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Appellate Reports

COURT OF APPEAL REJECTS CACI 2334 FORMULATION OF WHAT CONSTITUTES A BAD-FAITH FAILURE TO SETTLE

Pinto v. Farmers Ins Exchange (2021) __ Cal.App.5th __ (Second Dist., Div. 1.)

Who needs to know about this case: Lawyers litigating insurance bad-faith claims based on the insurer's failure to accept a policy-limits demand.

Why it's important: (1) Holds that an insurer's rejection of a reasonable policy-limits demand is not *per se* unreasonable; rather, to succeed on a failure-to-settle bad-faith claim, the policyholder must prove that the insurer's failure to accept the demand was unreasonable. (2) As drafted, the CACI failure-to-settle instruction, CACI 2334, is erroneous because it does not instruct the jury that the insurer cannot be held liable for bad faith unless its rejection of the settlement offer was unreasonable; (3) holds that the plaintiff's reliance on the defective instruction and verdict form based on that instruction resulted in a defective verdict, leading to a reversal and entry of judgment for the insurer.

Synopsis:

CACI 2334 is titled "Bad Faith (Third Party) – Refusal to Accept Reasonable Settlement Within Liability Policy Limits." It provides that, to establish a bad-faith claim against a liability insurer for failing to accept a reasonable settlement demand, the plaintiff must establish three elements:

1. That [*name of plaintiff in underlying case*] brought a lawsuit against [*name of plaintiff*] for a claim that was covered by [*name of defendant*]'s insurance policy;

2. That [*name of defendant*] failed to accept a reasonable settlement demand for an amount within policy limits; and

3. That a monetary judgment was entered against [*name of plaintiff*] for a sum greater than the policy limits.

Note that the instruction does not speak to whether the insurer's rejection of the offer was reasonable or unreasonable. As drafted, the instruction therefore tells the jury that an insurer's failure to accept a reasonable settlement offer is bad faith.

In this case, plaintiff Martin was a passenger in a pickup truck with Orcutt, Pinto, and Williams as they returned from a party at Lake Havasu. The truck went off the road and all four occupants were injured. Martin had a Farmers policy that covered the truck and any permissive drivers. Policy limits were $50,000 per person and $100,000 per occurrence.

Martin's agent reported the accident on April 9, 2013. Farmers assigned the claim to Lawler, an adjuster. The next day Martin's mother told Lawler that Martin had suffered a head injury and could remember nothing before 1 p.m. on the day of the accident, and hence had no memory of the accident. She also told Lawler that Orcutt was driving when the accident occurred, but was now denying that she had been the driver; and that Pinto had been paralyzed in the accident. Orcutt refused to communicate with Lawler.

Farmers then appointed a different adjuster for the claim, Cannon. On April 29, 2013, Orcutt spoke to Cannon and told her that she had been injured in the accident but could not remember who was driving. She admitted that she had driven Martin's truck many times to Lake Havasu, and could not distinguish in her mind which trip had resulted in the accident. The next day Martin told Cannon that she now remembered that Orcutt had been driving but could not remember why. She admitted that there were lots of drugs and alcohol consumed at the party.

The police report stated that Orcutt was the driver and had been driving while under the influence of alcohol. At the scene, Orcutt told the officer that she thought Williams was supposed to be driving, but said, "Everyone keeps saying I was driving." The report said that a firefighter overheard Orcutt, Williams, and Martin say that Orcutt was driving. A witness said that Orcutt was highly intoxicated at the accident scene and that she said, "I'm going to jail for what I did."

Cannon tendered the policy's $100,000 liability limits to all injured parties except Orcutt, whom Cannon determined was likely the at-fault driver.

On July 1, 2019, Pinto's counsel, Algorri, sent Cannon a letter offering to settle Pinto's claim against Martin for the policy limits. The letter referred to Martin as the insured and did not mention Orcutt or her status as possible insured permissive user. The letter demanded that "the insured" provide a release, a declaration that "the insured" had not been acting within the course and scope of her employment at the time of the accident, and a copy of any applicable insurance policy. The offer had a 15-day deadline for acceptance.

Cannon assumed that Pinto's demand was directed to both Martin as the named insured and Orcutt as the permissive driver and additional insured, and forwarded the offer to them the following day, July 6.

On July 9, 2019, Algorri told Cannon that he needed to inspect Martin's truck to evaluate a potential claim against GM.

On July 11, 2019, Cannon, still not having heard back from Orcutt, retained a private investigator to locate her and obtain information about the accident and any other insurance she might have. On July 13, the investigator reported that Orcutt had been located. She told the investigator that she had no other insurance and had not been acting within the course and scope of any employment when the accident occurred. Orcutt never responded on this or any other occasion to Cannon's many requests for a declaration to this effect.

Also on July 11, Cannon called Algorri three times and left messages requesting an extension of time on the offer deadline. Algorri never responded.

Cannon retained an attorney, Limor Lehavi, to help with Pinto's claim. On July 15, 2019, Lehavi faxed a letter to Algorri tendering the $50,000 per person bodily injury policy limits to resolve

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Pinto's claims "against any and all insureds under the policy." In the letter, Lehavi asked whether Pinto's offer pertained to both the named insured and the permissive driver, and informed Algorri that Farmers could not pay policy limits without a release of all of its insureds. Lehavi noted that Algorri had not provided a declaration form as promised, and enclosed a proposed declaration form, asking if it was acceptable. Lehavi asked Algorri to confirm that Farmers providing the text of the policy satisfied Pinto's demand for policy information, as Orcutt had represented that she possessed no other insurance, and asked whether Pinto intended to pursue a claim against GM, which might expose Farmers' insureds to a cross-complaint by GM and therefore delay Farmers from paying out policy limits. Lehavi asked whether Pinto had any pending medical liens, which must be resolved as part of any settlement, and asked whether Pinto was married, as any spouse would need to be included in Pinto's release. Lehavi stated that Farmers had insufficient time to comply with all of the conditions of Pinto's demand, and requested an extension of 30 days.

Algorri responded that the term "insured" in Pinto's offer meant all insureds, including the driver, Orcutt. Algorri informed Lehavi that Pinto was unmarried, and advised that Farmers had until 5:00 p.m. the next day to meet all conditions of the offer. Algorri failed to respond to Lehavi's other inquiries.

Before the 5:00 p.m. deadline on July 16, Farmers hand-delivered a letter to Algorri's office accepting Pinto's offer. The letter enclosed a $50,000 check and a form releasing Martin and Orcutt. Farmers faxed Algorri a declaration from Martin that same day before the deadline, but was never able to obtain one from Orcutt.

The next day, Algorri rejected Farmers' tender on the ground that it had failed to unconditionally accept Pinto's offer to settle. On August 7, 2019, Pinto sued Orcutt and Martin for negligence. That case settled, with an agreement that Orcutt and Martin would assign all their rights against Farmers to Pinto, the settlement would be treated as the equivalent of a $10 million judgment; and the insurers (another insurer had been found for Orcutt) would pay Pinto their combined policy limits of $65,000.

Pinto then filed a bad-faith action against Farmers based on the assignment. The lawsuit alleged that Farmers acted in bad faith towards its insureds Martin and Orcutt by failing to accept Pinto's settlement demand.

At trial, much of the evidence concerned Farmers' claims adjustment prior to and after Pinto's settlement offer. Farmers repeatedly argued, over Pinto's repeated objections, that to establish bad faith, Pinto had to prove Farmers acted unreasonably in failing to accept his demand. The court declined to so instruct the jury, and the special verdict form contained no question relating to the reasonableness of Farmers' conduct. The jury returned a verdict in favor of Pinto for $9,935,000.

The Court of Appeal reversed. It held that a finding of bad faith against an insurer requires a finding that the insurer acted unreasonably: "To hold an insurer liable for bad faith in failing to settle a third party claim, the evidence must establish that the failure to settle was unreasonable." Under this standard, the insurer's failure to accept a reasonable settlement offer is not unreasonable per se. As the court put it, "Simply failing to settle does not meet this standard. A facially reasonable demand might go unaccepted due to no fault of the insurer, for example if some emergency prevents transmission of the insurer's acceptance."

Since the jury was not instructed on this point, and the verdict form – which was submitted to the jury over Farmers' objection that it was defective because it did not require the jury to find that Farmers had acted unreasonably in not accepting the offer – did not require the jury to make this finding, the verdict was fatally defective.

The special verdict and the jury instructions were patterned on CACI 2334, which the trial court gave in a slightly modified form. The court found, "Although CACI No. 2334 describes three elements necessary for bad faith liability, it lacks a crucial element: Bad faith. To be liable for bad faith, an insurer must not only cause the insured's damages, it must act or fail to act without proper cause, for example by placing its own interests above those of its insured."

The court found that no evidence suggested Farmers' conduct caused the settlement to fail. Farmers attempted to accept Pinto's settlement offer, and timely tendered both the policy limits and Martin's declaration. Settlement failed only because Pinto rejected the tender on the ground that it failed to include Orcutt's declaration. But no evidence established, and the jury did not find, that Farmers should have done more to obtain that declaration. On the contrary, the jury expressly found that Farmers "use[d] reasonable efforts to obtain Orcutt's cooperation," and her lack of cooperation prejudiced the insurer. Farmers therefore did all it could to achieve a settlement.

The court concluded that "the defective verdict was accomplished at Pinto's behest. Not only did he fail to propose an appropriate verdict, he also vigorously opposed Farmers' attempts to clarify the erroneous verdict. The proper remedy is to vacate the judgment and enter a new judgment for Farmers."

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