AMERICANBARASSOCIATION

ABA Publishing

Tort Trial & Insurance Practice Law Journal, Spring 2020 (55:2)

III. BAD FAITH LAW

Laura Meyer Gregory

A. *Is an Insurer in Bad Faith When It Did Not Settle a Claim Against Its Insured, Because Its Policy Required the Insured to Consent to the Settlement and He Would Not?*

Massachusetts' highest court has decided that an insurer did not violate Massachusetts statutes requiring insurers to settle claims in which liability has become reasonably clear, when it did not settle a claim because its policy required the insured's consent to settle a claim and the insured refused to provide that consent.[30] Specifically, the Court considered whether an insurer's failure to settle a claim due to the insured's refusal to consent to the settlement violated the statute requiring an insurer to "to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear" and whether such consent-to-settle provisions are against public policy.[31]

The Massachusetts Supreme Judicial Court took this case from the Appeals Court *sua sponte* and solicited amicus briefs regarding the following:

> Whether a liability insurer violated its duty, under G. L. c. 176D, § 3 (9) (f), to effectuate a prompt, fair, and equitable settlement of a claim in which liability had become reasonably clear, where the insured refused to consent to a settlement and the insurance policy provided that the insurer would not settle any claim without the informed consent of the insured; whether such a provision is unenforceable as against public policy.[32]

30. Rawan v. Cont'l Cas. Co., 136 N.E.3d 327 (Mass. 2019).
31. Mass. Gen. Laws ch. 176D, § 3(9)(f).
32. Docket at #2, *Rawan*, No. SJC-12691 (Feb. 15, 2019).
33. Amici Curiae briefs were filed on behalf of the American Council of Engineering Companies of Massachusetts, the Massachusetts Chapter of the American Institutes of Architects,

Five Amici Curiae briefs were filed.[33]

This case arose out of the insured's structural engineering work for the plaintiffs in the design and construction of their residence.[34] The homeowners sued the insured engineer for negligence, breach of contract, and violation of Massachusetts Unfair Trade Practices statute, M.G.L. c. 93A.[35] The insurance policy issued to the engineer provided that the insurer would "not settle any claim without the informed consent" of the engineer.[36]

After two settlement offers were rejected, the insured engineer refused to settle, instead seeking to go to trial.[37] Ultimately, the jury found against the insured and awarded $400,000 to the plaintiffs and also issued an "advisory verdict" finding the engineer had committed unfair business practices and awarding an additional $20,000 in damages, which the court later increased to $40,000 based on its determination that the insured had acted either knowingly or recklessly.[38] The judgment was paid in full, with the insurer paying its policy limits (reduced by defense costs) and the insured paying the remainder.[39]

The plaintiffs alleged bad faith by Continental Casualty Company ("Continental"), the insurer of the engineer, claiming violation of the Massachusetts Unfair Claims Settlement Practices Act by "[f]ailing to effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear."[40]

The trial court found in the insurer's favor, on summary judgment.[41] The Court determined that Continental counseled the insured engineer that the claims against him had substantial merit and that a judgment in excess of the policy limits could result, but the insured steadfastly refused to agree to increase the offer over the $100,000 that had been offered and rejected twice previously and refused any further settlement negotiations.[42] In these circumstances, the trial court concluded that "Continental's hands were tied, and it was legally precluded from making other efforts to settle the case. Accordingly, Continental cannot be found liable for violating c. 176D [the Unfair Claims Practices Act], and, by extension, c. 93A [the Unfair

the Professional Liability Foundation Ltd., the Boston Bar Association, the American Property and Casualty Insurance Association, Medical Professional Liability Association, the Massachusetts Insurance Federation, and the Massachusetts Defense Lawyers Association.

34. *Rawan*, 136 N.E.3d at 330.
35. *Id.*
36. *Id.*
37. *Id.*
38. *Id.* at 334.
39. *Id.*
40. Mass. Gen. Laws ch. 176D, § 3(9)(f).
41. *Rawan*, 136 N.E.3d at 330.
42. Brief of Appellants, Douglas M. Rawan & Kristen Rawan, at ADD. 2–3, https://www.ma-appellatecourts.org/pdf/SJC-12691/SJC-12691_01_Appellant_Rawan_Brief.pdf.

Trade Practices Act], because it engaged in all the settlement practiced which its insured … authorized."[43]

This case appears to be the first case to address whether an insurer's failure to settle a claim due to its compliance with the provision in the insurance contract requiring the insured's consent-to-settle a claim violates public policy or is an unfair claims practice. Such consent-to-settle provisions are common in professional liability, employment practices liability, and directors' and officers' policies.[44] And, like Massachusetts, the majority of states have enacted some form of the model Unfair Claims Settlement Practices Act promulgated by the National Association of Insurance Commissioners.[45]

The plaintiffs' counsel argued to the Massachusetts Supreme Judicial Court that these consent-to-settle clauses are against public policy.[46] Specifically, plaintiffs claimed that the statute requiring an insurer to "effectuate prompt, fair and equitable settlements of claims in which liability has become reasonably clear," is violated by a consent-to-settle clause.[47]

Such consent-to-settle clauses are not new, having been present in case law in Massachusetts going back nearly forty years.[48] A typical clause requiring that the insured consent in order for a settlement funded by the insurer to occur provides that the insurer "shall . . . not settle any claim without the written consent of the named insured which consent shall not be unreasonably withheld."[49] The consent-to-settle clause in *Rawan* did not include a reasonableness component. Additionally, the *Rawan* policy did not include a so-called "hammer clause," which is included in most policies that contain consent-to-settle clauses. The hammer clause limits the insurer's risk and requires the insured to bear at least a portion of the risk of a judgment against the insured in excess of the amount that the case could have settled for had the insured provided consent. The hammer clause at issue in *Freedman* was:

---

43. *Id.*

44. *See*, *e.g.*, Clauson v. New England Ins. Co., 83 F. Supp. 2d 278, 281 (D.R.I. 2000). In *Clauson*, the court recognized that most legal malpractice policies contain clauses requiring the insured's consent in order for the insurer to settle. It stated that these clauses "are included in professional liability policies in recognition of the fact that settlement of claims may adversely and unjustifiably affect the insured's professional reputation." *Id.* (citing R. Long, Law of Liability Insurance, § 12C.08[8] (1998)).

45. *See* Unfair Claims Settlement Practices Act, § 4D (NAIC 1997), https://www.naic.org/store/free/MDL-900.pdf ("Not attempting in good faith to effectuate prompt, fair and equitable settlement of claims submitted in which liability has become reasonably clear" it is an unfair claim practice).

46. *Rawan*, 136 N.E.3d at 337.

47. *Id.*

48. *See*, *e.g.*, Van Dyke v. St. Paul Fire & Marine Ins. Co., 448 N.E.2d 357 (Mass. 1983); Mut. Ins. Co. v. Murphy, 630 F. Supp. 2d 158, 170 (D. Mass. 2009); *see also* 14 Steven Plitt et al., Couch on Insurance § 203:10 (2019 supp.) and cases cited therein.

49. Freedman v. United Nat'l Ins. Co., 2011 WL 781919, at *1 (C.D. Cal. Mar. 1, 2011).

> If however, the named insured refuses to consent to a settlement recommended by [Insurer] and elects to contest the claim or continue legal proceedings in connection with such claim, [Insurer's] liability for the claim shall not exceed the amount for which the claim could have been settled, including claims expenses up to the date of such refusal, or the applicable limits of liability, whichever is less.[50]

A similar clause was noted as "standard" for professional liability policies by the court in *Transit Casualty Co. v. Spink Corp*.[51] The court in *Security Insurance Co. of Hartford v. Schipporeit, Inc.*,[52] discussed the application of a hammer clause stating:

> If an insured is presented with an opportunity to dispose of a claim and the insurer recommends that the claim be resolved, the insured may refuse to accept the insurer's recommendation only at his peril. The risk of loss over and above the proposed settlement passes to the insured. But the term "settlement" in this provision makes sense only if it means a full and final disposition of a claim, and that assumes that a release of liability will be issued.[53]

The policy at issue in *Rawan* does not include a hammer clause. The Rawans argued that the consent-to-settle clause without a "hammer" clause defeats the letter and spirit of Massachusetts Unfair Claims Practices Act[54] and therefor violates public policy. The Rawans suggested that it would not be violative of public policy if the consent-to-settle clause was accompanied by a hammer clause, a mandatory arbitration clause, or other process to address a disagreement between insurer and insured regarding settlement.[55]

As noted above, consent-to-settle clauses are common in professional liability policies. Further, as noted by the *Rawan* amici, the ability of an insured to obtain a policy that allows them to control settlement can be determinative of whether they obtain insurance, if they are not obligated to purchase insurance, and certainly will impact on future insurance rates, available public information, and potentially on their professional reputation.[56] For example, provisions allowing the insured to control settlement were not allowed in Florida medical malpractice policies until the law was

50. *Id.*
51. 156 Cal. Rptr. 360, 363 (Ct. App. 1979) (disapproved of on other grounds by Commercial Union Assurance Companies v. Safeway Stores, Inc., 164 Cal. Rptr. 709 (Ct. App. 1980)).
52. 69 F.3d 1377, 1383 (7th Cir. 1995).
53. *Id.*
54. Brief of Appellants, *supra* note 42, at 32.
55. *Id.*
56. *See* Brief of Amici Curiae American Property and Casualty Insurance Association, Medical Professional Liability Association, and Massachusetts Insurance Federation at 18–20, https://www.ma-appellatecourts.org/pdf/SJC-12691/SJC-12691_19_Amicus_American_Property_and_Casualty_Brief.pdf.

changed in 2011.[57] Prior to that time many doctors chose not to obtain malpractice coverage, with one of the reasons cited being insurers settling cases that the doctor believed were frivolous.[58] Further, prior to the revision of the law, the *Florida Bar Journal* outlined the following potential impacts of the "settlement of a medical malpractice case on a physician's livelihood and reputation, including (1) future insurance rates, (2) insurability, (3) the possibility of a 'strike,' (4) the potential for excess exposure, (5) reports to the administrative agencies, and (6) the potential for adverse publicity."[59]

On December 16, 2019, the Massachusetts Supreme Judicial Court issued a decision upholding consent-to-settle provisions requiring the insured's consent in order to settle a case against them, finding that such provisions are not against Massachusetts public policy.[60]

> A consent-to-settle provision in an insurance policy does not violate an insurer's duty to effectuate a prompt, fair, and equitable settlement under G.L. c. 176D, § 3(9) (f). However, a consent-to-settle provision is not a carte blanche for an insurer to engage in unfair or deceptive conduct with a third-party claimant merely because the insured declines to reach a settlement. An insurer still owes a duty to conduct a reasonable investigation and engage in good faith settlement attempts consistent with its duty to both its insured and the claimant.[61]

The Court outlined several bases for its decision, including: (1) professional liability policy are voluntary, not mandatory; (2) professional liability policies with consent to settle clauses predate the Massachusetts Unfair Claims Practices Act (G.L. c. 176D) and its revision to allow third parties to bring suit against insurers for violation of the act; and (3) consent-to-settle clauses serve valuable purposes—protecting professional's reputation and good will and encouraging professionals to purchase insurance, thereby creating more funding for third-party claims.

The Court further rejected the claimant's argument that consent-to-settle clauses should only be allowed when paired with hammer clauses, stating that there was not a specific legislative mandate to do so and without such a mandate the Court would not redraft voluntary insurance policies.[62] Further, the Court acknowledged that "The hammer clause also will diminish the incentive professionals have to purchase this voluntary

57. Fla. Stat. §627.4147.

58. Bob LaMendola, *Uninsured Doctors on Rise in S. Florida*, S. Fla. Sun Sentinel (July 27, 2008), https://www.sun-sentinel.com/news/fl-xpm-2008-07-27-0807260139-story.html.

59. Robert L. Rubin, *Legal, Practical, and Ethical Considerations of Medical Malpractice Settlements*, Fla. Bar J., Jan. 2009, https://www.floridabar.org/the-florida-bar-journal/legal-practical-and-ethical-considerations-of-medical-malpractice-settlements.

60. Rawan v. Cont'l Cas. Co., 136 N.E.3d 327, 327 (Mass. 2019).

61. *Id.* at 343.

62. *Id.* at 341 n.7.

insurance, which … serves a valuable purpose: it benefits third parties by providing deeper pockets for recovery."[63]

The court went on to hold that the existence of a consent-to-settle clause did not eliminate the insurer's obligations to act in good faith towards both its insured and the third-party claimant, stating:

> [t]he determination whether an insurer has complied with its dual obligations, despite the existence of a consent-to-settle clause, is a factual one to be measured in terms of the insurer's good faith efforts and transparency toward both its insured and a third-party claimant. These efforts would include a thorough investigation of the facts, a careful attempt to determine the value of a claim, good faith efforts to convince the insured to settle for such an amount, and the absence of misleading, improper, or 'extortionate' conduct towards the third-party claimant.[64]

Whether state law allows a plaintiff/claimant to bring a claim directly against the insurer for bad faith on a third party claim will greatly impact on the application of bad faith law in the context of consent-to-settle clauses. Massachusetts law provides for a direct cause of action by a claimant/plaintiff against an insurer for failing to settle a claim, but other states do not. Further, some jurisdictions and courts emphasize protecting insureds, while others emphasize protecting innocent third parties. It will be interesting to see whether other states follow the lead of the Massachusetts Supreme Judicial Court and rule that a policyholder's refusal to settle pursuant to a policy with a consent-to-settle clause offers the insurer some shelter from application of the Unfair Claims Handling Practices Act.

41, *Id.*
42, *Id.* at 341 (citations omitted).

857-321-7020
lgregory@sloanewalsh.com

Laura Meyer Gregory is a partner of Sloane & Walsh LLP in Boston. A member of the firm's insurance group, her practice concentrates on the representation of insurers and insureds in insurance coverage and bad faith matters, before state and federal trial and appellate courts. Additionally, she provides coverage opinions, advice and analysis to clients on coverage and bad faith issues, as well as preparing and responding to demands made pursuant to M.G.L. c. 93A. Ms. Gregory also handles cases involving bad faith and unfair claims handling claims, both within and without the context of coverage, and has litigated an insurance fraud claim successfully through trial. Ms. Gregory has specialized in insurance coverage and bad faith matters for more than 25 years and received the Chartered Property & Casualty Underwriter (CPCU) insurance industry designation in 1999.
#LauraHasItCovered