ORIGINAL

IN THE SUPREME COURT OF FLORIDA

STATE FARM FIRE & CASUALTY COMPANY,

Petitioner,

vs.

WAYNE ZEBROWSKI and CAROL ZEBROWSKI, his wife, a/k/a CAROL LORD,

Respondents.
_____/

Case No.: 88,338
District Courr of Appeal
4th District - No. 94-02626

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PETITIONER'S INITIAL BRIEF

ON CERTIFIED CONFLICT FROM THE FOURTH DISTRICT COURT OF APPEAL.

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PRELIMINARY STATEMENT

Petitioner, STATE FARM FIRE & CASUALTY COMPANY, the Defendant and Appellee below, is referred to as “State Farm”.

Respondents, WAYNE ZEBROWSKI and CAROL ZEBROWSKI, the Plaintiffs and Appellants below, are referred to as “Plaintiffs.”

References to the record on appeal are designated by the prefix "R."

STATEMENT OF THE FACTS AND CASE

State Farm seeks review of the Fourth District Court of Appeal's ruling in ***Zebrowski v. State Farm Fire & Casualty Co,, 673 So.*** 2d 562 (Fla. 4th DCA 1996), which allowed Plaintiffs to pursue a claim against State Farm under §624.155(1)(b) I., Florida Statutes. Plaintiffs are not insured by State Farm. Rather, Plaintiffs sued State Farm's insured, Haisfield Enterprises of Florida, d/b/a Village Shops, a Florida partnership ("Haisfield"), and recovered a judgment against Haisfield for less than the insured's policy limits.

State Farm paid the judgment in full, with interest, in a timely manner. State Farm's insured was never exposed to an excess judgement and never assigned any cause of action to the Plaintiffs. The Plaintiffs have no damages for which they have not already been compensated.

A. Plaintiffs' Amended Complaint against State Farm

The Amended Complaint[1] alleged damage arising from personal injuries to Plaintiff Carol Zebrowski which occurred at a Halloween block party held October 29, 1988, at the Village Shopping Center in Palm City. Ms. Zebrowski sustained her injuries when two stereo speakers fell on top of her. The Plaintiffs sued Haisfield, State Farm's insured, and named State Farm individually as a defendant.

The fourth count of the Amended Complaint is pled against State Farm and alleges State Farm violated §624.155(1)(b) 1. by not attempting in good faith to settle

[1]The Amended Complaint, the operative complaint in this case, is found as Exhibit A of State Farm's Motion to Supplement Record on Appeal, filed concurrently herewith.

Carol Zebrowski's third-party liability claim "when under all the circumstances it could and should have done, had it acted fairly and honestly towards its insured and with due regard for their interest."

The Amended Complaint alleges State Farm made no attempt to settle the claim or compensate Carol Zebrowski for her injuries. Based on State Farm's alleged refusal to negotiate and settle the claim of Ms. Zebrowski, the Plaintiffs claimed they ware entitled to judgment for an amount of the damages "notwithstanding STATE FARM's policy limits." (emphasis supplied) Additionally, the Plaintiffs claimed mental pain and anguish, loss of use of the "disputed funds" while the case was pending, and attorney's fees.

The trial court stayed prosecution of Count IV against State Farm pending resolution of the claims made against State Farm's insured Haisfield, among others. (R. 22) The case against Haisfield and the other Defendants was tried to a jury in November 1991. The jury verdict rendered in Plaintiffs' favor on November 27, 1991, assessed damages against Haisfield in an amount which did not exceed the policy limits provided by State Farm. (R. 24; 44-45)

State Farm appealed the judgment against its insured, but, ultimately, paid the judgment in full, plus interest. (R. 6-7) There was never an excess verdict. (R. 24; 44-45) State Farm's insured never assigned any cause of action to the Plaintiffs.

Plaintiffs then recommenced their action against State Farm as alleged in Count IV. State Farm moved for summary judgment on May 26, 1994. (R. 21-31)

B. State Farm's Motion for Summary Judgment

In its motion, State Farm argued that third-party claimants like the Zebrowskis had no cause of action for an alleged bad faith failure to settle pursuant to §624.155(1)(b)1., where the judgment received by the claimants did not exceed the insured's policy limits. (R. 21) State Farm also argued that in a situation where it defends its insured, no excess judgment is rendered against that insured, and the judgment is satisfied with interest, no cause of action for bad faith lies as there are no damages arising from the alleged failure to settle. (R. 21) State Farm further argued that §624.155(1)(b) I., by the specific terms of the statute, governs the duties owed by the insurer to its insured and not to persons not a party to that contractual relationship. (R. 22)

The trial court granted State Farm's Motion for Summary Judgment, relying on the authority of ***Cardenas v. Miami-Dade Yellow Cab*** Co., 538 So. 2d 491 (Fla. 3d DCA 1989) and ***Conquest v. Auto-Owners Ins. Co.,*** 637 So. 2d 40 (2d DCA 1994). (R. ***45-46)*** Both ***Cardenas*** and ***Conquest*** held that a claimant injured by an insured tortfeasor did not have a claim for a bad faith failure to settle under §624.155(1)(b)l . In each of those cases, as in ***Zebrowski,*** the claimants obtained a judgment against the insured for less than policy limits. Both ***Conquest*** and ***Cardenas*** concluded that the insurer did not owe an independent duty to settle to the injured third party.

The trial court made the following relevant findings of fact on which it based its conclusion that Plaintiffs failed to state a cause of action against State Farm:

1. State Farm defended its insured against Plaintiffs' personal injury suit. (R. 44)

2. The amended judgment entered against Haisfield did not exceed State Farm's policy limits. (R. 44-45)

3. State Farm fully satisfied both the amended final judgment and the cost judgment entered against Haisfield with interest. (R. 45).

4. Plaintiffs are third-party claimants to the insurance policy between Haisfield and State Farm, whose claim against State Farm was based on failure to settle the claim against Haisfield, in alleged violation of §624.155(1)(b)1, (R. 45)

C. The Fourth District's Opinion

In its May 22, 1996 opinion, the Fourth District reversed the trial court, concluding that an action by the Zebrowskis against State Farm premised on a duty to settle owed directly to them was authorized under §624.155(1)(b)l . *Zebrowski,* 673 So. 2d at 565. The Fourth District relied on the Florida Supreme Court's holding in *Auto-Owners Ins. Co. v. Conquest,* 658 So. 2d 928 (Fla. 1995), which allowed a third-party claimant to pursue a tortfeasor's insurer directly for alleged violations of §624.155(1)(a)--not (1)(b) 1.-- finding as follows:

> [W]e see no reason that the result would be different when the injured party brings suit directly against the insurer based on alleged unfair failure to settle a particular claim under §624.155(1)(b) 1. The words 'any person' contained in §624.155(1) are not limited to (a), but would apply to (b) as well. The notion that the term 'any person' in §624.155(1) meant 'any insured person' was dispelled by the Supreme Court in *Auto-Owners Ins. Co. v. Conquest.*

> The words 'any person' are 'precise and their meaning unequivocal.' 658 So. 2d at 929.

Id. at 564.

The Fourth District acknowledged that the Second District in ***Conquest*** and the Third District in ***Cardenas*** had concluded that no duty to settle owed to a claimant was created by §624.155(1)(b)1 . and thus no cause of action existed where the claimant did not obtain an excess judgment. The Fourth District ignored these cases despite the fact that both cases directly considered the identical issues considered by the Fourth District and notwithstanding the fact that the Second District's holding on this issue was undisturbed by this Court's ruling in ***Auto-Owners V. Conquest.'*** Even though this Court expressly adopted the Second District's decision, the Fourth District concluded it was not bound to follow the Second District's opinion or the remaining applicable portions of ***Cardenas,*** Recognizing its decision that § 624.155(1)(b) 1. created a direct duty to settle owed to a third-party claimant and allowed the action brought by Plaintiffs to go forward even though they had not obtained an excess judgment against State Farm's insured conflicted with the Second District's opinion in ***Conquest*** and with the Third District's opinion in ***Cardenas,*** the Fourth District certified the conflict.

State Farm seeks review of the Fourth District's conclusion that §624.155(1)(b)1 . creates a direct duty to settle owed a claimant by an insurer and

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[2]In ***Auto-Owners V. Conquest,*** this Court specifically approved the decision of the Second District in Conquest v. Auto-Owners and adopted the decision under review. The decision in ***Cardenas,*** while disapproved, was disapproved only to the extent it conflicted with the Supreme Court's decision. *Id.* at 930.

permits a cause of action for statutory bad faith to proceed, even though the third-party claimant has not recovered an excess judgment against the insured and even though the judgment rendered against the insured has been satisfied in full, with interest.

ISSUES ON APPEAL

I. WHETHER THE FOURTH DISTRICT ERRED IN HOLDING THAT §624.155(1)(b)1. CREATES A DUTY TO SETTLE OWED BY AN INSURER TO A CLAIMANT INJURED BY AN INSURED?

II. WHETHER, AS A MATTER OF PUBLIC POLICY, FLORIDA SHOULD REFUSE TO RECOGNIZE AN INDEPENDENT DUTY ON THE PART OF AN INSURER TO SETTLE THE CLAIM OF AN INJURED THIRD PARTY?

SUMMARY OF ARGUMENT

The Fourth District erred in concluding the §624.155(1)(b)1. creates a duty to settle owed by an insurer to a third party claimant and allowing Plaintiffs' claim to go forward, despite the fact that the judgment they obtained against State Farm's insured was less than policy limits and has been fully satisfied. The Second and Third Districts squarely addressed this issue under similar facts and both concluded there is no duty to settle under §624.155(1)(b)1. that flows directly to a third-party claimant. The Second District's decision in Conquest which so held was adopted and approved by this Court, *in toto*. The Fifth District in *Dunn,* 631 So. 2d 1 103 (Fla. 5th DCA 1993) while considering the issue in the context of an excess judgment, similarly concluded that §624.155(1)(b) 1. did not afford a claimant a cause of action premised on breach of a duty to settle owed to the claimant.

Section 624.155(1)(b)1. defines the following conduct as a violation of the statute:

> 1. Not attempting in good faith to settle claims when, under all the circumstances, it could and should have done so, had it acted fairly and honestly toward its insured and with due regard for his interest

As explicitly recognized in the Second District's *Conquest* decision and in *Dunn,* the language employed in the statute establishes a duty which runs to the insured and not to third parties. This interpretation is consistent with the long standing principles applied in common law bad faith actions, which allowed a claimant to sue to recover the amount of an excess judgment, standing in the shoes of the insured. The claimant's recovery at common law is limited to the damage to the insured which

results from the insurer's failure to settle the case brought by the claimant within policy limits. As noted in ***Dunn,*** there is no indication from the legislature that it intended to change the derivative nature of a cause action for bad faith failure to settle as established by the common law. Thus, as here, where there is no excess judgment against the insured, the insurer has fully defended the insured and has satisfied the judgment, i.e., the insured has no damages, the claimant has no claim for violation of §624.155(1)(b)1. which he can pursue.

There are manifest public policy reasons why this court should reject the Fourth District's reading of §624.155(1)(b) 1. as creating a duty to settle owed directly to claimants and its decision to allow Plaintiffs' case to go forward, even though the findings of fact establish that no damages have been sustained by State Farm's insured in this case. The duty to a claimant recognized by the Fourth District conflicts with the duties owed by an insurer to its insured pursuant to the contract, common law and 5624.155, It is easily foreseeable that instances will arise where it is not in the insured's best interest to settle the case at the amount demanded by the claimant. The Fourth District's decision would force an insurer to choose between honoring its contractual and extra-contractual obligations to its premium paying insured and the duty to settle owed directly to claimants. The duty recognized by the Fourth District also interferes with the constitutionally guaranteed freedom to contract, creating an obligation outside the contract which eliminates the purpose for which the contract was originally made.

The dramatic departure from existing law which the Fourth District has taken effectively creates a two-tiered litigation system. When a defendant is uninsured, the traditional adversarial system applies. When the defendant has purchased insurance to protect itself, however, the system would now be one of "no fault" because the insurer, on behalf of its insured, could no longer challenge the liability and damages allegations of the claimant without being faced with the threat of violating its duty to settle owed to that claimant.

Dire economic consequences will result from the recognition of a duty to settle owed directly to a claimant. Every tort claim involving an insured tortfeasor will spawn two lawsuits -- one to determine the tortfeasor's liability to the claimant and one challenging the settlement negotiations during the litigation. This impacts the insurance consumer who ultimately pays for the increased costs associated with this double litigation in the form of higher premiums. The court system is also impacted by the increase in lawsuits and the need to litigate the parameters pursuant to which recovery will be afforded to claimants.

None of this is necessary as there are already adequate mechanisms in place which compel an insurer to try to settle cases in good faith. First and foremost, the insurer has a duty to settle owed to its insured. Procedural remedies exist in the form of sanctions under § §57.105 and 768.79 which award attorney's fees and costs to prevailing parties in litigation where there is alternatively no basis in fact or law to defend or in which an appropriate demand for judgment has been made. When employed by claimants, these statutes offer further incentives to insurers to resolve

claims reasonably or be faced with the prospect of paying the claimant's attorney's fees and costs.

ARGUMENT

I. THE FOURTH DISTRICT ERRED IN HOLDING 5624.15511)(b)1. CREATES A CAUSE OF ACTION FOR BAD FAITH FAILURE TO SETTLE BASED ON A BREACH OF A DUTY OWED BY AN INSURER TO AN INJURED THIRD PARTY.

The Fourth District held an injured party has a direct cause of action against a tortfeasor's insurer for bad faith failure to settle based on a duty created by §624.155(1)(b)1. running from the insurer to the third party. That issue, however, was squarely before the courts in Second District in *Conquest,* the Third District in *Cardenas* and the Fifth District in *Dunn v. National Security Fire and Casualty Co., 631* So. 2d 1103 (Fla. 5th DCA 1993). In each of these cases, the court held §624.155(1)(b)1, does not permit an injured party to bring a direct action against the tortfeasor's insurer for bad faith failure to settle premised on a duty to settle owed directly to the injured party. *Zebrowski, 673 So.* 2d at *563-64; Conquest, 637 So.* 2d at *42; Dunn, 631 So.* 2d at 1107; *Cardenas, 538 So.* 2d at *496. Conquest, Cardenas* and *Dunn* all held the duty under §624.155(1)(b)1. runs to the insured and not to third parties.

This Court approved and adopted the Second District's decision in *Conquest,* which held there was no basis for the third-party action in that case under §624.155(1)(b)1. because the duty under that section ran only to the insured. Despite the fact that this Court approved and adopted the Second District's decision in *Conquest* without limitation, the Fourth District claimed this Court did not address that finding and took a contrary position.

The Fourth District took the position that a third-party action would lie for violation of §624.155(1)(b)1 . based on the reference in the lead-in language of 9624.155 to "any person" and on the court's conclusion that the statute itself created a direct duty of the insurer to the third-party claimant. ***Zebrowski, 673 So.*** 2d at 564. By so holding, the Fourth District ignored the clear language of §624.155(1)(b)1 . limiting an insurer's duty to settle to its insured, the existing authority considered and approved by this Court, and long-standing Florida law which has recognized that any liability for a breach of the duty to settle arises out of the obligations owed by an insurer to its insured.

The cause of action created by the Fourth District creates an irreconcilable conflict for an insurer. The Fourth District's decision would impose a duty running from an insurer to both its insured -- to whom the insurer owes a duty to defend -- and a duty running to the party who has brought suit against the insured. The permutations on this conflict are endless and will generate endless litigation in the future.

In essence, the Fourth District's holding destroys liability insurance agreements as they presently exist in Florida. Allowing a claimant to directly sue a carrier for the failure to settle a liability claim, where there is no excess judgment in the claimant's favor, would subject the insurer to an almost absolute duty to settle every case presented to it within policy limits, even if the demand is unjustified and even if an insurer's decision to litigate with the claimant yields a result that in no way negatively impacts its insured. The Fourth District, by its expansive interpretation of

§624.155(1)(b)1., judicially imposes a "no fault" liability system on the insurance industry and the people of Florida.

A. Existing Florida case law has consistently and correctly held a third-party claimant has no cause of action under 3624.15511)(b)1. premised on a duty between the insurer and the third party.

The Second District in ***Conquest,*** the Third District in ***Cardenas,*** and the Fifth District in ***Dunn*** all reached the correct conclusion that an insurer does not owe to a claimant a direct duty to settle, and third parties have no cause of action against insurers for alleged violation of §624.155(1)(b)l . based on breach of a duty owed by the insurer to the third party. This Court has previously recognized that the decisions in ***Conquest,*** which relied on ***Dunn,*** and ***Cardenas*** are correct in this regard. Specifically, this Court approved and adopted the Second District's decision in ***Conquest*** and disapproved of ***Cardenas*** only to the extent that ***Cardenas*** disallowed a claimant's suit against an insurer for alleged violations of §624.155(1)(a)1 .

Contrary to the Fourth District's statement that this Court did not address the Second District's holding in ***Conquest*** that a third party may not bring a direct action under §624.155(1)(b)1 . (*Zebrowski,* 673 So. 2d at 563), this Court's approval and adoption of the Second District's holding in ***Conquest*** was in no way limited to only certain issues. In no fewer than three separate places -- the beginning, middle, and end of the opinion -- this Court said it approved and adopted the decision of the Second District in ***Conquest.***

In that case, the Second District was asked to review the trial court's decision dismissing Conquest's Complaint. Conquest was injured in a horseback riding accident

which occurred on property owned by Auto-Owners' insured. Conquest sued Auto-Owners' insured and ultimately obtained a judgment against the insured. Although the jury verdict was $327,000, which was in excess of the $300,000 policy limit, Conquest's award was reduced because of her comparative negligence to a net verdict of $130,800.

After the conclusion of her lawsuit against Auto-Owners' insured, Conquest filed a three-count Complaint against Auto-Owners. Count I alleged violations of §624.155(1)(a)1.; Count II alleged Auto-Owners violated §624.155(1)(b) 1.; and Count III alleged a common law bad faith claim. The trial court dismissed all three counts with prejudice for failure to state a cause of action.

The Second District affirmed in part and reversed in part the trial's court's decision. The Second District affirmed that absent an excess judgment, Conquest could not state a claim for common law bad faith. *Id.* at 42. The Second District then examined the ruling as to Count I and Count II.

As part of its analysis, the Second District reviewed the Third District's decision in ***Cardenas.*** The court disagreed with the conclusion reached in ***Cardenas*** that the words "any person" in §624.155 meant "any **insured** party." *Id.* at 42 (emphasis added). Specifically, the Second District found:

> We hold that the words 'any person' constitute clear, unambiguous, all-inclusive language that requires no interpretation of legislative intent. . . . We find additional support for the plain reading of 'any person' to authorize appropriate third-party suits because the section elsewhere recognizes third parties. See §624.155(2)(b)4 (excusing third-party claimants from a requirement of attaching policy language if it has not been provided by the insurer). Having

> concluded, however, that a third-party suit may be generally allowed, we must next look to whether the particular violation will support a third-party claim.

Id. at 42 (citations omitted)(footnote omitted).

The Second District then looked to the language of the statute and determined that, while a claimant could pursue a cause of action for an alleged violation of §624.155(1)(a)1., the language of §624.155(1)(b)1. created a duty to settle owed solely to the insured. The court emphasized the legislature's use of the word insured in §624.155(1)(b) 1. to conclude that the duties imposed by that portion of the statute ran only between an insurer and its policyholder:

> Section 624.155(1)(b)1. defines bad faith refusal to settle in terms of acting fairly and in the *insured's* best interest. By the very language of the statute, the insurer's duty runs to its insured and not to third parties. We agree with the Fifth District that this section provides protection only for the insured. *Dunn v. National Sec. Fire & Casualty Co.,* 631 So. 2d 1 103 (Fla. 5th DCA 1993). Thus, we conclude §624.155(1)(b)1. provides no basis for this third-party claim and we affirm the trial court's dismissal with prejudice of Count II.

Id. at 42 (emphasis original).

The Fourth District erroneously relies on this Court's decision in *Auto-Owners Ins. Co. v. Conquest* to support its conclusion that a third-party claimant likewise has a cause of action under §624.155(1)(b) 1. The court in *Conquest* endorsed the Second District's interpretation of the phrase "any person" and upheld the Second District's conclusion that a third-party claimant has a cause of action under §624.155(1)(a).

The Second District's opinion in *Conquest,* which, as already noted, this Court adopted in its entirety, contradicts the Fourth District's apparent conclusion that the

definition of "any person" is the end of the inquiry and means that, regardless of what any other part of §624.155 might explicitly say, a claimant can pursue a claim for violation of §624.155(1)(b)1. because of a direct duty an insurer owes a claimant thereunder. In *Conquest,* the Second District said "[h]aving concluded, however, that a third-party suit may be generally allowed, we must next look to whether the particular violation will support a third-party claim." *Conquest 637 So.* 2d at 42. It then concluded "section 624.155(1)(b)1. provides no basis for this third-party claim and we affirm the trial court's dismissal with prejudice of [that Count]." *Id.*

In *Conquest,* the Second District acknowledged that *Cardenas* reached the right result, but for the wrong reason. In *Cardenas,* the third-party claimant was injured when a taxicab ran over his foot. The claimant obtained a judgment against the cab company. Cardenas also sued the taxicab company's insurer, contending it violated both §§624.155(1)(a)1. and (1)(b)1. by failing to settle the case filed by him. The Third District held that 9624.155 did not create a direct third-party action, construing the words "any person" to mean "any insured person." *Id.* at 496. The court emphasized the duty of good faith and fair dealing imposed by the statute "is one the *parties'* to the contract owe to *each other,* not to a third party who is not in privity of contract. *Id.*

Cardenas remains good law to the extent it does not conflict with the Second District's opinion in *Conquest* as approved and adopted by this Court. While Cardenas'conclusion that "any person" means "any insured person" is wrong in light of *Conquest,* the Third District's determination in *Cardenas* that a third-party claimant

cannot directly sue an insurer under §624.155(1)(b)1. for allegedly failing to settle the claimant's claim is ultimately correct.

In ***Dunn,*** the third-party claimed the insurer, under §624.155, "owed ***him*** a duty to act in good faith with regard to settlement negotiations." 631 So. 2d at 1105 (emphasis original). The Fifth District rejected that assertion as follows:

> The insurer has no insurance contract with the injured third party, and thus breaches no fiduciary duty with regard to that person, when it wrongfully refuses to settle a suit for its insured. The injured third party only has a derivative claim as the insured's stand-in. Most courts in other jurisdictions have refused to recognize a separate independent fiduciary cause of action for an injured party against a tortfeasor's liability carrier.
>
> Section 624.155 does not appear to change this concept for third party suits. The gravamen for the statutory cause of action is similar to the common law cause of action: 'An insurer's not attempting in good faith to settle claims when, under the circumstances, it could and should have done so, had it ***acted fairly and honestly toward its insured and with due regard for his interests.'***

Id. at 1107 (emphasis added by the court).

The court concluded the duty breached by violation of that section is a duty the insurer owes to the insured, not a third-party claimant. Further, the ***Dunn*** court said:

> Our supreme court has not recognized the existence of a fiduciary duty owed by an insurer to a third party injured by its insured to settle the suit within the policy limits. . . . [R]ecognizing such a duty under section 624.155 would greatly expand the theory and extent of liability of insurance carriers beyond that established by common law, for third party bad faith cases. Although the legislature can expand by statute the common law concept of third party suits and recoverable damages, we are reluctant to interpret the statute as having made such a drastic change without

> clear and more express language in the statute indicating that intent.

Id. at 1 108.

In contrast, the Fourth District was not reluctant to interpret the statute in a way drastically different as evidenced by its holding in *Zebrowski.* The court recognized that under the common law "an injured third-party's right to sue the insurer was considered to be merely derivative of the insured's rights." *Id.* at 564. However, the court said the statute changed the common law concept of third-party suits because it found "no indication in the statute that the insured party's cause of action against the insurer is merely subordinate to, and derivative of, the insured's cause of action," *Id.* at 565.

The Fourth District's holding is a drastic change from and contrary to established Florida authority, which has consistently and correctly held a third-party claimant has no cause of action under §624.155(1)(b)1. premised on a duty between the insurer and the third party.

B. Section 624.155 was not enacted to create a direct third-party action for failure to settle under §624.155(1)(b)1. premised on a duty between the insurer and the third party.

The Fourth District found "the statute itself creates the insurer's duty to the third party claimant." *Zebrowski, 673 So.* 2d at 564. However, a review of the historical development of bad faith law in Florida and the events which led up to the promulgation of 5624.155 supports the conclusion that the statute was not adopted to create a good faith duty to settle claims running directly to third-party claimants.

Rather, 5624.155 was adopted to codify the covenant of good faith and fair dealing between the insurance company and its policyholder and provide a means by which an insured could sue to enforce the covenant in a first-party context, supplementing the remedy available to third parties at common law. The plain language of the statute, its legislative history, and case law construing it bear this out and do not support the view that the legislature intended the statute to create a good faith duty to settle claims running directly to a third-party claimant or to otherwise benefit a stranger to the contractual relationship between insurer and insured.

1. Common law bad faith principles do not support an extension of an independent cause of action for bad faith by a claimant against an insurer based on a direct duty to settle in good faith between the insurer and the claimant

Historically, Florida common law has long recognized the existence of the duty of good faith and fair dealing an insurer owes an insured when an insured is sued by an injured party and defended by an insurer pursuant to a liability insurance policy. In this context, the insurance company is required to act in good faith to negotiate a settlement to protect the interests of its insured, rather than protecting only its own interests. ***Auto Mutual Indemnity*** Co. v. ***Shaw,*** 185 So. 852, 134 Fla. 815 (Fla. 1938). Breach of this duty is measured by any judgment in excess of policy limits, where an insurance company had the opportunity to settle the case within policy limits and thereby protect its insured from direct, personal exposure. ***American Fire and Casualty Co. v. Davis,*** 146 So, 2d 615 (Fla. 1st DCA 1962); ***Thompson v. Commercial Union Insurance*** Co. ***of*** New ***York,*** 250 So. 2d 259 (Fla. ***1971); Baxter v. Royal Indemnit y Co.,*** 285 So. 2d 652 (Fla. 1st DCA 1973).

Absent an excess judgment or allegations that would support an independent tort claim, such as fraud or intentional infliction of emotional distress, Florida common law limited the insured to a breach of contract claim against the insurer. See, *Butchikas v. Travelers Indemnity* Co., 343 So. 2d 816 (Fla. *1976); Allstate Ins, Co.* v. *Kelley*, 481 So. 2d 989 (Fla. 5th DCA *1986); Smith v. Standard Guaranty Ins. Co.,* 435 So. 2d 848 (Fla. 2d DCA 1983); *Industrial Fire & Casualty Co. v. Romer, 432 So.* 2d 66 (Fla. 4th DCA 1983). Thus, until the legislature enacted §624.155, a first-party insured had no cause of action for an insurer's bad faith refusal to settle. *Opperman v. Nationwide Mutual Fire Ins.* Co., 515 So, 2d 263, 266 (Fla. 5th DCA 1987).

Thompson did away with the necessity of an express assignment of the bad faith failure to settle a claim from the insured to the claimant, but any claim of a third party remained derivative of the duties owed by an insurer to its insured. In *Fidelity and Casualty Company of* New *York v. Cope,* 462 So. 2d 459 (Fla. 1985), this Court explained:

> Nowhere in *Thompson,* however, did we change the basis or theory of recovery. We did not extend the duty of good faith by an insurer to its insured to a duty of an insurer to a third party. The basis for an action remained the damages of an insured from the bad faith action of the insurer which caused its insured to suffer a judgment for damages above his policy limits. *Thompson* merely allowed the third party to bring such an action in his own name without an assignment.
>
> An essential ingredient to any cause of action is damages. In this case [the insured] originally suffered a judgment in excess of his policy. Before this action was filed, however, the judgment was satisfied. Upon its being satisfied [the insured] no longer had a cause of action; if he did not, then [the claimant] did not, [The claimant's] action was not

> separate and distinct from, but was derivative of the [insured's].

Id. at 460-461.

Because of the derivative nature of the duty, this Court in *Thompson* held that, absent an assignment of the insured's cause of action for bad faith failure to settle, the claimant's full release of the tortfeasor or, alternatively, the tortfeasor's complete satisfaction of the underlying judgment, destroyed the claimant's bad faith cause of action.

In *McLeod v. Continental Ins.* Co., 591 So. 2d 621, 625 n.4 (Fla. 1992), this court expounded on its intent in *Thompson,* noting that a direct third-party cause of action in the excess judgment situation was simply a procedural mechanism and that damages in a third party case are still measured solely in terms of a breach of the duties owed an insured by its insurer:

> *Thompson* did not remove the requirement that recoverable damages be sustained by the insured as a result of the bad faith of the insurer. It merely allowed the judgment creditor to step into the shoes of the insured and bring an action without an assignment by the insured. The purpose of the suit is to remove the burden of the excess judgment from the shoulders of the insured, not to compensate the injured party for the damages arising from the underlying occurrence. Had the insured not sustained any damage as the result of the insurer's bad faith, the judgment creditor would not have had a bad faith cause of action against the insurer.

Thus, this Court has recognized continually and without exception that there is no cause of action at common law for bad faith failure to settle based on a duty directly between the insurer and a third-party claimant, Third parties have a cause of

action under the common law only when there is an excess judgment which caused damage to the insured. Damage to the insured is the critical element of the cause of action because the third party's action rested upon and was derived from the duty existing between the insurer and the insured. For that reason, this Court has recognized there is no bad faith, and no damages as a consequence to the insured for which recovery can be had, where the ultimate judgment is within policy limits and the insurer has properly discharged its duty to defend to the insured.

2. Section 624.155 was not intended to change the common law by creating a duty owed directly to a claimant by an insurer to settle claims in good faith

As the Fifth District recognized in ***Dunn,*** §624.155 was not intended to change the common law concept that an injured third party's cause of action for an insurer's wrongful failure to settle a claim for the insured is derivative of the duty between the insurer and the insured. ***Dunn,*** 631 So. 2d at 1107. The decision in ***Conquest*** addressed other sections of the statute and other duties of an insurer owed to "any person." ***No*** where, however, does ***Conquest*** impose a good faith claims settlement duty to a third-party who has sued the person or entity which the insurance company is by contract required to defend and to whom the insurer's duty and loyalty extends.

Section 624.155 was specifically adopted to create liability for bad faith failure to settle to claims made by first-party insureds, just as it already existed in the third-party context. A staff report to the House Committee on Insurance demonstrates the legislature knew the extent of the existing common law of bad faith and manifested the intent to afford the same cause of action to all insureds, regardless of whether

liability under the insurance policy in question arose out of a first-party claim or a suit brought against the insured by a third party:

> [Section 624.1551 requires insurers to deal in good faith to settle claims. Current case law requires this standard in liability claims, but not in uninsured motorist coverage; the sanction is that the company is subject to a judgment in excess of policy limits. This section would apply to all insurance policies.

Staff Report, 1982 Insurance Code Sunset Revision (H.B. 4 F; as amended H.B. 1 OG)(June 3, 1982), as quoted in ***Opperman, 515 So.*** 2d at 266.

The legislature did not, however, create a duty to settle outside of the relationship of insurer to insured. Although it used the words "any person" as a preface to describe who might sue for purported violations of §624.155(1), the legislature separated potential liabilities into two distinct subsections, one of which is not limited to parties to the insurance contract and the other which is specifically limited on its face to the duties arising from the relationship of insurer to policyholder.

As acknowledged by this court in ***Conquest,*** §624.155(l)(a) dictates obligations which run concurrently to insureds and claimants alike, "as there is nothing in the sections that would restrict claims to insureds only." ***Conquest, 658 So.*** 2d at 929. The portions of §624.155 and the portions of §626.9541 incorporated therein which were considered by this court in ***Conquest*** provide as follows:

> **Section 624.155:**
>
> (1) Any person may bring a civil action against an insurer when such person is damaged:
>
> (a) By a violation of any of the following provisions by the insurer"

1. Section 626.9541 (i), (o) or (x) . . . .

Section 626.9541(1)(i)3. a., c., and d.:

3. Committing or performing with such frequency as to indicate a general business practice any of the following:

a. Failing to adopt and implement standards for the proper investigation of claims; . . .

c. Failing to acknowledge and act promptly upon communications with respect to claims;

d. Denying claims without conducting reasonable investigations based upon available information. . . .

In marked contrast, §624.155(1)(b)1 . expressly limits its application to the insurer-insured relationship, defining an insurer's liability for bad faith failure to settle claims strictly in terms of acting "fairly and honestly toward its insured and with due regard for his interests." If the legislature wanted to create a new obligation to settle claims in good faith owed to a person other than the insured, the legislature would not have made liability under §624.155(1)(b) 1. turn on whether the insured's interests had been protected.

The legislature further expressed its intent not to change the derivative basis of a third-party bad faith claim under common law by adopting §624.155(7), which provides in relevant part:

(7) The civil remedy specified in this section does not preempt any other remedy or cause of action provided for pursuant to any other statute or pursuant to the common law of this state. Any person may obtain a judgment under either the common law remedy of bad faith or this statutory remedy, but shall not be entitled to a judgment under both remedies. This section shall not be construed to create a common law cause of action. The damages recoverable

> pursuant to this section shall include those damages which are a reasonably foreseeable result of a specified violation of this section by the insurer and may include an award or judgment in an amount that exceeds the policy limits.

The language in §624.155(7) limits the damages recoverable to those "which are a reasonably foreseeable result of a specified violation of this section by the insurer." Violation of § 624.155(1)(b) 1. occurs only when the insurer fails to settle a case with regards to the insured's interests. While a claimant may be allowed to sue for the damages which an insured suffers due to a violation of §624.155(1)(b)l ., there is no duty to settle owed a third party claimant and no direct damages suffered by a claimant which are recoverable.

As the Fifth District recognized in ***Dunn,*** where an insurer properly defends its insured and satisfies any excess judgment, absent egregious circumstances which would warrant the imposition of punitive damages, there are no damages for which any person, including a claimant, could sue to recover. *Id.* at 1 107-1 109. Likewise, where a matter is fully defended and the judgment against the insured does not exceed policy limits, the insured has no damages caused by the insurer's choice to litigate the matter rather than accede to a demand from a claimant. If the insurer does not breach the duty imposed by §624.155(1)(b) 1. and subject its insured to damages, the claimant does not have any claim which it could pursue either.

Even the Fourth District recognized "the injured party attempting to bring suit against the insurer for a bad faith refusal to settle . . . must be able to plead and prove damages." ***Zebrowski, 673 So.*** 2d at 564. A cause of action will not lie for a claimant who has not at least pled recoverable damages.

The nature of damages recoverable under §624.155(1)(b)l. were addressed by the Fifth District in ***Dunn, supra.*** In that case, the court concluded that the only damages recoverable under that statute are damages sustained by the insured caused by the insurer's breach of its fiduciary duty to its insured, regardless of whether the insured or the claimant brings the lawsuit. *Id.* at 1 107-1 108.

In ***Dunn,*** the claimant obtained an excess judgment against the insured and then sued the tortfeasor's insurer, alleging he was entitled to recover damages for his own emotional distress and the additional attorney's fees he incurred resulting from the failure of the tortfeasor's insurer to settle the case within policy limits. The Fifth District noted that under Florida law, pain and suffering damages were not recoverable in a bad faith suit absent conduct "so gross and extreme as to amount to an independent tort and to merit the award of punitive damages." *Id.* at 1 107.

The court said the allegations in the complaint that the third party claimant was entitled to recover for his own emotional pain and suffering, as opposed to the insured's, did not fit the scheme of third-party bad faith suits. The court further explained that §624.155(1)(b)l. did not allow recovery of pain and suffering damages allegedly sustained by the claimant himself because the duty imposed by §624.155(1)(b)l . ran only between the insurer and the insured:

> The duty breached is owed to the insured, and only damages for pain and suffering caused to the insuredn failure to settle requires allegation of damages sustained by the insured in breach of the duty between it and the insurer.

None of the damages pled by the Plaintiffs in this action are damages sustained by the insured. Nor does it appear in this factual context that Plaintiffs would be able to plead such damages because they did not obtain an excess judgment and the insurer provided a defense in the underlying action. (R. 44-45) For that reason, Plaintiffs have no claim they can bring under §624.155(1)(b)1.

II. AS A MATTER OF PUBLIC POLICY, THIS COURT SHOULD NOT CREATE A DIRECT DUTY OWED BY AN INSURER TO A THIRD PARTY CLAIMANT UNDER §624.155(1)(b)1.

The Fifth District was correct in its decision in *Dunn.* Recognizing a duty to settle a third-party claim would "greatly expand the theory and extent of liability of insurance carriers." *Dunn* at 1 108. In contravention of the plain meaning of the statute and established Florida case law consistently holding that §624.155(1)(b)I . does not create a direct duty to settle owed to an injured third party, the Fourth District has dramatically expanded bad faith liability by creating such a duty and, in doing so, has imposed a liability not contemplated by the contract of insurance. Such a judicial expansion of the exposure to an insurer under traditional liability insurance contracts cannot be said to have been contemplated in the current premium rate structure or the actuarial calculations with respect to exposure to damages.

There are numerous undesirable policy ramifications which would result from such a radical departure from the existing law. Further, there is no reason to create such a duty because existing Florida law provides adequate remedies for any bad faith failure to settle third-party claims.

A. The creation of a duty to settle owed to a third-party claimant directly conflicts with the good faith duty owed by an insurer to its insured to act in the insured's best interests and disregards the adversarial relationship between the insurer and the third-party claimant

Creating a new duty owed directly by an insurance company to third party claimants injured by its insured places an insurer in a position of conflict. Florida law recognizes that an insurer defending an insured pursuant to a liability policy owes its insured a good faith duty requiring the insurer to act in the best interests of its insured and "use the same degree of care and diligence as a person of ordinary care and prudence should exercise in the management of his own business." ***Boston Old Colony ins.*** Co. v. *Gutierrez,* 386 So. 2d 783, 785 (Fla. 1980).

The contractual duty owed by an insurer to its insured would conflict with the wholly independent duty running from an insurer to a third-party claimant which the Fourth District decision creates. The insurer would be left in a position of choosing between honoring its contractual and good faith obligations to its premium-paying insured and complying with a newly established duty to settle owed to the injured claimant.

The Fourth District decision imposing a good faith claims settlement duty under §624.155(1)(b)1. between injured third parties and insurers ignores the inherently adversarial relationship between them, which arises from the contractual and extra-contractual duties owed by the insurer to its insured. In ***Dunn,*** the Fifth District explained the difference in the relationship between an insurer and its insured on the one hand and the relationship between an insurer and an injured third party on the other hand with regard to §624.155(1)(b)1. as follows:

> The insurer has no insurance contract with the injured third party, and thus breaches no fiduciary duty with regard to that person when it wrongfully refuses to settle a suit for its insured. . . . The duty breached is owed to the insured . . . The relationship between the insurance company and the injured party (not its insured) is as adverse and arms length as the relationship between the tortfeasor and the injured party.

Id. at 1 107.

The Texas supreme court in ***Allstate Ins. Co. v. Watson, 876*** S.W.2d 145 (Tex. 1994) highlighted the conflict, concluding the Texas version of the Unfair Claims Practices Act[3] did not afford a direct duty to settle in favor of a third party claimant. As the court explained:

> Were we to extend to third party claimants the same duties insurers owe to their insureds, insurers would be faced with owing coextensive and conflicting duties. An insurer owes to its insured a duty to defend the insured against the claims asserted by a third party. Recognizing concomitant and coextensive duties under art. 21.21 to third party claimants, parties adverse to the insured, necessarily compromises the duties the insurer owes to its insured. In fact, the logical result of permitting a separate and direct cause of action in favor of third party claimants allows third parties to sue for unfair claim settlement practices even though the insured has no claim for an unfair claim settlement practice. As troublesome, it is conceivable that in attempting to settle claims pursuant to the demands of a third party claimant, insurers may be liable to the insured for settling too quickly. ***See Texas Farmers Insurance Co. v. Soriano,*** 844 S.W.2d 808 (Tex. App.--San Antonio 1993, writ granted)(affirming a judgment for actual and punitive

[3]The statute at issue in ***Watson*** was Art. 21.21, §1 6, which reads much like §624.155 in that it allows "any person who has sustained actual damages as a result of another's engaging in an act or practice declared in Section 4 of this Article...to be unfair methods of competition or unfair or deceptive acts or practices in the business of insurance" to sue an insurer.

> damages against an insurer and in favor of the insured for breach of the common law duty of good faith and fair dealing where the insurer attempted to settle multiple claims for its underinsured by offering the full policy limits against the insured's wishes. In refusing to provide a direct cause of action for third party claimants, the legislature may well have been aware of this potential for conflicting duties. We will not construe art. 21.21 or *Vail,* absent explicit directive from the legislature, so as to compromise the insurer's loyalties and obligations owed to the insured.

Id. at 150.

The adverse relationship between the insurer and the injured third-party claimant is inherently contradictory to the type of fiduciary duty which runs between the tortfeasor's insurer and its own insured. Yet, the Fourth District would impose the same duty which exists between an insurer and its insured upon an insurer in its relationship with a third-party claimant. By so doing, the Fourth District has injected a conflict situation into every lawsuit where the defendant has had the foresight to purchase liability insurance, in essence, writing the adversarial litigation system out of existence when an insured person is sued.

The conflict issue will arise in a variety of contexts. For example, §627.4147(1)(b), Fla. Stat. (1995), dictates the following with regard to the content of medical malpractice liability insurance policies issued in Florida after October 1, 1985:

> (1) In addition to any other requirements imposed by law, each self-insurance policy as authorized under s. 627.357 or insurance policy providing coverage for claims arising out of the rendering of, or the failure to render medical care or services . . . shall include:
>
> * * *

> **(b) A clause authorizing the insurer or self-insurer to determine, to make, and to conclude, without the permission of the insured, any offer of admission of liability and for arbitration pursuant to s. 766.106, settlement offer, or offer of judgment, if the offer is within the policy limits. It is against public policy for any insurance or self-insurance policy to contain a clause giving the insured the exclusive right to veto any offer for admission of liability and for arbitration made pursuant to s. 766.106, settlement offer or offer of judgment, when such offer is within policy limits. However, any offer of admission of liability, settlement offer, or offer of judgment made by an insurer or self-insurer shall be made in good faith and in the best interests of the insured.**

Thus, the statute empowers the insurer to settle cases within policy limits at its discretion, limited, however, by the obligation to respond in the best interest of the insured. There are plenty of reasons why a settlement might not be in an insured's best interest, even though a claimant offers to settle for less than policy limits. Doctors and other similarly positioned professionals rely on their reputations and while it may seem expedient to pay a claim because it can be settled for a nominal amount, settlement of a spurious claim potentially damages the professional's reputation and potentially interferes with the insured's ability to maintain or obtain staff privileges at a hospital or the ability to enter into health care management contracts with providers of health insurance.

Settlement of a malpractice claim also subjects a physician to additional scrutiny by various administrative bodies. For example, §458.311(6), Fla. Stat. (1995) mandates that the Agency for Health Care Administration investigate the underlying claims where a physician has had three or more claims in which payment of more than $25,000 has been made to settle the case, to determine if the agency must take

further action against the physician. Given the expense of malpractice litigation, a $25,000 settlement could be viewed as a nominal or nuisance value settlement even in an instance where the insured has a legitimate defense to the claim being made.

By settling such cases as rapidly as possible, the insurer finds itself in the untenable position of reasonably resolving the underlying case, only to damage its insured in the process. Lest this appear an alarmist's wistful prediction of the future, this Court has already addressed this issue at least initially in *Shuster v. South Bro ward Hospital District Physicians ' Professional Liability Insurance Trust, 5 9 1 So.* 2d 174 (Fla. *1* 992).[4] In *Shuster,* the insured alleged he was damaged by his insurer's settlement of several cases pending against him, even thought the settlements were made within policy limits. The insured claimed that because of the settlements, he could not obtain malpractice insurance permitting him to perform certain procedures requiring such coverage. He also claimed the settlements damaged his reputation, and that he sustained mental and emotional distress because of his insurer's conduct..

The insured had requested the insurer deny liability and defend the suits. The policy provided the insurer could make "such settlement of any claim or suit as it deems expedient." *Shuster,* 591 So. 2d at 176. Part of the dictionary definition of "expedient" was "guided by self interest." *Id.* This Court held the insured had no bad faith cause of action against his carrier because the policy provision put the insured "on notice that the agreement granted the insurer the exclusive authority to control

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[4]The policy in ***Shuster*** **was issued before the effective date of §627.4147(1) and the court declined to comment on the effect of that section on the issues in the case. *Id.* at 176.**

settlement and to be guided by its own self interest when settling the claim for amounts within the policy limits." *Id.* at 176-77.

This court then explained that the "deems expedient" language did not give an insurer absolute discretion to settle claims. *Id.* at 177. This court then identified "unusual circumstances" where an insurers settlement of a claim against the insured could damage the insured, giving rise to a claim of bad faith. *Id.* at 177-178. See ***also, Swamy v. Caduceus Self Insurance Fund, Inc., 648 So.*** 2d 758, 759-760 (1st DCA 1994), denying an insured recovery under §624.155 and common law for alleged lost profits and damage to reputation caused by an excess verdict, which the insurer had already paid in full, but noting that the insured tortfeasor's damages were not necessarily limited to the amount of the excess judgment against the insured.

What if the insurer had a duty running to the third-party claimants exposing it to liability for bad faith refusal to settle so that its own self-interest would be served by settling the claims despite its insured's interests or wishes? Would it be the legislature's intent or serve public policy to make an insurer's only choice in this type of situation whether to face a bad faith action brought by its own insurer or one brought by the third-party claimants?

There also may be instances where it is not in the insured's best interest to effect early settlements of all claims presented under an insured's policy. For instance, consider an insured who has an annual aggregate policy limit which caps the total dollars an insurer will pay on the insured's behalf for claims arising within a given year. There is typically, however, no cap on the amount of money an insurer is

required to expend to defend claims made against the insured. The insured's goal in purchasing the policy is to provide itself enough indemnity dollars to resolve anticipated claims against it. One way to achieve this goal is to defend the claims made against the insured as appropriate and maximize the number of claims which can be settled within the policy limits.

Assume there are certain claims pending where liability is probable but defenses exist; yet, the insured and insurer are also aware certain other catastrophic claims are about to be made where liability is certain and would involve dollars subject to the same aggregate limit. Should the insurer proceed to investigate and then settle the "probable liability" claims, and thereby exhaust the aggregate limit, relieving itself of any duty to defend any suit, under the rationale that it is discharging its good faith settlement obligation to the various third-party claimant? Or, does the insurer have an obligation to its insured to put the insured's interests first so that the "catastrophic claims" are considered and the insurer utilizes all available dollars for indemnity and defense in a way that affords the insured the greatest protection?

A similar conflict arises in the context of the relationship between the primary insurer and excess insurers. As the Fourth District itself recently recognized, a primary insurer owes the same duty to settle to an excess insurer as is owed to the insured. ***North American Van Lines, Inc. V. Lexington Ins. Co.,*** ____ ***So.*** 2d ____ 1996 Fla. App. LEXIS 6888, 21 Fla. L. Weekly D1564 (Fla. 4th DCA 1996). Just as an insured without an excess policy wants to maximize the defense and indemnification availability under the policy, so too does an excess carrier want the primary carrier to

vigorously defend cases and reduce the excess carrier's exposure. Excess carriers could and would contend primary carriers were offering their policy limits to a third-party claimant to eliminate the primary insurer's duty to defend which continues so long as any portion of the policy limit remains unpaid. This damages not only the excess carrier, but potentially impacts the insured as well in the situation where the excess policy does not contain a duty to defend the insured.

Worse still is the situation where there is no excess insurance. An insurer who, following a claim, quickly offers the third party claimant its policy limits will be accused by a wealthy insured of having acted to protect the insurer's own interests in saving defense dollars and protecting itself from the claimant's bad faith claim, with the consequence of having diluted the opportunity to effect a lower settlement using a more protracted settlement negotiation process and depriving the insured of the defense it is entitled to under the policy.

Similarly, consider the corporation that often opts for a large deductible in the range of $250,000 to $500,000. Under most liability policies, the insured's obligation to pay the deductible is triggered by the payment of a settlement. While the good faith settlement duty recognized by the Fourth District would run from the insurer to the third-party claimant, the insured corporation is not be subject to a similar duty to settle. The insured has an active interest in seeing the case vigorously defended so as to limit its exposure to pay the deductible. Should a different result obtain because there is an insurer who believes liability might be found and a jury misht award damages? Would an insurer be obliged to settle a claim for $275,000 where there is

a $250,000 deductible? Moreover, should an insurer settle with the third-party claimant for $275,000, where $250,000 is the insured's money, thereby relieving the insurer of any bad faith exposure to the third party claimant and relieving the insurer from incurring continued defense dollars?

What all of these scenarios highlight is that, first and foremost, it is the contractual relationship between insurer and insured that creates both a duty to defend and a duty to indemnify which is at the center of any obligation to settle in good faith. In the face of a lawsuit by a third-party claimant against its insured, an insurer is in exactly the same adversarial position as its insured and should not be subjected to exposure to any bad faith claim threatened by the third-party claimant. To find otherwise would fracture long established principles and cast serious doubt on the ability of any insurer to make the correct choice between the obligation to its insured and its duty to a third party claimant. There is, in fact, only one consideration. The insurer should act in the best interests of its insured at all times. And an insurer should remain free to make this choice without fear of liability to its insured's adversary.

B. The creation of a direct duty to settle owed to a third-party claimant would interfere with the constitutionally guaranteed freedom to contract

Beyond disrupting contractual and good faith duties running from insurer to insured, the imposition of a duty running from an insurer to a third-party claimant impermissibly interferes with the right to contract as guaranteed by both the Florida and United States Constitutions. The imposition of an independent duty to settle running from an insurance company to a third party claimant directly impacts the

insured's prime motivation for entering into an insurance contract in the first place -- namely, to finance the defense of claims made against it and have funds available to settle those claims or pay any judgment arising out of them.

"[S]ubsequent legislation which diminishes the value of a contract is repugnant to the [Florida] Constitution. *Dewberry v. Auto-Owners Ins. Co,, 363 So.* 2d 1077, 1080 (Fla. 1978). Thus, if it were really the intent of the Florida legislature to create an independent duty running from an insurer to a third-party claimant, §624.155(1)(b)l , is void as an unconstitutional restraint on the ability of parties to contract as they see fit. The constitutional problems raised by such a reading of §624.155(1)(b) 1. can be avoided by finding the legislature did not intend insurers to be liable to third-party claimants for breach of a duty separate and apart from the ones arising from the contract with its insured.

C. The duty to settle owed a claimant as created by the Fourth District in effect imposes a no-fault tort liability system in actions where a defendant is also an insured

The practical effect of the Fourth District's determination that there is a duty owed directly to a claimant is to carve out a no-fault tort liability system which would apply only in those actions prosecuted against defendants who have purchased insurance. This dramatic alteration of existing Florida law yields an unworkable result which is ultimately detrimental to conscientious defendants who purchase insurance to protect themselves.

Florida currently operates under a fully adversarial litigation system which does not differentiate between tortfeasors who have insurance and tortfeasors that do not.

Under the current system, the defendant/tortfeasor may contest his or her liability, asserting various affirmative defenses. The defendant/tortfeasor may also contest damages both in terms of the ultimate amount which a claimant is damaged, as well as contesting the tortfeasor's proportion of liability for the particular damages sustained by a claimant.

A person who purchases liability insurance receives two benefits under that liability insurance policy. First, the insurer is obliged to provide a complete defense at its own expense to its policy holder, provided allegations are made which would be covered by the policy. The insured also chooses an amount of damages, for which the insurer agrees to provide indemnity pursuant to the coverage afforded under the policy. The obligations of the insurance contract itself, coupled with the good faith duties recognized at both common law and pursuant to §624.155 as between the insureds and their insurers compels the insurer to make its best efforts to resolve claims within policy limit, with the best interests of its insured in mind.

The newly recognized duty to settle owed directly to a claimant turns the current system on its head. This new duty places the insurer in a vacuum such that it now has a duty to pay the claimant whatever is demanded without question or be faced with a claim of breaching this new-found duty. A recognition of this duty destroys the ability of insurers and insureds alike to contest the insured's liability and the amount of damages for which the insured is ultimately responsible, Contrary to the Fourth District's determination that an insurer owes a claimant a direct duty to

settle exists, there is nothing in 5624.155 to suggest the legislature intended to transform Florida's present tort liability system into a pure no-fault insurance system.

Practically speaking, every case brought against an insured defendant would automatically be a policy limits case. Even in the event the insurer conducts a successful defense by either achieving a verdict for less than the amount of those policy limits or reaching a settlement with the claimant, the game is not over. The insurer is still left facing the accusation from the claimant that regardless of the results achieved in the underlying litigation, the insurer should have done something sooner to resolve the case, entitling the claimant to recover his litigation costs and "delay" damages. (i.e. interest on a unliquidated claim) from the hypothetical point where the lawsuit against the insured should have been settled.

D. Creation of a direct duty to settle owed to third-party claimants would result in substantial economic consequences

Substantial economic consequences result from creating a direct duty to settle owed to third-party claimants under §624.155(1)(b) 1. The imposition of an independent duty owed to a third-party claimant to settle in good faith opens the floodgates of litigation by inviting a second lawsuit by the third-party claimant directly against the insurer any time the claimant is dissatisfied with either the result obtained by the claimant in the trial against the insured or a settlement offered before trial. Not only does this double litigation of every tort judgment rendered against a defendant who has insurance increase the costs to insurance consumers, it burdens the courts with duplicative litigation of every tort claim where a defendant had the foresight to purchase liability insurance.

The most obvious result of recognizing the existence of a duty running directly from an insurer to a third-party claimant under §624.155(1)(b)1 . is the virtual sanctioning of the filing of a second action by the third-party claimant against the insurer every time a claimant is dissatisfied with the judgment it receives in litigation against the insured. Third-party claimants who were not offered a settlement and who were forced to prove their cases at trial would complain that their cases should have been settled and would file their bad faith claims.

Even if a matter were resolved short of trial, no settlement would ever be final as the claimant would settle the claim it has against the insured and turn around and sue the insurer on the basis that the settlement was not made fast enough. Regardless of whether the insurer responded appropriately and in a timely fashion to settlement demands from the claimant, it will be faced with paying something "extra" to rid itself from this exposure or pay attorney's fees to defend itself against such allegations.

California's nine year experiment in allowing claimants to sue based on a duty to settle owed to the claimant is proof positive that the double litigation of every claim will occur. In ***Royal Globe Insurance Co, v. Superior Court, 592*** P.2d 329, 341 (Cal. 1979), when California first recognized a duty to settle running directly between an insurer and a third-party claimant, dissenting Justice Richardson prophesied:

> It seems predictable that in almost every case in which an insurer hereafter declines a settlement offer the injured Third-party Claimant will be tempted to file an independent action against the carrier despite the clear admonition in our recent unanimous ***Murphy v. Allstate Ins. Co., 553*** P.2d

584 (Cal. 1976)] decision that the insurer's duty to settle runs to the insured and not to the injured party.

That prophesy came true and after nine years, the California Supreme Court reversed itself and found the California version of the Unfair Claims Practices Act did not authorize a third-party claimant's lawsuit directly against an insurance company. *See Moradi-Shalal v. Fireman's Fund Ins. Cos., 758* P.2d 58, 69 (Cal. 1988). Commentators evaluating the impact of the California Supreme Court's decision in *Royal Globe* concurred in concluding that a duty running directly to a third-party claimant gives rise to double litigation: an initial suit against the insured, followed by the second suit against the insurer for bad faith refusal to settle.[5]

Creation of a cause of action under §624.155(1)(b)1. by a third-party claimant directly against an insurer also breeds litigation regarding the nature and the extent of the duty owed to the third-party claimant. Within those secondary lawsuits, a myriad of issues relating to the procedural aspects of the prosecution of a statutory third-party bad faith claim will arise and require resolution by the courts. The courts will reach widely disparate results, fostering more litigation and adding uncertainty to the entire process of handling claims. The litigation itself is likely to be more expensive than traditional litigation to the extent that punitive damages are sought requiring extensive discovery missions looking for proof of a pattern of bad faith claims settlement practices.

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[5]Price, *Royal Globe Insurance Company v. Superior Court: Right to Direct Suit Against an Insurer by a Third Party Claimant,* 31 Hastings L.J. 1161, 1186-1187 (1980); Allen, *Insurance Bad Faith Law: The Need for Legislative Intervention,* 13 Pacific L.J. 833, 851 (1982).

Some of the more obvious questions which would require resolution include:

1) What triggers the accrual of a cause of action for bad faith failure to settle against an insurer";

2) What is the nature of the claimant's recoverable damages for breach of the duty to settle owed directly to the third party claimant[7]; and

3) What are the methods of proving whether an alleged breach of the duty to settle owed a third-party claimant is a sufficiently "regular business practice" to a warrant an award of punitive damages.[8]

The economic consequences that flow from allowing a third-party claim for failure to settle based on a duty owed to the claimant are not limited to the fact that

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[6]In California, this issue arose in the context of whether settlement of the underlying litigation against the insured was a sufficient conclusion to allow a third party to bring a 5790.03 claim against an insurer. ***See Rodriguez v. Fireman's Fund Ins. Cos.,*** 190 Cal. Rptr. 705, 709 (Cal. Ct. App. 1983), holding that settlement of the third party's claim against the insured was a sufficient conclusion to allow the third party to proceed against the insurer for statutory violations; ***but see Nationwide Ins. Co. v. Superior Court, 180*** Cal. Rptr. 464, 466 (Cal. Ct. App. 1982), holding that adjudication of the insured's liability to the third party claimant was a necessary pre-requisite to maintenance of a 5790.03 action, The resolution of this conflict, in fact, was the basis upon which the California Supreme Court accepted review in *Moradi-Shalal, **supra.***

[7]*See* ***Schlauch v. Hartford Acc. Indem.*** Co., 194 Cal. Rptr. 658, 661 (Cal. Ct. App. 1983), allowing for recovery of emotional distress and punitive damages in appropriate circumstances by a third party claimant for the insurer's violation of its duty to the claimant under the Unfair Practices Act.

[8]*See* ***Colonial Life & Acc. Ins. Co. v. Superior Court, 647*** P.2d 86, 90 (Cal. 1982), approving the trial court's discovery order requiring an insurer to identify all claimants with whom a particular adjuster had attempted settlements so that claimant's counsel could obtain authorizations from other claimants regarding their claims files for purposes of establishing a pattern of unfair practices.

there will now be two lawsuits springing from every claim. Litigating the third-party claim against the insurer for bad faith failure to settle under §624.155(1)(b) 1. will be more expensive than the typical lawsuit. The extensive discovery required to establish a pattern of unfair claims practices in support of a punitive damage claim is expensive and burdensome, potentially impacting dozens or even hundreds of persons over a lengthy period of years. Settlement costs are increased, even within the litigation of the underlying tort claim between the claimant and the insured, because settlement of the potential follow-up statutory bad faith suit becomes a factor in every case. *Moradi-Shalal, 758* P.2d at *66;* Note, ***Extending the Liability of Insurers for Bad Faith Acts: Royal Globe Insurance Company v. Superior Court,*** 7 Pepperdine L. Rev. 777, 790-791 (1980); Price, *supra* note 2 at 1 186-1 187; Allen, *supra* note 3 at 851.

Springing from the increased claims handling costs associated with the imposition of a duty on an insured running to third-party claimants for bad faith failure to settle are the increased insurance premiums, which inevitably must result, as well as the likelihood of a decrease in the number of carriers willing to provide insurance coverage or both.[9] The reduced availability of affordable liability insurance has a ripple effect economically in that the increase in uninsured risks also increases the costs society as a whole must pay to compensate those who are injured and have no other source of recompense.

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[9]White, ***Liability Insurers and Third Party Claimants: The Limits of Duty, 48*** Univ. Chi. L. Rev. 125, 139-140 (1981).

The negative economic impact of a recognition of a duty owed by an insurance company directly to a third-party claimant under §624.155(1)(b)1. cannot be overdramatized. By sanctioning the double litigation of every tort liability claim, this new duty increases the costs to insurers. It will cost additional sums to resolve the second suit either by settlement or litigation of the claims based on breach of the independent duty to settle owed to claim amounts. These costs ultimately filter down to consumer. The increased burden on the court system is likewise a negative economic consequence of the recognition of this duty which ultimately filters down to the taxpayers.

E. Existing Florida law and the remedies afforded thereby serve as an adequate check on any bad faith failure to settle third party claims

Alarmist contentions from the plaintiff's bar aside, there are existing remedies under Florida law which already adequately check improper behavior by an insurer in the context of a third-party claim, The sanctions which can be imposed if the insurer breaches the duty to settle already owed to its insured are sufficient to compel an insurer to act with the utmost good faith in deciding to settle a case. There is no need to establish a new cause of action based on a duty owed directly to a claimant.

The duty to settle which an insurer owes its policyholder already acts to compel an insurer to settle a claim. If a plaintiff/claimant obtains a judgment in excess of policy limits, the insured may bring a bad faith claim for the excess amount under either existing common law principles or under §624.155(1)(b)1. Alternatively, based on the principles of *Thompson, supra,* the claimant can directly pursue the insurer, or the plaintiff/claimant can receive an assignment of any claim the insured may have

against its insurer and prosecute the insured's bad faith action against an insurance company under §624.155(1)(b)1. This type of suit provides a vehicle by which compensatory damages are recoverable and raises the possibility of recovering: 1) the amount of any judgment in excess of the policy limits; 2) attorney's fees based upon what the insured has expended because of the insurer's wrongful conduct; and 3) punitive damages, upon submission of proper proof.

Section 768.79, Fla. Stat. (1996) is another means available to sanction an insurer who fails to make an appropriate effort to settle a case. The statute allows for recovery of attorney's fees and other litigation costs if a plaintiff achieves a result at trial at least 25 percent in excess of the amount of the demand. Absent a showing by the losing party that a demand for judgment was made in bad faith, an award of fees and costs incurred by the prevailing party from the date of the demand forward is mandatory. As the insurer controls its insured's defense and the decision to respond to any demand for settlement within policy limits, the insurer who fails to accept a demand becomes liable not only for the attorney's fees expended on behalf of its insured, but for the plaintiff/claimant's fees and costs as well.

Likewise, an insurer who opts to defend a case without reliance upon a justiciable issue of either fact or law would be liable for the third-party claimant's reasonable attorney's fees if the third-party claimant prevailed in a Chapter 57 action against the insured. 957.105, Fla. Stat. (1993). Again, the insurer would end up paying not only its insured's attorney's but also the fees and costs incurred by the claimant forced to prosecute a case for which there is no defense.

In sum, there is simply no need to create a direct duty owed to a third-party to provide a check on potential insurer misconduct in the settlement of third-party claims. Sufficient incentives already exist in the form of the duty to settle owed an insured and procedural remedies under § § 57.105 and 768.79 to prohibit gamesmanship by insurers.

CONCLUSION

This Court should affirm the conclusion of the Second District in *Conquest,* echoed by the Third District in *Cardenas* and the Fifth District in *Dunn,* and overturn the Fourth District's decision in this case. Section 624.155(1)(b)1. does not create a duty to settle owed directly to a third party claimant, as *Conquest, Cardenas,* and *Dunn,* all correctly held. The language employed in §624.155(1)(b)1., defining a violation of the duty to settle in terms of whether an insurer has acted "fairly and honestly toward its insured and with due regard for his interest" compels such a conclusion. Florida common law regarding third party bad faith supports this interpretation of §624.155(1)(b)1.

The only damages which can be recovered for violation of §624.155(1)(b) 1. are damages sustained by an insured. Where, as here, the insured is defended and the judgment against it is within policy limits and has been fully paid with interest, the insured has suffered no damages. Therefore, Plaintiffs cannot proceed with their claim against State Farm because there are no damages to the insured which can be recovered .

As a matter of public policy, this Court should refuse to recognize that §624.155(1)(b) 1. creates a duty to settle owed directly to a third-party claimant by an insurer. Such a duty would directly conflict with the existing duties owed by the insurer to its policyholder pursuant to the insurance contract, common law and 9624.155, forcing an insurer to choose between honoring the duty to the insured and

the duty to the claimant. This duty to the claimant interferes with the constitutionally guaranteed freedom to contract.

Recognizing a duty to settle owed to a claimant in effect creates a no-fault tort liability system for tortfeasors who carry insurance. The economic consequences which would result include increased insurance costs and undue burden on the court system, with every tort liability case spawning two lawsuits -- one arising out of the accident in question and one arising from the way settlement negotiations are conducted in the course of the lawsuit about the accident. None of this is necessary to compel an insurer to act properly to settle the case. The duty it owes to its insured and the procedural remedies afforded by § §57.105 and 768.79 all work as incentives for an insurer to act in good faith.

The Fourth District's decision in this case is wrong. This court should reinstate the trial court's grant of summary judgment in favor of State Farm.

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