cir. 1992) (noting conflict of interest when insurer provides defense while reserving right to contest coverage); San Jose Prod. Credit Ass'n v. Old Republic Life Ins. Co., 723 F.2d 700, 704 (9th Cir. 1984) (noting absence of conflict when insured faced no danger of financial injury). The following scenario may help illuminate the nature of the conflict:

> Suppose that Hardy has a policy with Old Reliable, covering him against liability for up to $20,000 for injury to an individual. Laurel sues Hardy, alleging liability that will be covered by Hardy's policy if the allegations prove to be true. Laurel's damages exceed Hardy's policy limits—suppose that these damages are $60,000 in total but that the chances of Laurel's proving liability are only about 50 percent. The claim then has an expected value of $30,000 [expected value equals damages sought multiplied by probability of recovery].
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> Now suppose that Laurel offers to settle for $20,000. Hardy's economic interest favors settlement. He has nothing to gain and everything to lose if Old Reliable refuses to settle. But Old Reliable's interest is not the same as Hardy's. Old Reliable will lose $20,000 if it settles. If it refuses to settle and the case is tried, its expected loss is only $10,000 (50 percent of $20,000) plus costs of litigation.

KENNETH S. ABRAHAM, DISTRIBUTING RISKS 189 (1986); *see also* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1128–30 (1990) (analyzing conflicts of interest between insurer and insured arising from insurer's control of settlement decisions); Darrell Waas, Comment, *Expanding the Insurer's Duty to Attempt Settlement*, 49 U. COLO. L. REV. 251,

tractual duty to settle upon insurers.[29] Courts imply the duty to settle from the special contractual relationship between the insurer and insured.[30] Thus, a breach of the duty to settle exposes the insured to an

257 (1978) (discussing jurisdictional differences with respect to whether conflict of interest exists when plaintiff does not make offer of settlement).

29. *See* Douglas v. United States Fidelity & Guar. Co., 127 A. 708, 711 (N.H. 1924) (finding that duty of care stemmed from special relationship created by insurance contract); Mowry v. Badger State Mut. Casualty Co., 385 N.W.2d 171, 187–88 (Wis. 1986) (Steinmetz, J., concurring) (distinguishing contractual duties to defend and to indemnify from extra-contractual duty to settle, which is grounded in tort and not contract); *see also* N.D. CENT. CODE § 26.1-04-03(9)(d) (1989) (defining "unfair or deceptive act[s] or practice[s] in the business of insurance" to include breach of duty to settle); Farmer's Union Cent. Exch. v. Reliance Ins., 626 F. Supp. 583, 590 (D.N.D. 1985) (asserting that purpose of § 26.01-04-03 is to protect insured's interests by prohibiting unfair claim settlement practices). Some decisions speak of the duty in extra-contractual terms whereas others find a duty implied from the contract. *Compare* Delancy v. St. Paul Fire & Marine Ins. Co., 947 F.2d 1536, 1546 (11th Cir. 1991) (assessing duty to settle as "independent of the contract") *and* Wilson v. Aetna Casualty & Sur. Co., 76 A.2d 111, 115 (Me. 1950) (framing issue as whether negligent failure to settle may increase contractual liability) *with* Murphy v. Allstate Ins. Co., 553 P.2d 584, 586 (Cal. 1976) (discussing duty to settle arising from implied covenant within contract) *and Comunale*, 328 P.2d at 203 (asserting that implied covenant of good faith exists and that "[t]he promise which the law implies as an element of the contract is as much a part of the instrument as if it were written out"). *See generally* Christina K. Boyer, *Strict Liability for Insurers Refusing Settlements Within Policy Limits: Let's Quit Talking About It and Just Do It*, 17 J. CORP. L. 615, 621-22 (1992) (comparing justifications for duty-to-settle liability between jurisdictions); R. Kent Livesay, Comment, *Levelling the Playing Field of Insurance Agreements in Texas: Adopting Comparative Bad Faith as an Affirmative Defense Based on the Insured's Misconduct*, 24 TEX. TECH. L. REV. 1201, 1202–04 (1993) (tracing historical development of implied duty in insurance agreements).

30. *See Delancy*, 947 F.2d at 1545-46 (noting that insurer-insured relationship creates duty to settle not otherwise explicit in contract). "As the right of control goes to the insurer . . . so, too, the duty of the insurer to act reasonably towards the liability of the insured, which he has in charge, is to be implied for like reasons." *Douglas*, 127 A. at 712; *see also* Olympia Fields Country Club v. Bankers Indem. Ins. Co., 60 N.E.2d 896, 901 (Ill. App. Ct. 1945) (recognizing special relationship between insurer and insured that imposes duty to settle "flowing from" contract); Dumas v. Hartford Accident & Indem. Co., 56 A.2d 57, 60 (N.H. 1947) (finding that insurance contract "created a relation out of which grew the duty to use care"); Douglas R. Richmond, *Insured's Bad Faith as Shield or Sword: Litigation Relief for Insurers?*, 77 MARQ. L. REV. 41, 42–43 (1993) (explaining that special relationship arises from "unequal bargaining power and the nature of insurance contracts" conferring potentially abusive power on insurer); *cf.* Arnold v. National County Mut. Ins. Co., 725 S.W.2d 165, 167 (Tex. 1987) (recognizing special relationship in first-party context and imposing duty of good faith and fair dealing). The general rule recognizing an inherent inequality in bargaining power between insured and insurer may not necessarily hold true when the insured is a commercial entity. *See* Lawrence P. McLellan, Note, *Insurance Settlements: An Insured's Bad Faith*, 31 DRAKE L. REV. 877, 880 (1981) (asserting that commercial insureds generally possess sufficient bargaining power to negotiate contracts).

excess judgment and affords the insured a cause of action against the insurer for the amount of the excess judgment.[31]

The duty-to-settle doctrine requires insurers to consider the interests of their insureds and exercise care in determining whether to settle a claim.[32] The most pervasive rationale for the implied duty to settle rests upon recognition of the relative helplessness of an insured facing the possibility of an excess judgment.[33] The insurer, with superior expertise,[34]

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31. *See* American Mut. Liab. Ins. Co. v. Cooper, 61 F.2d 446, 448 (5th Cir. 1932) (allowing recovery of excess judgment for bad faith failure to settle). Writing in 1932, the *Cooper* court noted that "it is well settled in cases of limited liability insurance that the insurer may so conduct itself as to be liable for the entire judgment recovered against the insured, although that judgment exceeds the amount of liability named in the policy." *Id.*; *see* Aetna Casualty & Sur. Co. v. Kornbluth, 471 P.2d 609, 612 (Colo. Ct. App. 1970) (allowing insured to recover excess judgment after insurer indemnified for policy limits); *Hilker*, 235 N.W. at 414 (permitting insured to recover judgment in excess of policy limits when insurer breached duty to settle); *see also Comunale*, 328 P.2d at 202 (interpreting California statute as authorizing recovery of excess judgment for breach of duty to settle). *See generally* Kelly H. Thompson, Comment, *Bad Faith: Limiting Insurers' Extra-Contractual Liability in Texas*, 41 Sw. L.J. 719, 719–21 (1987) (tracing development of extra-contractual liability for failure to settle). Historically, courts limited damages recoverable for breach of an obligation under an insurance policy to the amount of the policy. *See id.* at 720 (noting traditional limitations placed on breach of insurance contract damages). The basic dynamics of the duty-to-settle doctrine are further complicated when an excess insurer's financial interest is at stake. *See* V. Eileen Stuhr, Comment, *Excess Carrier Tort Suits: Are Primary Insurers Up the* Canal *Without a Paddle?*, 29 HOUS. L. REV. 661, 688–704 (1992) (commenting on implications of bad-faith tort law in insured-insurer-excess insurer context).

32. *See* Fidelity & Casualty Co. v. Robb, 267 F.2d 473, 476 (5th Cir. 1959) (construing Texas law as precluding insurer from "subordinating and sacrificing the insured's interest to its own"); Jordan v. United States Fidelity & Guar. Co., 843 F. Supp. 164, 171 (S.D. Miss. 1993) (stating that insurer may not permit its own interests to compromise those of insured); Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. MICH. J.L. REF. 1, 2–33 (1992) (tracing evolution of duty-to-settle doctrine and underlying justifications and policies); *see also* Bohemia, Inc. v. Home Ins. Co., 725 F.2d 506, 513 (9th Cir. 1984) (requiring insurer to consider interests of insured and excess insurer); Portland Gen. Elec. v. Pacific Indem. Co., 574 F.2d 469, 473 (9th Cir. 1978) (asserting that insured's interests must be considered even when excess insurance policy exists); Robert E. Keeton, *Ancillary Rights of the Insured Against His Liability Insurer*, 28 INS. COUNS. J. 395, 395 (1961) (considering insured's right to have insurer consider her interests in settlement to be right ancillary to insurance contract).

33. *See* Rova Farms Resort, Inc. v. Investors Ins. Co., 323 A.2d 495, 507 (N.J. 1974) (justifying decision in part upon recognition of insured's lack of control over own interests); Matthew J. Barrett, Note, *"Contort": Tortious Breach of the Implied Covenant of Good Faith and Fair Dealing in Noninsurance, Commercial Contracts—Its Existence and Desirability*, 60 NOTRE DAME L. REV. 510, 523 (1985) (expounding public policy basis for duty as recognition of special relationship and vulnerability of insured); *see also* Carver v. Workers' Compensation Appeals Bd., 266 Cal. Rptr. 718, 722 (Ct. App. 1990) (stating that rationale of duty-to-settle doctrine "relates to protection of the right of the insured to

bargaining power,[35] and sole control of the settlement decision,[36] is in a

receive the benefit of the bargain represented by the insurance contract"); Brown v. Guarantee Ins. Co., 319 P.2d 69, 72 (Cal. Ct. App. 1957) (noting that duty to settle arises because insured "has bartered to the insurance company all of the rights possessed by him to enable him to discover the extent of the injury and to protect himself"); *Kornbluth*, 471 P.2d at 611 (asserting that root of all standards of care is insurer's absolute control over settlements coupled with insured's exclusion from any interference therewith); Cernocky v. Indemnity Ins. Co., 216 N.E.2d 198, 203–04 (Ill. App. Ct. 1966) (recognizing insurer's contractual reservation of exclusive right to settle as creating duty to insured); *cf. Arnold*, 725 S.W.2d at 167 (noting disparity in bargaining power that would allow insurer to take advantage of insured). *See generally* Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136, 1138 (1954) (contending that basis for imposing duty to settle is insurer's exclusive control over settlement decisions when interests of insured are adverse from insurer's); Kerry L. Macintosh, *Gilmore Spoke Too Soon: Contract Rises From the Ashes of the Bad Faith Tort*, 27 LOY. L.A. L. REV. 483, 518–19 (1994) (interpreting evolution of bad faith cause of action as judicial response to insurer's "overwhelming incentive to breach"); R. Kent Livesay, Comment, *Levelling the Playing Field of Insurance Agreements in Texas: Adopting Comparative Bad Faith as an Affirmative Defense Based on the Insured's Misconduct*, 24 TEX. TECH. L. REV. 1201, 1214 (1993) (asserting that original purpose of imposing duty of good faith was to offer protection from superior power held by insurer).

34. *See* Certain Underwriters of Lloyd's v. General Accident Ins. Co., 909 F.2d 228, 234 (7th Cir. 1990) (disallowing defense of consent when insurer failed to use its superior expertise to inform insured); Home Ins. Co. v. Davila, 212 F.2d 731, 742 (1st Cir. 1954) (presuming that insurance agent possesses superior knowledge of insurance law); Byrd v. Mortenson, 298 S.E.2d 170, 172 (N.C. Ct. App. 1982) (assessing insurer's superior expertise in matters of litigation); *see also* McNally v. Nationwide Ins. Co., 815 F.2d 254, 259 (3d Cir. 1987) (stating "reasonable insurer" standard in duty-to-settle case as requiring consideration of insurer's expertise in field); Bernard L. Balkin & Keith Witten, *Current Developments in Bad Faith Litigation Involving the Performance and Payment Bond Surety*, 28 TORT & INS. L.J. 611, 613 (1993) (listing common duties imposed upon insurers in their handling of claims against insureds); *cf.* Portland Gen. Elec. v. Westinghouse Elec. Corp., 842 F. Supp. 161, 165 (W.D. Pa. 1993) (analogizing insurer liability for failure to properly use expertise to other agency relationships giving rise to similar liability). *See generally* 7C JOHN A. APPLEMAN, INSURANCE LAW AND PRACTICE § 4711, at 395 (1979) (discussing insurer's expertise in handling claims and litigation).

35. *See* Puerto Rico Elec. Power Auth. v. Phillips, 645 F. Supp. 770, 773 (D.P.R. 1986) (recognizing traditional presumption that insurer holds superior bargaining position); *Gray*, 419 P.2d at 171–72 (assuming "disparate bargaining status of the parties" to insurance contract that justifies application of doctrine of reasonable expectation). Courts have long regarded insurance policies as contracts of adhesion. *See* Mitchell v. California Fair Plan Ass'n, 260 Cal. Rptr. 3, 6 (Ct. App. 1989) (classifying insurance contracts as contracts of adhesion because of insurer's superior bargaining power); *see also* Garrick v. Northland Ins. Co., 460 N.W.2d 920, 924 (Minn. Ct. App. 1990) (noting widely recognized inequality of bargaining power between insurer and insured), *rev'd*, 469 N.W.2d 709 (Minn. 1991); Caserotti v. State Farm Ins. Co., 791 S.W.2d 561, 565 (Tex. App.—Dallas 1990, writ denied) (noting extra-contractual duty imposed upon insurers by virtue of their superior bargaining power). *But see* R. Kent Livesay, Comment, *Levelling the Playing Field of Insurance Agreements in Texas: Adopting Comparative Bad Faith as an Affirmative Defense Based on the Insured's Misconduct*, 24 TEX. TECH. L. REV. 1201, 1214 (1993) (arguing that insureds

position to harm the insured if its discretion is left unchecked.[37] Thus, a breach of the duty to settle shifts the burden of an excess judgment to the imprudent insurer, who must pay its policy limits as well as any amount

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have recently enjoyed general increase in bargaining power). *See generally* Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 966–77 (1970) (tracing development of common law doctrine regarding insurance agreements as adhesion contracts).

36. *See* Rawlings v. Apodaca, 726 P.2d 565, 571–72 (Ariz. 1986) (stating that insurer's absolute control of decision that could cause great damage to insured required insurer to consider insured's interests). In *Rawlings*, the Arizona Supreme Court held "that one of the benefits that flow from the insurance contract is the insured's expectation that his insurance company will not wrongfully deprive him of the very security for which he bargained or expose him to the catastrophe from which he sought protection." *Id.* at 571; *see also* Fireman's Fund Ins. Co. v. Security Ins. Co., 367 A.2d 864, 876 (N.J. 1976) (Clifford, J., dissenting) (noting that insured, by seeking expertise of insurer in disposing of claims, necessarily relinquishes control over such claims to insurer); *Mowry*, 385 N.W.2d at 186–87 (Steinmetz, J., concurring) (distinguishing duty to settle arising from reservation of sole control of settlement negotiations from duty to defend or indemnify arising from express terms of contract); Note, *Control of Settlement and Litigation by Liability Insurers*, 34 COLUM. L. REV. 511, 511–12 (1934) (discussing insurer's purpose in retaining sole control to prevent overpayment and collusion). Insurers commonly retain sole control over settlement negotiations and decisions by virtue of two or three standard contractual clauses. One clause typically states that the insurer "may make such investigation and settlement of any claim or suit as it deems expedient." *See* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1118–19 (1990) (quoting INSURANCE SERVS. OFFICE, INC., COMPREHENSIVE PERSONAL LIABILITY ENDORSEMENT 2 (1973), *reprinted in* 1A ROWLAND H. LONG, THE LAW OF LIABILITY INSURANCE 10-138, 10-139 (1990)). Another clause prohibits the insured from unilaterally settling, except at its own expense, or from interfering with the insurer's settlement. *Id.* In addition, a no-action clause bars the insured from obtaining indemnification if the insured unilaterally effects a settlement. *See id.* (discussing typical liability insurance policy clauses conferring absolute control of settlement decisions on insurer).

37. *Rawlings*, 726 P.2d at 571; *see* Spencer v. Aetna Life & Casualty Ins. Co., 611 P.2d 149, 155 (Kan. 1980) (answering certified question concerning whether Kansas recognized first-party bad faith cause of action). Absolute control over settlement gives rise to the fiduciary relationship, which in turn requires the insurer to protect the insured's interests. *Spencer*, 611 P.2d at 155; *see* Charlie D. Dye, Comment, *Insurer's Liability for Judgments Exceeding Policy Limits*, 38 TEX. L. REV. 233, 234 (1959) (discussing application of principal-agent relationship in liability insurance context as entailing responsibility for protecting insured's interests); *see also* Stevedores, Inc. v. London Guar. & Accident Co., 232 F. 298, 299 (D. Or. 1915) (addressing insurer's attempt to "hold up" insured by insisting on contribution to settlement); Central Armature Works, Inc. v. American Motorists Ins. Co., 520 F. Supp. 283, 295 (D.D.C. 1980) (justifying punitive damages when insurer attempted to coerce insured into surrendering rights before insurer would participate in settlement); Tan Jay Int'l v. Canadian Indem. Co., 243 Cal. Rptr. 907, 912 (Ct. App. 1988) (recognizing availability of damages for emotional distress when insurer refuses to settle); Daniel S. Bopp, *Tort and Contract in Bad Faith Cases: Is the Honeymoon Over?*, 59 DEF. COUNS. J. 524, 524 (1992) (discussing treatment of insurance disputes as "David-and-Goliath" relationships).

awarded in excess of those limits.[38] Although nearly all jurisdictions embrace some form of the duty-to-settle doctrine,[39] the particular standards

38. Smith v. Blackwell, 791 P.2d 1343, 1347 (Kan. Ct. App. 1989); *see* Allstate Ins. Co. v. Campbell, 639 A.2d 652, 658 (Md. 1994) (declaring that ordinary measure of damages for bad-faith breach of duty to settle is amount of excess judgment); Soto v. State Farm Ins. Co., 635 N.E.2d 1222, 1224 (N.Y. 1994) (evaluating damages recoverable for bad-faith failure to settle as "'the amount for which the insured becomes charged in excess of his policy coverage'" (quoting 7C JOHN A. APPLEMAN, INSURANCE LAW & PRACTICE § 4711, at 414 (Walter F. Berdal ed., 1979)); Howard S. Chapman, *Liability of Insurers and Defense Attorneys for Judgments in Excess of Policy Limits*, 36 TRIAL LAW. GUIDE 481, 481 (1992) (noting that insurers and defense attorneys may be exposed to significant liability for third-party claims exceeding policy limits); *see also* Walbrook Ins. Co. v. Liberty Mut. Ins. Co., 7 Cal. Rptr. 2d 513, 517 (Ct. App. 1992) (basing measure of damages to excess insurer resulting from primary insurer's failure to settle third-party claim on damages in excess of primary insurer's policy limits). For a discussion of extra-contractual recovery in first-party bad faith cases, see 1 JOHN C. MCCARTHY, RECOVERY OF DAMAGES FOR BAD FAITH §§ 1.56-1.66 (5th ed. 1990) (analyzing cases on compensatory and punitive damages for first-party bad faith actions).

39. *E.g.*, Bohna v. Hughes, 828 P.2d 745, 768 (Alaska 1992); Hartford Accident & Indem. Co. v. Aetna Casualty & Sur. Co., 792 P.2d 749, 753 (Ariz. 1990); Moradi-Shalal v. Fireman's Fund Ins. Cos., 758 P.2d 58, 62 (Cal. 1988); Government Employees Ins. Co. v. Campbell, 288 So. 2d 513, 515 (Fla. Dist. Ct. App. 1973); United States Fidelity & Guar. Co. v. Evans, 156 S.E.2d 809, 811 (Ga. Ct. App. 1967), *aff'd*, 158 S.E.2d 243 (Ga. 1967); White v. Unigard Mut. Ins. Co., 730 P.2d 1014, 1016 (Idaho 1986); Van Vleck v. Ohio Casualty Ins. Co., 471 N.E.2d 925, 927 (Ill. App. Ct. 1984); Winchell v. Aetna Life & Casualty Ins. Co., 394 N.E.2d 1114, 1116-17 (Ind. Ct. App. 1979); Loudon v. State Farm Mut. Auto. Ins. Co., 360 N.W.2d 575, 578–79 (Iowa Ct. App. 1984); Guarantee Abstract & Title Co. v. Interstate Fire & Casualty Co., 618 P.2d 1195, 1199 (Kan. 1980); State Farm Mut. Auto. Ins. Co. v. Marcum, 420 S.W.2d 113, 121 (Ky. Ct. App. 1967); Keith v. Comco Ins. Co., 574 So. 2d 1270, 1275 (La. Ct. App. 1991); Fireman's Fund Ins. Co. v. Continental Ins. Co., 519 A.2d 202, 204 (Md. 1987); Hartford Casualty Ins. Co. v. New Hampshire Ins. Co., 628 N.E.2d 14, 16 (Mass. 1993); Frankenmuth Mut. Ins. Co. v. Keeley, 447 N.W.2d 691, 691-92 (Mich. 1989); Hartford Accident & Indem. Co. v. Foster, 528 So. 2d 255, 265 (Miss. 1988); Ganaway v. Shelter Mut. Ins. Co., 795 S.W.2d 554, 556 (Mo. Ct. App. 1990); St. Paul Fire & Marine Ins. Co. v. Cumiskey, 665 P.2d 223, 226 (Mont. 1983); Fireman's Fund Ins. Co. v. Security Ins. Co., 367 A.2d 864, 870 (N.J. 1976); Ambassador Ins. Co. v. St. Paul Fire & Marine Ins. Co., 690 P.2d 1022, 1024–25 (N.M. 1984); Gordon v. Nationwide Mut. Ins. Co., 285 N.E.2d 849, 861 (N.Y. 1972), *cert. denied*, 410 U.S. 931 (1973); Dvorak v. American Family Mut. Ins. Co., 508 N.W.2d 329, 331 (N.D. 1993); Hoskins v. Aetna Life Ins. Co., 452 N.E.2d 1315, 1319 (Ohio 1983); Niemeyer v. United States Fidelity & Guar. Co., 789 P.2d 1318, 1322 (Okla. 1990); Radcliffe v. Franklin Nat'l Ins. Co., 298 P.2d 1002, 1011 (Or. 1956); Gedeon v. State Farm Mut. Auto. Ins. Co., 188 A.2d 320, 322 (Pa. 1963); Trotter v. State Farm Mut. Auto. Ins. Co., 377 S.E.2d 343, 349 (S.C. Ct. App. 1988); Helmbolt v. LeMars Mut. Ins. Co., 404 N.W.2d 55, 57 (S.D. 1987); State Auto. Ins. Co. v. Rowland, 427 S.W.2d 30, 33 (Tenn. 1968); Ranger County Mut. Ins. Co. v. Guin, 723 S.W.2d 656, 658–59 (Tex. 1987); Campbell v. State Farm Mut. Auto. Ins. Co., 840 P.2d 130, 138 (Utah App. 1992); Fidelity & Deposit Co. v. Wu, 552 A.2d 1196, 1199–2000 (Vt. 1988); Tyler v. Grange Ins. Ass'n, 473 P.2d 193, 199 (Wash. Ct. App. 1970); *Mowry*, 385 N.W.2d at 178. *See generally* Henry A. Hentemann, *Uninsured Motorist Coverage Claims and the Bad Faith Issue*, 55 DEF. COUNS. J. 168, 169 n.8 (1988) (noting "almost unanimous acceptance" of third-

of care imposed and the relative weight ascribed to insureds' interests vary greatly.[40] Some jurisdictions employ a "bad faith" standard,[41] while some utilize a negligence standard,[42] and still others combine the two.[43]

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party bad faith cause of action); Guy O. Kornblum, *The Current State of Bad Faith and Punitive Damage Litigation in the U.S.*, 23 TORT & INS. L.J. 812, 813–27 (1988) (characterizing evolution of bad faith liability over past 30 years as "revolution"). One of the most recent extensions in bad faith law has been the allowance of damages for emotional distress. *See* Gregory G. Sarno, Annotation, *Liability of Insurer, or Insurance Agent or Adjuster, for Infliction of Emotional Distress*, 6 A.L.R.5TH 297, § 43 (1992) (listing cases considering emotional distress damages for failure to settle claims).

40. *See Brown*, 319 P.2d at 72-75 (tracing divergent theories of insurers' failure to settle); *Campbell*, 840 P.2d at 138 n.16 (noting spectrum of bad faith standards applied in other jurisdictions ranging from willfulness or recklessness to mere negligence). *Compare* Pavia v. State Farm Mut. Auto. Ins. Co., 626 N.E.2d 24, 27 (N.Y. 1993) (requiring proof of insurer's "gross disregard" of insured's interests) *with* Maryland Casualty Co. v. Dixie Ins. Co., 622 So. 2d 698, 701 (La. Ct. App. 1993) (requiring insurer to give insured's interests "paramount" consideration) *and* Nationwide Mut. Ins. Co. v. Public Serv. Co., 435 S.E.2d 561, 564 (N.C. Ct. App. 1993) (predicating liability on failure to give insured's interests "due regard"). *See generally* Terry A. Halbert, *Insurer's Bad Faith Refusal to Settle: Excess Liability Consequences*, 57 PA. B. ASS'N Q. 38, 39 (1986) (listing jurisdictions that apply bad faith standard and those that apply combination of bad faith and negligence); Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. MICH. J.L. REF. 1, 37 (1992) (postulating that courts' discomfort with labeling relationship between insured and insurer led to commingling of objective and subjective standards of care).

41. *See, e.g.*, Fulton v. Woodford, 545 P.2d 979, 983 (Ariz. Ct. App. 1976) (opting for bad faith standard); *Brown*, 319 P.2d at 75 (disapproving negligence standard in favor of bad faith and recognizing tendency of courts to coalesce both standards); Murach v. Massachusetts Bonding & Ins. Co., 158 N.E.2d 338, 341 (Mass. 1959) (requiring something more than evidence of mere negligence); *see also* STEPHEN S. ASHLEY, BAD FAITH ACTIONS: LIABILITY AND DAMAGES § 2.05, at 9-17 (1991) (stating that majority of jurisdictions purport to apply bad faith standard); Richard J. Phelan, *Bad Faith Litigation* (discussing treatment of bad faith standard of care), *in* 1985 INS. LITIG. INST. 123, 123–31 (Sheila L. Birnbaum & David R. Gross eds.).

42. *See, e.g.*, Foremost County Mut. Ins. Co. v. Home Indem. Co., 897 F.2d 754, 757 (5th Cir. 1990) (applying Texas negligence standard derived from *G.A. Stowers Furniture Co. v. American Indemnity Co.*, 15 S.W.2d 544 (Tex. Comm'n App. 1929, holding approved)); *Kornbluth*, 471 P.2d at 611 (deciding that negligence constituted proper standard, but holding that jury charge injecting bad faith standard was not prejudicial); Spray v. Continental Casualty Co., 739 P.2d 40, 43 (Or. Ct. App. 1987) (distinguishing decisions that injected subjective bad faith element into standard); Tyger River Pine Co. v. Maryland Casualty Co., 170 S.E. 346, 348 (S.C. 1933) (predicating liability on negligence in absence of evidence with respect to bad faith); *see also* Charlie D. Dye, Comment, *Insurer's Liability for Judgments Exceeding Policy Limits*, 38 TEX. L. REV. 233, 236–40 (1959) (discussing factors indicating negligence and, conversely, due care in duty-to-settle cases); Comment, *An Insurance Company's Duty to Settle: Qualified or Absolute?*, 41 S. CAL. L. REV. 120, 127–29 (1968) (comparing various norms applied to determine reasonableness of insurer's refusal to settle).

Comunale v. Traders & General Insurance Co.,[44] a 1958 California Supreme Court case, established the principle that a liability insurance contract, like all contracts, contains an implied covenant of good faith and fair dealing.[45] To avoid liability for bad faith failure to settle, the insurer,

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43. *See, e.g.*, American Fidelity & Casualty Co. v. Greyhound Corp., 258 F.2d 709, 716-17 (5th. Cir. 1958) (construing Florida law as allowing consideration of negligence in bad faith determination); Waters v. American Casualty Co., 73 So. 2d 524, 528 (Ala. 1953) (allowing liability for failure to settle on either bad faith or negligence theories); *Brown*, 319 P.2d at 75 (rejecting negligence standard while allowing consideration of negligence in finding bad faith); Ferris v. Employers Mut. Casualty Co., 122 N.W.2d 263, 266 (Iowa 1963) (injecting elements of negligence into determination of bad faith); *Bollinger*, 449 P.2d at 511–12 (dispelling notions of independence of either standard and holding that both are required); *Foster*, 528 So. 2d at 266 (permitting question of liability to go to jury when party has raised evidence on either bad faith or negligence); State Farm Mut. Auto. Ins. Co. v. White, 236 A.2d 269, 273 (Md. 1967) (combining elements of negligence and good faith); *see also* Robert E. Keeton, *Liability Insurance and Responsibility For Settlement*, 67 HARV. L. REV. 1136, 1140 nn.7, 8 (1954) (citing jurisdictions employing bad faith and negligence standards); Annotation, *Duty of Liability Insurer To Settle or Compromise*, 40 A.L.R.2D 168, § 6 (1955) (identifying cases treating negligence as relevant in determination of bad faith).

44. 328 P.2d 198 (Cal. 1958).

45. *Comunale*, 328 P.2d at 200. Although courts had traditionally treated bad faith claims as sounding in tort, the *Comunale* court stated that "[t]he promise which the law implies as an element of the contract is as much a part of the instrument as if it were written out"; thus, the action sounded in contract and in tort. *Id.* at 203; *see* Daniel S. Bopp, *Tort and Contract in Bad Faith Cases: Is the Honeymoon Over?*, 59 DEF. COUNS. J. 524, 526 (1992) (discussing significance of *Comunale* in allowing insureds to thereafter rely on implied covenant to convert breach of contact into tort); *see also* Gray v. Nationwide Mut. Ins. Co., 223 A.2d 8, 12 (Pa. 1966) (concluding that cause of action in tort or in assumpsit exists for breach of duty to settle). *But see* Wolfe v. Continental Casualty Co., 647 F.2d 705, 709 (6th Cir. 1981) (distinguishing *Comunale* and holding that action for breach of duty to settle sounds exclusively in tort); Tyson v. Casualty Corp. of Am., 560 P.2d 238, 239 (Okla. Ct. App. 1976) (holding that failure-to-settle action sounds in tort, not contract, and is subject to tort statute of limitations). *See generally* Kerry L. Macintosh, *Gilmore Spoke Too Soon: Contract Rises From the Ashes of the Bad Faith Tort*, 27 LOY. L.A. L. REV. 483, 503-11 (1994) (tracing initial expansion and eventual demise of quasi-fiduciary model of contract law). Numerous California decisions following *Comunale* interpreted bad faith to include some intentional act equivalent to fraud. *See, e.g.*, Critz v. Farmers Ins. Group, 41 Cal. Rptr. 401, 405 (Ct. App. 1965) (announcing that "[b]ad faith implies unfair dealing rather than mistaken judgment or poor prognostication"); Palmer v. Financial Indem. Co., 30 Cal. Rptr. 204, 208 (Ct. App. 1963) (comparing requirements for good faith and bad faith and concluding that latter implies "dishonesty, fraud and concealment"); Davy v. Public Nat. Ins. Co., 5 Cal. Rptr. 488, 493 (Ct. App. 1960) (predicating bad faith on "dishonesty, fraud and concealment" rather than mistaken judgment); *see also* Robert W. Peterson, Note, *Excess Liability: Reconsideration of California's Bad Faith Negligence Rule*, 18 STAN. L. REV. 475, 477 (1966) (noting confusion in subsequent cases regarding appropriate standard in determining bad faith). For an examination of the bad faith standard before the landmark *Comunale* decision, see John A. Appleman, *Circumstances Creating Excess Liability*, 452 INS. L.J. 553, 553–61 (1960). In Texas, liability for

giving the insured's interests equal weight, must settle the claim when a great risk of recovery beyond policy limits is present.[46] Moreover, an action for bad faith failure to settle may sound in contract or tort[47] and does

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failure to settle is predicated upon negligence and does not require any showing of subjective bad faith. Highway Ins. Underwriters v. Lufkin-Beaumont Motor Coaches, Inc., 215 S.W.2d 904, 931 (Tex. Civ. App.—Beaumont 1948, writ ref'd n.r.e.).

46. Larraburu Bros., Inc. v. Royal Indem. Co., 604 F.2d 1208, 1210 (9th Cir. 1979); Fulton v. Woodford, 545 P.2d 979, 984 (Ariz. Ct. App. 1976); *Comunale*, 328 P.2d at 201; Lysick v. Walcom, 65 Cal. Rptr. 406, 414–15 (Ct. App. 1968); Kelley v. British Commercial Ins. Co., 34 Cal. Rptr. 564, 568 (Ct. App. 1963); *see* Smith v. Blackwell, 791 P.2d 1343, 1346 (Kan. Ct. App. 1989) (requiring insurer to act in insured's best interests when settling or defending claims); Robert W. Peterson, Note, *Excess Liability: Reconsideration of California's Bad Faith Negligence Rule*, 18 STAN. L. REV. 475, 477 (1966) (arguing that standards articulated in *Comunale* may lead to different conclusions when considered separately). An early articulation of this equality-of-interests standard is found in Professor Robert E. Keeton's authoritative text on duty-to-settle law. *See* Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136, 1142–45 (1954) (clarifying courts' use of standard requiring insurer to weigh interests equally as "equal consideration" standard rather than equal weight standard).

47. Crisci v. Security Ins. Co., 426 P.2d 173, 178–79 (Cal. 1967) (en banc); *see* 1 JOHN C. MCCARTHY, RECOVERY OF DAMAGES FOR BAD FAITH § 1.7, at 25-27 (5th ed. 1990) (discussing evolution of bad faith tort from roots in *Crisci*); *see also* Rawlings v. Apodaca, 726 P.2d 565, 579 (Ariz. 1986) (explaining that, although breach of ordinary covenants sounds in contract, insurer's breach of implied covenant of good faith is also actionable in tort because of special relationship between insurer and insured); Careau & Co. v. Security Pac. Bus. Credit, 272 Cal. Rptr. 387, 400 n.18 (Ct. App. 1990) (reaffirming California rule that breach of implied covenant of good faith sounds in contract and tort); *cf.* Hillman v. Nationwide Mut. Fire Ins. Co., 855 P.2d 1321, 1330 (Alaska 1993) (Compton, J., dissenting) (criticizing majority for permitting exculpatory defense of "reasonable contractual basis for a denial of liability" notwithstanding bad faith sounding in tort, not contract). The distinction between tort and contract has critical implications regarding the type and extent of damages recoverable as traditional contract damages are ordinarily limited by the terms of the contract. *See* Chris M. Kallianos, *Bad Faith Refusal to Pay First-Party Insurance Claims: A Growing Recognition of Extra-Contract Damages*, 64 N.C. L. REV. 1421, 1422 (1986) (discussing traditional restrictions on contract damages); *see also* Farmers Group, Inc. v. Trimble, 658 P.2d 1370, 1376 (Colo. Ct. App. 1982) (reversing summary judgment for factual determination of whether insurer breached covenant of good faith in refusing to protect insured's interests such as would support award of mental anguish damages), *aff'd*, 691 P.2d 1138 (Colo. 1984); Gibson v. Western Fire Ins. Co., 682 P.2d 725, 738-39 (Mont. 1984) (upholding $300,000 punitive damage award for bad faith failure to settle and affirming, in theory, recoverability of mental anguish damages); Farris v. United States Fidelity & Guar. Co., 587 P.2d 1015, 1016-17 (Or. 1978) (considering emotional distress damages when action sounds in tort notwithstanding traditional contract rule precluding such recovery). *See generally* Kerry L. Macintosh, *Gilmore Spoke Too Soon: Contract Rises From the Ashes of the Bad Faith Tort*, 27 LOY. L.A. L. REV. 483, 487–88 (1994) (discussing leading case of *Crisci* in evolution of quasi-fiduciary conception of contracts); Kelly H. Thompson, Comment, *Bad Faith: Limiting Insurers' Extra-Contractual Liability in Texas*, 41 SW. L.J. 719, 733-36 (1987) (contrasting "aggressive" California law on extra-contractual liability in first- and third-party cases with Texas law regarding same); David Rand, Jr., Annotation,

not necessarily entail dishonesty, fraud, or concealment.[48] The negli-

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Recoverability of Punitive Damages in Action By Insured Against Insurer for Failure to Settle Claim Against Insured, 85 A.L.R.3D 1211, 1217–30 (1978) (addressing decisions and statutes on recoverability of extra-contractual damages). How an action is characterized—as one sounding in tort, contract, or both—will also determine the defenses available to the insurer. *See* Daniel S. Bopp, *Tort and Contract in Bad Faith Cases: Is the Honeymoon Over?*, 59 DEF. COUNS. J. 524, 539 (1992) (advocating that traditional tort defenses should be available to insurers when bad faith is applied as sounding in tort). Although the characterization of *Stowers* claims is unclear, the Supreme Court of Texas recently intimated that the first-party bad faith cause of action sounds in tort. *See* Transportation Ins. Co. v. Moriel, 879 S.W.2d 10, 20–21 (Tex. 1994) (discussing availability of punitive, compensatory, and "benefit of bargain" damages and stating that "[t]he threshold of bad faith is reached when a breach of contract is accompanied by an independent tort").

48. *Crisci*, 426 P.2d at 176. Notwithstanding the language in earlier decisions purportedly requiring evidence of fraud, dishonesty or concealment, the *Crisci* court held that bad faith may be established absent a showing of actual fraud. *Id.*; *see* General Fire & Life Assurance Corp. v. Little, 443 P.2d 690, 699 (Ariz. 1968) (en banc) (approving bad faith standard not entailing actual fraud, but rather, failure to give equal consideration to insured's interests); Palatine Ins. Co. v. Gilleland, 52 S.E.2d 537, 542 (Ga. Ct. App. 1949) (intimating first-party bad faith standard as "not the equivalent of . . . fraud"); *see also* James R. Sutterfield, *Relationships Between Excess and Primary Insurors: The Excess Judgment Problem*, 52 INS. COUNS. J. 638, 640 (1985) (defining bad faith as intentional disregard, fraud, dishonesty, or concealment though factors actually considered may allow liability for less). In explaining that the bad faith standard does not require actual dishonesty or fraud, the Supreme Court of Michigan considered the following factors instructive, though not determinative:

> 1) failure to keep the insured fully informed of all developments in the claim or suit that could reasonably affect the interests of the insured,
> 2) failure to inform the insured of all settlement offers which do not fall within the policy limits,
> 3) failure to solicit a settlement offer or initiate settlement negotiations when warranted under the circumstances,
> 4) failure to accept a reasonable compromise offer of settlement when warranted under the circumstances,
> 5) rejection of a reasonable settlement offer within the policy limits,
> 6) undue delay in accepting a reasonable offer to settle a potentially dangerous case within the policy limits where the verdict potential is high,
> 7) an attempt by the insurer to coerce or obtain an involuntary contribution from the insured in order to settle within policy limits,
> 8) failure to make a proper investigation of the claim prior to refusing an offer of settlement within policy limits,
> 9) disregarding the advice or recommendations of an adjuster or attorney,
> 10) serious and recurrent negligence by the insurer;
> 11) refusal to settle the case within the policy limits following an excessive verdict when the chances of reversal on appeal are slight or doubtful, and
> 12) failure to take an appeal following a verdict in excess of policy limits where there are reasonable grounds for such an appeal, especially where trial counsel so recommended.

Commercial Union Ins. Co. v. Liberty Mut. Ins. Co., 393 N.W.2d 161, 165–66 (Mich. 1986) (footnotes omitted); *see* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1123–24

gence standard in the duty-to-settle doctrine, outlined by the New Hampshire Supreme Court in *Douglas v. United States Fidelity & Guaranty Co.*,[49] requires the insurer to exercise reasonable care because of the special relationship created by the insurance contract.[50] Under the negligence standard, the insurer's conduct is subject to a higher duty of care than that required in other agency relationships precisely because the insurer's interests often conflict with those of the insured.[51]

(1990) (listing numerous frequently considered factors in bad faith cases from various jurisdictions). In Texas, several factors are relevant in determining whether an insurer breached its duty to settle. *See* Globe Indem. Co. v. Gen-Aero, Inc., 459 S.W.2d 205, 208 (Tex. Civ. App.—San Antonio 1970, writ ref'd n.r.e.) (listing factors relevant in *Stowers* context, including (1) opportunity to settle, (2) failure to negotiate, (3) likelihood of liability of insured, (4) negligence, fraud, or bad faith, and (5) strength of insurer's defense).

49. 127 A. 708 (N.H. 1924).

50. *Douglas*, 127 A. at 712–13. In upholding the cause of action for negligent failure to settle, the *Douglas* court stated that "[t]he contrary holding involves the anomalous situation, where, as to settlement, the insurer has no duty and the insured has no rights." *Id.*; *see* G.A. Stowers Furniture Co. v. American Indem. Co., 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved) (contemplating harshness of rule that would allow insurer to disregard insured's interests in negligently failing to effect settlement); *cf.* McCombs v. Fidelity & Casualty Co., 89 S.W.2d 114, 118 (Mo. Ct. App. 1936) (asserting that insurer should not be allowed to escape responsibility for its negligent acts which result in harm to its insured); Joan B. Lefkowitz, *New York Third Party Bad Faith: Is It a Plaintiff's Dream or a Defendant's Nightmare?*, 12 PACE L. REV. 543, 563 (1992) (explaining particular effectiveness of negligence standard in promoting public interests); Beverly A. Neblett, Note, *Refusal to Settle Claim Below Policy Limits—Insurer's Excess Liability—Damages for Mental Suffering*, 22 SW. L.J. 374, 376–77 (1968) (contrasting due care standard with good faith standard). The *Douglas* court found that, even aside from questions of insurance, the contract's allocation of rights and powers gave rise to the special relationship and the duty of care. *Douglas*, 127 A. at 711; *see* Ballard v. Citizens Casualty Co., 196 F.2d 96, 102 (7th Cir. 1952) (adopting conception that insurance contract creates fiduciary relationship "with the resulting duties that grow out of such a relationship"); Barry Perlstein, *Crossing the Contract-Tort Boundary: An Economic Argument for the Imposition of Extracompensatory Damages for Opportunistic Breach of Contract*, 58 BROOK. L. REV. 877, 902–03 (1992) (discussing development of extra-contractual damages predicated upon recognition of special relationship); *see also* Maryland Casualty Co. v. Elmira Coal Co., 69 F.2d 616, 618 (8th Cir. 1934) (applying concept of insurer's duty to act in good faith, which flows from insurance contract by virtue of relationship between insurer and insured). *But cf.* Garden State Community Hosp. v. Watson, 465 A.2d 1225, 1226 (N.J. Super. Ct. App. Div. 1982) (refusing to find analogous special relationship within context of health or accident insurance contract). *See generally* Guy O. Kornblum, *The Current State of Bad Faith and Punitive Damage Litigation in the U.S.*, 23 TORT & INS. L.J. 812, 813–14 (1988) (finding jurisdictional roots of duty-to-settle doctrine in recognition of special relationship between insurer and insured).

51. *Douglas*, 127 A. at 711; *see* Traders & Gen. Ins. Co. v. Rudco Oil & Gas Co., 129 F.2d 621, 627 (10th Cir. 1942) (holding that public liability insurer's conduct, in acting as agent of its insured, will undergo heightened scrutiny when conflict of interest arises because of insurer's adverse interest); *see also* Weese v. Nationwide Ins. Co., 879 F.2d 115, 120 (4th Cir. 1989) (recognizing that bad faith tort rests on insurer's fiduciary duty to in-

Although bad faith entails a nominally greater burden than negligence, many courts coalesce the bad faith and negligence standards in practice and focus upon the amount of consideration given to the insured's interests.[52] Courts require insurers to give the insured's interests no consider-

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sured); McNally v. Nationwide Ins. Co., 815 F.2d 254, 265 (3d Cir. 1987) (stating that insurer was fiduciary from whose expertise insured could expect to benefit); Tannerfors v. American Fidelity Fire Ins. Co., 397 F. Supp. 141, 145 (D.N.J. 1975) (considering contractual reservation of control as giving rise to agency relationship and duty to settle in good faith), *aff'd*, 535 F.2d 1247 (3d Cir. 1976); United States Fire Ins. Co. v. Morrison Assurance Co., 600 So. 2d 1147, 1158 (Fla. Dist. Ct. App. 1992) (declaring that insurer is "an expert and a fiduciary" who must ascertain insured's best interests); Short v. Dairyland Ins. Co., 334 N.W.2d 384, 387 (Minn. 1983) (characterizing relationship between insurer and insured as fiduciary with corresponding duty to exercise good faith). *See generally* Eileen A. Scallen, *Promises Broken vs. Promises Betrayed: Metaphor, Analogy, and the New Fiduciary Principle*, 1993 U. ILL. L. REV. 897, 934 (discussing enhanced duties imposed upon insurers by virtue of fiduciary relationship); Robert M. Phillips, Comment, *Good Faith and Fair Dealing Under the Revised Uniform Partnership Act*, 64 U. COLO. L. REV. 1179, 1210 (1993) (discussing creation of quasi-fiduciary relationship between liability insurers and their insureds).

52. *See* Brown v. Guarantee Ins. Co., 319 P.2d 69, 75 (Cal. Dist. Ct. App. 1957) (noting tendency of contemporary cases indicating "coalescence of the bad faith and negligence tests"); Campbell v. State Farm Mut. Auto. Ins. Co., 840 P.2d 130, 138 n.16 (Utah App. 1992) (explaining tendency toward coalescence of negligence and different degrees of bad faith); ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.12, at 256-58 (1982) (asserting that, in practice if not in theory, most courts allow liability predicated on negligence). Professor Robert Keeton recognized a combination of good faith and negligence elements in one of the earliest cases imposing liability for failure to settle. *See* Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136, 1139 n.6 (1954) (analyzing *Hilker v. Western Automobile Insurance Co.*, 235 N.W. 413 (Wis. 1931) as containing mixed elements of negligence and bad faith); *see also* Jessen v. O'Daniel, 210 F. Supp. 317, 320 (D. Mont. 1962) (considering recovery for breach of duty to settle when insurer acted negligently or in bad faith), *aff'd*, 329 F.2d 60 (9th Cir. 1964); Thomas v. Lumbermens Mut. Casualty Co., 424 So. 2d 36, 38 (Fla. Dist. Ct. App. 1982) (considering negligence in determining whether insurer's conduct was in bad faith); United States Fidelity & Guar. Co. v. Evans, 156 S.E.2d 809, 811 (Ga. Ct. App. 1967) (stressing that difference between negligence and bad faith is merely semantical); Country Mut. Ins. Co. v. Anderson, 628 N.E.2d 499, 503 (Ill. App. Ct. 1993) (permitting recovery for breach of duty to settle when insurer acts fraudulently, in bad faith, or negligently); Rogers v. Government Employees Ins. Co., 598 So. 2d 670, 673 (La. Ct. App. 1992) (considering factors indicating negligence in determining whether insurer acted in bad faith); Commercial Union Ins. Co. v. Liberty Mut. Ins. Co., 393 N.W.2d 161, 164 (Mich. 1986) (distinguishing bad faith from negligence and fraud but advocating consideration of negligence); Eastham v. Oregon Auto Ins. Co., 542 P.2d 895, 895 (Or. 1975) (en banc) (stressing that little difference exists in application of negligence and bad faith standards). *But cf.* Texas Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 319 (Tex. 1994) (Cornyn, J., concurring) (suggesting that acceptance of bad faith standard would supplant negligence standard and result in increased burden of proof for insured). *See generally* Thomas B. Alleman, *The Reasonable Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured*, 50 UMKC L. REV. 251, 267 (1982) (noting elasticity of bad faith con-

ation,[53] paramount consideration,[54] or roughly equal consideration.[55]

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cept and listing cases applying standards between extremes of "arbitrary and capricious" standard and stringent duty); Ronald S. Range, Note, *The "Set Up" Defense and the Comparative Fault Defense: New Wrinkles in Bad Faith Claims Against Insurers*, 45 WASH. & LEE. L. REV. 321, 329 (1988) (concluding that courts have generally reached uniform decisions whether using bad faith or negligence standard).

53. *See, e.g.*, New Orleans & C.R. Co. v. Maryland Casualty Co., 38 So. 89, 91 (La. 1905) (indicating that, by express terms of contract, insurance company retained absolute right to compromise claim as it saw fit); St. Joseph Transfer & Storage Co. v. Employers' Indem. Corp., 23 S.W.2d 215, 220 (Mo. Ct. App. 1930) (stating that requiring insurer to consult insured's interests would pervert policy provisions giving insurer control of settlement); C. Schmidt & Sons Brewing Co. v. Travelers Ins. Co., 90 A. 653, 654 (Pa. 1914) (holding that plain words of policy dictate construction that insurer had no obligation to settle); G.A. Stowers Furniture Co. v. American Indem. Co., 295 S.W. 257, 261 (Tex. Civ. App.—Galveston 1927), *rev'd*, 15 S.W.2d 544 (Tex. Comm'n App. 1929, holding approved) (stating that indemnity company's sole duty was to "faithfully defend the suit"). *See generally* Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. MICH. J.L. REF. 1, 34 (1992) (tracing evolution of bad faith from early decisions grappling with problem of which standard of care to impose); Kevin F. Cox, Comment, *Insurance Bad Faith Refusal to Settle: What's an Insured to Do?*, 7 J.L. & COMM. 143, 145–46 (1987) (discussing early cases that did not require insurer to consider insured's interests).

54. Tyger River Pine Co. v. Maryland Casualty Co., 170 S.E. 346, 348 (S.C. 1933). In dissenting from language in a previous decision indicating that the insurer *may* consider the insured's interests, the court stated: "If, in the effort to [defend the insured], [the insurer's] own interests conflicted with those of respondent, it was duty bound, under its contract of indemnity, and in good faith, *to sacrifice its interests in favor of those of the respondent.*" *Id.*; *see* Maryland Casualty Co. v. Dixie Ins. Co., 622 So. 2d 698, 701 (La. Ct. App. 1993) (contending that "[t]he insurer is the champion of the insured's interests" and may not gamble with insured's funds); *Rogers*, 598 So. 2d at 672 (mandating elevation of insured's interests to level of paramount importance in determining whether to settle claim); Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136, 1142 (1954) (discussing divergent views concerning weight to be given insured's interests). *But see* Southern Gen. Ins. Co. v. Holt, 409 S.E.2d 852, 864 (Ga. Ct. App. 1991) (Andrews, J., concurring and dissenting) (criticizing majority for purportedly adopting standard that requires insurer to give insured's interests paramount importance). Taken literally, this "paramount interest" formulation appears to lead to a strict liability standard. *See* Timothy N. Brittle, *Avoiding Insurer's Excess Liability*, 28 FED'N INS. COUNS. Q. 298, 308–09 (1978) (discussing strict liability for failure to settle).

55. *Crisci*, 426 P.2d at 176–77; *see* Farmers Ins. Exch. v. Henderson, 313 P.2d 404, 406 (Ariz. 1957) (imposing rule of equality of consideration of insurer's and insureds' interests when insurer decides whether to settle); *Fulton*, 545 P.2d at 984 (assuming duty to give insured's interests equal consideration); *Gibson*, 682 P.2d at 730 (declaring that insurer must give insured's interests at least equal consideration); American Fidelity & Casualty Co. v. L.C. Jones Trucking Co., 321 P.2d 685, 687 (Okla. 1957) (noting "predominant majority rule" that insurer must give insured's interests same consideration); *Campbell*, 840 P.2d at 138 (requiring insurer to consider insured's interests at least equally with its own). *See generally* Robert E. Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136, 1146 (1954) (illustrating that equal weight standard is unsound if strictly applied because, when decision is made, one interest necessarily carries more

The more temperate formulation of at least equal consideration of the insured's interest requires insurers to act as a reasonably prudent insurer would if no policy limits applied to the claim.[56] To avoid unreasonably elevating the insurer's interests above the insured's, this model mandates settlement when a significant risk of an excess judgment exists.[57]

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weight); Beverly A. Neblett, Note, *Refusal to Settle Claim Below Policy Limits—Insurer's Excess Liability—Damages for Mental Suffering*, 22 Sw. L.J. 374, 380-82 (1968) (analyzing "triple impact" of *Crisci* in its effect on California good-faith law in general and recoverable damages and strict liability in particular).

56. Maine Bonding & Casualty Co. v. Centennial Ins. Co., 693 P.2d 1296, 1299 (Or. 1985); Tank v. State Farm Fire & Casualty Co., 686 P.2d 1127, 1131 (Wash. Ct. App. 1984); *see* Employers' Nat'l Ins. Corp. v. Zurich Am. Ins. Co., 792 F.2d 517, 519 (5th Cir. 1986) (suggesting that better view is to disregard conflicting interests and measure decision by standard of informed reasonable person ignoring policy limits); Bohemia, Inc. v. Home Ins. Co., 725 F.2d 506, 512 (9th Cir. 1984) (imposing duty to balance insured's interests in good faith "as if [insurer] were liable for any excess judgment"); Farmers Ins. Exch. v. Schropp, 567 P.2d 1359, 1364 (Kan. 1977) (phrasing duty in terms of "ordinary prudent person in the management of his own business, with no policy limits applicable to the claim"); ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.03, at 190 (1982) (preferring "disregard the limits" rule to rule requiring settlement demand within policy limits); Charles Silver, *A Missed Misalignment of Interests: A Comment on Syverúd*, The Duty to Settle, 77 VA. L. REV. 1585, 1588–89 (1991) (analyzing insurer's economic incentives in accepting settlement demands). A reasonably prudent insurer, considering policy limits, will not always act as would a sole holder of liability. Charles Silver, *A Missed Misalignment of Interests: A Comment on Syverúd*, The Duty to Settle, 77 VA. L. REV. 1585, 1588–89 (1991). This is so because the insurer will not consider any amount of an expected judgment that exceeds policy limits in calculating its expected trial losses, whereas a sole holder must fully consider the expected judgment on a potentially infinite scale. *Id.*; *cf.* KENNETH S. ABRAHAM, DISTRIBUTING RISKS 189-95 (1986) (postulating risk-distribution effects of holding insurers liable for excess judgments).

57. *See Crisci*, 426 P.2d at 177 (noting that rejection of settlement offer in such instances only favors insurer). Specifically, the *Crisci* court stated that

> the rejection of a settlement within the limits where there is any danger of a judgment in excess of the limits can be justified, if [at] all, only on the basis of interests of the insurer. . . . [A]n insurer should not be permitted to further its own interests by rejecting opportunities to settle within the policy limits unless it is also willing to absorb losses which may result from its failure to settle.

Id.; *see* Neil A. Goldberg et al., *Can the Puzzle Be Solved: Are Punitive Damages Awardable in New York for First-Party Bad Faith?*, 44 SYRACUSE L. REV. 723, 727 n.13 (1993) (noting dictum in *Crisci* that appears to advocate strict liability standard); *see also Fulton*, 545 P.2d at 984 (requiring insurer to initiate settlement negotiations when "there is a high potential of claimant recovery and a high potential of damages exceeding policy limits"); *Lysick*, 65 Cal. Rptr. at 414-15 (affirming rule that insured must settle claim when great risk of excess judgment is present); *Kelley*, 34 Cal. Rptr. at 568 (insisting that insurer may not sacrifice insured's interests in considering its own); *cf. Smith*, 791 P.2d at 1346 (stating that insurer, in settling or defending claims, must act in insured's best interests). *See generally* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1122 (1990) (explaining that Professor Keeton's disregard-the-limits standard received its most significant endorsement in *Crisci*).

Prior to *American Physicians Insurance Exchange v. Garcia*,[58] the Texas duty-to-settle doctrine appeared to be evolving in line with the jurisdictions employing a more expansive duty to settle.[59] In 1929, the Supreme Court of Texas first recognized a liability insurer's duty to settle in *G.A. Stowers Furniture Co. v. American Indemnity Co.*[60] In *Stowers*, the indemnity company claimed that it had a contractual option "of settling or defending the suit as it might deem best" and that it had no duty to accept a settlement offer for $1,000 less than the policy limits.[61] Per-

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58. 876 S.W.2d 842 (Tex. 1994).

59. *See* Cherry D. Williams, *A New Twist in Insurance Litigation*: Stowers *Suits by Excess Carriers Against Primary Carriers*, 33 S. TEX. L.J. 1, 8–11 (1992) (tracing evolution of Texas duty-to-settle law from *Stowers* to *Ranger County Mutual Insurance Co. v. Guin*). *Compare* American Centennial Ins. Co. v. Canal Ins. Co., 843 S.W.2d 480, 482 (Tex. 1992) (acknowledging that insurer's duty to "act as an ordinarily prudent person in business management extends to claim investigation, trial defense and settlement negotiations") *and* Chancey v. New Amsterdam Casualty Co., 336 S.W.2d 763, 765 (Tex. Civ. App.—Amarillo 1960, writ ref'd n.r.e.) (stating that duty to settle encompasses duty to negotiate because "[i]t is difficult to see how any controversy could be settled without some measure of negotiation") *with* Rova Farms Resort, Inc. v. Investors Ins. Co., 323 A.2d 495, 507 (N.J. 1974) (imposing duty to exercise good faith throughout duration of claim whether or not claimant made offer to settle) *and* State Auto. Ins. Co. v. Rowland, 427 S.W.2d 30, 35 (Tenn. 1968) (imposing upon insurer duty to negotiate despite absence of settlement offer within policy limits). *See generally* Beverly A. Neblett, Note, *Refusal to Settle Claim Below Policy Limits—Insurer's Excess Liability—Damages for Mental Suffering*, 22 Sw. L.J. 374, 376–79 (1968) (comparing Texas duty-to-settle doctrine with California bad faith law).

60. G.A. Stowers Furniture Co. v. American Indem. Co., 15 S.W.2d 544, 548 (Tex. Comm'n App. 1929, holding approved); *see* Note, 8 TEX. L. REV. 151, 152 (1930) (contrasting new Texas standard with traditional contract doctrine and similar duty-to-settle standards elsewhere). The Texas Commission of Appeals adopted a negligence standard based on an "ordinarily prudent person . . . in the management of his own business." *Stowers*, 15 S.W.2d at 547; *see* Highway Ins. Underwriters v. Lufkin-Beaumont Motor Coaches, Inc., 215 S.W.2d 904, 931 (Tex. Civ. App.—Beaumont 1948, writ ref'd n.r.e.) (distinguishing Texas standard based upon negligence and other standards based upon bad faith); *cf.* Seguros Tepeyac, S.A. v. Jernigan, 410 F.2d 718, 722–26 (5th Cir. 1969) (discussing now-obsolete rule requiring insured to pay excess judgment before proceeding with *Stowers* suit against insurer). *See generally* R. Kent Livesay, Comment, *Levelling the Playing Field of Insurance Agreements in Texas: Adopting Comparative Bad Faith as an Affirmative Defense Based on the Insured's Misconduct*, 24 TEX. TECH. L. REV. 1201, 1204–07 (1993) (analyzing development of bad faith in Texas from third-party to first-party context); Kelly H. Thompson, Comment, *Bad Faith: Limiting Insurers' Extra-Contractual Liability in Texas*, 41 Sw. L.J. 719, 722-26 (1987) (discussing development of third-party bad faith in Texas and implications of Texas Insurance Code provisions defining unfair claim settlement practices).

61. *Stowers*, 15 S.W.2d at 545. The underlying litigation in *Stowers* arose from an accident that occurred when the car in which the plaintiff was riding collided with an unattended furniture truck, which an employee of the furniture company abandoned in the street. *Id.* Originally, the plaintiff sought $20,000 from the furniture company even though the indemnity policy limit was $5,000. *Id.* Before trial, the plaintiff offered to settle for $4,000, but the indemnity company refused to pay more than $2,500. *Id.*

suaded by the reasoning in *Douglas*, the court held that the special relationship created by a liability insurance policy requires the insurer to exercise ordinary care in determining whether to settle a third-party claim.[62] The court reasoned that the liability insurer assumes the position of the insured's exclusive agent for litigation purposes and, accordingly, must exercise ordinary care to protect the insured within the policy limits.[63] Subsequent to the *Stowers* decision, Texas courts recognized an implied duty to negotiate under the *Stowers* doctrine[64] and provided broad

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62. *Stowers*, 15 S.W.2d at 547. In adopting a clear negligence standard not expressly limited to responding to settlement offers, the court stated:

> The provisions of the policy giving the indemnity company absolute and complete control of the litigation, as a matter of law, carried with it a corresponding duty and obligation, on the part of the indemnity company, to exercise that degree of care that a person of ordinary care and prudence would exercise under the same or similar circumstances, and a failure to exercise such care and prudence would be negligence on the part of the indemnity company.

Id. Compare Georgetown Realty, Inc. v. Home Ins. Co., 831 P.2d 7, 14 (Or. 1992) (articulating appropriate standard for determining breach of insurer's duty to settle as one of negligence) *with* Stroman v. Fidelity & Casualty, 792 S.W.2d 257, 260 (Tex. App.—Austin 1990, writ denied) (reaffirming *Stowers* duty as obligation to exercise care of ordinarily prudent businessperson); *see also* McCombs v. Fidelity & Casualty Co., 89 S.W.2d 114, 120-21 (Mo. Ct. App. 1935) (comparing Texas's newly created *Stowers* duty with similar duties imposed in other jurisdictions); R. Kent Livesay, Comment, *Levelling the Playing Field of Insurance Agreements in Texas: Adopting Comparative Bad Faith as an Affirmative Defense Based on the Insured's Misconduct*, 24 TEX. TECH. L. REV. 1201, 1208 (1993) (arguing for inverse application of *Stowers* doctrine to address insureds' misconduct); Note, 8 TEX. L. REV. 151, 151–52 (1930) (discussing *Stowers* decision within context of early law regarding expansion of contract remedies). Evidently, some uncertainty remains concerning whether an insured may sue for bad faith, as opposed to negligent, failure to settle. *See* Texas Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 319 (Tex. 1994) (Cornyn, J., dissenting) (appealing for rejection of bad faith standard in Texas and affirmation of negligence standard as sole recourse for insured when insurer refuses to settle).

63. *Stowers*, 15 S.W.2d at 547. The insurer's duty to settle does not arise unless a third party claims damages in excess of the insured's policy limits. *Id.*; *see* Westchester Fire Ins. Co. v. Rhoades, 405 S.W.2d 812, 819 (Tex. Civ. App.—Austin 1966, writ ref'd n.r.e.) (holding that insurer's *Stowers* duty to negotiate settlement in good faith did not apply because damages claimed did not exceed policy limits).

64. *Chancey*, 336 S.W.2d at 765; *see* Ranger County Mut. Ins. Co. v. Guin, 723 S.W.2d 656, 659 (Tex. 1987) (including duty to enter into reasonable settlement negotiations within duty to settle); Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 544 (1981) (citing *Chancey* in discussion of coexistent duties to settle and negotiate, latter of which renders claimant's within-limits settlement demand unnecessary to finding of bad faith); *see also* Wood Truck Leasing, Inc. v. American Auto. Ins. Co., 526 S.W.2d 223, 225 (Tex. Civ. App.—San Antonio 1975, no writ) (reversing summary judgment for determination of whether insurer settled in bad faith by making negligent investigation); Pattison v. Highway Ins. Underwriters, 278 S.W.2d 207, 211 (Tex. Civ. App.—Galveston 1955, writ ref'd n.r.e.) (noting that insurer has exclusive right to negotiate settlements); *cf.* Robert E. Keeton, *Liability Insurance and Reciprocal Claims from a*

guidelines for determining whether a negligent breach of the duty to settle had occurred.[65] However, in 1987, the Supreme Court of Texas revisited and revised the *Stowers* doctrine in *Ranger County Mutual Insurance Co. v. Guin*,[66] extending the duty to settle "to the full range of the agency relationship."[67] The court eschewed an argument that an offer to settle

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Single Accident, 10 Sw. L.J. 1, 2–3 (1956) (discussing liability insurer's ordinarily unfettered right to settle).

65. Globe Indem. Co. v. Gen-Aero, Inc., 459 S.W.2d 205, 208 (Tex. Civ. App.—San Antonio 1970, writ ref'd n.r.e.). In rejecting the insurer's argument that it received no unconditional offer to settle, the San Antonio Court of Civil Appeals approved consideration of the following factors in determining negligence:

(A) An opportunity to settle during the course of investigation or trial.

(B) Failure to carry on negotiations to settle or make a counter offer after receipt of an offer to settle.

(C) Failure to investigate all the facts necessary to protect properly the insured against liability.

(D) Question of liability—if liability is clear, greater duty to settle may exist.

(E) Element of good faith—whether insurer acts negligently, fraudulently, or in bad faith.

(F) If there are conflicts in evidence which increase the uncertainty of the insured's defense to the injured party's claim, the possibility of the insurer being held negligent increases.

Id. (citations omitted); *see* Howard Nations, *Excess Liability Damages: The* Stowers *Doctrine*, 18 S. TEX. L.J. 465, 465 (1977) (discussing *Globe* factors and noting that Texas courts also consider (1) insured's failure to give proper notice, (2) whether offer was unconditional, (3) whether insured demanded acceptance, and (4) competence of insurer's counsel); *cf.* Pruett v. Farmers Ins. Co., 857 P.2d 1301, 1305-06 (Ariz. Ct. App. 1993) (listing factors to be considered in determining insurer's bad faith failure to settle); Commercial Union Ins. Co. v. Liberty Mut. Ins. Co., 393 N.W.2d 161, 164 (Mich. 1986) (enumerating factors relevant to bad faith analysis including failure to solicit offer or attempt settlement negotiations). Prior to *Globe*, courts recognized that the duty to evaluate and investigate fell upon the insurer and could not be satisfied by good faith reliance on retained counsel's opinions. *See Lufkin-Beaumont Motor Coaches*, 215 S.W.2d at 928 (stating that good faith judgment of insurer's agents was immaterial to question of insurer's liability for negligent failure to settle); W. James Kronzer, *The Present Status of the* Stowers *Doctrine in Texas*, 1 S. TEX. L.J. 167–74 (1954) (tracing development of *Stowers* doctrine through *Lufkin-Beaumont Motor Coaches* decision).

66. 723 S.W.2d 656 (Tex. 1987).

67. *Guin*, 723 S.W.2d at 659; *see American Centennial Ins. Co.*, 843 S.W.2d at 482 (noting that *Stowers* duty of reasonable care extends to investigation and settlement negotiations); Emscor Mfg., Inc. v. Alliance Ins. Group, 879 S.W.2d 894, 909 (Tex. App.—Houston [14th Dist.] 1994, n.w.h.) (describing insurer's duty to settle after *Guin* as extending to all aspects of agency relationship); C. Michael Moore & David P. Blanke, *Ethics in the Settlement Process* (discussing significance of *Guin* in extending insurers' duty to settle), *in* STATE BAR OF TEXAS, EVALUATING AND SETTLING INSURANCE CLAIMS B-27 (1987); *c.f.* Fidelity & Casualty Co. v. Robb, 267 F.2d 473, 479 (5th Cir. 1959) (affirming judgment on jury finding that insurer was negligent in failing to initiate settlement after initial offer had lapsed); *Rova Farms*, 323 A.2d at 507 (extending insurer's duty to negotiations). *See generally* Randy Papetti, Note, *The Insurer's Duty of Good Faith in the Context of Litigation*, 60

within policy limits is a necessary prerequisite to a *Stowers* breach, holding instead that the *Stowers* duty extends to investigation, preparation for defense, trial, and reasonable attempts at settlement.[68]

Currently, much debate in duty-to-settle cases centers on determining the point at which the parties' interests diverge such that the insurer may be held liable for failing to guard those of its insured.[69] Historically, many courts have recognized a conflict of interest arising only upon the third-party claimant's offer to settle within policy limits.[70] For example,

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GEO. WASH. L. REV. 1931, 1933–34 (1992) (asserting that "ultimate inquiry" in bad-faith cases is reasonableness of insurer's actions).

68. *Guin*, 723 S.W.2d at 659; *see* Michael K. Clann et al., *Judicial Interpretation of Insurance Contracts in Maritime Law: The Duty of Good Faith in Handling Claims*, 66 TUL. L. REV. 479, 495 nn.86, 87 (1991) (citing *Guin* for proposition that insurer may be held liable for negligent failure to settle if claimant makes reasonable offer, whether offer is conditional or exceeds policy limits); *cf. Commercial Union Ins. Co.*, 393 N.W.2d at 165 (indicating that bad faith liability may be predicated on failure to attempt settlement or solicit offers from claimant); *Rova Farms*, 323 A.2d at 507 (stating that insurer must attempt settlement when fiduciary duty so requires); Shearer v. Reed, 428 A.2d 635, 638 (Pa. Super. Ct. 1981) (affirming bad faith judgment in which insurer refused to actively pursue settlement); *Rowland*, 427 S.W.2d at 35 (imposing duty to make counteroffers or actively pursue settlement on insured's behalf). For an early analysis of Texas law advocating adoption of a strict liability standard, see Beverly A. Neblett, Note, *Refusal to Settle Claim Below Policy Limits—Insurer's Excess Liability—Damages for Mental Suffering*, 22 Sw. L.J. 374, 383 (1968) (suggesting that strict liability rule would adequately protect insureds' interests when then-current law may not).

69. *Compare* Merritt v. Reserve Ins. Co., 110 Cal. Rptr. 511, 518 (Ct. App. 1973) (noting conflict of interest that arises upon settlement offer within policy limits and creates duty to exercise good faith) *and* United States Fidelity & Guar. Co. v. Copfer, 400 N.E.2d 298, 298 (N.Y. 1979) (precluding recovery by insured absent showing that "actual opportunity to settle" was lost because of insured's bad faith) *with* Powell v. Prudential Prop. & Casualty Ins. Co., 584 So. 2d 12, 14 (Fla. Ct. App. 1991) (rejecting assertion that offer to settle necessarily precedes duty to exercise good faith) *and* Rector v. Husted, 519 P.2d 634, 642 (Kan. 1974) (requiring insurer to make reasonable effort to settle notwithstanding offers received). Some courts allow the insured to recover upon proof that the insurer rejected an offer within policy limits *or* otherwise failed, in bad faith, to effect a settlement within limits when such settlement was possible. *See, e.g.*, Cotton States Mut. Ins. Co. v. Fields, 128 S.E.2d 358, 359 (Ga. Ct. App. 1962) (suggesting that either settlement offer from claimant or evidence that claim could otherwise be settled precedes liability for bad faith). *See generally* Thomas B. Alleman, *The Reasonable Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured*, 50 UMKC L. REV. 251, 253 (1982) (discussing courts' failure to agree on much of anything other than that insurers must afford insured's interests some consideration); Willy E. Rice, *Judicial Bias, The Insurance Industry and Consumer Protection: An Empirical Analysis of State Supreme Courts' Bad-Faith, Breach-of-Contract, Breach-of-Covenant-of-Good-Faith and Excess Judgment Decisions, 1900-1991*, 41 CATH. U. L. REV. 325, 333 (1993) (discussing inconsistent application of rules imposing extra-contractual obligations upon insurers).

70. *See, e.g.*, Manchester Ins. & Indem. Co. v. Grundy, 531 S.W.2d 493, 496 (Ky. Ct. App. 1975) (suggesting that conflict of interest becomes apparent when claimant offers to

in *Merritt v. Reserve Insurance Co.*,[71] the California Court of Appeal concluded that, a claim seeking damages above policy limits does not, in itself, create a conflict of interest between insurer and insured.[72] The *Merritt* court reasoned that, before any settlement offer is tendered, the insured's and insurer's interests are parallel, thus avoiding the "good faith" dilemma.[73] An increasing number of courts, however, currently

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settle suit for damages in excess of policy limits); *Shearer*, 428 A.2d at 639 (recognizing "inherent conflict of interest . . . once an offer to settle within policy limits has been received"); *see also* Bush v. Allstate Ins. Co., 425 F.2d 393, 396 (5th Cir. 1970) (interpreting Florida law as requiring settlement demand within policy limits), *cert. denied*, 400 U.S. 833; Van Vleck v. Ohio Casualty Ins. Co., 471 N.E.2d 925, 928 (Ill. App. Ct. 1984) (holding that insured failed to state claim when insurer did not receive within-limits settlement demand); Kriz v. Government Employees Ins. Co., 600 P.2d 496, 501 (Or. Ct. App. 1979) (indicating necessity of offer within policy limits before liability may be imposed); ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.02, at 235 n.15 (1982) (listing cases requiring settlement offer from claimant before imposing liability for breach of duty to settle). *See generally* David Pomerantz, Comment, *The Insurer's Exploding Bottle: Moving From Good Faith to Strict Liability in Third and First Party Actions*, 46 OHIO ST. L.J. 157, 162 n.40 (1987) (discussing insured's additional option of proving that insurer failed to settle for amount above policy limits, excess of which insured would have paid).

71. 110 Cal. Rptr. 511 (Ct. App. 1974).

72. *Merritt*, 110 Cal. Rptr. at 518; *see Bush*, 425 F.2d at 396 (stating that liability in excess of policy limits will not obtain in absence of settlement offer from within-limits claimant); *Van Vleck*, 471 N.E.2d at 928 (suggesting that insurer need not consider insured's interests until claimant makes offer to settle within policy limits); *see also* Clinton R. Ashford, Comment, *Insurance: Liability of Insurer for Judgment in Excess of Policy Limits*, 48 MICH. L. REV. 95, 100–03 (1949) (analyzing discordant application of rules regarding insurers' duty of care). *But see* Smith v. Blackwell, 791 P.2d 1343, 1346 (Kan. Ct. App. 1989) (requiring insurer, by virtue of its fiduciary relationship with insured, to initiate settlement negotiations although claimant has made no demand). *See generally* Thomas B. Alleman, *The Reasonable Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured*, 50 UMKC L. REV. 251, 261-63 (1982) (explaining that interests of insurer and insured diverge whenever claim seeks damages in excess of insured's coverage).

73. *Merritt*, 110 Cal. Rptr. at 518. The court illustrated its reasoning by way of an example in which the insurer's and insured's interests diverged only upon the claimant's settlement offer. *Id.* at 518–19. The example is faulty, however, because it ignores the insured's ever-present interest in disposing of the claim within policy limits regardless of whether the claimant has offered to settle. *See* Farmers Ins. Exch. v. Schropp, 567 P.2d 1359, 1366 (Kan. 1977) (contending that duty to balance interests arises not from claimant's offer, but from claim seeking damages above policy limits); *Rova Farms*, 323 A.2d at 504 (recognizing conflict of interest arising notwithstanding any settlement demand either above or below policy limits); Douglas L. Getter, Note, *Standard of Care in Malpractice Actions Against Insurance Defense Counsel: Inapplicability of the Code of Professional Responsibility*, 51 FORDHAM L. REV. 1317, 1318–19 (1983) (recognizing inherent conflict of interest between insurer and insured arising when third-party claims damages in excess of policy limits); *see also* Fulton v. Woodford, 545 P.2d 979, 984 (Ariz. Ct. App. 1976) (holding that conflict of interest may require insurer to consider insured's interests equally when great risk of excess judgment exists). *See generally* Thomas B. Alleman, *The Reasonable*

recognize a latent conflict of interest whenever a third-party claimant asserts damages exceeding policy limits.[74] These courts refuse to exonerate an insurer simply because the insured did not make a demand for settlement within policy limits.[75] Because of the special relationship between insurer and insured,[76] the "'insurer has an affirmative duty to explore

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Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured, 50 UMKC L. REV. 251, 262 (1982) (intimating difficulties in harmonizing conflict-of-interest approach with realities of insurer-insured relationship); Alan O. Stykes, *"Bad Faith" Refusal to Settle by Liability Insurers: Some Implications of the Judgment-Proof Problem*, 23 J. LEGAL STUD. 77, 89-94 (1994) (analyzing implications of alternatively formulating insurer's obligation to consider insured's interests).

74. *See, e.g.*, *Rova Farms*, 323 A.2d at 504 (stating that conflict of interest existed even in absence of settlement offer); *Rowland*, 427 S.W.2d at 34 (rejecting argument that conflict of interest existed only upon tender of within-limits settlement demand); *see also* ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.02, at 190-91 (1982) (asserting that absence of offer to settle within limits should be but one factor considered in finding causation); Darrell Waas, Comment, *Expanding the Insurer's Duty to Attempt Settlement*, 49 U. COLO. L. REV. 251, 259 (1978) (stating that recent trend appears to favor view that conflict arises because of claim, not settlement offer). Other courts implicitly recognize an inherent conflict of interest by imposing an affirmative duty to attempt settlement. *See, e.g.*, Puritan Ins. Co. v. Canadian Universal Ins. Co., 586 F. Supp. 84, 87 (E.D. Pa. 1984) (approving imposition of affirmative duty to attempt settlement), *rev'd*, 775 F.2d 76 (3d Cir. 1985); *Powell*, 584 So. 2d at 14 (stating that when excess damages beyond policy limits are probable, insurer has "affirmative duty to initiate settlement negotiations"); *see also* Zidan v. USAA Property & Casualty Ins. Co., 622 So. 2d 265, 267 (La. Ct. App. 1993) (suggesting that insurer has affirmative duty to make effort to settle first-and third-party claims); Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 544 (1981) (advocating imposition of duty on insurer to negotiate, which is inseparable from duty to settle).

75. Bohemia, Inc. v. Home Ins. Co., 725 F.2d 506, 512 (9th Cir. 1984); Coleman v. Holecek, 542 F.2d 532, 537 (10th Cir. 1976); *Schropp*, 567 P.2d at 1366; *Rova Farms*, 323 A.2d at 505; Spray v. Continental Casualty Co., 739 P.2d 40, 44 (Or. Ct. App. 1987); *Guin*, 723 S.W.2d at 659; Alt v. American Family Mut. Ins. Co., 237 N.W.2d 706, 715 (Wis. 1976). *See generally* Neil A. Goldberg et al., *Can the Puzzle Be Solved: Are Punitive Damages Awardable in New York for First-Party Bad Faith?*, 44 SYRACUSE L. REV. 723, 725 n.5 (1993) (noting common third-party bad faith claims involving insurers' failure to "create or seize" opportunities to settle); Randy Papetti, Note, *The Insurer's Duty of Good Faith in the Context of Litigation*, 60 GEO. WASH. L. REV. 1931, 1935–36 (1992) (discussing origins of good faith standard in Wisconsin and its expansion beyond third-party context).

76. *Alt*, 237 N.W.2d at 711; *see* Disalvatore v. Aetna Casualty & Sur. Co., 624 F. Supp. 541, 544 (D.N.J. 1986) (recognizing fiduciary relationship in third-party cases not necessarily present in first-party context); Moskau v. Insurance Co. of N. Am., 366 So. 2d 1004, 1006 (La. Ct. App. 1978) (stating that insurer must give insured's interest paramount consideration); Thompson v. State Farm Mut. Auto. Ins. Co., 505 P.2d 423, 428 (Mont. 1973) (asserting that liability insurance policy places fiduciary obligation on insurer); Myers v. Ambassador Ins. Co., 508 A.2d 689, 691 (Vt. 1986) (noting fiduciary relationship between insured and insurer); Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Stat-*

settlement possibilities'" when excess liability is probable.[77] Thus, insurers, vested with exclusive control of the case, cannot avoid the duty to settle simply because an offer is not legally binding as tendered.[78]

Writing on behalf of a five to four majority,[79] Justice Cornyn effected an apparent retreat from the Texas Supreme Court's previous conception of the *Stowers* doctrine in *American Physicians Insurance Exchange v. Garcia*.[80] Justice Cornyn established three prerequisites to activation of

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ute, 26 U. MICH. J.L. REF. 1, 34-35 (1992) (stating that number of courts saw relationship between insurer and insured as fiduciary in essence); *see also* Sanner v. Government Employees Ins. Co., 376 A.2d 180, 184 (N.J. Super. Ct. App. Div. 1977) (permitting excess insurer to enjoy benefit of fiduciary relationship between insurer and insured), *aff'd*, 383 A.2d 429 (N.J. 1978). *See generally* Eileen A. Scallen, *Promises Broken vs. Promises Betrayed: Metaphor, Analogy, and the New Fiduciary Principle*, 1993 U. ILL. L. REV. 897, 934 (analyzing cases in which courts found fiduciary relationship to be fact-specific inquiry rather than dogmatic). From the inception of the Texas duty-to-settle doctrine, Texas courts have held that liability insurance contracts create an agency relationship between insurer and insured. *See Stowers*, 15 S.W.2d at 548 (stating that indemnity insurer becomes agent of insured for litigation purposes). The duty to exercise reasonable care extends "to the full range of the agency relationship." *Guin*, 723 S.W.2d at 659.

77. *Alt*, 237 N.W.2d at 713 (quoting *Rova Farms*, 323 A.2d at 505); *see* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1167 (1990) (commenting on courts' response to manipulative insurer conduct with duty to initiate settlement attempts). Having contractually restricted the insured's right to negotiate, the insurer must take charge and attempt to effect a settlement within its policy limits. *Puritan Ins. Co.*, 586 F. Supp. at 87; *Schropp*, 567 P.2d at 1365; *Rova Farms*, 323 A.2d at 507; *Spray*, 739 P.2d at 43. *See generally* Thomas B. Alleman, *The Reasonable Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured*, 50 UMKC L. REV. 251, 252 (1982) (asserting that "the interests of insured and insurer diverge sharply" when claim against insured seeks damages in excess of policy limits).

78. *Alt*, 237 N.W.2d at 712; *see Guin*, 723 S.W.2d at 659 (holding insurer liable for failure to exercise reasonable care in controlling settlement decisions in spite of settlement offer's alleged defects); *see also* Baker v. Northwestern Nat. Casualty Co., 132 N.W.2d 493, 497 (Wis. 1965) (holding that insurer must remain ready to settle though only offers made may be frivolous or jocular); Note, *Control of Settlement and Litigation by Liability Insurers*, 34 COLUM. L. REV. 511, 511–12 (1934) (recognizing inherent conflicts of interest in liability insurance relationship). *But see* Henke v. Iowa Home Mut. Casualty Co., 97 N.W.2d 168, 173 (Iowa 1959) (refusing to attach liability for failure to settle when claimant's offer was conditional). In jurisdictions that require a settlement offer to trigger a duty to settle, "hiding" behind a conditional offer may nonetheless be unwise. *See* Lloyd E. Williams, Jr. & Donald V. Jernberg, *Conflicts of Interest in Insurance Defense Litigation: Common Sense in Changing Times*, 31 FED'N INS. COUNS. Q. 111, 121 (1981) (discussing prudent course of action for defense counsel or insurers).

79. American Physicians Ins. Exch. v. Garcia, 876 S.W.2d 842, 843, 855 (Tex. 1994). Chief Justice Phillips and Justices Gonzalez, Hecht, and Enoch joined Justice Cornyn's majority opinion. *Id.* at 843. Justices Doggett, Gammage, and Spector joined Justice Hightower in dissent. *Id.* at 855.

80. *See id.* at 849 (asserting that *Stowers* duty does not arise until claimant tenders settlement demand within policy limits).

an insurer's *Stowers* duty: (1) the claim against the insured must fall within the scope of policy coverage; (2) there must be a demand for settlement within policy limits; and (3) the terms of the settlement offer must be such as "an ordinarily prudent insurer would accept, considering the likelihood and degree of the insured's potential exposure to an excess judgment."[81] Justice Cornyn reasoned that the Cardenases' failure to allege malpractice within APIE's policy period until their sixth amended petition gave rise to APIE's *Stowers* duty, if at all, only after that petition was filed.[82] The Cardenases' settlement offer of $1,600,000 constituted the sole offer tendered after the sixth amended petition; thus, the previous offers of $600,000 and $1,100,000 did not trigger any *Stowers* duty.[83] Justice Cornyn then asserted that the $1,600,000 offer, albeit reasonable, did not trigger APIE's *Stowers* duty because it exceeded APIE's $500,000 policy limit.[84] The $1,600,000 offer would have triggered a duty to settle only if the APIE and ICA policies could be stacked; however, Justice Cornyn decided that they could not.[85]

In addressing the apparent conflict with *Ranger County Mutual Insurance Co. v. Guin*, Justice Cornyn asserted that the "reasonable attempts to settle" language in *Guin* did not alter an insurer's underlying duty to settle.[86] Although he recognized the adversarial nature of settlement negotiations, Justice Cornyn stated that insurers owe no duty to make or solicit settlement offers.[87] Any consideration of investigation, defense, and conduct during negotiations is, according to Justice Cornyn, subsidiary to the issue of the reasonableness of the claimant's demand.[88] Justice Cornyn labeled the "reasonable attempts to settle" language of *Guin* as

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81. *Id.* The significance of Justice Cornyn's three prerequisites lies in the way the majority rephrased the *Stowers* duty as contingent upon the claimant's settlement demand. *See id.* at 865 (Hightower, J., dissenting) (criticizing majority for its "formalistic" approach).

82. *Garcia*, 876 S.W.2d at 848. Justice Cornyn noted that insurers generally are not required to settle claims falling outside the scope of coverage. *Id.* (citing Western Heritage Ins. Co. v. River Entertainment, 998 F.2d 311, 312 (5th Cir. 1993)).

83. *Id.* at 853.

84. *See id.* at 849 (stating that demands above policy limits do not trigger *Stowers* duty even if reasonable). Justice Cornyn reasoned that an insurer has no duty to accept demands above policy limits because liability policies set contractual limits on the insurer's obligation to indemnify. *Id.* at 849 n.13.

85. *Id.* at 853. In deciding that the policies could not be stacked, Justice Cornyn noted that the contrary holding would assume that Dr. Garcia bought three times the coverage than he actually paid for. *Id.* at 854.

86. *Garcia*, 876 S.W.2d at 849.

87. *Id.* Justice Cornyn reasoned that requiring an insurer to make reasonable attempts to settle would afford insurers no protection from *Stowers* suits unless the insurer tendered its policy limits. *Id.* at 850.

88. *Id.* at 849.

dictum, but nonetheless conceded that a formal demand is not an absolute prerequisite for insurer liability predicated on something other than a *Stowers* breach.[89] Justice Cornyn asserted, however, that the "*Stowers* remedy of shifting the risk of an excess judgment onto the insurer is inappropriate absent proof that the insurer was presented with a reasonable opportunity to prevent the excess judgment by settling within the applicable policy limits."[90] Justice Cornyn reasoned that, because an insurer can not be certain of the reasonableness of any action short of offering policy limits until after a subsequent *Stowers* trial, imposing an affirmative duty to attempt settlement would, in effect, shift the burden of making settlement offers and require the insurer to bid against itself.[91] Justice Cornyn concluded that requiring a settlement offer within policy limits before invoking *Stowers* would encourage earlier settlements by providing third-party claimants with an incentive to tender a within-limits offer as early as possible.[92]

In dissent, Justice Hightower lambasted the majority opinion on a number of fronts.[93] Justice Hightower's primary critique concerned the court's insistence on a formal settlement demand within policy limits.[94] Justice Hightower argued that APIE created a duty to settle before the Cardenases' sixth amended petition by assuming Dr. Garcia's defense, by failing to act to determine whether Dr. Garcia actually had coverage, and by providing unconditional coverage for sixteen months.[95] Noting that

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89. *See id.* (interpreting *Guin* language as dictum because that case concerned only negligent *Stowers* breach, not allegation that insurer was negligent in trial or in investigation of claim).

90. *Garcia*, 876 S.W.2d at 849. Justice Cornyn found that APIE had no reasonable opportunity to settle during the 16 months between filing and trial or at any time after trial commenced. *See id.* at 849–50 (contending that APIE clearly had no opportunity to settle claim because all of Cardenases' settlement offers exceeded $500,000).

91. *Id.* at 850–51.

92. *Id.* at 851 n.18. According to Justice Cornyn, the new rule would benefit claimants who tender early policy-limits demands by potentially increasing the capital available to satisfy any excess judgment. *Id.* Justice Cornyn also asserted that the rule would promote early settlements by forcing the insurer to act on early settlement demands. *Id.*

93. *Garcia*, 876 S.W.2d at 855 (Hightower, J., dissenting). Although he agreed that APIE fulfilled its duty to defend, Justice Hightower criticized the majority for dodging the covenant not to execute issue, ignoring APIE's "reprehensible handling" of Dr. Garcia's case, and characterizing the case as solely based on the *Stowers* doctrine. *Id.*

94. *Id.* at 865. Justice Hightower recently restated his objection to the majority's insistence on a settlement demand prior to invoking the *Stowers* duty. *See* Texas Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 318 (Tex. 1994) (Hightower, J., concurring) (disagreeing with majority's "requirement of a formal settlement demand within policy limits").

95. *Garcia*, 876 S.W.2d at 866 (Hightower, J., dissenting). Justice Hightower noted that APIE was aware of the likelihood of an excess judgment and failed to take action to determine Dr. Garcia's coverage. *Id.* at 865–67.

the Cardenases' attorney attempted to settle for what he believed to be the policy limits, Justice Hightower sharply criticized the majority's assertion that "APIE never had an opportunity to settle for its policy limits."[96] Characterizing the assertion as outrageous, Justice Hightower found that APIE made no reasonable or unreasonable attempt to settle at any time before or during trial.[97] In any event, Justice Hightower maintained, APIE had an affirmative duty to pursue settlement negotiations following the sixth amended petition, which APIE did nothing to discharge.[98] In attacking the majority's insistence on a formal demand within policy limits, Justice Hightower warned that an insurer could now do absolutely nothing toward facilitating settlement and still not breach its duty to the insured.[99] Finding this result unreasonable, Justice Hightower referred to other jurisdictions that have construed the duty to settle as involving an affirmative duty to explore settlement possibilities.[100] Citing *Guin*, Justice Hightower concluded that imposing a duty to act as an "ordinarily prudent person in business management in making reasonable attempts to settle" would promote early settlements.[101]

In *American Physicians Insurance Exchange v. Garcia*, the Supreme Court of Texas clarified crucial aspects of the *Stowers* doctrine, but left other important issues unaddressed.[102] For example, the court clarified

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96. *Id.* at 865.

97. *Id.* Justice Hightower sharply criticized the majority for remaining "fixated on the requirement of a settlement demand within policy limits." *Id.* Justice Hightower further asserted that requiring reasonable attempts to settle would not force insurers to make initial settlement offers, bid against themselves, make unilateral offers, or tender the policy limits in every case with potential for an excess judgment. *Id.* at 865–66. However, Justice Hightower asserted that insurers would be required to take some action toward facilitating settlement. *See id.* at 865-66 (recognizing that litigants make reasonable attempts to settle by evaluating and investigating claims in good faith and by discussing settlement and engaging in negotiations).

98. *Id.* at 866.

99. *Garcia*, 876 S.W.2d at 865 (Hightower, J., dissenting).

100. *Id.* at 863-64.

101. *See id.* at 865–66 (criticizing majority's interpretation of *Guin* and stating that requiring reasonable attempts to settle reduces litigation costs and promotes settlements which benefits "plaintiffs, insureds, insurers, purchasers of liability insurance and taxpayers who subsidize much of the cost").

102. *See* American Physicians Ins. Exch. v. Garcia, 876 S.W.2d 842, 843 n.1 (Tex. 1994) (stating that "[g]iven our disposition of this case, we need not, and do not, decide whether the pretrial non-execution agreement between Garcia and the Cardenases negated all of Garcia's damages"). Ironically, the court declined to "address the *Stowers* duty when a settlement requires funding from multiple insurers and no single insurer can fund the settlement within" its own applicable policy limits. *Id.* at 849 n.13. Moreover, the court did not decide the question of when a *Stowers* duty might be triggered if the insured alerts the insurer to her willingness to pay a sum above policy limits to effect a settlement. *Id.*; *cf.* V. Eileen Stuhr, Comment, *Excess Carrier Tort Suits: Are Primary Carriers Up the* Canal

the rule that insureds cannot stack multiple, temporally distinct "claim-occurrence policies" to create coverage greater than that under the single largest policy.[103] Also important is the court's holding that neither the Texas Deceptive Trade Practices Act nor Article 21.21 of the Insurance Code affords a remedy for breach of the *Stowers* duty.[104] Most signifi-

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Without a Paddle?, 29 HOUS. L. REV. 661, 671 (1992) (asserting that insurers may be liable though settlement offer exceeds policy limits if insured "can prove it would have contributed the deficit in order to effect the settlement"). Finally, the court cautioned against interpreting its silence on any issue included in the initial opinion as an agreement with the prior resolution of such issues. *Garcia*, 876 S.W.2d at 855 n.25.

103. *Garcia*, 876 S.W.2d at 855; *see* Janet Elliott & Robert Elder, Jr., *Insured's Can't Stack Policy Limits, Court Rules*, TEX. LAW. Mar. 14, 1994, at 8 (quoting APIE's attorney recognizing significance of court's ruling that insureds cannot stack multiple policies because "'[t]hat's always been an issue of argument between plaintiffs and defense lawyers'"). Although most jurisdictions do not permit insureds to stack multiple, temporally distinct policies, some have allowed such stacking. *See* Ducre v. Mine Safety Appliances Co., 645 F. Supp. 708, 713–14 (E.D. La. 1986) (requiring insurer to absorb liability for multiple policy periods during which claimant was exposed to source of injury), *aff'd per curiam*, 833 F.2d 588 (5th Cir. 1987); *see also* Eileen M. Dacey, *Allocation: Whose Burden Is It?* (stating that majority rule does not permit stacking of policy limits of consecutive policy periods), *in* INSURANCE COVERAGE LITIGATION 1993: CRITICAL ISSUES AND STRATEGIES—A SATELLITE PROGRAM, at 183, 213 (PLI Litig. & Admin. Practice Course Handbook Series No. 183, 1993). In deciding that Garcia's multiple, temporally distinct policies could not be stacked the court did not fashion a rule to decide "which of several policies are triggered by a single 'continuing' occurrence." *Garcia*, 876 S.W.2d at 853 n.20. Noting considerable disagreement among the courts considering-coverage-trigger issues, the court decided that "it would be unwise to select among these tests, or formulate our own, when the outcome of the case does not require resolution of this issue." *Id.* at 853 nn.20–21. The different "trigger tests" employed in other jurisdictions vary greatly. *Compare* Keene Corp. v. Insurance Co. of N. Am., 667 F.2d 1034, 1049-50 (D.C. Cir. 1981) (employing broad "multiple trigger" approach and permitting insured to choose which of triggered policies "under which it is to be indemnified"), *cert. denied*, 455 U.S. 1007 (1982) *with* Eagle-Picher Indus., Inc. v. Liberty Mut. Ins. Co., 523 F. Supp. 110, 118 (D. Mass. 1981) (embracing "manifestation theory," under which "coverage shall be provided when the . . . disease becomes manifest, as measured by the date of actual diagnosis" or death), *aff'd*, 682 F.2d 12, 24 (1st Cir. 1982), *cert. denied*, 460 U.S. 1028 (1983). *See generally* Chandra Lantz, Note, *Triggering Coverage of Progressive Property Loss: Preserving the Distinctions Between First- and Third-Party Insurance Policies*, 35 WM. & MARY L. REV. 1801, 1803 (1994) (discussing development of different "trigger of coverage" theories in response to "difficult factual, legal and public policy questions").

104. *Garcia*, 876 S.W.2d at 847 & nn.10–11; *cf.* Cherry D. Williams, *A New Twist in Insurance Litigation*: Stowers *Suits By Excess Carriers Against Primary Carriers*, 33 S. TEX. L.J. 1, 12–15 (1992) (discussing implications of Insurance Code and Texas DTPA for causes of action based upon first-party bad faith or third-party *Stowers* doctrine). In 1988, the Texas Supreme Court held that the DTPA provides a remedy to insureds for bad faith failure to settle first-party claims. *See* Vail v. Texas Farm Bureau Mut. Ins. Co., 754 S.W.2d 129, 134 (Tex. 1988) (permitting insured to incorporate State Board of Insurance order and definition under § 21.21-2 of Insurance Code into their cause of action to recover under § 17.50(a)(4) of DTPA and Article 21.21, § 16 of Insurance Code). Although the *Garcia*

cantly however, the court provided a three-pronged test to determine if and when an insurer's *Stowers* duty arises.[105] Unfortunately, Justice Cornyn's three-pronged test effectively, if not formally, overruled *Ranger County Mutual Insurance Co. v. Guin*[106] and, in so doing, replaced the *Stowers* doctrine's bedrock concern for insureds' interests with a purportedly pragmatic rule favoring insurers' interests.[107] The court's decision suspended the sixty-five-year-old duty of an insurer to refrain from negli-

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court did not articulate the differences between first-party bad faith and the *Stowers* doctrine, it summarily distinguished *Vail* as inapposite because *Vail* involved first-party bad faith. *Garcia*, 876 S.W.2d at 847 n.10. Prior to *Garcia*, courts disagreed with respect to whether an insured could maintain a claim under the DTPA for breach of the *Stowers* doctrine. *Compare* Allstate Ins. Co. v. Kelly, 680 S.W.2d 595, 605 (Tex. App.—Tyler 1984, writ ref'd n.r.e.) (authorizing cause of action for *Stowers* breach directly under DTPA) *with* Rosell v. Farmers Tex. County Mut. Ins. Co., 642 S.W.2d 278, 279 (Tex. App.—Texarkana 1982, no writ) (rejecting cause of action for *Stowers* breach under DTPA because "any post-sale conduct of an insurer is not conduct occurring in connection with the purchase of goods or services"). *See generally* TEX. BUS. & COM. CODE ANN. § 17.44 (Vernon 1987) (stating that DTPA should be "liberally construed and applied to promote its underlying purpose"); Lorette Bauarschi, Comment, *Survival Under the Texas Deceptive Trade Practices Act*, 28 HOUS. L. REV. 591, 594–98 (1991) (analyzing purposes and policies undergirding DTPA).

105. *Garcia*, 876 S.W.2d at 849; *see* Texas Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 314 (Tex. 1994) (reaffirming *Garcia*'s three prerequisites that trigger insurer's *Stowers* duty as: (1) third-party claim within scope of coverage; (2) settlement demand within policy limits; and (3) terms of demand such that prudent insurer would ordinarily settle, considering likelihood and degree of potential excess judgment); *see also* Philip K. Maxwell & Tim Labadie, *Insurance Law*, 47 S.M.U. L. REV. 1227, 1405–06 (1994) (analyzing *Garcia* decision and discussing *Garcia*'s three prerequisites to invoke *Stowers* duty); David Nadvorney, *Insurers Needn't Initiate Settlement Offers*, NAT'L L.J., May 2, 1994, at B20 (discussing *Garcia*'s requirement that insurers have opportunity to settle via demand within policy limits).

106. 723 S.W.2d 656 (Tex. 1987).

107. *See Garcia*, 876 S.W.2d at 851 (protecting insurer's bargaining position by refusing to "shift the burden of making settlement offers" onto insurers). The *Stowers* doctrine ultimately rests upon widespread recognition of the harm that may come to insureds when insurers control settlement decisions with unfettered discretion. *See* G.A. Stowers Furniture Co. v. American Indem. Co., 15 S.W.2d 544, 547 (Tex. Comm'n App. 1929, holding approved) (creating duty to exercise reasonable care regarding settlement decisions when insurer retains sole control over such decisions); W. James Kronzer, *The Present Status of the* Stowers *Doctrine in Texas*, 1 S. TEX. L.J. 167, 167 (1954) (characterizing *Stowers* as extension of insurance coverage notwithstanding contractually fixed policy limits); *see also* American Centennial Ins. Co. v. Canal Ins. Co., 843 S.W.2d 480, 483 (Tex. 1992) (stating that *Stowers* and *Guin* imposed clear obligations to protect insured's interests); Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1117–23 (1990) (explaining typical duty-to-settle case and reasons for imposing duty upon insurers); *cf.* Arnold v. National County Mut. Fire Ins. Co., 725 S.W.2d 165, 167 (Tex. 1987) (explaining that imposition of *Stowers* duty protects insureds from potentially abusive practices of insurers); English v. Fischer, 660 S.W.2d 521, 524 (Tex. 1983) (Spears, J., concurring) (noting rationale underlying imposition of extra-contractual obligations arising from special relationship between insurer and insured).

gence in exercising sole control over settlement decisions until the insurer receives a within-limits settlement demand.[108] A re-examination of the policies underpinning the *Stowers* doctrine and duty-to-settle doctrine at large will expose the unreasonableness of this formalized requirement.[109]

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108. *Garcia*, 876 S.W.2d at 849; *see Soriano*, 881 S.W.2d at 314–15 (stating that settlement demands above policy limits, even if reasonable, impose no *Stowers* duty upon insurers); State Farm Lloyds Ins. Co. v. Maldonado, No. 04-93-00046-CV, 1994 WL 723670, at *2 (Tex. App—San Antonio, Dec. 30, 1994, n.w.h.) (restating *Garcia's* requirement that plaintiff prove that insurer rejected offer of settlement within policy limits). *Garcia*'s holding—that insurers cannot be liable for failure to settle in the absence of a settlement demand within policy limits—clearly does not represent the pre-*Garcia* understanding of the scope of the *Stowers* duty. *See Guin*, 723 S.W.2d at 659 (extending duty of reasonable care to "full range of the agency relationship"); Wheelways Ins. Co. v. Hodges, 872 S.W.2d 776, 780 (Tex. App.—Texarkana 1994, n.w.h.) (citing *Guin* for extension of *Stowers* duty to settle); American Centennial Ins. Co. v. Canal Ins. Co., 810 S.W.2d 246, 254 (Tex. App.—Houston [1st Dist.] 1991) (stating that insurer could be liable for *Stowers* breach in absence of settlement demand because "insurer's duty is not limited to accepting reasonable settlement offers within policy limits"), *aff'd in part and rev'd in part*, 843 S.W.2d 480 (Tex. 1992); *see also* C. Michael Moore & David P. Blanke, *Ethics in the Settlement Process* (noting significance of *Guin* in expanding duty to settle), *in* STATE BAR OF TEXAS, EVALUATING AND SETTLING INSURANCE CLAIMS B–26 to B–27 (1987); Cherry D. Williams, *A New Twist in Insurance Litigation*: Stowers *Suits By Excess Carriers Against Primary Carriers*, 33 S. TEX. L.J. 1, 10 (1992) (contending that *Guin* "greatly expanded a carrier's obligation under the *Stowers* Doctrine"); Kelly H. Thompson, Comment, *Bad Faith: Limiting Insurers' Extra-Contractual Liability in Texas*, 41 SW. L.J. 719, 724 (1987) (explaining how *Guin* relegated "the requirement of an unconditional settlement offer to an evidentiary point").

109. *See Garcia*, 876 S.W.2d at 865 (Hightower, J., dissenting) (criticizing majority's holding for allowing insurers to do "absolutely nothing" to protect insured's interests until claimant makes formal settlement offer within policy limits); *see also Guin*, 723 S.W.2d at 659 (characterizing as "narrow" insurer's claim that its duty was limited to responding to within-limits settlement demands); Rova Farms Resort, Inc. v. Investors Ins. Co., 323 A.2d 495, 508-09 (N.J. 1974) (explaining propriety of adopting rule that does not turn on whether claimant has offered to settle); State Auto. Ins. Co. v. Rowland, 427 S.W.2d 30, 35 (Tenn. 1968) (noting that suspending insurer's duty until claimant makes formal demand could lead to inequitable results); ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.02, at 236 (2d ed. 1988) (stating that rationale behind insisting on formal settlement demand is that, without such demand, insured cannot prove causation). Because the insured carries the burden of proving causation, an absolute bar to recovery absent a settlement demand removes from consideration any other proof insured may proffer. *See* ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.02, at 190–91 (1982) (proposing that insureds be allowed to prove causation in absence of settlement demands). *See generally* Joseph A. Bosco, *Insurance Companies: Exposure to Liability for Wrongful Treatment of Claimants*, 32 TRIAL LAW. GUIDE 105, 129 (1988) (reiterating that purpose of duty-to-settle doctrine and claim-settlement statutes is "to compel *prompt, fair and equitable* settlements"); Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 539–58 (1981) (detailing affirmative duties of insurers arising from insurer's position of control over settlement negotiations). Public policy favoring early settlements should not permit plaintiffs to "hide"

The *Stowers* doctrine represents a judicial construct fashioned in response to the special relationship present between insurer and insured, a relationship absent in most other commercial contexts.[110] Because of the exigencies of handling a third-party claim, the insurer ordinarily retains sole control over decisions regarding settlement.[111] The insured purchases liability insurance primarily for protection; therefore, the insured reasonably expects its insurer to discharge its contractual and extra-contractual duties with that protection in mind.[112] To treat the *Stowers*

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behind settlement offers. *See* Edward F. Sherman, *Court-Mandated Alternative Dispute Resolution: What Form of Participation Should Be Required?*, 46 S.M.U. L. REV. 2079, 2103 (1993) (concluding that policy underpinning *Stowers* coupled with alternative dispute resolution policy favoring settlement should require plaintiff's continued participation in settlement negotiations).

110. Christensen v. Integrity Ins. Co., 709 S.W.2d 724, 729 (Tex. App.—Houston [14th Dist.]), *rev'd on other grounds*, 719 S.W.2d 161 (Tex. 1986); Aetna Casualty & Sur. Co. v. Marshall, 699 S.W.2d 896, 901 (Tex. App.—Houston [1st Dist.] 1985), *aff'd*, 724 S.W.2d 770 (Tex. 1987); *see* Kewin v. Massachusetts Mut. Life Ins. Co., 295 N.W.2d 50, 71 (Mich. 1980) (Williams, J., dissenting) (describing special relationship created by insurance contract that gives rise to duty to settle); John Monaghan, *Extending the Bad Faith Tort Doctrine to General Commercial Contracts*, 65 B.U. L. REV. 355, 377 (1985) (discussing tort of bad faith as predicated on existence of special relationship and courts' reluctance to extend doctrine beyond insurance context); *see also* Stephens v. Liberty Mut. Fire Ins. Co., 821 F. Supp. 1119, 1122 (D. Md. 1993) (stating that simple breach of contract, "absent a duty or obligation imposed by law independent of the contract itself," cannot sustain tort cause of action).

111. *See* Tank v. State Farm Fire & Casualty Co., 686 P.2d 1127, 1130 (Wash. Ct. App. 1984) (describing insurer's reservation of control over case as "a necessity of insurance practice"); Note, *Control of Settlement and Litigation by Liability Insurers*, 34 COLUM. L. REV. 511, 512 (1934) (explaining that insurer retains control "to prevent collusion and overpayment"); *see also* Traders & Gen. Ins. Co. v. Rudco Oil & Gas Co., 129 F.2d 621, 626 (10th Cir. 1942) (discussing insurer's reservation of control over litigation and settlement decisions); New Orleans & C.R. Co. v. Maryland Casualty Co., 38 So. 89, 91 (La. 1905) (illustrating old rule that insurer's contractual reservation of control gave insurer unfettered discretion by express terms of contract); V. Eileen Stuhr, Comment, *Excess Carrier Suits: Are Primary Insurers Up the* Canal *Without a Paddle?*, 29 HOUS. L. REV. 661, 666 (1992) (discussing contractual reservation of control over claim and prohibition against unilateral conduct by insured). The ordinary allocation of rights under a liability insurance policy is further complicated when the insurer agrees to defend under a reservation of rights. *See* William C. Carpenter, Note, *Reservation of Rights in Insurance Contracts*, 32 ARIZ. L. REV. 387, 399 (1990) (considering complications arising when insurer reserves right to refuse coverage).

112. *See* Rawlings v. Apodaca, 726 P.2d 565, 571 (Ariz. 1986) (observing that "one of the benefits that flow from the insurance contract is the insured's expectation that his insurance company will not wrongfully deprive him of the very security for which he bargained or expose him to the catastrophe from which he sought protection"); Kevin F. Cox, Comment, *Insurance Bad Faith Refusal to Settle: What's an Insured to Do?*, 7 J.L. & COM. 143, 143–44 (1987) (acknowledging "usual expectation" that insurer becomes insured's agent for purposes of protecting insured's assets). One of the primary means by which an

doctrine as arising only upon a formal offer to settle within the policy limits is to suggest that a true conflict of interest arises only upon a formal tender of such offer.[113] This view misapprehends the nature of the tripartite relationship between the insurer, insured, and third-party claimant.[114] Absent special interests in exoneration, an insured presumably has an un-

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insurance policy affords protection is in providing ready capital for settlement of claims. *See* Bartlett v. Travelers Ins. Co., 167 A. 180, 183 (Conn. 1933) (asserting that, as matter of common knowledge, "the great majority of [third-party automobile insurance claims] are adjusted"); Douglas v. United States Fidelity & Guar. Co., 127 A. 708, 712 (N.H. 1924) (recognizing that "great majority" of third-party claims are settled as matter of common knowledge); *cf.* Gray v. Zurich Ins. Co., 419 P.2d 168, 171-72 (Cal. 1966) (applying adhesion contract doctrine to insurance policy to determine "meaning of the contract which the insured would likely expect"). *See generally* EDWIN W. PATTERSON, ESSENTIALS OF INSURANCE LAW 131-59 (1935) (outlining interests properly subject to protection under insurance policies); Guy O. Kornblum, *The Current State of Bad Faith and Punitive Damage Litigation in the U.S.*, 23 TORT & INS. L.J. 812, 813–19 (1988) (detailing evolution of bad faith litigation as founded upon special relationship between insurer and insured).

113. *See* Merritt v. Reserve Ins. Co., 110 Cal. Rptr. 511, 524 (Ct. App. 1973) (claiming that insured's and insurer's interests were "at all times . . . parallel and not divergent" even though claimant sought damages well above policy limit); *see also* Pavia v. State Farm Mut. Ins. Co., 626 N.E.2d 24, 27 (N.Y. 1993) (indicating that conflict arises upon offer to settle within policy limits). Because the duty-to-settle doctrine initially emerged in reaction to conflicts of interest, requiring a settlement demand to trigger a duty of care, in effect, denies that any previously existing conflict of interest exists or is worthy of protection. *See Rova Farms*, 323 A.2d at 504 (declaring that conflict of interest always existed "in fact and in law" after likelihood of excess recovery became apparent); Darrell Waas, Comment, *Expanding the Insurer's Duty to Attempt Settlement*, 49 U. COLO. L. REV. 251, 258 (1978) (asserting that better rule recognizes conflict of interest independent of settlement offer); *see also* Allstate v. Campbell, 639 A.2d 652, 656–57 (Md. 1994) (recognizing possibility of inherent conflict of interest that requires insurers to exercise good faith in settling third-party claims). In *Campbell*, the insurer initially rejected a within-limits settlement offer, but subsequently settled the case and obtained a release of the insured. *Campbell*, 639 A.2d at 653-54. In ruling that the insured failed to state a viable claim, the court noted that the conflict of interest, though preexisting, did not justify requiring the insurer to give up defending the claim. *Id.* at 659; *see also* Short v. Dairyland Ins. Co., 334 N.W.2d 384, 387 (Minn. 1983) (stressing tension between insurer's fiduciary duty to protect insured and its interests in minimizing capital outlay). *See generally* Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. MICH. J.L. REF. 1, 19–22 (1992) (analyzing conflicts of interest giving rise to duty to consider insured's interests and to do so reasonably or in good faith).

114. *See Rova Farms*, 323 A.2d at 507 (discussing inherent conflict of interest by virtue of allocations of control over settlement). The Supreme Court of New Jersey noted:

> The assured is not in a position to exercise effective control over the lawsuit or to further his own interests by independent action, even when those interests appear in serious jeopardy. The assured may face the possibility of substantial loss which can be forestalled only by action of the carrier. Thus the assured may find himself and his goods in the position of a passenger on a voyage to an unknown destination on a vessel under the exclusive management of the crew.

qualified interest in disposing of the entire claim with the insurance policy purchased precisely for such circumstances.[115] The insurer, however, has only a finite financial responsibility—its policy limits.[116] By requiring no

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Id. (quoting Merritt v. Reserve Ins. Co., 110 Cal. Rptr. 511, 519 (Ct. App. 1973)); Note, *Control of Settlement and Litigation by Liability Insurers*, 34 COLUM. L. REV. 511, 512 (1934) (recognizing need for duty of care because of ever-present chance of excess judgment); *see also* Coleman v. Holecek, 542 F.2d 532, 537 (10th Cir. 1976) (recognizing that claim asserted in excess of policy limits creates conflict of interest justifying imposition of duty of care); *Campbell*, 639 A.2d at 659 (recognizing that conflict of interest arises from insurer's reservation of control over settlements, claim seeking more than policy limits, and insured's interest in minimizing its liability exposure); State Farm Mut. Auto. Ins. Co. v. White, 236 A.2d 269, 271 (Md. 1967) (stating as prevailing view that "insurer has exclusive control, under the standard policy, of investigation, settlement and defense of any claim or suit against the insured, and there is a potential, if not actual, conflict of interest giving rise to a fiduciary duty"); Patrick F. Koenen, *Bad Faith and Negligence Approaches to Insurer Excess Liability for Failing to Settle Third-Party Claims: Problems and Suggestions*, 54 DEF. COUNS. J. 179, 186 (1987) (recognizing common difficulty in judicial approaches to bad faith liability as "inherent conflict of interest" between insurer and insured); Sharon K. Hall, Note, *Confusion Over Conflicts of Interest: Is There a Bright Line for Insurance Defense Counsel?*, 41 DRAKE L. REV. 731, 733 (1992) (listing possible sources of conflict of interests, including when claim exceeds limits of policy).

115. *See Rova Farms*, 323 A.2d at 508 (stating that insured always benefits from settlement and subsequent foreclosure of possibilities of exposure to excess damages); Crisci v. Security Ins. Co., 426 P.2d 173, 177 (Cal. 1967) (commenting that "[o]bviously, it will always be in the insured's interests to settle within the policy limits when there is any danger, however slight, of a judgment in excess of those limits"). *But see* Marginian v. Allstate Ins. Co., 481 N.E.2d 600, 601 (Ohio 1985) (addressing situation in which insured claimed that insurer wrongfully settled within policy limits); Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1158–59 (1990) (surveying instances in which insured has additional stakes in disposition of claim beyond otherwise unqualified interest in settlement). *See generally* Kevin F. Cox, *Insurance Bad Faith Refusal to Settle: What's an Insured to Do?*, 7 J.L. & COM. 143, 144 (1987) (asserting that insured reasonably expects insurer will become agent). "It is clear that insurers try to convince purchasers of insurance that their policies will relieve the policyholder of fear, anxiety and insecurity. This deliberate portrayal of insurers as a 'benign fiduciary' is a standard practice in the insurance industry." *Id.* at 144 n.3.

116. *See* Noble v. National Am. Life Ins. Co., 624 P.2d 866, 870 (Ariz. 1981) (emphasizing insurer's potential tendency to gamble with insured's money because "insurer stands to lose little and gain much"); Scheuch v. Western World Ins. Co., 145 Cal. Rptr. 294, 297 (Ct. App. 1979) (noting insurer's position of having nothing to lose by refusing to settle, whereas insured feared significant liability if claim was not settled); Southern Gen. Ins. Co. v. Holt, 409 S.E.2d 852, 861 (Ga. Ct. App. 1991) (commenting that insurer had nothing to lose but its policy limits by refusing to settle and taking case to trial); Thomas B. Alleman, *The Reasonable Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured*, 50 UMKC L. REV. 251, 252 (1982) (noting dangers inherent in allowing insurers to refuse to settle because they have "nothing to lose"). In passing on the propriety of imposing a strict liability standard, the Supreme Court of California noted that "[t]here is more than a small amount of elementary justice in a rule that would require that, in this situation where the insurer's and insured's interests necessarily conflict, the insurer, which may reap the benefits of its determination not to settle, should also suffer the detriments of its decision."

standard of care absent a formal settlement demand within policy limits, *Garcia* in effect invites insurers to gamble with the insured's money in derogation of their fiduciary duties.[117]

Uniquely positioned to determine whether to settle or try a case, insurers must be permitted to do so; however, the decision to settle or not to settle should be well calculated and reasonable in light of the insured's otherwise unprotected financial interests.[118] The calculus employed to

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Crisci, 426 P.2d at 177. This strict liability dictum has spurred much criticism of the current duty-to-settle doctrine, with several commentators advocating a strict liability rule. *See, e.g.*, Christina K. Boyer, *Strict Liability for Insurers Refusing Settlements Within Policy Limits: Let's Quit Talking About It and Just Do It*, 17 J. CORP. L. 615, 625-37 (1992) (advocating strict liability as easier and more equitable standard); Clinton R. Ashford, Comment, *Insurance: Liability of Insurer for Judgment in Excess of Policy Limits*, 48 MICH. L. REV. 95, 102 (1949) (noting propensity of strict liability for correcting insurer misconduct); Gilbert G. Lundstrom, Comment, *Approaching Strict Liability of Insurer for Refusing to Settle Within Policy Limits*, 47 NEB. L. REV. 705, 717–21 (1968) (noting possible benefits of adopting strict liability system, such as reduction of litigation, ability of insurer to spread loss, "elimination of the unenlightened jury question," and decrease in cost of handling claims).

117. *See Garcia*, 876 S.W.2d at 849 (refusing to invoke duty of care in absence of "proof that the insurer was presented with a reasonable opportunity to prevent the excess"). Recognition of the insurer's propensity to gamble with the insured's money is, of course, the foundation for imposing a duty to exercise care in the first instance. *E.g.*, Allen v. Allstate, 656 F.2d 487, 489 (9th Cir. 1981); Herges v. Western Casualty & Sur. Co., 408 F.2d 1157, 1161 (8th Cir. 1969); Tennessee Farmers Mut. Ins. Co. v. Wood, 277 F.2d 21, 34 (6th Cir. 1960); Pacific Employers Ins. Co. v. United Gen. Ins. Co., 664 F. Supp. 1022, 1023 (W.D. La. 1987); *see also* Venetsanos v. Zucker, 638 A.2d 1333, 1340 (N.J. Super. Ct. App. Div. 1994) (stating that insured need not prove existence of demand within policy limits to recover). *See generally* Richard J. Phelan, *Bad Faith Litigation* (asserting that "modern rule" requires insurer to initiate settlement negotiations when significant probability of excess judgment exists) *in* 1985 INS. LITIG. INST. 123, 127 (Sheila L. Birnbaum & David R. Gross eds.). Allowing the insurer to wait for a demand within policy limits puts the insured at an advantage in protecting its interests, but it does so at the expense of the insurer's interests. *See* Lloyd E. Williams, Jr. & Donald V. Jernberg, *Conflicts of Interest in Insurance Defense Litigation: Common Sense in Changing Times*, 31 FED'N INS. COUNS. Q. 111, 120 (1981) (illustrating tactical advantage that insurers enjoy in those jurisdictions which impose no general obligation to initiate settlement negotiations).

118. *See* Hilker v. Western Auto. Ins. Co., 235 N.W. 413, 414 (Wis. 1931) (asserting that insurer's reservation of right to control free from interference by insured is necessary for insurer to carry out its obligations). Given the insurance company's expertise in claims handling, and considering its own important interest in protection, the insurance company must retain control over the claim. *See* Tyler v. Grange Ins. Ass'n, 473 P.2d 193, 197 (Wash. Ct. App. 1970) (noting "necessity of insurance practice" for insurers to retain control over claims). The insurer's necessarily retained control must be tempered, however, when the insured's interests diverge from its own. *See Short*, 334 N.W.2d at 387 (discussing settlement conflicts of interest). Although it acknowledged the insurer's interest in obtaining the lowest settlement possible, the Minnesota Supreme Court noted that "the insurer's right to control the negotiations for settlement must be subordinated to the purpose of the insurance contract—to defend and indemnify the insured within the limits of the

make a decision to litigate or settle involves a complex and imperfect methodology.[119] As recognized in *Chancey v. New Amsterdam Casualty Co.* and other cases,[120] the duty to settle implies the duty to negotiate.[121] Effective negotiations require a thorough understanding of the position

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insurance contract." *Id.*; *see also Douglas*, 127 A. at 712 (accepting insurer's necessary reservation of control, but stating that duty of care is necessary because "[t]he contrary holding involves the anomalous situation where, as to settlement, the insurer has no duty and the insured has no rights"). *See generally* Kevin F. Cox, *Insurance Bad Faith Refusal to Settle: What's an Insured to Do?*, 7 J.L. & COM. 143, 145 (1987) (describing situation in which insurer's gamble causes insured to bear excess judgement). Some commentators would effectively strip insurers of any discretion when assessing settlement demands within policy limits by imposing strict liability for any failure to accept. *See* Christina K. Boyer, *Strict Liability for Insurers Refusing Settlements Within Policy Limits: Let's Quit Talking About It and Just Do It*, 17 J. CORP. L. 615, 625–31 (1992) (advocating strict liability for failure to settle within policy limits, because "current systems do not work," strict liability would eliminate confusing "realm of conflicts of interest," and strict liability is simple and "best represents the expectations of the average insured").

119. *See* Garner v. American Mut. Liab. Ins. Co., 107 Cal. Rptr. 604, 608 (Ct. App. 1973) (stating that insurer must independently evaluate claim by carefully considering all medical evidence in light of accepted community standards and must give careful consideration to all legal aspects of case); Bowers v. Camden Fire Ins. Ass'n, 237 A.2d 857, 861 (N.J. 1968) (identifying factors that insurer must consider in making settlement decision). The *Bowers* court stated that, in deciding whether to settle, the insurer must ascertain:

> the anticipated range of the verdict, should it be adverse; the strengths and weaknesses of all the evidence to be presented on either side so far as known; the history of the particular geographic area in cases of similar nature; and the relative appearance, persuasiveness, and likely appeal of the claimant, the insured, and the witnesses at trial.

Id.; *see also* Samuel R. Gross & Kent D. Syverúd, *Getting to No: A Study of Settlement Negotiations and the Selection of Cases for Trial*, 90 MICH. L. REV. 319, 323 (1991) (describing "selection hypothesis" as means by which trial decisions are made). *See generally* Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions: Refining the Standard of Culpability and Reformulating the Remedies by Statute*, 26 U. MICH. J.L. REF. 1, 35 (1992) (analyzing complexities inherent in determining insurer's bad faith); Alan O. Sykes, *"Bad Faith" Refusal to Settle By Liability Insurers: Some Implications of the Judgment-Proof Problem*, 23 J. LEGAL STUD. 77, 86–107 (1994) (illustrating economic and negotiating complexities in imposing different duties upon liability insurers regarding how they must consider insureds' interests).

120. 336 S.W.2d 763 (Tex. Civ. App.—Amarillo 1960, writ ref'd n.r.e.).

121. *Chancey*, 336 S.W.2d at 765; *e.g.*, Seguros Tepeyac, S.A. v. Bostrom, 347 F.2d 168, 172 n.2 (5th Cir. 1965); Danner v. Iowa Mut. Ins. Co., 340 F.2d 427, 428 (5th Cir. 1964); Riggs v. Sentry Ins., 821 S.W.2d 701, 707 (Tex. App.—Houston [14th Dist.] 1991, writ denied); Ranger County Mut. Ins. Co. v. Guin, 704 S.W.2d 813, 816 (Tex. App.—Texarkana 1985), *aff'd*, 723 S.W.2d 656 (Tex. 1987). In *Guin*, the court of appeals approved the following jury instruction as an accurate statement of the law:

> "NEGLIGENCE" as used in this special issue means the failure to exercise that degree of care and diligence which an ordinarily prudent person would exercise in the management of his own business. If an ordinarily prudent person in the exercise of ordinary care, as viewed from the standpoint of the insured, would have settled the

of the adversary; thus, to make a reasonable decision regarding settlement, the insurer must compile sufficient knowledge to form a reasonable basis for that decision.[122] Accordingly, in *Guin*, the Texas Supreme Court held that the insurer's duty extends to investigation, preparation, and reasonable attempts to settle.[123] Though derived from a recognition of the

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case, but the defendant failed or refused to do so, then the defendant is negligent. The duty to settle implies the duty to negotiate.

Guin, 704 S.W.2d at 816 n.2; *see* Clinton R. Ashford, Comment, *Insurance: Liability of Insurer for Judgment in Excess of Policy Limits*, 48 MICH. L. REV. 95, 97 (1949) (discussing application of negligence standard in duty-to-settle cases). One short step beyond recognition of an implied duty to negotiate is imposition of a duty to initiate negotiations. *See Guin*, 723 S.W.2d at 659 (extending duty to exercise reasonable care in making reasonable attempts to settle); *see also* Powell v. Prudential Property & Casualty Ins. Co., 584 So. 2d 12, 14 (Fla. Dist. Ct. App. 1991) (asserting that, when excess damages are likely, insurer has "an affirmative duty to initiate settlement negotiations"); Guarantee Abstract & Title Co. v. Interstate Fire & Casualty Co., 618 P.2d 1195, 1199 (Kan. 1980) (noting Kansas rule requiring insurer to take affirmative steps to facilitate settlement because conflict of interest does not hinge upon offers by claimant). *See generally* Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1166 (1990) (asserting that rule requiring settlement demand as prerequisite to bad faith liability motivates insurers to manipulate settlement negotiations such that claimant makes no reasonable demand).

122. *See* Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 545 (1981) (discussing dynamics of settlement negotiations, including collection of information); *see also* United States Fire Ins. Co. v. Royal Ins. Co., 759 F.2d 306, 310 (3d Cir. 1985) (taking notice of Pennsylvania cases requiring insurer to conduct thorough investigation in deciding whether to litigate). As the Pennsylvania Superior Court noted:

> The decision to litigate must be a thoroughly honest, intelligent and objective one. It must be a realistic one when tested by the necessarily assumed expertise of the company. This expertise must be applied in a given case, to a consideration of *all the factors* bearing upon the advisability of a settlement for the protection of the insured.

Shearer v. Reed, 428 A.2d 635, 638 (Pa. Super. Ct. 1980) (citations omitted); *see* Wasserman v. Buckeye Union Casualty Co., 277 N.E.2d 569, 575 (Ohio Ct. App. 1972) (requiring insurer to exercise diligence and intelligence in guarding insured's interests); *see also* C. Michael Moore & David P. Blanke, *Ethics in the Settlement Process* (assessing defense counsel's quandary in which excess damages are imminent and claimant has failed to make offer, and counseling for open communication of those facts), *in* STATE BAR OF TEXAS, EVALUATING AND SETTLING INSURANCE CLAIMS B-27 (1987). To afford the insured the bargained-for protection, this accumulation should include knowledge of the claimant's position regarding settlement. *See* Chris M. Kallianos, *Bad Faith Refusal to Pay First-Party Insurance Claims: A Growing Recognition of Extra-Contract Damages*, 64 N.C. L. REV. 1421, 1421 (1986) (recognizing that insured seeks assurance that insurer will afford bargained-for relief to prevent hardship in case of serious financial setback).

123. *Guin*, 723 S.W.2d at 659; *see* Campbell v. State Farm Mut. Auto. Ins. Co., 840 P.2d 130, 138 (Utah App. 1992) (citing *Guin* for proposition that insurer must initiate settlement negotiations when claimant has made no offer to settle); Cherry D. Williams, *A New Twist in Insurance Litigation*: Stowers *Suits By Excess Carriers Against Primary Carriers*, 33 S. TEX. L.J. 1, 11 (1992) (contending that *Guin* extended insurer's duty by approving negligence predicated on handling of claim and lawsuit); *see also* Puritan Ins. Co. v.

special relationship giving rise to a duty to exercise care, the decision in *Garcia* abrogates any such responsibility absent a prodding by the third-party claimant.[124]

The reasonableness of the insurer's actions need not hinge upon settlement demands alone; rather, any settlement demand, or the absence thereof, should be considered in light of all circumstances surrounding the claim.[125] A patently unreasonable offer should not require the same

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Canadian Universal Ins. Co., 586 F. Supp. 84, 87 (E.D. Pa. 1984) (noting propriety of requiring insurer to initiate settlement discussions), *rev'd*, 775 F.2d 76 (3d Cir. 1985); *Rowland*, 427 S.W.2d at 34 (discussing ever-present conflict of interest that justifies imposing affirmative duty to negotiate); *Rova Farms*, 323 A.2d at 503-04 (listing factors for insurer to consider when discharging affirmative duty to settle). *See generally* Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 539 (1981) (asserting that failure to properly investigate and evaluate claims is most common basis for bad faith suit).

124. *See Garcia*, 876 S.W.2d at 849 (introducing settlement demand within policy limits as prerequisite to activation of duty to settle); *see also* Seward v. State Farm Mut. Auto. Ins. Co., 392 F.2d 723, 725–26 (5th Cir. 1968) (refusing to find bad faith when critical issue involved claimant who did not offer to settle within limits); Mission Ins. Co. v. Aetna Life & Casualty Co., 687 F. Supp. 249, 254 (E.D. La. 1988) (refusing to find bad faith when record showed that all settlement demands were above policy limits); *Merritt*, 110 Cal. Rptr. at 518-19 (discussing conflict of interests arising upon tender of within-limits settlement demand and refusing to find liability in absence of such demand); Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1166 n.134 (1990) (listing cases holding insurer harmless in absence of settlement demand within limits); *cf.* Fulton v. Woodford, 545 P.2d 979, 984 (Ariz. Ct. App. 1976) (imposing affirmative duty to attempt settlement only when conflict of interest or great risk of excess judgment exists). Whenever the duty to settle arises, insurers are required to exercise care in conducting the defense and controlling other aspects of litigation concerning the claim. *See* Richard J. Phelan, *Bad Faith Litigation* (equating duty to settle with court imposed duty to act in accordance with standard of care), *in* INSURANCE LITIGATION INSTITUTE 123, 126 (Sheila L. Birnbaum & David R. Gross eds., 1985).

125. *See Powell*, 584 So. 2d at 14 (stating that offer to settle represents only one factor to be considered in determining whether insurer breached duty to settle); Farmers Ins. Exch. v. Schropp, 567 P.2d 1359, 1365 (Kan. 1977) (invoking duty to settle when claim is above policy limits and reasonable person would settle despite policy limits); Kent D. Syverúd, *The Duty to Settle*, 76 VA. L. REV. 1113, 1124–25 (1990) (analyzing relevant factors for jury to consider in determination of reasonableness of insurer's conduct). The broadest formulation of the duty to settle asks whether the decision was reasonable considering all the circumstances. *Campbell*, 840 P.2d at 138–39; *see Campbell*, 639 A.2d at 656 (listing considerations relevant to determination of bad faith, including seriousness of claimant's injuries indicating likely excess verdict, lack of adequate investigation, failure to inform insured of offer near policy limits, pressuring of insured into contributing to settlement within policy limits, and actions indicating greater concern for insurer's interests than for those of insured); Gibson v. Western Fire Ins. Co., 682 P.2d 725, 735-37 (Mont. 1984) (detailing analysis of multiple factors to be considered in determination of bad faith). *See generally* Willy E. Rice, *Judicial Bias, the Insurance Industry and Consumer Protection: An Empirical Analysis of State Supreme Courts' Bad-Faith, Breach-of-Contract, Breach-of-Covenant-of-Good-Faith and Excess-Judgment Decisions, 1900-1991*, 41 CATH. U. L. REV.

attention as an offer near the policy limits because an unreasonable offer may not evidence a true opportunity to settle the claim within policy limits.[126] Reasonable consideration of the insured's interests requires, at a minimum, that an insurer thoroughly investigate and assess the claim, respond to all settlement offers, and make reasonable attempts to settle in the absence of such offers.[127] A broad-based negligence standard, as articulated in *Guin*, requires the insurer to initiate settlement negotiations if it would do so on its own behalf absent applicable policy limits.[128] Rec-

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325, 333 (1992) (listing many possible ways insureds and third parties may recover for insurers' wrongful conduct); James R. Sutterfield, *Relationships Between Excess and Primary Insurors: The Excess Judgment Problem*, 52 INS. COUNS. J. 638, 641 (1985) (enumerating common factors utilized in determining whether insurer acted negligently or in good faith).

126. *See* Young v. American Casualty Co., 416 F.2d 906, 911 (2d Cir. 1969) (stating as matter of common knowledge that exploration of settlement possibilities upon receipt of initial settlement demand will result in substantial reduction of settlement amount), *cert. dismissed*, 90 S. Ct. 580 (1970); Baker v. Northwestern Nat'l Casualty Co., 132 N.W.2d 493, 497 (Wis. 1965) (contending that, although not all settlement communications are meant seriously, insurers must be circumspect in communication of "all offers which are not patently jocular or frivolous"); *see also* Eastham v. Oregon Auto. Ins. Co., 540 P.2d 364, 368 (Or. 1975) (asserting that insurer should not be required to negotiate when claimant's offer significantly exceeds policy limits and liability is not established); 2 JOHN C. MCCARTHY, RECOVERY OF DAMAGES FOR BAD FAITH § 3.42, at 583 (5th ed. 1990) (urging insurers to always remain open to possibility of settlement and to factor into settlement decisions loss of goodwill, administrative burdens, and ever-increasing trial costs); Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 544 (1981) (stating that, although insurer avoids liability if it could not settle within limits, offer to settle is not necessarily required before liability may be imposed).

127. *See Coleman*, 542 F.2d at 538 n.7 (imposing affirmative duty to continue negotiations after receiving settlement offer). If the circumstances of the case, taken together, would induce a reasonable person with no liability limit to initiate settlement negotiations, then the insurer must do so. *Id.*; *see Eastham*, 540 P.2d at 368 (stating that insurer need not make counteroffer when expected judgment is within policy limits and offer is above limits); Darrell Waas, Comment, *Expanding the Insurer's Duty to Attempt Settlement*, 49 U. COLO. L. REV. 251, 258–59 (1978) (noting trend advocating acceptance of *Coleman* analysis concerning insurer's affirmative duty); *see also Rova Farms*, 323 A.2d at 507 (resolving doubts in insured's favor concerning whether settlement could have been effected if insurer took initiative to do so); *Venetsanos*, 638 A.2d at 1340 (declaring affirmative fiduciary duty to take charge of affairs and attempt to negotiate settlement within coverage). For a general analysis of the negligence standard in duty-to-settle cases, see Joan K. Lefkowitz, *New York Third Party Bad Faith: Is It a Plaintiff's Dream or a Defendant's Nightmare?*, 12 PACE L. REV. 543, 547–48 (1992) (stating requirements of negligence and other standards of care imposed upon liability insurers). *See generally* Annotation, *Duty of Liability Insurer to Settle or Compromise*, 40 A.L.R.2D 168, § 7 (1955) (discussing cases imposing duty of due care in settlement decisions upon insurer).

128. *See Guin*, 723 S.W.2d at 659 (imposing duty to exercise "that degree of care and diligence which an ordinary person would . . . in the management of his own business," which includes "reasonable attempts to settle"); *see also Coleman*, 542 F.2d at 537 (con-

ognition of the insurer's affirmative duty to settle upon assertion of a third-party claim exceeding policy limits is most consistent with the purposes of imposing a *Stowers* duty in the first instance.[129]

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struing Kansas negligence standard as requiring insurer to initiate settlement if it would do so in absence of policy limits). *Guin* appeared to have eradicated an insurer's ability to hide behind the absence of a settlement offer. *See* Russell W. Schell, *Bad Faith and DTPA Claims* (discussing significance of *Guin* in reducing unconditional offer to settle to "merely an evidentiary issue"), *in* STATE BAR OF TEXAS, EVALUATING AND SETTLING INSURANCE CLAIMS G-13 (1987); *see also* Morrell Constr., Inc. v. Home Ins. Co., 920 F.2d 576, 580 (9th Cir. 1990) (recognizing propriety of affirmative duty to attempt settlement in some instances, but refusing to impose such duty before complaint is filed); Meijer, Inc. v. General Star Indem. Co., 826 F. Supp. 241, 247 (W.D. Mich. 1993) (noting relevance of insurer's failure to initiate settlement negotiations in determination of bad faith); Stetler v. Fosha, 809 F. Supp. 1409, 1424 (D. Kan. 1992) (stating standard of care as that of reasonable person with no policy limits), *aff'd*, 7 F.3d 1045 (10th Cir. 1993); ALLAN D. WINDT, INSURANCE CLAIMS AND DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSUREDS § 5.03, at 189–90 (1982) (asserting that courts' insistence on demand within settlement limits makes sense regarding proof of causation, but that imposing positive duty to explore settlement possibilities is better rule because insureds could prove causation despite absence of claimant demands); *cf. Bowers*, 237 A.2d at 861 (stating that only way to serve both insurer's and insured's interests is to require insurer to make settlement decision without regard to policy limits). *See generally* Lloyd E. Williams, Jr. & Donald V. Jernberg, *Conflicts of Interest in Insurance Defense Litigation: Common Sense in Changing Times*, 31 FED'N INS. COUNS. Q. 111, 120–21 (1981) (urging insurers to initiate settlement negotiations rather than hide behind claimant's failure to make within-limits settlement offer).

129. *See Stowers*, 15 S.W.2d at 547 (upholding cause of action for breach of duty to settle because of insurer's unchecked control over settlements that may be in insured's best interests); Alt v. American Family Mut. Ins. Co., 237 N.W.2d 706, 713 (Wis. 1976) (positing that duty imposed upon insurers for insured's benefit extends to reasonable attempts to settle); *see also Rova Farms*, 323 A.2d at 507 (noting insured's unenviable position in which insurer is allowed to ignore insured's interests until claimant makes settlement demand); Chris M. Kallianos, *Bad Faith Refusal to Pay First-Party Insurance Claims: A Growing Recognition of Extra-Contract Damages*, 64 N.C. L. REV. 1421, 1421 n.1 (1986) (asserting that duty-to-settle doctrine initially developed in response to insurers' abusive settlement practices in third-party cases). *See generally* ROBERT E. KETTON ET AL., INSURANCE LAW § 7.8(c) (1988) (discussing propriety of affirmative duty to attempt settlement). The continued development of the duty-to-settle doctrine has incited calls for adoption of comparative bad faith, which would consider the misconduct of both the insured and the insurer. *See, e.g.*, Texas Farmers Ins. Co. v. Soriano, 844 S.W.2d 808, 851 (Tex. App.—San Antonio 1992) (Butts, J., dissenting) (advocating application of comparative bad faith because "the relationship of the insured and insurer [is] a 'two way street'"), *rev'd*, 881 S.W.2d 312 (Tex. 1994); Patrick E. Shipstead & Scott S. Thomas, *Comparative and Reverse Bad Faith: Insured's Breach of the Implied Covenant of Good Faith and Fair Dealing as Affirmative Defense or Counterclaim*, 23 TORT & INS. L.J. 215, 221–24 (1987) (proposing extension of doctrine to encompass insured's bad faith); James W. Walker, *Comparative Bad Faith Its Time Has Come In Texas*, 55 TEX. B.J. 792, 797 (1992) (characterizing adoption of defense of comparative bad faith as next logical step in development of Texas' insurance and tort law).

Nearly all courts agree that the insured's interests must be considered in determining whether to settle.[130] In Texas and a few other jurisdictions, however, the insured's interests are cast aside, to be considered equally with those of the insurer only upon manifestation of a "true" conflict of interest.[131] The insurer has charged itself with discretion in making a decision to settle and must reasonably weigh both its own interests and the interests of the insured, eventually elevating one above the other.[132] Insurers may avoid extra-contractual liability for failure to set-

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130. *E.g.*, Manchester Ins. & Indem. Co. v. Grundy, 531 S.W.2d 493, 496 (Ky. Ct. App. 1975); Holtzclaw v. Falco, Inc., 355 So. 2d 1279, 1283-84 (La. 1978); Larson v. Anchor Casualty Co., 82 N.W.2d 376, 386 (Minn. 1957); Knobloch v. Royal Globe Ins. Co., 362 N.Y.S.2d 492, 504 (App. Div. 1974) (Hopkins, J., concurring and dissenting), *rev'd.*, 344 N.E.2d 364 (N.Y. 1976). *See generally* Christina K. Boyer, *Strict Liability for Insurers Refusing Settlements Within Policy Limits: Let's Quit Talking About It and Just Do It*, 17 J. CORP. L. 615, 619 (1992) (noting that insurer-insured relationship is "often riddled with conflicts of interest" giving rise to insurer's duties of care); Stephen B. Fillman, Note, Braesch v. Union Insurance Co., 237 Neb. 44, 464 N.W.2d 769 (1991): *Policy Rationales of the Bad Faith Cause of Action and Implications to Non-Insurance Commercial Contracts*, 72 NEB. L. REV. 608, 626 (1993) (urging broader recognition of conflicts of interest in insurance context because of absence of disincentives for insurers to breach duty to settle).

131. *See Garcia*, 876 S.W.2d at 865 (Hightower, J., dissenting) (criticizing rule requiring formal demand within policy limits before imposing liability for failure to settle because such rule allows insurers to do "absolutely nothing" toward protecting insured from excess judgment); Joan B. Lefkowitz, *New York Third Party Bad Faith: Is It a Plaintiff's Dream or a Defendant's Nightmare?*, 12 PACE L. REV. 543, 564 (1992) (analyzing conflict of interest as arising upon claimant's offer to settle); *see also Merritt*, 110 Cal. Rptr. at 518 (refusing to find breach of duty to settle when claimant did not offer to settle within limits); State Farm Fire & Casualty Co. v. Metcalf, 861 S.W.2d 751, 756 (Mo. Ct. App. 1993) (refusing to find bad faith in absence of claimant's settlement demand); *Pavia*, 626 N.E.2d at 28 (assuming that proof of demand within policy limits is prerequisite to bad faith suit). *See generally* Lloyd E. Williams, Jr. & Donald V. Jernberg, *Conflicts of Interest in Insurance Defense Litigation: Common Sense in Changing Times*, 31 FED'N INS. COUNS. Q. 111, 120–21 (1981) (analyzing conflict of interest when insured must make offer within policy limits and asserting that "the insurance industry must simply recognize that it will not be able to rely upon the failure of the plaintiff to make a policy demand").

132. *See* Commercial Union Ins. Co. v. Liberty Mut. Ins. Co., 393 N.W.2d 161, 167 (Mich. 1986) (Levin, J., concurring) (noting that insurer, by logical necessity, may elevate its interests above insured's, but may not do so in bad faith); *see also* Wilkie v. Home Sec. Life Ins. Co., 514 F. Supp. 896, 900 (D.S.C. 1981) (recognizing "high duty of good faith and fair dealing" imposed by courts to force insurers to fairly consider insured's interests in deciding whether to settle or litigate); Farris v. United States Fidelity & Guar. Co., 587 P.2d 1015, 1020 (Or. 1978) (stating that, because insured has nothing to gain and everything to lose if insurer fails to effect settlement, courts impose "'high duty of good faith and fair dealings when conducting settlement negotiations on behalf of their insured'" (quoting Santilli v. State Farm Life Ins. Co., 562 P.2d 965, 969 (Or. 1977))); Charlie D. Dye, Comment, *Insurer's Liability for Judgments Exceeding Policy Limits*, 38 TEX. L. REV. 233, 240 (1959) (noting that insurer may not be liable for reasonable mistakes). Insurer misconduct is not altogether rare and, when existent, can severely damage the insured. *See* Joseph A.

tle by affording insureds the full benefit of their insurance bargain and reasonably attempting to settle.[133] Instead of creating a threshold triggered solely upon a within-limits settlement demand, the determination of reasonableness should be made in consideration of all the circumstances surrounding the claim, both parties' attempts to negotiate, and the evaluation of the claim.[134]

To suspend the *Stowers* duty pending a formal within-limits settlement demand misconceives the special relationship between insurer and insured giving rise to the duty to exercise care. A conflict of interest between insurer and insured arises the moment a third-party asserts a claim for damages in excess of policy limits. Simultaneously, the insurer's resulting duty to exercise its discretion in settling the claim with reasonable

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Bosco, *Insurance Companies: Exposure to Liability for Wrongful Treatment of Claimants*, 32 TRIAL LAW. GUIDE 105, 106 (1988) (discussing typical case of insurer's procrastination and indecisiveness when insured was exposed to avoidable excess damages).

133. *See Garcia*, 876 S.W.2d at 863 (Hightower, J., dissenting) (stating that reasonable attempts to settle may include good faith evaluation of case, investigation and exploration of settlement chances, and entering into reasonable negotiations); *Guin*, 723 S.W.2d at 659 (intimating insurer's duty of care as including reasonable efforts to settle); *see also Rova Farms*, 323 A.2d at 507 (reasoning that insurer may escape extra-contractual liability by exercising good faith in attempting to settle); *Rowland*, 427 S.W.2d at 34 (suggesting that "always present" conflict of interest requires insurer to reasonably attempt settlement); Eric M. Holmes, *Third Party Insurance Excess Liability and Its Avoidance*, 34 ARK. L. REV. 525, 539-48 (1981) (discussing insurer's affirmative duties to investigate, evaluate, and negotiate third-party claims).

134. *See Garcia*, 876 S.W.2d at 863 (Hightower, J., dissenting) (noting that insurer's duty need not hinge upon settlement demands and does not require insurer to make unilateral or initial settlement offers or to bid against itself); *Guin*, 723 S.W.2d at 659 (stating that duty to exercise care extends to investigation, preparation for trial, trial, and reasonable attempts at settlement); Globe Indem. Co. v. Gen-Aero, Inc, 459 S.W.2d 205, 208 (Tex. Civ. App.—San Antonio 1970, writ ref'd n.r.e.) (providing relevant factors for determination of *Stowers* breach, including opportunities for settlement, failure to negotiate or counteroffer, and failure to investigate); *see also Bowers*, 237 A.2d at 861 (requiring that insurer's decision not to settle be "honest, intelligent and objective"). *See generally* Joan B. Lefkowitz, *New York Third Party Bad Faith: Is It a Plaintiff's Dream or a Defendant's Nightmare?*, 12 PACE L. REV. 543, 563–69 (1992) (advocating negligence standard of care in lieu of bad faith standard as former would force insurers to consider insured's interests more carefully). Most jurisdictions allow consideration of several factors in the determination of negligence or bad faith. *See Commercial Union Ins. Co.*, 393 N.W.2d at 165–66 (listing several factors that may be considered by factfinders); Thomas B. Alleman, *The Reasonable Thing to Do: The Insurer's Duty to Settle Claims Against Its Insured*, 50 UMKC L. REV. 251, 271–76 (1982) (comparing factors used by different jurisdictions to determine bad faith or negligent breach of duty to settle); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. d, illus. 3 (1981) (providing example of breach of obligation of good faith performance by evading spirit of bargain); Howard S. Chapman, *Liability of Insurers and Defense Attorneys for Judgments in Excess of Policy Limits*, 36 TRIAL LAW. GUIDE 481, 495–97 (1992) (analyzing cases in which court held insurer liable for failure to settle claim reasonably or in good faith).

care arises as well. *Garcia* denies this conflict of interest and its attendant responsibilities, giving insurers carte blanche to abuse their contractual discretion. If the Supreme Court of Texas fails to give true effect to the special contractual relationship with its extra-contractual duties, the legislature should reinvest insureds with the protection *Stowers* and its progeny formerly provided. At present, however, *Garcia* has supplanted the *Stowers* doctrine, and insurers owe only an occasional duty of care in making reasonable attempts to settle claims against their insureds.

James Martin Truss