Tort Liability for an Insurer's Bad Faith Refusal to Settle: A Developing Trend Appropriate for Adoption in Missouri

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I. INTRODUCTION

When the Joneses come into your office, they are distraught. Their house had been destroyed by fire some time ago, and they have been having nothing but trouble with their insurance company. After filing a claim with XYZ Insurers, they had been called into the agent’s office for a two and one-half hour session of interrogation that included such questions as, “How did you start the fire?” XYZ refused to pay shelter and living expense benefits, even conditionally. Months after the fire, XYZ demanded that the Joneses submit to another examination, submit a sworn statement, and take a polygraph test. The Joneses became afraid of an accusation or even a prosecution for an arson they had not committed. They were in what the insurance industry calls a “favorable attitude” for settlement. They did settle, for thirty cents on the dollar. They want to know what you can do to help, and you agree to look into the matter.

You write to the XYZ Insurers and in due course receive a copy of the file, including the original statement taken at the first interview with the Joneses. There are no questions suggestive of arson in that statement—they have all been edited out. You investigate further. You discover that XYZ maintains a school for their agents to teach them how to obtain the most “economically feasible” settlement. The agent who dealt
with the Joneses is a graduate of that school. You discover that XYZ advertises to prospective clients that XYZ will take care of its clients; the brochure which influenced the Joneses to insure with XYZ contained the bold print claim: "Protect yourself from the ruin and disastrous consequences of fires and other casualties. We do the worrying for you."

In fact, the XYZ company had only aggravated the worrying the Joneses had done themselves. They had delayed the analysis of debris which could have provided evidence of arson by sending the test out of state instead of to the routinely used St. Louis laboratory, and had refused to settle any claim until it was returned. When received, the report was used as leverage to deny the original claim even though it was so inconclusive that such trifling items as grease on a shirt could result in an indication of possible arson. This is, in essence, the description of an actual case. The Joneses—and others like them—have been maltreated by their insurance company and seek a lawyer's help to redress their injury.

In Missouri, the Joneses are limited in their possible remedies for the wrongful treatment they have received at the hands of XYZ. In California, however, and in a growing number of jurisdictions following its trend, the Joneses can recover for their injuries, including mental dis-

1. Since an insurance policy is an ordinary contract, an action would lie for damages resulting from its breach. Damages available would be those contracted for, the face amount of the policy, or the amount of the loss if less than the policy limits. Moss v. National Life & Acc. Ins. Co., 385 F. Supp. 1291 (W.D. Mo. 1974). The Missouri vexatious refusal to pay statutes consist of two sections in the insurance chapter of the revised statutes. RSMo § 375.296 (1978) provides:

  In any action, suit or other proceeding instituted against any insurance company, association or other insurer upon any contract on insurance issued or delivered in this state to a resident of this state, or to a corporation incorporated in or authorized to do business in this state, if the insurer has failed or refused for a period of thirty days after due demand therefor prior to the institution of the action, suit or proceeding, to make payment under and in accordance with the terms and provisions of the contract of insurance, and it shall appear from the evidence that the refusal was vexatious and without reasonable cause, the court or jury may, in addition to the amount due under the provisions of the contract of insurance and interest thereon, allow the plaintiff damages for vexatious refusal to pay and attorney's fees as provided in section 375.420.

  Failure of an insurer to appear and defend any action, suit or other proceeding shall be deemed prima facie evidence that its failure to make payment was vexatious without reasonable cause.

V.A.M.S. § 375.420 (Supp. 1979) provides:

  In any action against any insurance company to recover the amount of any loss under a policy of automobile, fire, cyclone, lightning, life, health, accident, employers' liability, burglary, theft, embezzlement, fidelity, indemnity, marine or other insurance except automobile liability insurance, if it appears from the evidence that such company has refused to pay such loss without reasonable cause or excuse, the court or jury may, in addition to the amount thereof and interest, allow the plaintiff damages not to exceed twenty percent of the first fifteen hundred dollars of the loss, and ten percent of the amount of the loss in excess of fifteen hundred dollars and a reasonable attorney's fee; and the court shall enter judgment for the aggregate sum found in the verdict.
tress occasioned by the delay in settlement and possibly punitive damages, if they can prove the tort of "bad faith" by their insurer, XYZ. Missouri has not yet adopted this independent tort of bad faith, but neither have Missouri courts conclusively rejected it. This Comment will analyze the development of the bad faith tort in insurance law from its genesis to its present status. It will also analyze the concomitant development of Missouri law and conclude that the Missouri courts are in a position to now adopt this cause of action.

The new tort of "bad faith" applies to both third party excess judgment claims and first party claims in every form of insurance available. A third party excess judgment claim arises when an insured becomes liable to a third party for his actions, but his liability is covered, in part or in full, by a policy of insurance which he acquired for that purpose. The third party claimant makes an offer to settle within the policy limits. The insurer refuses to settle even though the liability of the insured is clear, on the chance that he may win in court and be absolved from the duty to pay anything. The parties go to court and the third party is awarded a judgment against the insured far in excess of the policy limits. The insurer, who defended the action, hands over a check for the policy limits. The third party then settles with the insured for what he can get of the judgment, including an assignment of the insured's rights against the insurer. Finally, the third party or the insured sues the insurer for bad faith refusal to settle within the policy limits and seeks the excess of the judgment over the policy amount tendered.

1. 2. For an introductory discussion of the California tort, see Parks & Heil, Insurers Beware: Bad Faith is in Full Bloom, 9 FORUM 63 (1973); Thornton & Blout, Bad Faith and Insurers: Compensatory and Punitive Damages, 12 FORUM 699 (1977).

3. In Young v. United States Fidelity & Guar. Co., No. 10,480 (Mo. App., S.D., Aug. 2, 1979), an employee of Ozark Engineering Company alleged he was injured while in the course of his employment. Defendant-insurer discontinued disability payments to insured, prompting a suit by insured claiming "defendant's refusal to pay further benefits . . . was intentional, malicious, and designed to 'deprive plaintiff of his rights' under the Workmen's Compensation Act and to force plaintiff to accept an inadequate settlement of his claim." Slip op. at 2. While defendant's motion to dismiss was upheld on grounds not relevant to this discussion, the court said, "reasonable research convinces us there is no sound reason why a first party bad faith action should not be entertained by our courts in a proper case." Id. at 3.


5. Although reported cases regarding all the various forms of insurance policies are not available, language from the cases comprising the development of the "bad faith" tort clearly indicates that the action applies to all contracts of insurance. See Gruenberg v. Aetna Ins. Co., 9 Cal. 3d 566, 573, 510 P.2d 1032, 1036; 108 Cal. Rptr. 480, 484-85 (1979).

6. Generally the third party sues for the excess judgment and is joined by
First party claims, on the other hand, are those made directly by an insured to his own insurer for a loss covered by his personal policy. The insurer and its insured are the sole parties. These include routine claims for fire loss, accident, disability, loss of life, and so forth.

Nearly every jurisdiction has accepted the "bad faith" theory in third party cases. Missouri expressly adopted this theory early in its development. The present move is to extend this theory to, and provide a tort remedy for, the first party "bad faith" cases. This movement is the focus of the discussion to follow. The development in the third party excess judgment cases will be discussed only as it brings about and precedes the first party movement. Although the acceptance of the first party "bad faith" tort cause of action will change the existing relationship between the insurance industry and the public, this change, like the innovations in products liability, is one necessary to protect a society which purchases insurance policies expecting peace of mind and freedom from the ruinous aftermath of disaster. The public more than ever relies on insurance and expects fiduciary-like treatment. This reliance must be supported by effective sanctions should that reliance and the mutual promises be breached in a "bad faith" or tortious manner.

II. DEVELOPMENT OF THE TORT OF BAD FAITH IN FIRST PARTY CLAIMS IN CALIFORNIA

A. Third Party Excess Judgment Cases as the Genesis

The concept of "bad faith" in the performance of insurance contracts by an insurer had its beginning in California in the third party excess judgment or failure to settle cases. The seminal bad faith case was Brown v. Guarantee Insurance Co. In that 1957 case, the insurer refused even to consider a settlement because the amount demanded so closely the insured who pleads for damages resulting from the bad faith acts of the insurer over and above the excess judgment, such as mental distress, punitive, and the like. In some instances, however, the insured alone sues for the excess judgment and the consequential damages resulting from the "bad faith" acts.

7. See authorities cited note 8 infra.


10. See note 121 and accompanying text infra.

11. 155 Cal. App. 2d 679, 319 P.2d 69 (1957) (automobile liability insurance; insured not notified of status of any settlement negotiations or advised as to the protection of his rights or interests).
approximated the policy limits that the carrier felt it had nothing to lose by rejecting the demand. The court considered this attitude to be evidence of callous disregard for the interest of the insured, and indicated that in such situations there should be no requirement that the insured pay the excess judgment before proceeding against the insurer. The court stated that whether an insurer is "guilty" of bad faith for refusal to negotiate a settlement is a question of fact, and developed a list of considerations relevant to that inquiry.\(^\text{12}\)

Decided in the same year was *Communale v. Trader's & General Insurance Co.*,\(^\text{13}\) in which the insurer refused to defend or settle a claim against its insured on the ground that the policy did not cover the loss, although the coverage was unquestionable. The company was obligated to defend any personal injury suit covered by the policy, but was given the right to make any settlement it deemed expedient. This retention of complete control over the settlement and litigation process by the insurer is a standard provision in most contracts of insurance. In third party cases this fact constitutes an important justification for placing the good faith duty on the insurer. The insured is in a sense contractually prevented from accepting or seeking a favorable settlement.

The Communales, the damaged third parties, obtained a judgment against the insured. They then sued the insurer pursuant to the contract and received a judgment for the excess over the policy amounts. The Supreme Court of California affirmed the jury verdict and held that the insurer wrongfully denied coverage to its insured, and failed to consider the insured's interest in having the suit compromised by a settlement within the policy limits. The court's holding was based on a principle which now forms the basis of the bad faith movement: "There is an implied covenant of good faith and fair dealing in every contract that neither party will do anything which will injure the right of the other to receive the benefits of the agreement."\(^\text{14}\) The court went on to say that the insurer, in deciding whether a claim should be compromised, must take into account the interest of the insured and give it *at least as much*

\(^\text{12}\) *Id.* at 689, 319 P.2d at 75. Considerations included:

[T]he strength of the injured claimant's case on the issues of liability and damages; attempts by the insurer to induce the insured to contribute to a settlement; failure of the insurer to properly investigate the circumstances so as to ascertain the evidence against the insured; the insurer's rejection of advice of its own attorney or agent; failure of the insurer to inform the insured of a compromise offer; the amount of financial risk to which each party is exposed in the event of a refusal to settle; the fault of the insured in inducing the insurer's rejection of the compromise offer by misleading it as to the facts; and any other factors tending to establish or negate bad faith on the part of the insurer.

\(^\text{13}\) 50 Cal. 2d 654, 328 P.2d 198 (1958) (automobile liability insurance; insurer claimed noncoverage but court held policy clearly applied).

\(^\text{14}\) *Id.* at 658, 328 P.2d at 200, citing Brown v. Superior Court, 34 Cal. 2d 559, 564, 212 P.2d 878, 881 (1949) (good faith in contracts principle equally applicable to contracts for insurance).
consideration as it does its own interest. The court recognized a special relationship between the insurer and its insured and imposed liability for breach of that relationship. The California court noted that wrongful refusal to settle generally has been treated as a tort, but also sounds in contract under an implied covenant. Where a case sounds both in contract and tort, the plaintiff will ordinarily be free to elect between the two. The form of action chosen affects the availability of compensatory and punitive damages beyond the policy amount, as will be seen in later cases.

The landmark case in the development of third party claims was Crisci v. Security Insurance Co., wherein the California Supreme Court affirmed a $25,000 compensatory damage award for mental suffering in addition to the excess judgment amount of $91,000. Mrs. Crisci, a seventy-year-old widow, owned an apartment building which was covered by a liability policy. Mrs. DiMare, a tenant in the building, fell through an outside wooden staircase and was left hanging fifteen feet above the ground. As a result she suffered physical injuries and developed a severe psychosis.

In her suit, the tenant alleged that Mrs. Crisci was negligent in maintaining the staircase and asked for $400,000 in compensation. Mrs. Crisci owned a $10,000 general liability policy; the plaintiff offered to settle for $9,000. The insurance company was willing to pay only $9,000 even though it had reason to know that a jury could find for Mrs. DiMare far in excess of its offer. The case went to the jury and a verdict of $101,000 was rendered.

The insurer paid only the policy limits, refusing to pay the excess. Mrs. DiMare attempted to collect $91,000 from Mrs. Crisci and reached a settlement in which Mrs. DiMare received cash, property, and an assignment of Mrs. Crisci's cause of action against the insurer. The settlement

15. 50 Cal. 2d at 659, 328 P.2d at 201. The court stated:

When there is a great risk of a recovery beyond the policy limits so that the most reasonable manner of disposing of the claim is a settlement which can be made within those limits, a consideration in good faith of the insured's interest requires the insurer to settle the claim.

Its unwarranted refusal to do so constitutes a breach of the implied covenant of good faith and fair dealing.


16. 50 Cal. 2d at 663, 328 P.2d at 203 (citing Eads v. Marks, 39 Cal. 2d 807, 811, 249 P.2d 257, 260 (1952), for this rule of election).


caused Mrs. Crisci to become indigent; the change in her financial condition caused a decline in her physical health, hysteria, and suicide attempts. Mrs. Crisci finally brought an action against the insurer.

Based upon the insurer's bad faith refusal to settle within the policy limits, the court ordered the insurance company to pay the $91,000 excess verdict. Additionally, the court awarded Mrs. Crisci $25,000 for mental suffering because, the court concluded, her insurance contract directly concerned her comfort, happiness, and personal esteem.19 As to the standard to be utilized in third party actions, the court measured bad faith by an objective rather than subjective standard.20

The importance of Crisci in the development of the "bad faith" tort is its inclusion of the mental distress damages in the recovery. The court repeated the general rule of tort damages that "the injured party may recover for all detriment caused whether it could have been anticipated or not."21 Mental suffering was defined as an aggravation of damages which naturally ensues from the act complained of, and which in this connection included nervousness, grief, anxiety, worry, shock, humiliation, and indignity, as well as physical pain. The court concluded that such awards for mental distress are not confined to cases where the mental suffering award is in addition to an award for personal injuries.22 The implications of this holding for expanding insurers' potential tort liability are significant.23

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19. The court recognized that "among the considerations in purchasing liability insurance, as insurers are well aware, is the peace of mind and security it will provide in the event of an accidental loss." Id. at 434, 426 P.2d at 179, 58 Cal. Rptr. at 19. This consideration was deemed a protected property interest in Fletcher v. Western Nat'l Life Ins. Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970), discussed in text accompanying notes 28-30 infra. The interference with this protected property interest was held by the Fletcher court to be an alternative ground for recovery. See Keenan & Gillespie, The Insurer and the Tort of the Intentional Infliction of Mental Distress: Fletcher v. Western Nat'l Life Ins. Co., 39 INS. COUNSEL J. 335, 339 (1972).


21. 66 Cal. 2d at 433, 426 P.2d at 18, 58 Cal. Rptr. at 178.

22. "[D]amages for mental distress have also been awarded in cases where the tortious conduct was an interference with property rights without any personal injuries apart from the mental distress." Id. at 433, 426 P.2d at 179, 58 Cal. Rptr. at 19.

23. The potential tort liability arising from this decision is magnified not merely by the holding that mental distress damages are recoverable where a protected property interest has been interfered with, but by the Crisci court's definition of mental suffering to include "nervousness, grief, anxiety, worry, shock, humiliation and indignity as well as physical pain." Id. at 433, 426 P.2d at 178, 58 Cal. Rptr. at 18. An insured may suffer many of these conditions as a mere result of the occurrence of the event for which the insurance was obtained. Because it would be virtually impossible for the trier of fact to segregate the damages ensuing naturally from the event and those caused by the insurer's bad
Further development in the third party excess judgment area estab-
lished that punitive damages are available against an insurer whose actions
are proven to be willful, malicious, and in serious disregard of an insured's
rights.24 Courts in California and other jurisdictions have refused, how-
ever, to hold an insurer strictly liable for failure to settle within the
policy limits.26 The importance these cases bear to first party cases is in
laying the basis of the tort of "bad faith" and in opening the way to
recovery of compensatory damages, including mental distress damages, and
punitive damages. The availability of punitive damages is notable be-
cause most states by legislation or judicial decree do not permit punitive
damages when the violated obligation arises from contract.28 An insurance
company cannot rely on such precedent where the action against it is
based on violation of an implied duty of good faith,27 i.e., one of tort.

B. Extension of the Tort into First Party Actions

Fletcher v. Western National Life Insurance Co.,28 in allowing a
first party recovery, drew heavily on the principles enunciated in Crisci,
but went further than Crisci by recognizing an independent tort recovery.
Both cases were grounded on a breach by the insurer of its implied duty
of good faith and fair dealing. However, while the recovery in Crisci was
in both contract and tort, the theory in Fletcher was entirely one of tort.
The Fletcher decision was weakened somewhat because the action was
based on the tort of intentional infliction of emotional distress,29 and dis-

faith acts, the likely result of this dilemma is that the fact finder will not segre-
gate the damages, thus leaving the insurer, if found liable for some portion,
liable for all such damages.

rev'd on other grounds, 386 N.Y.S.2d 87 (1976). See cases cited in J. McCARThY,
PUNITIVE DAMAGES IN BAD FAITH CASES § 3.40 (1975). See also Annot., 85 A.L.R.
3d 1211 (1978).

25. Gibbs v. State Farm Mut. Ins. Co., 544 F.2d 423 (9th Cir. 1976); Johansen
v. California State Auto. Assoc. Inter-Ins. Bureau, 15 Cal. 3d 9, 538 P.2d 744,
123 Cal. Rptr. 288 (1975); See Annot., 63 A.L.R.3d 627 (1975). For discussions
favoring strict liability for insurers, see Kelly, The Workable Sanction and Solution
in Excess Liability Cases: Strict Liability for Insurance Carriers, 1976 INS. L.J.
846; Schwartz, Statutory Strict Liability for an Insurer's Failure to Settle: A
Balanced Plan for an Unresolved Problem, 1975 DUKE L.J. 901.

26. 22 AM. JUR. 2d Damages § 64 (1965) (general rule).


28. 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970) (allowing punitive damages
of $180,000 and compensatory damages of $60,000 where insurer canceled dis-
cability payments to father of nine children on basis of manufactured medical
evidence, offered negligible compromise settlement, and attempted to trick
insured into signing a release when cashing a check).

29. Id. at 394, 89 Cal. Rptr. at 86. See RESTATEMENT (SECOND) OF TORTS §
46 (1) (1965) ("[O]ne who by extreme and outrageous conduct intentionally or reck-
lessly causes severe emotional distress to another is subject to liability for such
emotional distress, and if bodily harm to the other results from it, for such bodily
harm.").
discussion of the tort of bad faith as applied to these first party actions must be considered dicta.30

In Richardson v. Employers Liability Assurance Corp.,31 a California appellate court ruled that a carrier of uninsured motorist coverage was liable both in contract and in tort for amounts above its policy limits where it in bad faith withheld payment for months after it knew that the claim was valid, and even tried to negotiate a better settlement after an arbitrator's award. Liability was imposed for compensatory damages, attorney's fees, intentional infliction of emotional distress, and exemplary damages.

As an action against an uninsured motorist carrier who for purposes of the lawsuit occupies the position of the defendant, the Richardson case is distinguishable from an actual first party suit by an insured against his own insurer. It nonetheless provided support for the eventual extension of the tort of bad faith to first party suits against insurers for failure to settle.

C. Gruenberg v. Aetna Insurance Co.—The Landmark Case for Bad Faith in First Party Actions

The Gruenberg case,32 decided by the California Supreme Court one year after Richardson, was the first case to apply "bad faith" to an insurance carrier in a first party action.33 The plaintiff alleged that following

30. The court stated:

Although it might be possible to rest our decision solely upon the first holding, [intentional infliction of emotional distress] we [rely upon] the latter holding [bad faith—intentional interference with a protected property interest] because we believe that it squares with the economic, social and legal realities of the problem presented. The tortious conduct in this case has resulted and could be expected to result, in both economic loss (not alleged here) and emotional distress. The emotional distress resulted, and could be expected to result, from both the immediate conduct of defendants and the economic losses caused by their conduct. Indeed, in a case such as this, the invasion of economic interests might well outweigh the direct invasion of emotional tranquility. The tort of intentional infliction of emotional distress is designed to redress primarily invasions of the personal interest in emotional tranquility, not economic losses, unless, of course, the economic losses result from the intentionally caused emotional distress . . . . A rule placing the emphasis where it belongs and permitting recovery of all proximately caused detriment in a single cause of action is more likely to engender public respect . . . .


33. 9 Cal. 3d at 573, 510 P.2d at 1038, 108 Cal. Rptr. at 484. The Gruenberg court recognized the existence of the independent tort of "bad faith," relying on language from Communale progressively to Crisci, Fletcher, and Richardson.
destruction of his property by fire, adjusters retained by his insurance company informed local authorities that he had an excessive amount of insurance, thereby implying a motive for arson. The police investigator issued a felony complaint. Prior to the probable cause hearing on the felony charge, the insurer requested the insured to submit to an examination under oath as required by the standard policy provisions. The insured asked if the examination could be delayed until the criminal process was completed to protect himself against self-incrimination, but the company denied this request.

Shortly thereafter, all criminal charges were dropped as a result of a probable cause hearing, but the company continued to deny liability even after Mr. Gruenberg agreed to an examination. Plaintiff sued Aetna, charging that the request for examination under oath was made solely to enable the insurer to gain further evidence to support the false implications of arson. As a proximate result of the insurer's conduct and accompanying insinuations, Mr. Gruenberg claimed to have suffered mental distress in addition to the following economic losses: substantial loss of earnings, losses due to the forced closing of his business, legal expenses to defend suits brought by creditors whom he could not pay, and medical expenses. The trial court held that the plaintiff's complaint for "extra-contract" damages failed to state a cause of action. The California Supreme Court reversed, holding that the plaintiff had stated a cause of action, and that the duty of the insurer to act in good faith involved a duty not unreasonably to withhold payments due under a policy.34

Gruenberg indicated that agents and employees of an insurance company could not be held personally subject to the implied duty of good faith and fair dealing since they were not parties to the agreement for insurance.35 The court further held that an insurer's duty is unconditional and independent of the performance of plaintiff's contractual ob-

34. We think that . . . the implied-in-law duty of good faith and fair dealing imposes upon a disability insurer a duty not to threaten to withhold or actually withhold payments, maliciously and without probable cause, for the purpose of injuring its insured by depriving him of the benefits of the policy.

Id. at 575, 510 P.2d at 1038, 108 Cal. Rptr. at 486. This is the definitive statement of acts which in the first party cases comprise bad faith on the part of insurers. For an informative article indicating that insurance counsel themselves accept the implied-in-law duty of an insurer to act in good faith as settled law, see Langdon & Sytsma, The Duty of Good Faith and Fair Dealing and the Pre-Adjudicatory Role of the Insurance Company Advocate, 45 Ins. Counsel J. 309, 312-13 (1978).

litiations,\textsuperscript{36} and that a plaintiff could state a claim for mental distress damages without alleging "extreme" or "outrageous" conduct by the defendant.\textsuperscript{37}

\section*{D. Post-Gruenberg Development of the Bad Faith Tort}

One question left unanswered by Gruenberg was the standard which would be utilized by the trier of fact to determine insurers' liability. In the third party cases, recall that Crisci's test for imposing liability because of failure to settle was the "prudent insurer" standard, an objective one. In describing bad faith in the first party insurance context, courts have used terms such as "deliberately, willfully,"\textsuperscript{38} "maliciously and without probable cause, for the purpose of injuring,"\textsuperscript{39} "without probable cause,"\textsuperscript{40} and "unreasonably."\textsuperscript{41} In using such conclusory legal terms, no method for analysis or precise definition is revealed. One commentator has distilled two elements from a review of the bad faith non-payment of policy benefits cases. The insured must allege and prove: (1) the absence of a

\begin{itemize}
\item \textsuperscript{36} Defendant's duty . . . arises from a contractual relationship existing between the parties . . . While it might be argued that defendants would be excused from their contractual duties (e.g. obligation to indemnify) if plaintiff breached his obligations under the policies, we do not think that plaintiff's alleged breach excuses defendants from their duty, implied by law, of good faith and fair dealing. In other words, the insurer's duty is unconditional and independent of the performance of plaintiff's contractual obligations.
\item \textsuperscript{37} 9 Cal. 3d at 577, 510 P.2d at 1040, 108 Cal. Rptr. at 488. Accord, Liberty Mut. Ins. Co. v. Altfillisch Constr. Co., 70 Cal. App. 3d 789, 139 Cal. Rptr. 91 (1977) (expressly holding that the implied covenant applied to acts of the insured as well).
\item \textsuperscript{38} 9 Cal. 3d at 579, 510 P.2d at 1040, 108 Cal. Rptr. at 488 (plaintiff need not allege and prove extreme and outrageous conduct as RESTATEMENT (SECOND) of Torts § 46 (1965) requires). The court based its holding on the fact that "we are concerned with mental distress resulting from a substantial invasion of property interests of the insured and not with the independent tort of intentional infliction of emotional distress." \textit{Id.} at 580, 510 P.2d at 1041, 108 Cal. Rptr. at 489.
\item In reaching its conclusion that the complaint was sufficiently pleaded since plaintiff had alleged substantial damages for loss of property apart from damages for mental distress, the court relied on and quoted at length the language in \textit{Crisci} concerning the recoverability of mental distress damages. The \textit{Crisci} rationale for limiting recovery of damages for mental distress was stated as follows: To permit recovery of such damages would open the door to fictitious claims, to recovery for mere bad manners, and to litigation in the field of trivialities . . . Obviously, where . . . the claim is actionable and has resulted in substantial damages apart from those due to mental distress, the danger of fictitious claims is reduced . . .
\item 41. \textit{Id.} at 575, 510 P.2d at 1038, 108 Cal. Rptr. at 486.
\end{itemize}
reasonable basis for denying benefits; and (2) the denial of benefits while knowing or perhaps recklessly disregarding that such denial was without reasonable basis.\textsuperscript{42} It would seem that an objective standard would be utilized in determining the first element,\textsuperscript{43} while the second element would require a subjective inquiry to determine intent.

A second question left open in \textit{Gruenberg} is the nature of the defendant's conduct needed to support a punitive damage award. In two cases preceding \textit{Gruenberg}, the availability of punitive damages in first party cases had been established where the underlying cause of action was a conventional tort.\textsuperscript{44} Because no punitive damages were prayed for in \textit{Gruenberg}, it was not until a year after the \textit{Gruenberg} decision that \textit{Silberg v. California Life Insurance Co.}\textsuperscript{45} addressed the unanswered question. In \textit{Silberg}, the California Supreme Court upheld an order for a new trial because the evidence was found insufficient to support the $500,000 punitive damages award returned by the jury for failure to pay a medical insurance claim.\textsuperscript{46} It was ruled that allegations necessary to create a sub-

\begin{itemize}
\item \textsuperscript{42} Parks & Heil, supra note 32, at 11.
\item \textsuperscript{43} "Grisci used an objective standard—the 'prudent insurer.' Since 'prudence' does not seem relevant in the first-party context, the 'reasonable man' standard would appear to be appropriate." \textit{Id.} at 12 n.49. Some of the factors going to the determination of reasonableness might include: (a) whether it was reasonable to conclude that there had been a proper investigation of the claim before a decision was made; (b) whether the result of such an investigation has been subjected to a fair and reasonable review and evaluation; and (c) based on the foregoing, whether the decision to deny benefits was reasonable. \textit{Id.} at 10.
\item The conclusion that intent is required is supported by \textit{Gruenberg}; the court, reviewing the complaint on demurrer, summarized its allegations charging that the insurer had:
\begin{quote}
Willfully and maliciously entered into a scheme to deprive [the policy holder] of . . . benefits . . . by falsely implying that he had a motive to commit arson, and in that, knowing plaintiff would not appear for an examination during the pendency of criminal charges against him, they used his failure to appear as a pretense for denying liability under the policies.
\end{quote}
\item 44. Fletcher v. Western Nat'l Life Ins. Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970) (intentional infliction of emotional distress); Weatherbee v. United Ins. Co., 265 Cal. App. 2d 921, 71 Cal. Rptr. 764 (1968) (constructive fraud found where contract action on same facts would not have supported punitive damages).
\item 45. 11 Cal. 3d 452, 521 P.2d 1103, 113 Cal. Rptr. 711 (1974) (insurer's refusal to pay accident claim during pendency of worker's compensation claim and subsequent refusal to pay under exclusory clause held bad faith tort; $75,000 compensatory award affirmed but $500,000 punitive award reversed).
\item 46. The court reasoned:
\begin{quote}
It does not follow that because plaintiff is entitled to compensatory damages that he is also entitled to exemplary damages. In order to justify an award of exemplary damages, the defendant must be guilty of oppression, fraud or malice . . . . He must act with intent to vex, injure or annoy, or with a conscious disregard of the plaintiff's rights . . . .
\end{quote}
While we have concluded that defendant violated its duty of good faith
\end{itemize}
possible case under the bad faith tort theory are, standing alone, not enough to support a punitive damage award. There must be further allegations of oppressive acts accompanied by the necessary intent, express or implied.47

Most recently, the California Supreme Court addressed its newly created tort of bad faith in *Neal v. Farmers Insurance Exchange.*48 There the defendant failed to make prompt payment of the insured's claim under an uninsured motorist provision. In affirming the trial court's award of compensatory and punitive damages, the court attempted to explain the terms "good faith" and "bad faith," noting again a distinction between the showing necessary to sustain a "bad faith" finding and that necessary for a punitive award incidental to the "bad faith" cause of action:

The terms "good faith" and "bad faith," as used in this context . . . are not meant to connote the absence or presence of positive misconduct of a malicious or immoral nature—considerations which . . . are more properly concerned in the determination of liability for punitive damages. Here we deal only with the question of breach of the implied covenant and the resultant liability for compensatory damages . . . Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes (from consideration) a variety of types of conduct characterized (in other contexts) as involving "bad faith" because they violate community standards of decency, fairness or reasonableness.49

In *Neal*, the defendant insurance company utilized a training course for its claims adjusters specifically to groom them for the actions here condemned. This fact was emphasized as strongly indicative of bad faith; the defendant's challenged actions were part of a conscious course of conduct grounded in established company policy.50

and fair dealing, this alone does not necessarily establish that defendant acted with the requisite intent to injure plaintiff.

*Id.* at 462, 521 P.2d at 1110, 113 Cal. Rptr. at 718.

47. The *Silberg* court further noted:

Although the evidence was in conflict on the issue whether it was customary in the insurance industry to make payments under the policy in these circumstances and the order granting a new trial declared there was insufficient evidence of such a custom, the failure to establish common practice in this regard cannot absolve the insurer. The scope of the duty of an insurer to deal fairly with its insured is prescribed by law and cannot be delineated entirely by customs of the insurance industry.

*Id.* at 462, 521 P.2d at 1109, 113 Cal. Rptr. at 717.

48. 21 Cal. 3d 910, 582 P.2d 980, 148 Cal. Rptr. 389 (1978) (insurer's prolonged refusal to make payment under uninsured motorist provision despite unfavorable opinion by insurer's attorney held made in bad faith even though all payments were made before suit following arbitration decision; $748,000 punitive award affirmed on basis of insurer's net worth).

49. *Id.* at 921 n.5, 582 P.2d at 986 n.5, 148 Cal. Rptr. at 395 n.5 (citations omitted).

50. *Id.* at 923, 582 P.2d at 987, 148 Cal. Rptr. at 396.
Other jurisdictions soon followed the Gruenberg rationale in cases involving similar fact situations. The first such case was decided by an Illinois intermediate appellate court in 1975 in Ledingham v. Blue Cross Plan.51 Ledingham underwent surgery due to an abrupt physical disorder and submitted timely claims for medical and hospital bills under her health and accident policy. The defendant-insurer refused payment on the ground that Ledingham's condition fell under a policy exclusion for pre-existing illnesses; Ledingham's doctor stated he could not tell whether the illness had existed prior to issuance of the policy. At the trial the insurer produced no other evidence substantiating its claimed defense, but appeared to deny the insured's claim solely because of her doctor's uncertainty concerning the source of the illness. In affirming the award of compensatory damages, the court specifically recognized the new tort given birth in Gruenberg.52

The Illinois court was influenced by that state's previous recognition of the tort of intentional infliction of emotional distress as a basis for award of extra-contractual compensatory damages in insurance cases.53 Ledingham went on, however, to disapprove a previous Illinois holding which did not allow punitive damages in such cases.54 The court distinguished Illinois cases holding punitive damages inappropriate in contract cases, saying that those cases involved traditional contract situations between private parties of reasonably equal bargaining power. "In the court's view, these situations did not involve the relative vulnerability of one party as is quite often presented in insurable matters."55 The court suggested for Illinois a framework allowing both the cause of action and punitive damages.56 Two recent intermediate appeals cases in Illinois

52. Id. at 349, 330 N.E.2d at 548.
55. Lev, Punitive Damages in First Party Insurance Claims; Reaching the Age of Maturity, 83 Case & Com. 48, 54 (1978).
56: The framework as suggested by the court was as follows:
   1) Punitive damages may not be awarded generally in an action on a contract.
   2) However the breach of a contract itself may constitute an 'unusual case where an independent willful tort will be found.'
   3) In the life and health insurer-insured relationship there is a duty upon both parties to act in good faith and deal fairly with the other party to the contract.
   4) Breach of this duty implied by law is both a breach of the contract and a tort.
29 Ill. App. 3d at 350, 330 N.E.2d at 548. The court did not call the new tort specifically by its Gruenberg title, i.e., "bad faith." Instead, it chose to call it, as did the Fletcher court, a "tortious interference with a protected property interest." 10 Cal. App. 3d at 410, 89 Cal. Rptr. at 93. It did so, specifically avoid-
have refused to follow *Ledingham*, 57 and the Illinois Supreme Court has yet to resolve the split.

A federal court applying Florida law followed suit in *Escambia Treating Co. v. Aetna Casualty & Surety Co.*, 58 reasoning that an insured purchases insurance and not an unjustified court battle when he enters into an insurance contract. The development of the first party action in California was traced and the court concluded that since Florida recognized the good faith duty in the third party cases, it should be extended to the handling of claims of a company's own insured. 59 It also indicated that in the proper case punitive damages would be appropriate, although noting that a different quantum and type of proof than mere breach of contract would be required for an award of punitives. 60

The Oklahoma Supreme Court recognized the tort of bad faith in *Christian v. American Home Assurance Corp.* 61 The plaintiff received injuries in the scope of his employment, leaving him totally and permanently disabled. He filed proper proof of disability and made demands for the full amount of his $50,000 disability policy. The insurer neither paid the claim nor stated a reason for withholding payment. During the subsequent trial of Christian's breach of contract action, it became apparent that the insurer "did not have, or had never had, [any] defense to [the insured's] claim." 62

The insured then filed a separate action asserting tort liability for the insurer's bad faith refusal to process his claim, alleging that the insurer's acts were intentional, malicious, and in total disregard of its duty to pay his claim. The Oklahoma Supreme Court concluded that plaintiff had stated a cause of action and specifically recognized "a distinct tort based upon an implied duty of the insurer to act in good faith and deal fairly with its insured." 63

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59. *Id.* at 1370-71.
62. 577 P.2d at 900. Defendant's refusal to pay the claim was at all times unknown to the plaintiff.
The *Christian* case can be distinguished from the California cases in two respects. First, in the California cases, either the bad faith conduct of the insurance companies was outrageous, or the resulting consequences to the insured were extreme. In *Christian*, however, the insurer's conduct was substantially more subtle—a mere refusal to settle promptly. Second, the court found as a source of the duty to deal in good faith with its insured not only the contract but also the Oklahoma Insurance Code. The court stated: "This statutory duty imposed upon insurance companies to pay claims immediately, recognizes that a substantial part of the right purchased by the insured is the right to receive the policy benefits promptly." Thus the defendant was found to be in direct violation of a duty imposed both judicially and legislatively.

Another portion of the Oklahoma opinion addressed the defendant's claim that third party excess judgment cases limited the availability of the new tort to situations where the insurer represents the insured in the settlement of third party claims. This is because, the insurer argued, a special fiduciary obligation is created where the insurer assumes the complete defense of the suit against the insured to the point that he is expressly prohibited from participating therein. This relationship is thought to create a greater obligation on the part of the insurer to act in the best interests of the insured, an obligation not imposed in most first party cases. *Christian* disagreed, however, and followed the philosophy of the California court in *Fletcher*, holding that the duty attaches to all relationships established by the insurance industry because of its quasi-public nature, the insured's lack of bargaining power, and the justifiable reliance placed on the insurer by the insured. In both the third party and first party cases, the court reasoned, the insurance company is in a

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64. The court noted:

Our Insurance Code requires insurance companies to make immediate payment of claims. Title 36, O.S. 1971 § 4405 A.8, requires the following provision to be included as a standard clause in all individual accident and health policies:

**TIME OF PAYMENT OF CLAIMS:**

Indemnities payable under this policy for any loss . . . will be paid immediately upon receipt of due written proof of such loss.

While this provision would not deter an insurance company from refusing payment on a claim that it had reasonable cause to believe was factually or legally insufficient, it does express the intent of our legislature to impose upon insurance companies an obligation to pay a valid claim on a policy promptly.

The obligation of an insurance company . . . on a disability policy is not for the payment of money only, it is the obligation to pay the policy amount immediately upon receipt of proper proof of loss . . . and to deal fairly with its insured . . .

577 P.2d at 903-04. This language is important since Missouri's vexatious refusal to pay statute, supra note 1, arguably indicates the same legislative intent which could form a basis for adopting the "bad faith" tort.

65. 577 P.2d at 903.

66. *Id.* at 902 (quoting Fletcher v. Western Nat'l Life Ins. Co., 10 Cal. App. 3d 376, 403, 89 Cal. Rptr. 78, 95 (1970)).
position to cause the insured great emotional difficulties, either by refusing to settle a potentially ruinous claim or by refusing to recoup the insured for an already distressing injury. Both situations justify the imposition of liability for the tort of bad faith.67

Without citing the California cases, New York adopted the Gruenberg rationale in Frizzy Hairstylists, Inc. v. Eagle Star Insurance Co.68 The insured suffered a fire loss in her beauty parlor and submitted a $4,870 claim to the defendant under her fire insurance policy. Defendant, approximately six months after the fire, offered her $1,250. The insured's business had limited capital and could not continue without prompt payment of the claim; she eventually was evicted by her landlord due to the resultant failure of her business. The defendant's only defense for non-payment of the claim was an accusation of arson, although no competent supporting evidence could be produced. The basis for the accusation was third-hand hearsay which hinted at arson, but did not implicate the plaintiff-insured.69

The New York court found that the defendant acted with malice in "low balling" plaintiff's claim, forcing plaintiff out of business, requiring plaintiff to sue and wait years for collection, and necessitating the sharing of its award with an attorney. The court awarded the plaintiff punitive damages, relying primarily on the public policy in New York evidenced by statutory provisions70 and related regulations71 which required insurance companies to process claims fairly and promptly and prohibited unfair claim settlement practices. Following these legislative pronouncements and a previous case,72 the New York court imposed a duty of good faith73 on insurers, suppliers of what they saw as a virtual necessity of modern life.74

67. See Note, supra note 61. The writer concluded that the existence of a "special" relationship between an insured and the insurer, giving rise to a duty or responsibility on the part of the insurer to deal in good faith with the insured, is a requisite element of the new tort of "bad faith." Id. at 613-16.


69. Defendant's sole witness, its claims adjuster, testified that someone at the New York Board of Fire Underwriters had told him that the fire marshall's report supported arson and that he had confirmed the fact by his own observations of the premises.


71. 11 N.Y.C.R.R. § 216.6 (a) (1973).


73. The obligation of good faith was defined as "the duty to consider, in good faith, the insured's interest as well as its own when making decisions as to settlement." Frizzy Hairstylist, Inc. v. Eagle Star Ins. Co., 89 Misc. 2d 822, 824, 392 N.Y.S.2d 554, 556 (Civ. Ct. 1977).

74. This public policy was necessitated, the court stated, by the recognition of the tremendous power wielded by the insurer:

Very few New Yorkers are immune from purchase of insurance. From the "cradle to the grave" we attempt to protect ourselves and our loved ones. In some instances it is mandated by statute. You can't drive an automobile in New York (and in most other states) unless you pur-
The New York court further observed that although under state law the insurance department had standing to enforce regulations, a private person injured by violation of those regulations would be left without an effective remedy. Implication of a tort cause of action was essential to the public policy of forcing insurance companies to deal with consumers in good faith.

Other jurisdictions also have adopted the bad faith tort originated in Gruenberg, and still more have reached the transitory Fletcher stage where liability is based on a previously accepted tort theory such as intentional infliction of emotional distress, tortious interference with a protected property interest, fraud, or deceit. The most beneficial effect of this increasingly accepted cause of action would be the institution of an in terrorem influence on the insurance companies, causing them to police themselves in a desire to avoid liability.

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chase an auto insurance policy. To the small businessman it is essential—not having fire, liability and other business coverages would spell the “death knell” for the victim of a casualty. A huge industry—the insurance industry—has been spawned as a result of tremendous need and demand for multitudinous forms of insurance coverage.

*Id.* at 823, 392 N.Y.S.2d at 555.

75. The Missouri statutes contain provisions regulating unfair practices and frauds in the insurance industry. See V.A.M.S. §§ 575.930-948 (Supp. 1979); RSMo § 375.445 (1978) (company operating fraudulently or in bad faith). As in New York, the remedies under these statutes are penal in nature and are enforced by the administrative agency which regulates the insurance industry in the state. In Missouri this is the Department of Consumer Affairs, Regulation and Licensing of the Division of Insurance. The agency, pursuant to the above statutory provisions, may issue cease-and-desist orders, assess a fine not to exceed $1,000 payable to the school fund (RSMo § 374.280 (1978)), or suspend an insurer’s certificate. Before the agency may find a violation subject to the remedies above, the conduct alleged must have been frequent enough to constitute a business practice as determined by the agency (departmental discretion as to whether “business practice” exists—no inter-departmental guidelines).

Because the monetary remedy does not run to the insured, the conduct must constitute a business practice. The cease-and-desist order has proven ineffective and the remedies provided are inadequate to redress the wrongs done the individual claimant; they have little in terrorem effect on the industry as a whole.

For an indication of legislative intent that the standards of good faith and fair dealing be followed in Missouri, see 4 C.S.R. § 190.060 (Mo. 1978) (constituting the regulations issued under RSMo § 375.445 (1978)), setting forth the proscribed unfair claims settlement practices. The form chosen for setting out these unfair claims practices in many instances indicates what the legislature interprets as fair, and prescribes what claims practices are preferred.


78. Faced with the prospect of paying punitive damages such as were awarded in a jury verdict of $5,000,000 (on appeal reduced to $2,500,000) in Egan v. Mutual of Omaha Ins. Co., 63 Cal. App. 3d 659, 133 Cal. Rptr. 899 (1976), the insurance
IV. THE NEW TORT IN MISSOURI

A. Missouri's Vexatious Refusal to Pay Statutes

Under Missouri's vexatious refusal to pay statutes, if an insurer fails or refuses for thirty days after demand "to make payment under . . . terms and provisions of the contract of insurance, and . . . [such] refusal was vexatious," a court or jury may award damages in addition to the amount due under the provisions of the contract. These damages may not exceed twenty percent of the first $1,500 of loss, ten percent of the loss in excess thereof, interest thereon, and a reasonable attorney's fee. Section 375.420 defines "vexatious" as "without reasonable cause or excuse." Because this statute is penal in nature and must be strictly construed, it has been held that refusal to pay is not vexatious if the defendant has any reasonable ground to deny payment. The burden is on the plaintiff-insured to prove that the refusal to pay was willful and without reasonable cause. In most cases, the insurer is able to refute a lack of reasonable cause, often relying on broadly worded escape clauses in the policy itself.

In Groves v. State Farm Mutual Auto Insurance Co., the Missouri Supreme Court set out a strict test of both objective and subjective bad faith on the part of the insurer to establish a vexatious refusal to pay.

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industry may concern itself with measures to avoid such awards. See Bogert, Liability of Insurers in California Beyond Policy Limits—Updated, 1978 Ins. L.J. 185 (example of proposed industry reactions).

79. See statutes cited note 1 supra.
80. RSMo § 375.296 (1978).
81. The text of § 375.420 is set out at note 1 supra.
86. 540 S.W.2d 39 (Mo. En Banc 1976).
87. The court stated:
[The penalty for vexatious refusal of an insurance company to pay the claim of its insured should not be imposed unless the facts and circumstances surrounding the company's refusal to pay show that the refusal was willful and without reasonable cause or excuse, as the facts would have appeared to a reasonable person before trial. An insurance company may question and contest an issue of fact relating to its liability if it has reasonable cause to believe, and does believe, that there is no liability under its policy and that it has a meritorious defense. The mere fact that the trial judgment is adverse to a defendant's contention is not sufficient reason for imposing the penalty.

Id. at 42.
In *Hounihan v. Farm Bureau Mutual Insurance Co.*, the plaintiff met this burden. Following an investigation of a fatal fire, the insurance company denied liability because of "foul play" and "suspicious circumstances" and the possible motive of strained marital relations after the insured's wife and child had moved out of the house which burned. No evidence was adduced at trial to support this theory; in fact, the defendant's own eyewitness refuted it. In affirming the vexatious refusal to pay award, the court of appeals observed that an unsubstantiated suspicion of arson does not justify an insurer's refusal to pay, even if supported by a later investigation. In *Hounihan*, it was noted, the defendant was still seeking facts to justify its denial of liability one year after the fire.

It has also been deemed a vexatious refusal to pay where the insurer has made a settlement offer even though the policy claimed under was a "valued fire insurance policy" which provided a set formula of stated value less depreciation for determination of the compensable loss. There was no possible dispute as to the amount due under the policy, and an offer to settle for a different amount was violative of the statute.

It is apparent from the cases under the Missouri vexatious refusal to pay statutes that the conduct of the insurer in question is the same as that creating liability under the tort of "bad faith." Differences in remedial value arise because the focus in a vexatious refusal to pay case is on the insurer's activity, not on the injury to the insured. This is due to the penal nature of the action and the fact that damages are fixed by statute. Recovery thereunder is inadequate because the insured will not be compensated for his economic losses or mental distress if they exceed the statutory limits. In addition there can be no recovery of punitive or exemplary damages which would result in an effective deterrent from bad faith conduct, nor is there an incentive for the insurer and the industry as a whole to deal in good faith with the people they insure.

Although the absence of cases recounting the effects of "bad faith" activities on insureds can lead to an illusion that the problem is nonexistent in Missouri, it should be recalled that these cases have been brought exclusively under the statutes and not under an independent tort theory. In fact these consequences do occur, but Missouri plaintiffs remain without a remedy.

**B. The Missouri Development of the Tort of Bad Faith Refusal to Settle Within the Policy Limits—Excess Judgment Cases**

The Missouri courts early recognized a duty of good faith owed by insurance companies to their insureds in third party settlement cases.

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88. 523 S.W.2d 173 (Mo. App., D. Spr. 1975).
89. *Id.* at 175.
92. See cases cited note 82 supra.
Two appellate cases, *St. Joseph Transfer & Storage Co. v. Employers' Indemnity Corp.* and *McCombs v. Fidelity & Casualty Co.*, laid the foundation for the tort cause of action in this area. The *McCombs* opinion adopted language from a New York case:

> [I]t would be a reproach to the law if there were no remedy for so obvious a wrong as was inflicted upon this plaintiff. His rights, as we have said, go deeper than the mere surface of the contract written for him by the defendant. Its stipulations imposed obligations based upon those principles of fair dealing which enter into every contract. Even the defendant has invoked this implied obligation of good faith and fair dealing not expressed in the terms of its written contract. . . .

The duty of good faith was recognized as arising not from the direct language of the insurance contract, but from the "relation of the parties, one of whom has reserved the exclusive control over the decision to settle or to litigate." The Missouri Supreme Court recognized the third party tort of bad faith in 1950 in *Zumwalt v. Utilities Insurance Co.* The court found

93. 28 S.W.2d 215, 220 (K.C. Mo. App. 1930). The court stated:

"Good faith requires that the insurance company do nothing to the prejudice of the assured which is not beneficial to itself . . . ." If the evidence showed the case was one where, under the conceded facts and upon settled principles of law, it would have been the duty of the court to direct a verdict for plaintiff for an amount in excess of the insurance, then we would be inclined to hold that the insurance company acted in bad faith in refusing to settle for an amount within the limits of the policy . . . .

The case was brought on a theory of negligent failure to settle, and the court held that the insurer was not negligent in considering its own interest as well as that of the insured's. Significantly, the court refused to hold that in fulfilling its duty to act with due care, an insurer must consider the interest of the insured to the exclusion of its own. However, a foundation was laid for a good faith requirement not to prejudice an insured when in doing so the insurer would receive no benefit. This recognition that the insurer has some duty to consider the interest of the insured as well as its own was called "good faith."

94. 89 S.W.2d 114 (St. L. Mo. App. 1936) (refusal to settle for policy limits because of company procedure even where insurer's own attorney advised that judgment would certainly be adverse and in excess of policy limits; held, bad faith refusal to settle).

95. *Id.* at 121, quoting *Brassil v. Maryland Cas. Co.*, 210 N.Y. 235, 237, 238 N.E. 622, 624 (1914). After reviewing several cases from other jurisdictions concerning the bad faith issue, the *McCombs* opinion went on to say, "The courts are not in agreement in holding the insurer liable for negligence in refusing to settle, but there is no disagreement with respect to the insurer's liability where bad faith appears. In such a case all the courts, without exception . . . hold the insurer liable. . . ." 89 S.W.2d at 121.

96. 89 S.W.2d at 121. This special relationship between the insurer and the insured has been said to be the genesis of the duty of the insurer to deal in good faith and a requisite element of the new tort of "bad faith." Note, *supra* note 61, at 618.

97. 360 Mo. 362, 228 S.W.2d 750 (1950). Burneson was injured by an overhead garage door on the defendant's premises. Defendant's insurer had issued a liability policy covering the premises which gave it sole control over litigation and settlement. Burneson filed an action seeking $40,000 for his injuries. De-
that the insurance company's bad faith refusal to settle within the policy limits was predicated on "intentional disregard of the financial interest of the insured in the hope of escaping the responsibility imposed upon it by its policy."98 Zumwalt, like McCombs,99 placed emphasis on the insurer's exclusive power to settle or litigate the case. This factor is always

fendant's policy was limited to $10,000, but his insurer refused to settle for $8,500 because it had reinsured $5,000 of the policy amount, and the reinsurer refused to entertain such a possibility. During the trial, Burneson again offered to settle, this time for $6,500, but defendant's insurer refused. The trial resulted in a judgment for Burneson for $15,000; the insurer paid $10,000 and the defendant-insured paid $5,000 plus interest. Insured, now plaintiff, filed suit against his insurer on the grounds of its bad faith and negligence in failing to settle the previous lawsuit within the policy limits. Plaintiff recovered $7,012.77 actual damages, the excess plaintiff had paid over the policy limits.


98. 360 Mo. at 371, 228 S.W.2d at 754. Plaintiff in the Zumwalt case also sought to recover attorney's fees, penalties for vexatious delay, and punitive. The trial court refused to submit this question to the jury and plaintiffs appealed from that action. Regarding the applicability of the vexatious refusal to pay statute, the supreme court stated:

We think this section applied only to actions ex contractu to recover for refusal to pay under the terms of a policy of insurance. If defendants had not paid the limit of their policy on the judgment obtained by [plaintiff], then this section would be applicable. But that is not the case. This action is a tort action. It is not an action to recover "any loss under a policy" of insurance. It is true it grew out of a contract, a policy of insurance.

Id. at 373, 228 S.W.2d at 756.

On the issue of punitive damages, the court said that before such damages can be awarded there must be evidence that the defendant "maliciously, willfully, intentionally, or recklessly injured the plaintiffs," but that this showing had not been made in this case. The court concluded that, at most, defendant did not act in good faith in handling the Burneson case.

[D]efendant looked after its own interest only, while under the law it owed a duty to have considered the Zumwalt Company's interest. If, in the effort to do this, its own interest conflicted with those of respondent [insured], it was bound under its contract of indemnity, and in 'good faith, to sacrifice its interests in favor of those of respondent...'. This the defendant failed to do.

Id. at 374, 228 S.W.2d at 756 (citation omitted) (emphasis in original). This represents a clear expansion of the insurer's duty of "good faith" from the early cases formulating such a duty. Compare this statement with the quotation from St. Joseph Transfer & Storage Co., set out at note 93 supra.

99. The Zumwalt court noted that the question of a "bad faith" tort theory presented a case of first impression for the Missouri Supreme Court, but that it had been addressed by the Court of Appeals, St. Louis District, in McCombs. The Zumwalt opinion noted McCombs' finding of a consensus among the jurisdictions, imposing liability against the insurer for bad faith conduct. 360 Mo. at 370, 228 S.W.2d at 753.
present in cases of first party claims since the insurer controls the funds on which the insured relies.\textsuperscript{100}

Second, the court implied that there is no exclusive remedy for a wrongful refusal of an insurance company to settle a claim. In \textit{Zumwalt} it was indicated that in some cases both contractual actions and actions under the vexatious refusal to pay statute might lie.\textsuperscript{101} Since in third party cases like \textit{Zumwalt} the policy limits will almost always be exhausted and the contract will have been discharged, the simultaneous use of both contract and statutory theories would more likely come up in a first party case. In such a case, a tort cause of action should also be allowed, with the plaintiff able to elect among the alternatives.\textsuperscript{102}

In \textit{Zumwalt}, although the evidence was found insufficient to sustain a punitive damages claim even with the finding of bad faith on the part of the defendant, the court indicated that punitive damages would be available in third party excess judgment cases upon a showing of malicious,

\begin{itemize}
\item \textsuperscript{100} \textit{Id}. In the third party cases, the insured’s hands are tied because the power to defend or settle has been contractually taken away from him. He can only sit and wait to see what his insurer will do. In first party cases, the insured is also helpless because his ability to economically or psychologically survive a disaster is in the hands of the insurer who controls the funds which provide the needed help to “pick up and go on.” Being in this dependent position strengthens the insurer’s ability to procure a favorable settlement from the victim or deny the claim altogether. In both types of cases, the insured’s economic well-being is at the mercy of the insurer.

\item \textsuperscript{101} \textit{See} note 98 \textit{supra}.

\item \textsuperscript{102} In a third party situation, an insured would have the option of an ordinary action for breach of contract or an action under the vexatious refusal to pay statute only if the insurer failed to pay at least the policy limits and the judgment against the insured exceeded that amount. \textit{See Zumwalt v. Utilities Ins. Co., 360 Mo. 362, 228 S.W.2d 750 (1950). See also Craig v. Iowa Kemper Mut. Ins. Co., 565 S.W.2d 716, 720 (Mo. App., D.K.C. 1978), where the court stated:}

These statutes were enacted, not as additional recovery, but that the amount due under the insurance policy shall be paid without arbitrary refusal or recalcitrant delay by the insurer. By the terms of Sec. \textit{375.420} only those actions \textit{ex contractu} and not \textit{ex delicto}—even where the tort arises from contract—may recover penalties. (Citations omitted.)

This remedy was meant to be a recovery on the contract, a penalty for unnecessary delay in performing that contract. The tort of “bad faith” on the other hand is a distinct recovery intended to compensate the insured for the tortious behavior of the insurer. The penalty should be available in all cases where the insurer vexatiously and unreasonably delays payment of the proceeds. This would include cases where the insured is actually harmed very little or none at all, but punishment of the insurer is appropriate. In cases where the blatant acts of the insurer cause serious economic, psychological, or social injury to the insured, however, the tort of “bad faith” with its damages should be available. If courts or the legislature are concerned about a “double recovery,” the availability of the “bad faith tort” theory could be conditioned on a waiver of the statutory action.

Regarding the relationship of the tort and statutory actions, the \textit{Craig} court held, “we need not consider whether the remedy of § \textit{375.420} precludes the tort cause of action . . . because, for reasons given there was no relationship of insurer and insured—essential to the tort recovery as pleaded—at the time of the bad faith conduct alleged.” 565 S.W.2d at 722.
\end{itemize}
willful, intentional, or reckless infliction of injury upon the insured.\footnote{103} Under a contract cause of action in Missouri, as in the majority of jurisdictions,\footnote{104} such damages are otherwise unavailable; the defendant's conduct must be shown to constitute an independent tort.\footnote{105}

C. The Extension of "Bad Faith" into First Party Cases

In Dyer v. General American Life Insurance Co.,\footnote{106} the plaintiff brought suit under an individual accident policy claiming tortious damages for alleged tortious breach of duty of good faith in failure to pay. The court recognized the viability of such a claim as undecided in Missouri and discussed the bad faith tort in the third party context, but resolved the case without deciding the first party bad faith tort question.\footnote{107}

The Dyer court in dicta opined that plaintiff's allegations of defendant's acts would not have constituted bad faith should such an action have been recognized. This finding was based on an earlier case holding that an insurer may, without penalty, insist on judicial determinations of open questions of fact or law determinative of the insurer's liability if such insistence is made in good faith.\footnote{108} Dyer also indicated that a punitive damage award would require not merely bad faith acts but a showing that the defendant's intent was malicious, willful, intentional, or reckless. For this proposition the court cited Zumwalt.\footnote{109}

Most recently, in Craig v. Iowa Kemper Mutual Insurance Co.,\footnote{110}

\footnote{103} See note 98 supra.
\footnote{104} See 25 C.J.S. Damages § 120 (1966).
\footnote{105} See Williams v. Kansas City Pub. Serv. Co., 294 S.W.2d 36 (Mo. 1956).
\footnote{106} 541 S.W.2d 702 (Mo. App., D. St. L. 1976) (after payment of disability benefits for 24 months and opinion by insurer's doctor that insured was totally and permanently disabled, insurer ceased payments upon learning that insured had worked for 8 months subsequent to injury).
\footnote{107} The court stated: [W]hether the plaintiff before us is totally and continuously disabled... is a matter upon which reasonable minds might differ. Under such circumstances, we cannot say that the insurer's decision to deny liability amounts to bad faith. This is so in spite of any medical evidence indicating the plaintiff's disability is total and permanent. If there is an "open question of fact or law determinative of the insurer's liability, the insurer, acting in good faith, may insist on a judicial determination of such questions without being penalized therefore."
\footnote{109} 541 S.W.2d at 705 (citations omitted).
\footnote{109} 541 S.W.2d at 706. The court also cited Zumwalt in discussing the bad faith tort in third party actions for failure to settle. Id. at 704.
\footnote{110} 565 S.W.2d 716 (Mo. App., D.K.C. 1978). This suit arose as a result of a collision in March 1970, which took the life of the infant son of the plaintiffs, the Craigs. The infant had been a passenger in the Ward automobile driven by Mrs. Craig's brother who was uninsured. Welborn, the other driver, was insured by Allstate. At the time of the collision, the plaintiffs were insured under a liability policy issued by defendant Iowa Kemper, which provided uninsured motorist coverage of $10,000 for a single injury or death. The plaintiffs notified the defendant of their claim under that provision. Defendants offered plaintiffs.
plaintiff-insured sued for satisfaction of an uninsured motorist provision. He included a count for the vexatious refusal to pay penalty and a count for actual and punitive damages for tortious breach of fiduciary duty to deal with policy holders in good faith. The Craig court interpreted the insurer-insured relationship in the uninsured motorist context so that no liability was found under the vexatious statute, and no fiduciary relationship was found to have existed when the bad faith acts occurred. The nominal insured was characterized as a third party claimant and the uninsured motorist was viewed as the actual insured under the court's interpretation of the relationships in issue. The court concluded that there existed an adversary, not fiduciary, relationship between the insurer and insured. 111 Because the duty to deal in good faith arises not merely from consent and contract but from the nature of the relationship, where there is no fiduciary relationship there is no duty, and where there is no duty there is no tort. 112 The court did discuss the bad faith tort, however, stating that:

[G]eneral jurisprudence recognizes that a policy of insurance imports the utmost good faith by the insurer to perform according to its terms. This principle extends to imply a covenant of good faith and fair dealing from every contract of insurance. The

$7,500 to settle their claim against Ward. In December, 1972, a jury returned a verdict of $23,500 for plaintiffs against both Ward and Welborn.

Within 30 days of judgment, defendants offered the plaintiffs $9,500 in full settlement of their claim under the uninsured motorist coverage. The plaintiffs originally demanded the full $10,000 coverage, but after counsel discovered that the Iowa Kemper policy covered more than originally anticipated, the plaintiffs withdrew the offer to settle.

Plaintiffs brought a petition in four separate counts against defendant. The first two counts were for policy amounts plus interest. Count III was for a vexatious refusal to pay penalty and count IV sought recovery for actual and punitive damages for tortious breach of duty by the insurer to deal with the plaintiffs as policy holders in fairness and good faith.

The trial court found for plaintiffs on the first two counts, for the defendant on count III, and for the defendant on count IV (the bad faith allegation) by summary judgment. The appeal from that summary judgment constitutes the main subject of interest here.

111. The court explained:

[T]o prove a claim under the Part IV [uninsured motorist] coverage the nominal insured must show the legal liability of the uninsured motorist. The insurer, for its part, in effect insures the uninsured motorist to the extent of the policy limits and so seeks to exonerate the uninsured motorist of liability to avoid payment to the policy insured. Put simply, the nominal insured and the insurer under this coverage are placed in an adversary relationship. Once the liability of the uninsured motorist has been adjudicated, the policy insured and the insurer are restored, not merely to their actual relationship, but to that of creditor and debtor as well. The claim then becomes a loss under the policy and vexatious refusal of the insurer to pay the loss becomes actionable under § 375.420.

Id. at 721 (citations omitted). Although this discussion was to show why the vexatious statute did not apply, it would be equally applicable to the first party tort.

112. Id. at 723-24.
law thereby assumes the agreement of an insurer not to injure the right of an insured to receive the benefits of the contract. The courts apply this principle of an implied [obligation to act in] good faith [by whatever designation] to give an insured a remedy both on the policy—ex contractu—and in tort.

As applied to a first party claim on the policy, the covenant facilitates an insured to recover the benefits payable directly to him by the contract.113

In a footnote the court conceded that Missouri law does not recognize the implied covenant in first party claims, but gives redress by "canons of construction."114 As to first party claims by the insured on a contract, the court said that the vexatious refusal statute created a substantive cause of action for a penalty against the insurer for unreasonable delay without good faith. "Thus, our law not only requires an insurer to meet the reasonable expectations of the insured on the contract, but by the statute shifts the expense of delay in payment of the claim onto the insurer."115 In discussing the statutory and contractual claims the court used language favorable to the recognition of the bad faith tort in first party cases, but then in unsupported dicta116 went on to say that "the tenor of our law suggests otherwise."117 This conclusory statement may have been made without consideration of the great extent to which the development of Missouri law parallels that of California or of the language in recent Missouri cases similar to that which appeared in California prior to Gruenberg's adoption of the bad faith tort.118

V. CONCLUSION

The insurance industry has grown into such a monolithic institution so intricately woven into our everyday lives that it is quasi-public in nature.119 Contracts of insurance are, for the typical consumer, adhesion

113. Id. at 722 (emphasis in original).
114. Id. at 722 n. 5.
115. Id.
116. Because the court determined that bad faith had not caused any injury to the plaintiffs, discussion of the existence of a bad faith tort cause of action was unnecessary to the holding. Id. at 724.
117. Id. The court did not support this statement with citation of Missouri cases.
119. In 1977, in the United States, there were in force 390 million policies of life insurance valued at 2,582.8 billion dollars. Total sales in 1977 were 392.9 billion dollars. In Missouri by the end of 1977 there were 8,631,000 policies of life insurance in force at a value of 56,285 million dollars. In the health insurance field in 1976, there was generated in the United States 24,265 million dollars in premium income. For property and liability insurance for the same year, the premiums totalled 60,813 million dollars. Included in that figure was 3,982
contracts because of the overwhelming bargaining power of the industry. Complete reliance is placed upon an insurer for peace of mind and for security from ruinous disaster. These factors form the basis for implication of a duty of good faith and fair dealing.

Some jurisdictions have legislatively determined the statutory penalty adequate as an exclusive remedy to the insured, finding the tort unnecessary.220 When the damage suffered by an insured is nominal, this is true. But, given an extreme situation, a statutory remedy with fixed percentage of loss damages and attorneys' fees can be wholly inadequate. What is needed is not a penalty but rather compensation for the insured who loses his business, his home, or his health because he believed the insurer would do as promised.

The extension of the bad faith tort into the first party area will not be without repercussions to plaintiffs and defendants, the bar, and the courts. These concern all phases of the insurer-insured relationship, but particularly the discovery techniques and claims handling practices used by both plaintiffs and defendants. As for the courts, they will have to settle on either a general standard or one applicable on a case-by-case basis to determine what conduct of an insurer constitutes "bad faith." These effects will be manageable because they have been considered and experienced, and have been analyzed in a considerable body of writing;221 the tort has been widely accepted, and case law exists to explain its nuances. The new tort should be adopted by Missouri courts.

LELAND C. SMITH II

million dollars in fire insurance premiums. In 1976, 76.8% of the population was covered under a hospital benefit plan and 93.2% 'had major' medical expense coverage.

