Insurer's Wrongful Refusal to Settle: A Note on Excess

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INTRODUCTION

The typical liability insurance policy reserves in the insurer the exclusive right to defend in any action on the policy, including the right to investigate, negotiate, and settle any claim or suit against the insured. By entering into the policy, the insured has surrendered a valuable right, that of conducting an investigation and considering possible offers for settlement. The contract gives the insurer complete discretion with regard to an action brought against the insured. Based on the duties created by the policy, a non-contractual, fiduciary relationship arises, so that the insurer and the insured owe to each other the duty to exercise the utmost good faith.

When the insured is sued for an amount in excess of the limits of the liability insurance policy, the insurance company has its

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1. The typical liability insurance policy contains the following language:
   (a) defend any suit against the insured alleging such injury, sickness, disease or destruction and seeking damages on account thereof, even if such suit is groundless, false or fraudulent; but the company may make such investigation negotiation and settlement of any claim or suit as it deems expedient.


Even if there is no express term in the policy giving the insurer the right to investigate and settle, the clause requiring the insurer to defend naturally encompasses investigation and negotiation of any settlement prior to trial. Cooley v. Mid-Century Ins. Co., 52 Mich. App. 612, 218 N.W.2d 103 (1974).

The exclusive right of the insurer to defend is not without public policy considerations. Insurance is a regulated industry clothed in the public interest. Large sums of money are involved, supported by insurance premiums paid by the public. The insurer has exclusive control over the litigation against the insured, who is required to surrender to the insurer all the control of the defense in order to insure an orderly and proper disbursement of these funds and to minimize unwarranted claims. 7C J. Appleman, Insurance Law & Practice 2 (1979).

2. 7C J. Appleman, supra note 1, at 512.
4. Ballard v. Citizens Casualty Co., 196 F.2d 96, 102 (7th Cir. 1952) (applying Illinois law) (citing American Fidelity & Casualty Co. v. G.A. Nichols Co., 173 F.2d 830 (10th Cir. 1949)).
own interests as well as those of the insured to protect. The insurer's goal is to dispose of the claim as inexpensively as it can; the insured usually desires a settlement within or at the policy limits so that he will not be exposed to any personal liability. The claimant generally desires to settle for the policy limits, preferring that certainty to the risk of trial and the possibility of having to enforce an excess judgment against a possibly insolvent insured.

The typical liability insurance policy covers the insured up to the policy limits. If a larger verdict is returned against the insured, the insured will be forced to pay all sums in excess of the policy coverage.

A suit for wrongful refusal to settle is a separate suit brought by the insured, the claimant, or an assignee of the insured against the insurer after an excess judgment.

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5. Keeton, supra note 1, at 1142.

6. For purposes of this note, "insurer" refers to the insured's liability carrier, "insured" refers to the party with insurance who is being sued, and "claimant" refers to the individual who brought the original cause of action against the insured.

7. The overwhelming majority of cases are settled. A 1959 study of New York personal injury litigation notes that 98% of the cases are disposed of through negotiation without direct judicial intervention. Franklin, Chenin, & Mark, Accidents, Money and the Law: A Study of the Economics of Personal Injury Litigation, 61 COLUM. L. REV. 1, 32 (1961). See also 1 ALL-INDUSTRY RESEARCH ADVISORY COMMITTEE, AUTOMOBILE INJURIES AND THEIR COMPENSATION IN THE UNITED STATES 14 (1979) (indicating that, on the average, 20% of all bodily injury claims produce lawsuits, 1.5% go to trial, and 0.9% proceed to judgment).

8. The typical liability insurance policy contains the following:

As respects the insurance afforded by the other terms of this policy . . . the company shall:

(c) pay all expenses incurred by the company, all costs taxed against the insured in any such suit and all interest accruing after entry of judgment until the company has paid, tendered or deposited in court such part of such judgment as does not exceed the limit of the company's liability thereon.

Keeton, supra note 1, at 1137 n.1.


11. The suit can be brought by the insured or by the claimant as assignee of the
is rendered in the original action. Under this cause of action, the insurer who has refused to settle may become liable for the entire


Insurers rarely assert that an insured cannot assign a claim. See Annot., 12 A.L.R.3d 1158 (Supp. 1979). There is disagreement among Illinois courts, however, as to whether a court can order the assignment of a claim. In Roundtree v. Barringer, 92 Ill. App. 3d 903, 416 N.E.2d 675 (1981), the court held that public policy precludes the involuntary assignment of a bad-faith claim. The court noted that the rationale typically advanced includes the following: the judgment creditor has not been harmed but rather has benefitted from the insurer's wrongful refusal to settle because it has received an excess judgment against the judgment debtor; if involuntary assignment were allowed, the insured would be deprived of his right to bargain with his judgment debtor for release of liability in consideration of an assignment; and involuntary assignment would constitute a legally enforceable form of champerty and encourage specious litigation because it would allow the judgment creditor to go on a "fishing expedition." Id. at 905-06, 416 N.E.2d at 677.

This conclusion was rejected in Phelan v. State Farm Mut. Auto. Ins. Co., 114 Ill. App. 3d 96, 448 N.E.2d 579 (1983). The issue of involuntary assignability arose in a citation-to-discover-assets proceeding, which is governed by ¶ 2-1402 of the Illinois Code of Civil Procedure, ILL. REV. STAT. ch. 110, ¶ 2-1402 (1981). Paragraph 2-1402 allows the court to "[c]ompel the judgment debtor to deliver up, to be applied in satisfaction of the judgment, in whole or in part... choses in action...." Id. at ¶ 2-1402(b)(1). Phelan found no limitation on the nature of the choses in action for which assignment may be compelled. Furthermore, the court found the mere possibility of collusive conduct on the part of the injured party and the insured against the insurer to be an insufficient basis to deny a right of action. In addition, an injured claimant can better determine whether an action for wrongful refusal to settle may lie against an insurer because it is the claimant who conducts the settlement negotiations with the insurer.

Illinois, like most jurisdictions, does not allow the claimant to bring an excess liability suit directly where no assignment has been made. Scroggins v. Allstate Ins. Co., 74 Ill. App. 3d 1027, 393 N.E.2d 718 (1979); Yelm v. Country Mut. Ins. Co., 123 Ill. App. 2d 401, 259 N.E.2d 93 (1970) (notwithstanding his position as judgment creditor against the insured, an injured party has no direct action against the insurer for breach of the duty to the insured to exercise good faith or due care). Accord Murphy v. Allstate Ins. Co., 17 Cal. 3d 907, 553 P.2d 584, 132 Cal. Rptr. 424 (1976).

Scroggins points out that since no excess judgment has been rendered against the insured, it is purely speculative whether the alleged breach of duty will ever result in the injury that normally gives rise to an action for breach of that duty. Furthermore, potential difficulties, such as the possibility that insurers will be coerced into settling where their liability has not and may never be established, outweigh the necessity of such an action.

Some courts have recognized direct actions by judgment creditors. One of the first was the California Supreme Court in Royal Globe Ins. Co. v. Superior Court, 23 Cal. 3d 880, 592 P.2d 329, 153 Cal. Rptr. 842 (1979). In allowing direct action, the court relied on language contained in the Unfair Claims Settlement Practices Act, CAL. INS. CODE § 790.03(h)(5) (West Supp. 1979), finding a vested right in the claimant to bring the cause of action. Scroggins found no similar wording in the Illinois equivalent of the California act, ILL. REV. STAT. ch. 73, ¶¶ 766.5-766.8 (1977).
judgment, regardless of the policy limits.\textsuperscript{12} The entry of that part of the judgment against the insured which exceeds the policy limits constitutes the damages the court will permit the insured to recover.\textsuperscript{13} It is the insurer’s wrongful failure to settle rather than the mere existence of the excess judgment which triggers the cause of action.\textsuperscript{14}

The purpose of this note is to examine the cause of action for wrongful refusal to settle in Illinois and to determine what type of activity on the part of the insurer will expose it to excess liability. The valid reasons of the insurer for declining to settle within the policy limits will be examined along with the insured’s and claimant’s reasons for desiring settlement. This note will analyze how the Illinois Appellate Court has balanced the parties’ conflicting interests in the setting of the wrongful refusal to settle suit by considering the recent Illinois cases of \textit{Adduci v. Vigilant Insurance Co.}\textsuperscript{15} and \textit{Phelan v. State Farm Mutual Automobile Insurance Co.}\textsuperscript{16} This note will discuss the differing positions that the Illinois Appellate Court has taken on the issue, examine the public policy implications of the decisions, and suggest a standard for Illinois courts to follow.


It is not a condition precedent to recovery that the insured has paid or has the ability to pay the excess judgment. Wolfberg v. Prudence Mut. Casualty Co., 98 Ill. App. 2d 190, 240 N.E.2d 176 (1968). Were payment or the ability to pay the rule, the insurer with an insolvent insured would be given encouragement to unreasonably refuse to settle, thus severely impairing the use of insurance for the poor. See also Schwartz v. Norwich Union Indem. Co., 212 Wis. 593, 250 N.W. 446 (1933) (to prevent the injustice of the insured being required to pay a judgment that is arguably wrongfully imposed).

\textsuperscript{12} See \textit{Phelan}, 114 Ill. App. 3d at 102, 448 N.E.2d at 583; \textit{Scroggins}, 74 Ill. App. 3d at 1030, 393 N.E.2d at 720; Cernoky v. Indem. Ins. Co. of N. Am., 69 Ill. App. 2d at 204, 216 N.E.2d at 203 (1966); Olympia Fields, 325 Ill. App. at 649, 60 N.E.2d at 895. See also Keeton, \textit{supra} note 1.

\textsuperscript{13} See \textit{Scroggins}, 74 Ill. App. 3d at 1030, 393 N.E.2d at 720; \textit{Wolfberg}, 98 Ill. App. 2d at 197, 240 N.E.2d at 180.

\textsuperscript{14} Kavanaugh v. Interstate Fire & Casualty Co., 35 Ill. App. 3d at 356, 342 N.E.2d at 121 (1975) (insurer’s refusal to settle within policy limits does not render it liable per se for the excess judgment to its insured); Browning v. Heritage Ins. Co., 33 Ill. App. 3d at 946, 338 N.E.2d at 915 (there is no precedent for a theory which would render the insurer liable per se to its insured).


BACKGROUND

 Origin of the Duty

 Illinois first recognized a cause of action against an insurer for wrongful refusal to settle within policy limits in *Olympia Fields Country Club v. Banker's Indemnity Insurance Co.* The court allowed the insured to sue the insurer for the damages awarded in excess of the policy limits where the evidence showed that the injured claimant had offered to settle within policy limits after the trial court awarded damages in excess of that amount.

 The *Olympia Fields* court struggled with whether the action should sound in tort or in contract, but did not clearly answer this question. The court did recognize a duty on the part of the insurer arising from the contract, although the duty is not expressed in the terms of the contract. The scope of the duty

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17. 325 Ill. App. 649, 60 N.E.2d 895 (1945). In *Olympia Fields* the policy limit was $10,000; the injured claimant offered to settle its claim for $3,500, but the insurer refused to settle. After a $20,000 verdict for claimant at trial, claimant offered to settle for $8,000, but the insurer again refused because it had appealed.

18. *Id.* at 670, 60 N.E.2d at 906. After the excess judgment was affirmed by the appellate court and the Illinois Supreme court denied an appeal, insurer paid to claimant $10,815.80, the balance due her, and sued to recover that amount from insurer. *Id.* at 651, 60 N.E.2d at 897.

19. In jurisdictions holding that this cause of action sounds in tort, it is said that the insurer has undertaken a duty to the insured to settle, under certain circumstances, by insisting on controlling the defense of the insured and any settlement negotiations that will bind it to pay. See, e.g., Zumwalt v. Utilities Ins. Co., 360 Mo. 382, 228 S.W.2d 760 (1950); Hart v. Republic Mut. Ins. Co., 152 Ohio St. 185, 87 N.E.2d 347 (1949); Carne v. Maryland Casualty Co., 208 Tenn. 403, 346 S.W.2d 259 (1961); Southern Fire & Casualty Co. v. Norris, 35 Tenn. App. 657, 250 S.W.2d 785 (1952); Keeton, supra note 1, at 1138.


21. The court examined what other states had done and found disagreement as to the nature and kind of proof necessary to make out a prima facie case of wrongful refusal to settle against the insurer. The court did note, however, that “[a]ll of [the cases in the sister states] acknowledge that an insurer may be liable for the entire judgment recovered against an insured although the judgment exceeds the amount of liability in the policy if the insurer be guilty of fraudulent conduct or a lack of good faith in refusing to settle.” 325 Ill. App. at 660, 60 N.E.2d at 891.

22. *Olympia Fields* quoted several cases, with apparent approval, which held that an insurer's duty to act in good faith and to deal fairly with the insured flows from the contract rather than from the specific terms of the contract. *Id.* at 649, 60 N.E.2d at 901. The court quoted American Mutual Liability Ins. Co. v. Cooper. 61 F.2d 446 (5th Cir. 1932): “We are of the opinion that this relationship imposed upon the insurer the duty,
does not turn on whether its breach is characterized as contractual or tortious, however, since in either event the duty itself springs from the contractual relationship between the parties. Consequently, most Illinois courts have since settled the issue of the scope of duty without answering the question of whether the action was in contract or in tort. The current view in Illinois is that the right of the insured to recover from the insurer for wrongful refusal to settle is an action in tort for breach of duty owed by the insurer, the duty arising from the insurer's exclusive contractual right to settle the claim.

*Olympia Fields* recognized that a duty on the part of the insurer to act in good faith toward the insured's interests arises when an injury occurs for which recovery may be had in a sum exceeding the amount of insurance. The duty arises because,
according to the express terms of the policy, the insured has bartered away all of his rights to discover the extent of the injury, and the insurer has retained the exclusive right to settle the claim. The court held that, absent fraud, negligence, or bad faith, an insurer cannot be held liable for refusing to settle a case within policy limits, even though such refusal may result in a judgment in excess of the policy limits. \textit{Olympia Fields} therefore established a check on the insurer by requiring that it give some deference to its insured's interests.

\textit{Behavior By the Insured Constituting Fraud, Negligence, or Bad Faith}

Conflicting Interests

The policy behind the wrongful refusal to settle cause of action is to allocate the costs of damages fairly when there is a judgment in excess of the policy limits. The main purposes of insurance are to protect the insured from sudden losses, to compensate the injured party, and to spread the costs of injury among those people who benefit from accident-causing activities. Balanced against these interests is the desire to keep the costs of

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14, 235 N.W. at 414-16). The \textit{Hilker} court applied agency law to hold against the insurer. The company was the insured's agent because of the control it exercised over the defense and settlement negotiations. The court held that the manner in which the insurer performed its agency violated its duty to its principal. \textit{Olympia Fields} did not apply agency analysis. Keeton, a well-known authority in the field of insurance law, states that the insured should not be considered a principal because it is the insurer who makes the decision to accept or reject settlement offers. Agency law is thus not properly analogous. R. \textit{KEETON, BASIC TEXT ON INSURANCE LAW} § 7.10(b) (1971).


28. \textit{Olympia Fields}, id., 60 N.E.2d at 906. The \textit{Olympia Fields} court quoted \textit{Hilker} as follows:

\begin{quote}
It is the right of the insurer to exercise its own judgment upon the question of whether the claim should be settled or contested. Its decision not to settle should be an honest decision. If upon such consideration it decides that its interest will be better promoted by contesting than by settling the claim, the insured must abide by whatever consequences flow from that decision.
\end{quote}

\textit{Id.} at 670-71, 60 N.W.2d at 905 (quoting \textit{Hilker}, 204 Wis. at 14, 235 N.W. at 416).

29. Liability insurance was originally intended solely for the benefit and protection of the insured. W. \textit{PROSSER, supra} note 9, at 544. By its terms, liability insurance does not provide compensation for injuries, but in most instances the injured party is compensated where legal fault on the insured's part is proved. \textit{Id.} at 557-58. In theory, an insured defendant is not required to pay the compensation himself. His or her liability is distributed among a large group by insurance premiums. \textit{Id.} at 569.
insurance to the public as low as possible.\textsuperscript{30} Although these factors have not been discussed in most courts' decisions, they are at least implicitly recognized in the courts' treatment of the cause of action.

An injured claimant is normally eager to settle. He likely has significant expenses; protracted litigation only serves to delay his ability to take care of these expenses.\textsuperscript{31} Furthermore, the claimant runs the risk of not recovering at all should he lose. The insured also desires to settle because a trial would expose him to the risk of liability in the event of a judgment in excess of the policy limits.\textsuperscript{32} Furthermore, because of the high costs of litigation, settlement is also almost always economically preferable to the insurer in cases where liability is likely.\textsuperscript{33}

Nevertheless, in some cases the insurer's interests may not be furthered by settling. The insurer has institutional goals that sometimes are adverse to the interests of the insured.\textsuperscript{34} These

\textsuperscript{30} If insurance premiums become prohibitive, the number who choose to do without insurance will increase. Prosser states that the uninsured, as a group, are often the least responsible financially and are unlikely to be able to pay a judgment. \textit{Id.} at 557.

\textsuperscript{31} J. \textsc{Mirza} \& J. \textsc{Appleman}, \textsc{Illinois Tort Law and Practice} 362 (1974). The plaintiff is most often on the "short side" of the settlement negotiations because of his immediate need for compensation. In addition, lawsuits are usually one-time affairs for most plaintiffs. \textit{See also} Phelan v. State Farm Mut. Auto. Ins. Co., 114 Ill. App. 3d 96, 448 N.E.2d 579 (1983) (the welfare of the claimant's family is important in determining whether the negotiations were such that the insurer was relieved of liability for the judgment in excess of the policy limits).

\textsuperscript{32} \textit{See supra} note 9.

\textsuperscript{33} Not surprinsingly, the more a case is worth, the more likely it is to go to trial, although once on trial, a large case is no more likely than a small one to persist to a verdict. Rosenberg \& Sovern, \textit{Delay and the Dynamics of Personal Injury Litigation}, 59 \textsc{Colum. L. Rev.} 1115, 1152 (1959).

Insurers will often pay off small amounts in order to protect against the possibility of having to pay more in the event the injury becomes more serious later on. R. \textsc{Keeton} \& J. \textsc{O'Connell}, \textsc{Basic Protection for the Traffic Victim} 36 (1965).

The nuisance value of claims and the insurer's desire to maintain good public relations are also factors that may explain the high frequency of settlements. \textit{See} F. \textsc{Harper} \& F. \textsc{James}, \textsc{Torts} 782 (1966). \textit{Cf.} Pretzel, \textit{The Economics of Trial versus Settlement}, 1965 \textsc{Ins. L.J.} 453, 460 (1965) (stating that more nuisance value cases should be tried).

Because the tort system generally requires a person to compensate another only if that person is at fault and, given the fact that not everyone is insured, it is not surprising that 55\% of those significantly injured in traffic accidents get absolutely nothing from the tort liability system. 1 \textsc{U.S. Department of Transportation, Economic Consequences of Automobile Accident Injuries} 37-38 (1970). \textit{See also} \textsc{Conrad}, \textsc{Morgan}, \textsc{Pratt}, \textsc{Votz}, \& \textsc{Bombaugh}, \textsc{Automobile Accident Costs and Payments: Studies in the Economics of Injury Reparation} 186 (1964) (stating that 45\% of the seriously injured get no damage recovery through the tort law system).

\textsuperscript{34} \textit{See Note, Excess Liability: Reconsideration of California's Bad Faith Negligence
institutional goals are primarily economic. Any saving of money by the insurance company is at least a partial saving in premiums by the insurance-paying public. When the insurer believes that the insured is not liable, it will almost certainly choose to go to trial. In addition, it may be more economical to go to trial when the claimant’s demand is too high. These are the types of situations where the court will not find an insurer liable even where there is an excess judgment.

It becomes a more difficult case where an insurer refuses to settle even though the cost of litigation exceeds that of settlement. The insurer may do this in order to create a body of low-verdict or company-victory precedents which can be used as a bargaining tool in later claims. To establish this favorable precedent, an insurer may choose to litigate regardless of the reasonableness of settlement offers. The insurer is in a position to take such action because it usually has the financial ability to withstand protracted negotiations. The claimant, on the other hand, is often on the “short side” of the settlement negotiations, because of immediate financial need.

The insurer’s choice not to settle may still be in the public interest in the sense that it has the effect of keeping the cost of insurance premiums down. On the other hand, by exposing the insured to potential liability, the insurer is not protecting him from sudden losses. Furthermore, the overall societal goal of adequately compensating the injured party is not served, because payment is substantially delayed by the pending litigation. Within this setting arises the action for wrongful refusal to settle.

35. See Pretzel, supra note 33, at 460.
36. An insurer will occasionally settle even when it believes its insured is not liable because of the nuisance value of claims and the insured’s desire to maintain good public relations. 2 F. HARPER & F. JAMES, supra note 33, at 782.
37. See, e.g., Olympia Fields, 325 Ill. App. at 672, 60 N.E.2d at 906 (The insurer has the right to exercise its own judgment. The insured must abide by the consequences of the insurer’s good faith decision to either contest or settle the claim.).
38. Note, supra note 33, at 460.
39. Note, supra note 34, at 480.
40. See supra note 31. The greater the injury, the weaker the victim’s bargaining position becomes and the less able he is to wait for the outcome of litigation. F. James, Accident Liability Reconsidered: The Impact of Liability Insurance, 57 YALE L.J. 549, 568 (1948).
Protection of the Insured’s Interests

Courts attempt to balance the conflicting interests of the insured and the insurer by requiring the insurer to give some consideration to the insured’s interests during the settlement process. The trier of fact is required to make the determination of liability or non-liability concerning wrongful refusal to settle. Jurisdictions differ concerning the extent to which an insurer must consider the insured’s interests in relation to its own. Earlier cases often held that the insurer could give exclusive consideration to its own interests in evaluating the claim and conducting negotiations. Some cases hold that the insurer must give “some” consideration to the insured’s interests. It is most frequently held that an insurer must give equal consideration to both interests, although there is some support for the view that the insurer is required to give the insured’s interests paramount consideration. Illinois courts apply the equal consideration standard, which, because the insurance contract is silent concerning whose interests prevail, the courts believe treats the parties involved most fairly.


42. See *Kleinschmit* v. Farmers Mut. Hail Ins. Assoc., 101 F.2d 987 (8th Cir. 1939) (the insurer is not required to accept even reasonable offers); *Rumford Falls Paper Co.* v. *Fidelity & Casualty Co.*, 92 Me. 574, 43 A. 503 (1899) (since the contract limits the liability of the insurer to the policy limits, the insurer is never liable for anything in excess of that limit).

43. See *Automotive Mut. Indem. Co.* v. *Shaw*, 134 Fla. 815, 184 So. 852 (1938); *Wynnewood Lumber Co.* v. *Travelers Ins. Co.*, 173 N.C. 269, 91 S.E. 946 (1917). In the absence of language to the contrary, all decisions recognizing any liability in negligence or in bad faith for wrongful refusal to settle can be construed to indicate that the insurer must give at least some consideration to the insured’s interests.


46. *Adduci*, 98 Ill. App. 3d at 475, 424 N.E.2d at 648; *DeGraw*, 40 Ill. App. 3d at 37, 351 N.E.2d at 311; *Cernocky*, 69 Ill. App. 2d at 207, 216 N.E.2d at 204; *Olympia Fields*, 325 Ill. App. at 671, 60 N.E.2d at 905; *Scroggins*, 74 Ill. App. 3d at 1029, 393 N.E.2d at 720.

47. *Adduci*, 98 Ill. App. 3d at 479, 424 N.E.2d at 650; *Keeton, supra* note 1, at 1145-46. The equal consideration standard fairly treats both parties because each has voluntarily
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This standard restrains the insurer from proceeding solely on its self-interest.\textsuperscript{48} Instead, while it may still properly give consideration to its own interests, it must also give at least equal consideration to the interests of the insured.\textsuperscript{49}

Grounds for an Action for Wrongful Refusal to Settle

\textit{Olympia Fields} held that an insurer can be liable for the amount in excess of the policy limits where there is “fraud, negligence or bad faith.”\textsuperscript{50} Although these terms have different meanings,\textsuperscript{51} the \textit{Olympia Fields} court seemed to find little significant difference.\textsuperscript{52} The result is that Illinois courts generally continue to use the \textit{Olympia Fields} language, but it is used more as a conclusory phrase than as a descriptive one.\textsuperscript{53}

\begin{itemize}
\item entered into a contract that gives rise to a conflict of interests, but does not specify that one interest or the other should prevail. Id. Cf. infra text accompanying notes 114-16.
\item \textit{Adduci}, 98 Ill. App. 3d at 479, 424 N.E.2d at 650 (1981). Cf. infra text accompanying notes 140-43.
\item Ballard v. Citizens Casualty Co., 196 F.2d at 102 (7th Cir. 1952) (applying Illinois law); \textit{Adduci}, 98 Ill. App. 3d at 479, 424 N.E.2d at 650 (1981); \textit{Cernocky}, 69 Ill. App. 2d at 207, 216 N.E.2d at 204 (1966).
\item \textit{Olympia Fields}, 325 Ill. App. at 673, 60 N.E.2d at 906.
\item In its general sense, “fraud” includes anything calculated to deceive. Illinois Fair Plan Ass’n v. Astirs, Inc., 89 Ill. App. 3d 422, 411 N.E.2d 1050 (1979). “Negligence” has been defined as want of ordinary or reasonable care. 65 C.J.S Negligence §1(2) (1966). “Every tort action grounded in negligence requires the showing of (1) a duty owed by the defendant to the plaintiff, (2) a breach of that duty, i.e., a negligent act or omissions, which (3) proximately cause a (4) resulting compensable injury.” Browning v. Heritage Ins. Co., 33 Ill. App. 3d at 948, 338 N.E.2d at 916. “Bad Faith” has been defined as “actual intent to mislead or deceive another; fraud, the opposite of good faith.” Economy Fire & Casualty Co. v. Western States Mut. Ins. Co., 49 Ill. App. 2d 59, 64, 198 N.E.2d 723, 726 (1964).
\item \textit{Olympia Fields}, 325 Ill. App. at 669, 60 N.E.2d at 904. The court quotes, with apparent approval, \textit{Hilker}, which states:
\begin{quote}
Terms which are not strictly convertible or synonymous have been used by different courts to indicate the same thing. Negligence has been used by some courts to mean the same thing that other courts have designated as bad faith. Bad faith, especially, is a term of variable significance and rather broad application. Generally speaking, good faith means being faithful to duty or one's obligation; bad faith means being recreant thereto.
\end{quote}
\textit{Id.} at 669, 60 N.E.2d at 904 (quoting Hilker, 204 Wis. at 13, 235 N.W. at 414).
\item See, e.g., \textit{Phelan}, 114 Ill. App. 3d at 104, 448 N.E.2d at 584-85 (plaintiff must show breach of good faith in order to recover on a bad-faith claim); \textit{Cernocky}, 69 Ill. App. 2d at 205-06, 216 N.E.2d at 203 (“good faith” and “bad faith” are not terms of art; they mean being faithful or unfaithful to the duty that is owed); \textit{Olympia Fields}, 325 Ill. App. at 669, 60 N.E.2d at 905 (good faith means being faithful to an obligation; bad faith means being recreant to it).
\end{itemize}
Illinois courts generally do not require that the insured prove fraud because such a standard would impose on the plaintiff an almost impossible burden of proving the actual state of mind of the insurer when it refused to accept a settlement. Bad faith, in the sense that the term contemplates a state of mind with an affirmative design of wrongdoing, likewise is not the Illinois standard. It is often stated that the insurer must act in good faith, which means that where an insurer reasonably believes it can win a lawsuit, a refusal to settle an action is not a breach of its duty of good faith. Although Illinois courts have not been entirely consistent in the language they have used in describing the standard, allegations of fraud, negligence, or bad faith are factual issues in which the trier of fact must determine whether the insurer gave equal consideration to its own interests.

54. Ballard, 196 F.2d at 100 (applying Illinois law); Cernocky, 69 Ill. App. 2d at 205, 216 N.E.2d at 203; Olympia Fields, 325 Ill. App. at 664, 60 N.E.2d at 902.


55. General Casualty Co. v. Whipple, 328 F.2d 353 (7th Cir. 1964); Ballard v. Citizens Casualty Co., 196 F.2d 96 (7th Cir. 1952).

56. Ballard, 196 F.2d at 102; Kavanaugh, 35 Ill. App. 3d at 356, 342 N.E.2d at 120; Olympia Fields, 325 Ill. App. at 674, 60 N.E.2d at 907. Kavanaugh stated that because the insurer owes the insured a fiduciary duty, it is therefore obligated to act in good faith.

The good faith standard, as it is used in wrongful refusal to settle cases, permits the insurer to be less responsive to the fiduciary obligation than is any other type of fiduciary. Rova Farms Resort v. Investors Ins. Co., 65 N.J. 474, 323 A.2d 495 (1974).

57. 7C J. APPLEMAN, supra note 2, at 448.

58. In practice there is probably little distinction between the negligence and bad faith standards because, with skillful advocacy for the insured, bad faith is the practical equivalent of negligence. See 7C J. APPLEMAN, supra note 2, at 425; Keeton, supra note 1, at 1140; Roos, A Note on the Excess Problem, 1952 INS. L.J. 192, 194.


Some jurisdictions hold that liability must be based on more than simple negligence. Bad faith may involve negligence, or negligence may indicate bad faith, but negligence alone is not sufficient to render the insurer liable. For a comprehensive discussion com-
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and the insured's interests in defending against the action.\textsuperscript{59}

\textbf{DEVELOPMENT OF ILLINOIS LAW}

\textbf{Insurer's Conduct}

Courts have considered many factors in attempting to determine whether the insurer has given sufficient consideration to the insured's interests.\textsuperscript{60} Illinois law does not demand that an insurer settle within policy limits or invariably suffer the consequences of excess judgment.\textsuperscript{61} The insurer generally has no duty


It has been suggested that jurisdictions like Illinois which use both negligence and bad faith do not include negligence within the concept of bad faith. Under this view, evidence showing that the insurer had an opportunity to settle within policy limits, but never offered more than a substantially lesser amount, together with the fact that the insurer was aware of the serious nature and extent of injuries suffered by the claimant, is sufficient to make a case submissible to the jury. 7C J. Appleman, \textit{supra} note 1, at 519-20.

\textsuperscript{59} See \textit{supra} text accompanying notes 46-49.

\textsuperscript{60} Some of the factors courts have considered are: (1) the strength of the injured claimant's case on the issue of liability and damages; (2) attempts by the insurer to induce the insured to contribute to a settlement; (3) failure of the insurer to properly investigate the circumstances so as to ascertain the evidence against the insured; (4) the insurer's rejection of the advice of its own attorney or agent; (5) the amount of financial risk to which each party is exposed in the event of a refusal to settle; (6) the fault of the insured in inducing the insurer's rejection of the compromise offer by misleading it as to the facts; (7) the insurer's rejection of a compromise offer after an excess judgment had been returned; (8) the existence of reinsurance protection held by the insurer; (9) the insurer's advice to its insured to transfer its assets so as to be immune from an excess judgment; (10) a statement by the insurer regarding the low limit as being an advantage of the case; (11) depreciating statements made by the insurer about the minority or religious status of a party as being grounds for an unreasonably low evaluation; (12) evidence that the insurer favored risking a trial because the insured is judgment-proof; (13) the insurer's rejection of a reasonable settlement offer because all the plaintiffs refused to join; (14) the insurer's increasing its reserves after rejecting a settlement offer; (15) the insurer establishing an arbitrary settlement figure below the policy limits; (16) the insurer's failure to have a representative at trial to increase the settlement offer if the trial went badly; and (17) an indication of willingness to offer the full amount and then a failure to do so by the insurer. The first six factors were mentioned in Brown v. Guarantee Ins. Co., 155 Cal. App. 2d 679, 319 P.2d 69 (1957). Factors seven through seventeen were mentioned in Jarrett, \textit{Lawsuits for Wrongful Refusal to Defend or to Settle}, 28 Ins. Couns. J. 58, 65 (1961).

\textsuperscript{61} Ballard v. Citizens Casualty Co., 196 F.2d 96 (7th Cir. 1952); Kavanaugh v. Interstate Fire & Casualty Co., 35 III. App. 3d 350, 342 N.E.2d 116 (1975) (insurer's refusal to settle within policy limits does not render it liable per se to its insured).

Some courts have discussed holding the insurer strictly liable for damages in excess of policy limits. See \textit{e.g.}, Crisci v. Security Ins. Co., 66 Cal. 2d 425, 426 P.2d 173, 58 Cal. Rptr. 13 (1967) (the court stopped short of applying strict liability, but noted several arguments
to initiate negotiations,62 for to place such a duty on the insurer would render it at a negotiating disadvantage.63 An insurer is not required to make a settlement offer where the claimants make it clear that they will not accept such an offer.64 On the other hand, liability does not depend on a claimant making an offer where the insurer refuses to discuss settlement.65 Likewise, no offer is required for liability where the insurer refuses to inform the claimant of the policy limits so that he can determine whether a settlement offer within the policy limits could be made.66 Courts have held this conduct to indicate that the insurer did not give equal consideration to the insured's interests.67

The general rule in Illinois is that where the probability of an adverse finding of liability is great and the amount of damages would greatly exceed coverage, the insurer is liable for the excess if the insurer has failed to settle within the policy limits.68 Thus, one court found that an insurer acted in bad faith when it failed to settle on four separate occasions, told the insured not to retain private counsel, and failed to advise the insured of the adverse verdict and the statutory time to appeal.69 Likewise, in


66. Id.

67. Id.

68. Kavanaugh v. Interstate Fire & Casualty Co., 35 Ill. App. 3d 350, 342 N.E.2d 116 (1975). The court stated this rule as an exception, apparently meaning that an insurer is normally not liable for the excess judgment unless these conditions are met. In Adduci, the court interpreted the Kavanaugh language to mean that if there is a strong probability of an excess judgment, the insurer is required to treat the insured's interests at least equally with its own. 98 Ill. App. 3d 472, 424 N.E.2d at 645.

One commentator characterized the Kavanaugh language as meaning that the court is imposing strict liability when the probability of an excess verdict is great and the probable damages would greatly exceed the available coverage. Haskell & Pope, The Insurer's Conflict of Interest Dilemma, 65 ILL. B.J. 220, 224 (1976).

other cases, courts have found the insurer's failure to settle to be negligent and in bad faith where the insured made numerous demands on the insurer to accept an offer to settle within the policy limits. In each of these cases, the possibility of a favorable decision was minimal.

The Illinois Appellate Court, in Kavanaugh v. Interstate Fire & Casualty Co., reversed an award for wrongful refusal to settle. The case involved the Illinois Guest Statute, which imposed a lower standard of care on the insured, thereby favoring the probability of success for the insured at trial. The court held that the insurer will not always be liable when a judgment in excess of the policy limits is rendered. The cause of action for wrongful refusal to settle does not require trial attorneys to be "endowed with the gift of prophecy so as to be able to predict the precise outcome of personal injury litigation." The court reversed the excess liability award because the issue of liability in the original action was not so clear cut as to make the insurer's liability sufficiently probable.

The Kavanaugh court required the insurer to settle within the policy limits only if the probability of an adverse finding on liability is great and the amount of damages would greatly exceed coverage. By setting out this test, the court struck a balance among the desire of the insured to settle within the policy limits, the societal goal of compensating injured claimants as quickly as possible, and the desire of the insurer to avoid paying damages.

Adduci and Phelan

Two recent Illinois cases illustrate different approaches to the wrongful refusal to settle suit and the problems courts have had in interpreting the Kavanaugh test. Both Adduci v. Vigilant In-

71. See Smiley, 13 Ill. App. 3d at 813, 301 N.E.2d at 21; Cernocky, 69 Ill. App. 2d at 203, 216 N.E.2d at 202.
73. ILL REV. STAT. ch. 95 1/2, § 10-201 (1981).
74. Kavanaugh, 35 Ill. App. 3d at 357, 342 N.E.2d at 121.
75. Id. at 356, 342 N.E.2d at 121.
76. Id. at 357, 342 N.E.2d at 121. For a criticism of the Kavanaugh result see J. Mirza & J. Appleman, supra note 31, § 13.7 (Cum. Supp. 1983) (calling the decision "ill-conceived").
77. Kavanaugh, 35 Ill. App. 3d at 356, 342 N.E.2d at 121.
78. Id.
surance Co. and Phelan v. State Farm Mutual Insurance Co. involved instances where the insurer responded to the injured claimant’s offer and made a tender of the policy limits. In both cases, however, the insurer tendered after the injured claimant’s deadline. The tender was then rejected.

The cause of action in Adduci arose out of a one-car accident involving the insured and three injured claimants. One of the claimants made an offer to settle at the policy limits, but the insurer requested a discount. Later, all of the claimants made an offer to settle at the policy limits, setting a twenty-eight day deadline, but the insurer did not respond within the time limit. Forty-four days after the offer had expired, the insurer offered to pay the policy limits. The claimants declined the offer. Two of the claimants settled; one went to trial and received a verdict for $70,000, of which the insurer paid the policy limits. The claimant accepted an assignment from the insured to bring the excess judgment action against the insurer.

In the pleadings, the claimant asserted that the insurer was aware that it would probably be held liable and had admitted that the claimant’s injuries alone were likely to exceed the policy limits. The appellate court held that the pleadings were sufficient to create a duty upon the insurer to treat the insured’s interest at least equal to its own. The pleadings stated that the claimant’s reason for refusing to accept the insurer’s offer some forty-four days after the claimant’s deadline was that it had expended additional effort in preparing for trial, thereby necessitating a

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81. Phelan, 114 Ill. App. 3d at 99, 448 N.E.2d at 581; Adduci, 98 Ill. App. 3d at 474, 424 N.E.2d at 647.
82. Adduci, 98 Ill. App. 3d at 474, 424 N.E.2d at 647.
83. Id.
84. Id.
85. Id.
86. Id. at 475, 424 N.E.2d at 647.
87. Id.
88. Id. After the first two claimants settled, $17,500 of coverage remained. After the insurer tendered this amount, there remained an unpaid balance of $52,500.
89. Typically, excess judgment suits are brought by the original claimant as assignee of the insured. See supra note 11 for a discussion on the nature and validity of the assignment.
90. Adduci, 98 Ill. App. 3d at 474, 424 N.E.2d at 647. The policy in question had a $25,000 single bodily injury liability limit.
91. Id.
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different fee arrangement. The court held, however, that even if the allegations in the complaint were proved, the claimant would not be allowed to recover because there were no facts in the complaint sufficient to show why the offer was unacceptable to the claimant.

The court in *Phelan* took a different view. In *Phelan*, the claimant was rendered a quadriplegic when the insured’s automobile struck the automobile in which the claimant was a passenger. The claimant offered to settle for the policy limits, setting an expiration date for the offer; after that date, the claimant would move for trial. After a counteroffer by the insurer and further negotiations, no agreement had been reached. One month after the claimant’s deadline, the insurer expressed concern that an excess judgment would be rendered and offered the policy limits. The claimant rejected this offer.

The jury found for the insurer, but the appellate court reversed and ordered a trial on the issue of damages. The jury then assessed damages at $350,000. The claimant received an assignment of the insured’s excess liability claim and went to

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92. *Id.* at 477, 424 N.E.2d at 649.
93. *Id.* The court gave controlling significance to the fact that the insured did respond with an offer of the policy limits.
95. *Id.* at 97, 448 N.E.2d at 580. A detailed account of the events leading up to the accident is given in *Phelan* v. Santelli, 30 Ill. App. 3d 657, 659-62, 334 N.E.2d 391, 393-95 (1975).
96. *Phelan*, 114 Ill. App. 3d at 98, 448 N.E.2d at 580. The liability policy limits were $100,000 per person and $200,000 per occurrence.
97. *Id.*
98. Insurer’s claim committee gave its claim superintendent leave to authorize $100,000 for settlement. The claim superintendent instructed the insurer’s attorney to offer only $85,000 to the claimant. After insurer offered $85,000 to settle the case, the claimant’s attorney said that he would accept $97,500 for a covenant not to sue or $100,000 for a release. Insurer held its offer firm at $85,000. Claimant rejected the offer and stated that its offer would remain in effect until November 6, after which it would be necessary to hire a trial specialist. The insurer refused to move on its offer of $85,000 and, after November 6, the claimant hired a trial specialist. *Id.* at 98-99, 448 N.E. 2d at 581.
99. *Id.* at 99, 448 N.E.2d at 581.
100. *Id.*
101. *Phelan* v. Santelli, 30 Ill. App. 3d 657, 334 N.E.2d 391 (1975). The appellate court ultimately held that the defense counsel’s statements to the jury interpreting the meaning of the court’s instruction as to the law were manifestly misleading and may have influenced the erroneous jury finding and verdict.
102. *Phelan*, 114 Ill. App. 3d at 100, 448 N.E.2d at 581. Prior to the beginning of trial on damages, insurer again attempted to settle with claimants for the policy limits.
103. See supra note 11.
trial on the excess liability issue, in which the jury rendered a verdict of $250,000 against the insurer.\textsuperscript{104} The trial court then entered a judgment n.o.v. in favor of the insurer.\textsuperscript{105}

The appellate court reversed the trial court’s judgment n.o.v. and reinstated the jury verdict\textsuperscript{106} because it appeared that the insurer was aware that damages would be in excess of policy limits, since the claimant was a quadriplegic with little or no chance of recovery\textsuperscript{107} and the insurer’s claim superintendent believed that a jury would find the insured negligent.\textsuperscript{108} The appellate court upheld the jury verdict for wrongful refusal to settle based on the evidence at trial which showed the necessity of the claimant’s attorney procuring the services of a trial attorney, the added expenses incurred in preparation for trial, and concern for the welfare of the claimant’s family.\textsuperscript{109} The court followed the Kavanaugh language, stating that in this situation the insurer must settle within the policy limits or face an excess liability claim for breach of duty of good faith owed to the insured.\textsuperscript{110}

The Adduci and Phelan courts considered remarkably similar fact situations in that both involved instances where the probability of an adverse finding on the issue of liability was great, the amount of probable damages greatly exceeded coverage, and the time of the insurers’ offers came after negotiations had ended.\textsuperscript{111} Since the results were opposite, Illinois courts may have

\begin{thebibliography}{9}
\bibitem{104} Phelan, 114 Ill. App. 3d at 100, 448 N.E.2d at 580.
\bibitem{105} Id.
\bibitem{106} Id. at 98, 448 N.E.2d at 580.
\bibitem{107} Id. at 105, 448 N.E.2d at 585. At the original trial, plaintiff’s physician testified that plaintiff would require continuous lifetime care by a licensed practical nurse and that plaintiff would, from time to time, require hospitalization and professional observation because of her susceptibility to infection. Phelan v. Santelli, 30 Ill. App. 3d 657, 334 N.E.2d 391 (1975).
\bibitem{108} Phelan, 114 Ill. App. 3d at 98, 448 N.E.2d at 580. The field representative of the insurer felt that the insured had little regard for safety when he backed up his automobile on a highway at the base of a hill.
\bibitem{109} Id. at 104, 448 N.E.2d at 585. This evidence is significant in that it shows that the claimant did not unreasonably refuse the insurer’s settlement offer.
\bibitem{110} Id. The court stated: “Where it appears that the probability of an adverse finding is great and the amount of damages would exceed the policy limits, the insurer has a duty to settle within the policy limits or face an excess liability claim for the breach of duty owed to the insured.” Id.
\bibitem{111} The Phelan court found Adduci to be distinguishable. The Phelan court stated that the instant case submitted the issue of the insurer’s wrongful refusal to settle to the jury. This allowed the jury to conclude that the insurer breached its duty to the insured in failing to settle with the claimant. Id., 448 N.E.2d at 584. In Phelan the evidence
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difficulty determining the proper grounds for wrongful refusal to settle. Both courts used the Kavanaugh standard, but interpreted it differently, striking different balances in the wrongful refusal to settle suit.

**ANALYSIS**

By refusing to allow the claimant to proceed against the insurer for excess liability, the Adduci court struck a balance among the competing interests, giving priority to the insurer's interest in low settlements. The opposite position was taken by the Phelan court, which more strongly protected the insured from the risk of loss resulting from possible excess liability. Furthermore, the Phelan decision gives the claimant more power in the settlement negotiations, potentially resulting in higher settlements than under Adduci.

**Adduci Gives Priority to Insurer**

The Adduci court created a lesser duty for the insurer to settle a claim where the Kavanaugh factors of a high probability of an adverse finding on liability and the likelihood that damages would greatly exceed coverage exist. The Adduci court held that the insurer's offer of the policy limits after negotiations had been terminated was sufficient to relieve it of liability. In so holding, the court placed little weight on the fact that the time of the offer was so late that it detracted from its reasonableness.

The Adduci decision subjects the insured to a greater risk of exposure to excess liability than would a contrary decision.\(^\text{112}\) This is so because the insurer has a less stringent duty to settle where the Kavanaugh test factors have been met. While the court may have valid reasons for placing a lower duty on the which the claimant adduced at trial concerning added expenses and the welfare of the claimant's family showed that it was unreasonable for the insurer to wait until well after the claimant's offer expired before offering the policy limits. Even though the items being pleaded were strikingly similar to those being pleaded in Phelan, the Phelan court felt Adduci was significantly different because Adduci involved pleadings which alleged insufficient facts to sustain a cause of action. The result was that even though the claimants in both Phelan and Adduci pleaded that they had incurred significant added expenses by the time the insurer offered the policy limits, the claimant in Phelan was afforded the opportunity to present evidence at trial while the claimant in Adduci was not.

\(^{112}\) Any time an action goes to trial the insured is exposed to potential liability.
the relative lack of power of the insured in relation to the insurer, as well as the purpose of insurance, emphasize the need for a higher duty on the insurer.

The insured has less bargaining power than the insurer in the original negotiations for the liability insurance contract. The insured enters into the liability insurance contract seeking to protect himself from sudden loss. In so doing, he gives up his right to negotiate or settle the claim. Moreover, it is most often the insurer who writes the contract. Consequently, when purchasing liability insurance, the insured cannot be expected to understand the conflicts of interest in the settlement process and the ramifications that flow from it. Furthermore, the insurer is primarily concerned with commercial gain while the insured is only trying to protect himself. It was in this setting that the Adduci court utilized the Kavanaugh test and the equal consideration standard to give the insurer more opportunity to expose the insured to excess liability.

In imposing a lower duty on the insurer, Adduci also gives the insurer more power in the settlement negotiations with the claimant. The cause of action for wrongful refusal to settle is a weapon that the claimant utilizes in the bargaining setting and is a factor that the insurer must consider in choosing whether or not to settle. The Adduci decision allows the insurer to minimize the possibility of excess liability by making an offer of the policy limits at a late stage of negotiations. By making the possibil-

113. See infra text accompanying notes 123-29.

114. See supra note 1.

115. The standard policy contains provisions that are intended to vest the insurer with complete control over the litigation. Keeton, supra note 1, at 1137. The policy provisions thus constitute a contract of adhesion, over which the insured has no choice if he desires to have insurance. 7 WILLISTON ON CONTRACTS 29-34 (3d ed. 1963).

116. Trimmer v. Nationwide Ins. Co., 540 F. Supp. 1188, 1193 (D.S.C. 1982) (an insured does not contract to obtain any kind of leverage but only to protect himself from the spectre of accidental or unavoidable loss); Tibbs v. Great Cent. Inc. Co., 57 Ill. App. 3d 866, 874, 373 N.E.2d 492, 497 (1978) (Moran, J., dissenting) (the insurer-insured relationship is unlike traditional contractual relationships in that the insured does not contract to secure a particular commercial advantage but rather to protect himself against the risk of accidental losses).

117. The Adduci court stated that it recognized in some circumstances an insurer's failure to respond to a settlement demand might constitute a breach of its duty to the insured, but that since the insurer did make an offer of the policy limits, the insurer was not liable because claimants showed no reason why it was impossible to accept the offer. Adduci, 98 Ill. App. 3d at 475, 424 N.E.2d at 649. There is always the possibility, however, that the insurer will be liable for a breach of its duty to the insured based on factors other than the timing of the offer. See supra note 60.
ity of insurer’s excess liability unlikely in this situation, the claimant’s incentive to risk going to trial is reduced. By attempting to hold out for the policy limits after a lesser offer, the claimant will incur additional expenses in preparing for trial with little probability of collecting any excess judgment absent a solvent defendant, thereby gaining little or nothing by waiting. Thus, the claimant is prompted to settle earlier and for a lower figure. The effect of Adduci is therefore that the size of settlements will be diminished, which, in turn, may fail to satisfy the public policy interest of fairly compensating an injured party.\footnote{118}{See supra note 29.}

The inequities of the bargaining setting greatly favor the insurer.\footnote{119}{See Note, supra note 34, at 480.} An insurer, because of its size and vast financial resources, has the opportunity to dominate negotiations.\footnote{120}{Id.} Furthermore, these financial resources enable the insurer to withstand protracted negotiation. The claimant, on the other hand, needs to settle quickly because he is most often in great financial distress.\footnote{121}{Because of court docket congestion, the injured may wait for a long period before his or her case can even be heard. Since, in the meantime, the claimant may be unable to work if seriously injured, he or she may be under extreme economic pressure to settle the claim on any terms available. Corstvet, \textit{The Uncompensated Accident and Its Consequences}, 3 \textit{Law \& Contemp. Probs.} 466 (1936); Hogan \& Stubbs, \textit{The Sociological and Legal Problem of the Uncompensated Motor Victim}, 11 \textit{Rocky Mt. L. Rev.} 12 (1938).} Moreover, his family may also be financially burdened because of the claimant’s medical needs.\footnote{122}{\textit{Phelan}, 114 Ill. App. 3d at 104, 448 N.E.2d at 584.} Delay in settlement works for the insurer, giving it an inherent advantage in the negotiations for settlement. The \textit{Adduci} court allowed the insurer to hold out even longer before making an offer of the policy limits without being concerned with excess liability. In so doing, the insurer was given more power than it previously possessed.

By lowering the insurer’s duty to settle a claim, the \textit{Adduci} court gave deference to the public’s interest in low insurance premiums.\footnote{123}{See supra note 30.} The \textit{Adduci} decision virtually took away the threat of a wrongful refusal to settle suit where the insurer is willing to make an offer of the policy limits.\footnote{124}{See supra note 117.} The decision resulted in less power to the claimant, which translates to earlier and lower set-
Lower settlements result in lower payouts by the insurer, leading to lower costs and lower premiums to the extent such premiums are passed on to the consumer. Furthermore, lower insurance premiums may result in more people carrying insurance, which benefits all. The cost is borne by the insured, who is liable for any excess damages, and the claimant, who may not be fairly compensated.

The *Adduci* decision gives priority to the insurer’s concern that if the insurer were subject to excess liability, the claimant would be able to cut off negotiations upon the insurer’s initial, and possibly valid, refusal to settle, in the hope of recovering an excess judgment. Allowing the claimant to constantly threaten the insurer with a wrongful refusal to settle suit would greatly restrict an insurer’s right to ask trial courts to decide any reasonably controversial case. If the claimant is given too much power, the insurer could be required to settle cases which it otherwise would not, ultimately requiring an increase in insurance premiums to the public. The *Adduci* court thought that to give the claimant the right to reject the insurer’s offer of the policy limits, even at a late stage of negotiations, with an opportunity to hold the insurer liable for any excess, would result in a balance strongly favoring the insured’s interests. Although it would eliminate the risk of loss to the insured and fulfill the claimant’s need for a larger settlement, it would also detract from the insurer’s goal of lower settlements.

*Phelan Gives Claimant More Power*

The *Phelan* court balanced the competing interests differently by creating a higher duty for the insurer than the *Adduci* court did. The *Phelan* court placed a greater emphasis on the timing of the offer by recognizing that the lateness of the offer detracted from its reasonableness, making it of lesser value to the claimant.

The court in *Phelan* balanced the interests in such a way that the interests in protecting the insured from sudden losses out-

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125. See *supra* text accompanying notes 117-18.
126. See *supra* note 30.
127. See *supra* note 29.
129. See Jarrett, *supra* note 60, at 63, in which the author emphasizes that the jury in a wrongful refusal to settle suit considers the fact that one jury has already found the insured negligent. With this benefit of hindsight, a jury will more than likely to find the
weighed the societal goal of lowering the cost of insurance. *Phelan* requires the insurer to offer the policy limits within a reasonable time if the probability of an adverse finding on liability is great and the amount of probable damages would greatly exceed the coverage. By placing more emphasis on early settlement in the *Kavanaugh* test situation, the court makes it more likely that a claimant will settle for the policy limits, thereby protecting the insured from any excess liability. In so holding, the *Phelan* decision is more in keeping with Illinois' stated policy of requiring the insurer to consider the interests of the insured in the settlement negotiations.\(^{130}\)

The insured contracts with the insurer to protect himself from the risk of sudden loss. In entering the insurance contract, the insured forfeits all rights to defend or settle the action, thereby losing control over the decision which subjects him to the risk of excess judgment.\(^{131}\) The insurer, on the other hand, has not undertaken the full share of the risk in deciding to defend rather than to settle.\(^{132}\) As the claimant's demand approaches the policy limits, the insurer is not proportionately jeopardized because it is not risking its own funds by choosing to go to trial rather than settling.\(^{133}\) If this is true, the insurer should be liable for any excess liability because it is subjecting the insured, but not exposing itself, to risk without any input from the insured. Likewise, if, as in *Phelan* and *Adduci*, the insurer waits until a stage in the settlement process where negotiations have long been terminated before making an offer of the policy limits, the

unpopular insurance company liable for the excess damages. See also Note, supra note 34, at 480. At an excess liability trial, the insurer is in a poor tactical position. The plaintiff is usually the injured claimant by reason of assignment. The plaintiff is often a pathetic figure, both because of physical injury and because, if not for the insurer's attempt to save money by refusing to settle, the injured party would not have to bear the delay of the second trial and the expense of additional attorney's fees.

130. The insurer must consider the insured's interests in the settlement negotiations. *Adduci*, 98 Ill. App. 3d at 475, 424 N.E.2d at 648; *Cernocky*, 60 Ill. App. 2d at 207, 216 N.E.2d at 294; *Scroggins*, 74 Ill. App. 3d at 1029, 393 N.E.2d at 720; *DeGraw*, 40 Ill. App. 3d at 37, 351 N.E.2d at 311; *Olympia Fields*, 325 Ill. App. at 671, 60 N.E.2d at 905.

131. See supra note 1.

132. *Rova Farms Resort v. Investors Ins. Co. of Am.*, 65 N.J. 474, 483 323 A.2d 495, 505 (1974) (when an opportunity for settlement approximates the limits of coverage, the insurer's exposure to liability is not considerably affected by a verdict in excess of coverage).

insurer is not jeopardizing its own funds in risking that the claimant will go to trial. In holding that it is not in good faith for the insurer to so act, the Phelan court more strongly requires the insurer to consider the insured's interests. Given that the insurer has more bargaining power than the insured in the initial insurance contract setting and the fact that the insured has no voice in the settlement process, the Phelan result is more equitable.\textsuperscript{134}

The higher duty placed on the insurer in Phelan gives the claimant more power in the settlement negotiations with the insurer. Where the Kavanaugh factors are met, the threat of a wrongful refusal to settle suit becomes a very real possibility for an insurer if it waits too long before making an offer of the policy limits. The insurer, upon evaluating the risk of the insured's liability and the amount of possible damages, must offer the policy limits within the negotiating period. The result of Phelan is that where the Kavanaugh factors are met, the claimant has the opportunity to opt for the policy limits at an earlier stage than under Adduci. In order for the Kavanaugh factors to be met, the claimant must have damages that will likely exceed policy limits. Thus, the public policy consideration of adequate compensation for injured parties is better realized by requiring earlier settlements in these situations.

Given the inequities of the bargaining power that strongly favor the insurer, a higher duty on the insurer does not give the claimant too much power. The insurer is skilled in the evaluation of claims. It will never be liable for an excess judgment unless the Kavanaugh requirements are met. Phelan recognized that delay works for the insurer and that the claimant, under tremendous pressure to settle the claim as quickly as possible, will not be able to force an insurer, which has large financial resources, to settle in every instance.\textsuperscript{135} Given that the insurer has the greater power, it is not desirable to accentuate the imbalance by increasing the insurer's power.

The Phelan decision, by raising the insurer's duty to settle, gives priority to the public policy considerations of protection from sudden loss and adequate compensation to injured parties. The countervailing public interest of lower premiums is not given as much weight by the Phelan court. By insisting that the

\textsuperscript{134} See supra notes 114-16 and accompanying text.

\textsuperscript{135} See supra notes 119-22 and accompanying text.
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*Kavanaugh* factors be met before requiring the insurer to make a settlement offer within a reasonable time, however, *Phelan* does not allow the claimant to wield so much power that settlements will become excessive. Furthermore, because the *Kavanaugh* factors must first be met, the insurer retains the right to go to trial without automatically risking excess liability. Given these factors, which tend to keep settlements low, the public policy interest in low premiums is not greatly compromised by *Phelan*.

The Inadequacy of the Kavanaugh Test

As the *Adduci* and *Phelan* decisions demonstrate, the *Kavanaugh* test may be inadequate. The *Kavanaugh* test does not consider all of the relevant factors when there is a high probability of an adverse finding on liability and the amount of probable damages would greatly exceed the coverage. The *Kavanaugh* test does not address the issue of the timing of the insurer’s offer. *Adduci* and *Phelan* accorded different duties on the insurer even though the factual situations of the two cases were very similar. A clearer refinement of the *Kavanaugh* test is needed so that courts will be better able to equitably and consistently settle the issues.

Some commentators in other jurisdictions have suggested imposing a standard that would hold the insurer strictly liable for any excess judgment in order to more adequately protect the insured’s interests.\(^{136}\) Although strict liability may have advantages,\(^{137}\) it would most likely upset the balance in the negotiations to unduly favor the claimant, ultimately increasing insurance premiums.\(^{138}\) Furthermore, given the fact that the negli-

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137. There are several advantages inherent in a strict liability approach. First, there is no need for a jury to determine whether the insurer gave equal consideration to its own interests and the insured’s interests. Second, there is no need for the claimant and insurer to jockey for position on the issue of wrongful refusal to settle. Finally, it saves the time and expense needed to litigate excess liability suits and absolutely protects the insured. See *supra* note 136.

138. *See supra* note 129 and accompanying text. In addition, allowing the claimant too much power through the use of the wrongful refusal to settle suit may result in high premiums for low limit policies. If the insurer is liable for the excess in too many cases, persons seeking insurance may be encouraged to buy low limit policies in the belief that the insurers will always be liable for the excess. Taken to its logical conclusion, the result
gence or bad faith standard is firmly entrenched in Illinois, there is very little possibility of a change to a strict liability standard.

**THE PARAMOUNT INTEREST TEST**

A much more viable, effective, and consistent manner in which to protect the interests of the parties would be for Illinois to adopt the standard that when there is a conflict, the insurer must make its paramount concern the insured's interests rather than its own. The current Illinois standard does not give the insured adequate protection because the court has room to allow the insurer to proceed in its self-interest even when the Kavanaugh factors are met. A paramount interests standard eliminates the ability of the insurer to effectively act in its self-interest when the Kavanaugh factors are present.

This standard would clarify the situation for Illinois courts. Since the Kavanaugh test does not address the issue of the timing of the insurer's offer, the Adduci court was able to use it in conjunction with the equal consideration standard to hold the insurer not liable. The lateness of the offer detracted from its reasonableness, making it of lesser value to the claimant.

Assuming Adduci was correct in stating that the insurer gave the insured's interests equal consideration, its result is inequitable because it does not correctly reflect the fact that the balance of power favors the insurer. The paramount interest standard would correct this inequity. If the paramount interest standard were used with the Adduci facts, the outcome would change, because the insurer would be required to defer to the insured's interests and make a strong effort to settle. The paramount interest standard, then, requires the insurer to consider

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140. See supra notes 112-28 and accompanying text.


142. See supra notes 68, 112-22, 130-33, and accompanying text.
more than Kavanaugh because it factors the timing of the offer into the cause of action.

The Adduci court rejected the paramount interest standard, stating that such a proposition lacks sound business sense because it requires the insurer to overlook its own fiscal concerns and focus on the concerns of its customers. Certainly the insurer’s financial concerns are valid in that increased settlements have an impact on the public through increased premiums. The paramount interest standard, however, does not require the insurer to overlook its own fiscal concerns. The paramount interest standard is not a strict liability standard because the insurer still can risk exposing the insured to excess liability if the probability of liability is not great and/or the probability of damages in excess of the policy limits is not high. Furthermore, the paramount interest standard balances the inequities inherent in the settlement negotiations without giving the claimant too much power, because the standard would hold the insurer liable only if there is some wrongful conduct on its part. The insurer can be threatened with excess liability only if the Kavanaugh factors are present. Thus, the claimant does not have an inordinate amount of power and, as a result, settlements and insurance premiums will remain relatively low.

CONCLUSION

A cause of action for wrongful refusal to settle arises out of the need to deter an insurer from disregarding the interests of its insured and the desire to compensate injured parties. Whenever there is an award for wrongful refusal to settle, it means that there were damages that could have been avoided at the settlement stage of the lawsuit. The paramount interest test properly balances the parties' bargaining positions so that the insurer is encouraged to settle when public policy deems it prudent to do so. The insured is adequately protected by its liability insurance policy, the injured claimant gets a prompt and satisfactory settlement, and the public, which eventually bears the cost of insurance, is saved any substantial increase in premiums.

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