Extra-Contractual Damages Still Problematic for Insurers in Rhode Island Ten Years After State Supreme Court's *Asermely Decision*

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For more than ten years insurers conducting business in Rhode Island have faced the risk of extra-contractual liability without a finding of bad faith. In Asermely v. Allstate Ins. Co., 728 A.2d 461 (R.I. 1999), the Rhode Island Supreme Court took the "opportunity to promulgate a new rule" and required insurers to pay any excess judgment where the insurer rejects a settlement demand within its policy limits.

Extra-contractual liability is imposed, moreover, even in circumstances where the insurer rejects the settlement offer in good faith. While the decision remains problematic for insurers in assessing settlement demands and determining litigation risk, few cases decided since Asermely have provided any meaningful guidance or attempted to restrict its scope. Ten years later, therefore, insurers continue to face significant uncertainty regarding extra-contractual liability in Rhode Island.

An Unprecedented Expansion of Extra-Contractual Liability

The Asermely Decision

Rhode Island long adhered to the traditional rule that a finding of bad faith was required before imposing extra-contractual liability on an insurer. Insurers were therefore exposed to extra-contractual liability for wrongfully refusing to pay or settle a claim, or failing to timely perform obligations under an insurance policy, among other things. Rhode Island codified a cause of action for bad faith in R.I. Gen. Laws § 9-1-33, and also recognized a bad faith cause of action at common law.[1] Prior to Asermely, Rhode Island permitted only a limited exception to this rule. In the event that an insurer rejected a settlement offer within its policy limits, R.I. Gen. Laws § 27-7-2.2 required the insurer to pay any pre- or post-judgment interest on an excess judgment.

Asermely expanded extra-contractual liability far beyond these well-recognized limitations. The plaintiff, Michelle Asermely, sought damages from an insured of Allstate Insurance Company ("Allstate") as a result of an automobile accident. Prior to trial, the parties submitted the matter to non-binding, court-annexed arbitration. That proceeding resulted an award in favor of Asermely in the amount of $47,557.37, which was within Allstate's policy limits of $50,000. Asermely accepted the award but, despite the award being within the policy limit, Allstate rejected it and proceeded to trial. At trial, the jury found that the plaintiff was sixty percent negligent and the defendant forty percent negligent. Ultimately, the jury awarded Asermely $86,333.57 in damages and interest. Allstate then issued a check to the plaintiff for $50,000, the limit of its policy. After cashing the check, the plaintiff brought suit against Allstate alleging, among other things, that Allstate acted in bad faith in settling the claim.

The Court began its analysis by concluding that the plaintiff's bad faith claim should be dismissed because it was "fairly debatable" whether Allstate had a "reasonable basis" for rejecting the award. However despite dismissing the bad faith claim, the Court then, sua sponte, announced that it was taking the "opportunity to promulgate a new rule to guide the trial courts in deciding these issues":

It is not sufficient that the insurance company act in good faith. An insurance company's fiduciary obligations include a duty to consider seriously a plaintiff's reasonable offer to settle within the policy limits. Accordingly, if it has been afforded

reasonable notice and if a plaintiff has made a reasonable offer to a defendant's insurer to settle within the policy limits, the insurer is obligated to seriously consider such an offer.

The Court went on to impose extra-contractual liability on insurers who fail to meet these requirements:

[T]he insurer is liable for the amount that exceeds the policy limits, unless it can show that the insured is unwilling to accept the offer of settlement. ... Even if the insurer believes in good faith that it has a legitimate defense against the third party, it must assume the risk of miscalculation if the ultimate judgment should exceed the policy limits.

The "new rule" announced by the Court was not based on analysis of existing precedent, nor was it grounded in legislative history. Indeed, the existing legislation at the time, R.I.G.L. § 27-7-2.2, stopped short of imposing such obligations on an insurer. Rather, the rule announced by the Court appears to have been fashioned in response to the unique facts before it, and in an effort to regulate the conduct of insurers in future cases.

Aftermath of Asermely

Cases decided in Rhode Island since Asermely have provided only modest guidance to insurers seeking to avoid extra-contractual liability. Beginning with Bolton v. Quincy Mutual Fire Ins. Co., 730 A.2d 1079 (R.I. 1999), the Court reaffirmed its decision in Asermely and demonstrated no retreat from the rule announced in that case. In Bolton, an issue arose regarding whether a plaintiff was entitled to discovery from his insurer regarding any investigation the insurer performed to determine whether the plaintiff should be given permission to settle with the tortfeasor. Relying on Asermely, the Court ruled that the plaintiff had a right to limited discovery to determine if the insurer performed an investigation, or whether it simply denied his request to settle within the policy limits. The Court reasoned that the insurer placed itself at risk for a bad faith claim because it denied its insured the right to settle within the tortfeasor's policy limits.

In Travelers Ins. Co. v. Hindle, 748 A.2d 256 (R.I. 2000), the Court again commented on the duty of an insurer to conduct a reasonable inquiry when considering a settlement offer. In Travelers, a motorist was injured when his car was struck by a vehicle owned by the defendant. After the accident, the plaintiff filed a claim for benefits with Travelers Insurance Co. ("Travelers") under a policy issued by his employer. Prior to trial, the defendant's insurance carrier offered to settle with the motorist for the policy limit. Pursuant to the underinsured motorist clause in his policy with Travelers, the plaintiff requested permission to settle with the defendant for his policy limits. Upon receiving this request, Travelers intervened in the action and asked for permission to conduct asset discovery of the defendant to assess its ability to maintain a future subrogation action. The Superior Court granted Travelers' request for asset discovery, but was reversed by the Rhode Island Supreme Court.

In reaching the decision that discovery was not permitted, the Court held that Bolton stands for the proposition that "an insurer's duty to its insured to seriously consider an offer by a tortfeasor to settle is deemed satisfied when that insurer has conducted a reasonable inquiry into the assets of the defendant to the extent permissible by means of private asset discovery", but "if the insurer then chooses to deny permission for its insured to settle based on that inquiry, that the decision should be supported by a reasonable and objective basis." Further complicating the analysis, the Court held that "the reasonableness standard in Asermely and its progeny, Bolton, is necessarily flexible, and we are reluctant to give it rigid judicial shape."

Following the decisions in Bolton and Travelers, the Court next addressed Asermely in Skaling v. Aetna Ins. Co., 799 A.2d 997 (R.I. 2002). In Skaling, the plaintiff brought suit against Aetna Insurance Co. ("Aetna"), alleging breach of contract for refusal to pay underinsured motorist insurance benefits and bad faith, both in the handling of the claim and in refusing to settle. Following a trial on the breach of contract claim, Aetna moved for and obtained summary judgment on Skaling's bad faith claim. The Rhode Island Supreme Court reversed the Superior Court's decision to grant Aetna summary judgment reasoning that there was a triable issue of fact regarding the issue of bad faith. In reinforcing its prior determination that extra-contractual liability exists even in the absence of bad faith, the Court concluded that "[i]n Asermely, although we concluded that Allstate did not act in bad faith . . . we held that Allstate must bear the risks attendant to its failure to settle

a claim within the policy limits" because the rule it announced placed the "risk of miscalculating the merits of a claim and proceeding to trial" on the insurer.

Ten Years Later Uncertainty Still Persists

Although the Rhode Island Supreme Court articulated a "new rule" for extra-contractual liability, it has failed to provide guidance regarding what steps an insurer must take to comply with Asermely's mandate to "consider seriously" a settlement offer, or what constitutes a "reasonable" offer. First, an insurer that declines a settlement offer within the policy limit faces a significant hurdle in establishing that the offer was not reasonable. Essentially, the insurer must persuade a court that the offer, even though within the policy limit, was unreasonable despite a jury verdict that the claim was worth more than the offer. Although not impossible, it is difficult to envision a court holding that a settlement offer within a policy limit was unreasonable, where a jury later returns a verdict with an award that is higher than the original settlement offer. Because of this dichotomy, insurers must recognize the difficulty they will confront after denying a settlement offer within their policy limits.

Secondly, although language from subsequent cases appears to contemplate an insurer's need for adequate information in seriously considering the settlement offer, the decisions in Travelers and Bolton demonstrate that an insurer faces significant obstacles in gathering that information in certain circumstances. Moreover, the Court has provided no guidance on what steps an insurer must take to "seriously consider" a settlement offer, nor has the Court indicated that an insurer would be insulated from liability if it complies with this directive. Rather, because the insurer "must assume the risk of miscalculation if the ultimate judgment should exceed the policy limits", it appears that, under Asermely, an insurer is subject to extra-contractual liability if it simply comes to the incorrect conclusion in rejecting an offer within the policy limits.

Conclusion

The Rhode Island Supreme Court's decision in Asermely represents an unprecedented expansion of extra-contractual liability for insurers. Although Rhode Island courts still apply the bad faith standard, insurers face significant risk of liability for an excess judgment where they refuse a settlement demand within the policy limits – even if the insurer acts in good faith in declining the offer. Moreover, cases decided since Asermely reinforce its holding while failing to provide significant guidance on what steps an insurer must take to "consider seriously" a settlement offer, or what constitutes a "reasonable" offer. Simply put, as the Rhode Island Supreme Court succinctly stated ten years ago, an insurer that declines an offer within its policy limit "does so at its peril."

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[1] See Bibeault v. Hanover Ins. Co., 417 A.2d 313 (R.I. 1980); see also Robertson Stephens, Inc. v. Chubb Corp., 473 F.Supp.2d 265, 271 (D.R.I. 2007) ("In Bibeault, the Rhode Island Supreme Court . . . recognized an independent cause of action in tort for an insurer's bad faith refusal to deliver payments."); Skaling v. Aetna Ins. Co., 799 A.2d 997, 1003 (R.I. 2002) (noting that Bibeault "recognized the common law tort of insurer bad faith in the context of the wrongful refusal to pay an uninsured or underinsured (UM-UIM) claim").