Howard v. American National Fire Insurance Co.: Unsettling Case Concerning an Insurer's Duty to Settle

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It once appeared to be settled in California that to establish bad faith against an insurer for breaching the duty to settle, the insurer must have rejected a reasonable settlement demand *within its policy limit*. So, an insurer confronted with a claimant's $2 million demand - but whose policy limit was only $500,000 - could not be found liable in bad faith for having rejected the demand.

But what if other liability carriers are added to the mix? In a progressive loss case, for example, how should an insurer respond to a settlement demand that is *more than* its policy limit, but *less than* the combined total of all the insurers' limits? Assume the demand is still $2 million, and the insurer's policy limit is $500,000 - but the aggregate limit of all carriers is $4 million. Because the demand obviously exceeds *its* policy limit, can the insurer reject such a demand without incurring bad faith liability?

Until a few weeks ago, many insurers likely would have been advised that they could reject such a demand with impunity. Not anymore. *Howard v. American National Fire Insurance Co.*, 187 Cal. App. 4th 498 (2010) appears to have changed the application of the "demand within policy limit" rule, at least where multiple insurers - as opposed to only a single insurer - may afford coverage for the loss.

In *Howard*, claimant James Howard sued the Roman Catholic Bishop of Stockton, alleging negligent hiring and supervision of a priest who sexually abused him for years as a child. Several of the Bishop's insurers agreed to defend, but American National did not. Howard's lowest settlement demand before trial was for $1.85 million. American National's limits were $500,000. And the aggregate total of all the multiple insurers was $4.3 million. American National did not tender its limits in response to the demand, and the case did not settle.

At trial, Howard obtained a multi-million dollar judgment against the Bishop. He then sued American National based on a "failure to settle" theory and obtained a nearly $3 million bench trial judgment against the company.

The First District Court of Appeal affirmed. The court held that an insurer who fails to tender its policy limits merely because the demand exceeds those limits - in a multiple insurer case - is not insulated from bad faith liability.

> American did not respond to the settlement demand with its policy limits and, had it and other insurers done so, could have settled the litigation . . . . [T]he law cannot excuse one insurer for refusing to tender its policy limits simply because other insurers likewise [refused to do so]. If this were not the case, insurers on the risk could simply all act in bad faith, thus immunizing themselves from bad faith liability.

Howard at 525.

Thus, *Howard* rejects the position often taken by insurers in multiple insurer cases - that an insurer is under no duty to settle where a reasonable settlement demand ($2 million) exceeds its policy limit ($500,000), but is less than the combined total of all insurers' limits ($4 million). Rather, each insurer that rejects such a demand now faces potential bad faith liability.

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Unfortunately, *Howard's* analysis is fundamentally flawed because it fails to take into account two critical issues. First, an insurer cannot offer to settle unless the claimant agrees to release all claims against the insured in return. Indeed, an insurer may be found liable for bad faith if it pays its limits without getting a release. *State Farm Mut. Auto. Ins. Co. v. Crane*, 217 Cal. App. 3d 1127, 1136 (1990) ("such an unconditional payment, which has the effect of bankrolling a plaintiff's case against the insured, is not made in good faith").

Second, in order to establish that an insurer's failure to settle a claim constituted actionable "bad faith," it must be shown that the claimant *would have accepted* the insurer's tender had it been made.

In *Howard*, there was no evidence whatsoever that the claimant would have released his claims against the Bishop in return for American National's limit. To the contrary, it was clear that the claimant would have been willing to release the Bishop only on obtaining $1.85 million, not $500,000. Thus, the *Howard* court erred because the causation requirement for establishing a bad faith failure to settle claim – that the claimant would have released all claims against the insured in exchange for the proffered settlement - was not (and could not have been) shown.

Currently, American National is challenging the decision. It is unclear if it will be reviewed by the California Supreme Court. For now, it remains a citable case - unsettling for many insurers.