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ARTICLES

Trust Me: Insurers Are Not Fiduciaries to Their Insureds

BY DOUGLAS R. RICHMOND*

I. INTRODUCTION

The duty of a fiduciary to his beneficiary is essentially that of a trustee. A fiduciary "is bound to act in the highest good faith toward his beneficiary" and he may never seek to gain an advantage over his beneficiary by any means. A fiduciary must give priority to his beneficiary's best interests whenever he acts on the

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I owe the title of this Article to Eugene R. Anderson of Anderson Kill & Olick in New York, the dean of the policyholders' bar and an insightful lawyer, who was kind enough to share with me a copy of an unpublished paper stating his views on insurers as fiduciaries. Suffice it to say that Mr. Anderson's views do not match my own.

2 Id. (citing MONT. CODE ANN. § 72-20-201 (1946) (repealed 1989)).
3 See id.
beneficiary's behalf. A fiduciary owes his beneficiary a duty of undivided loyalty, meaning that a fiduciary cannot abandon or stray from this relationship to further his own interests. Examples of fiduciary relationships include "an attorney for a client, a corporate director or officer for the corporation or its shareholders, an agent for the principal, a guardian for the ward, a bailee for the bailor, a partner for the other partners, joint venturers for one another, and a physician for his patient."

Fiduciary relationships may be found in many areas of law. One area of law generally thought to be free of restrictive fiduciary ties, however, is that of contract. Here the mores of the marketplace control. Subject to relatively limited duties of commercial honesty, contracting parties are entitled to treat one another as adversaries, and they are free to pursue their own interests in the transaction without regard for the interests of others. Unlike those who share a fiduciary relationship, parties to a contract determine their own needs and bargain to obtain them. The price of this independence is a lack of security. "No party to a contract has a general obligation to take care of the other, and neither has the right to be taken care of."

Insurance policies are contracts. The parties to an insurance contract are the insurer and the insured. Given that fiduciary relationships function in ways alien to contractual relationships, it stands to reason that an insurer's relationship with its insured is not a fiduciary one. Or does it? A number of courts have characterized or recognized the insurer-insured relationship in insurance contracts as fiduciary.

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4 See Committee on Children's Television, Inc. v General Foods Corp., 673 P.2d 660, 676 (Cal. 1983) ("A fiduciary assumes duties beyond those of mere fairness and honesty; he must undertake to act on behalf of the beneficiary, giving priority to the best interest of the beneficiary.").

5 See Burdett v Miller, 957 F.2d 1375, 1381 (7th Cir. 1992) ("A fiduciary duty is the duty of an agent to treat his principal with the utmost candor, rectitude, care, loyalty, and good faith—in fact to treat the principal as well as the agent would treat himself.").


8 See, e.g., Original Great Am. Chocolate Chip Cookie Co. v River Valley Cookies, Ltd., 970 F.2d 273, 280 (7th Cir. 1992) (stating that "[c]ontract law does not require parties to behave altruistically toward each other" and that "parties to a contract are not each other's fiduciaries").

9 See William T. Barker et al., *Is an Insurer a Fiduciary to its Insureds?*, 25 TORT & INS. L.J. 1, 3 (1989).

10 See Frankel, supra note 7, at 799

11 Id. at 800.
relationship as fiduciary, though many do so only in the most cursory fashion and with little thought or reasoning, and some commentators strenuously argue that insurers are in fact fiduciaries to their insureds. Furthermore, insurers routinely describe themselves as fiduciaries in court documents. Insurance companies' advertisements enhance this perception, often describing themselves as occupying special positions of trust: State Farm bills itself as a “good neighbor” ready to help its insureds in times of need, Shelter Insurance advertises “the Shield of Shelter” (its logo being a red, white, and blue shield), Prudential has long sold its strength and

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15 See Anderson & Fournier, Why Courts Enforce, supra note 14, at 385-89.
reliability by advising potential insureds to “get a piece of the rock,” while Allstate tells its insureds and prospective insureds that they are secure in the company’s “good hands.”

How is it that insurers, as contracting parties, are sometimes transformed into fiduciaries for their insureds and apparently assigned heightened duties? Can they transform their relationships with their insureds from contractual to fiduciary by way of their own pleadings in occasional cases or through their advertisements? The base answer to these questions, it seems, is that insurance policies are different. First, they are adhesion contracts. Most insurance policies are standardized form documents. Insureds typically do not negotiate or assent to the specific provisions in their policies; indeed, most insureds do not even see their policies until sometime well after they have purchased coverage. Second, insureds purchase their policies for peace of mind and security rather than for financial gain. These factors mix to create an environment in which

16 See 12 JOHN A. APPLEMAN & JEAN APPLEMAN, INSURANCE LAW AND PRACTICE § 7004, at 51-52 (1981) (suggesting that such advertising slogans cut against the idea that the parties to insurance contracts deal at arm’s length and may support the recognition of a fiduciary duty running from insurers to their insureds).

I would argue that insurance companies’ slogans and advertisements along the lines described here do not suggest the existence of a fiduciary relationship with policyholders. These slogans and advertisements simply convey what consumers can expect of responsible, reputable insurers: that they will act reliably and reasonably, pay valid claims that their policies cover, and defend claims or suits as provided in their policies. Insurance markets are competitive. It is common knowledge among the public that not every loss is covered by insurance. Many people are skeptical of insurers. That insurers may advertise in ways to promote the reliability of their products or services, or to lessen consumers’ skepticism, ought not be construed as assuming fiduciary duties.


unscrupulous insurers can exploit their insureds’ misfortunes when resolving or settling claims and suits. Courts that have cast insurers as fiduciaries have done so to fill the void created by the parties’ disparate bargaining power and insurers’ exclusive control over litigation, settlement, and claim processing.

This Article will demonstrate that insurers are not fiduciaries to their insureds in ordinary circumstances or situations. To hold insurers to the security and peace of mind through protection against calamity’’); Decker v Browning-Ferris Indus., 931 P.2d 436, 443 (Colo. 1997) (“[A]n insured who enters into a contract of insurance seeks to obtain ‘financial security and protection against calamity.’’) (quoting Farmers Group, Inc. v. Trimble, 691 P.2d 1138, 1141 (Colo. 1984)); Feathers v. State Farm Fire & Cas. Co., 667 S.W.2d 693, 696 (Ky Ct. App. 1978) (observing that a “purchaser of a fire insurance policy is buying peace of mind’’), overruled by Federal Kemper Ins. Co. v Hornback, 711 S.W.2d 844 (Ky. 1986); Andrew Jackson Life Ins. Co. v. Williams, 566 So. 2d 1172, 1179 n.9 (Miss. 1990) (“[A]n insured bargains for more than mere eventual monetary proceeds of a policy; insureds bargain for such intangibles as risk aversion, [and] peace of mind’’); Campbell v. State Farm Mut. Auto. Ins. Co., 840 P.2d 130, 139 (Utah Ct. App.) (“[A]n insured may purchase insurance not only to provide funds, but to provide peace of mind.”), cert. denied, 853 P.2d 897 (Utah 1992).

19 See, e.g., Birth Ctr. v. St. Paul Cos., 727 A.2d 1144, 1155 (Pa. Super. Ct. 1999); Prosser v. Leuck, 592 N.W.2d 178, 182 (Wis. 1999); see also Allsup’s Convenience Stores, Inc. v. North River Ins. Co., 976 P.2d 1, 15 (N.M. 1998) (“[An insurer’s] fiduciary duty is present ‘because of the fiduciary obligations inherent in insurance relationships and because of concerns arising from the bargaining position typically occupied by the insured and the insurer.’’) (quoting Romero v. Mervyn’s, 784 P.2d 992, 998 (N.M. 1989)).


high standards reserved for fiduciaries would prevent insurers from acting
to protect their own interests and those of other policyholders. To routinely
make insurers fiduciaries would preclude them from combating excessive
or fraudulent claims, thus harming the insured public. Insurers' implied
duty of good faith and fair dealing affords insureds all the protection they
need as the weaker party to insurance contracts. In short, there are a
number of valid reasons for rejecting fiduciary duty as a means of
protecting insureds from allegedly predatory or heavy-handed conduct by
insurers.

Part II sketches pertinent aspects of insurance law and fiduciary
relationships. It then explains why insurers are not fiduciaries to their
insureds. Finally, Part II argues that insurers' implied duty of good faith
and fair dealing adequately protects insureds against insurers' alleged
abuses, and that the insurer-insured relationship is a special kind of
contractual relationship. Part III looks at how the law has developed to this
point. It traces insurance law's infection with fiduciary duty and explains
that courts have wrongly used the label "fiduciary duty" to describe an
insurer's duty of good faith and fair dealing. In doing so they have created
needless confusion.

II. THE INSURER-INSURED RELATIONSHIP
AND FIDUCIARY DUTIES

A. Insurance Law Fundamentals

There are two general categories of insurance: third-party and first-
party. "Only liability insurance is truly third-party insurance. Liability
insurance is described as third-party insurance because the interests
protected by the policy ultimately are those of strangers to the contract who
are injured by the insured's conduct."21 First-party insurance protects
insureds against their own losses or injuries.22 Examples of first-party
coverages include disability, fire, health, life, property, and uninsured and
underinsured motorist insurance.23 Both first-party and third-party
coverages may be combined in a single policy, as in automobile and
homeowners insurance policies.

21 Douglas R. Richmond, An Overview of Insurance Bad Faith Law and
22 See Olds-Olympic, Inc. v. Commercial Union Ins. Co., 918 P.2d 923, 930
23 See Richmond, supra note 21, at 103.
Liability insurers owe their insureds three duties: a duty to defend, a duty to indemnify, and a duty to settle claims within policy limits when appropriate. The first two of these duties are expressly contractual. The insurer’s duty to settle third-party claims within policy limits is implied. It is the product of the implied duty of good faith and fair dealing found in every insurance policy. The implied duty of good faith and fair dealing fundamentally requires that neither party to a contract do anything to injure the other’s right to receive the benefits of their agreement.

Fiduciary duty proponents are attracted to liability insurance because an insured, when sued, turns over his defense to his insurer and trusts his personal and financial security to the insurer. The insurer controls the litigation and determines whether to settle the case or take it to trial. The insured is more spectator in this process than participant. With such a dependent relationship must come a standard of care that exists independent of the insurance policy and without specific reference to the policy terms.

\[24\] See 1 Allan D. Windt, Insurance Claims & Disputes § 5.01, at 295 (3d ed. 1995) ("One of an insurer's obligations under a contract of liability insurance, arising out of its implied duty of good faith and fair dealing, is to settle a claim against the insured.


\[26\] See Richmond, supra note 21, at 84.

The first-party insurance relationship is much simpler and more straightforward. A first-party insurer owes its insured a single contractual duty—to pay covered claims or losses. The duty of good faith and fair dealing supplies the additional requirements that the insurer pay its insured's covered claim within a reasonable time, that it investigate an insured’s claim before denying it, and so on. Unlike the third-party context, in which the insured surrenders to the insurer the exclusive right to litigate or settle a claim, no similar relationship of dependence exists in the first-party setting. Generally, insurer and insured are in an adversary relationship whenever there is any claim by an insured for loss under any [first-party] insurance policy.

B. Fiduciary Relationships

The term “fiduciary” connotes a relationship of trust and security. Although fiduciary relationships may exist in a great variety of circumstances, their extraordinary nature requires that they not be lightly created. Merely acting for another's benefit will not spawn fiduciary duties unless the alleged fiduciary consciously assumes such duties. Similarly, a person's unilateral decision to repose trust and confidence in another will not create a fiduciary relationship; the intended fiduciary must act or conduct himself in ways that justify such special reliance. Because

28 See Richmond, supra note 21, at 111-12.
29 See id. at 104-05.
30 State ex rel. Safeco Nat'l Ins. Co. of Am. v Rauch, 849 S.W.2d 632, 634 (Mo. Ct. App. 1993); see also Universe Life Ins. Co. v Giles, 950 S.W.2d 48, 60 (Tex. 1997) (Hecht, J., concurring) (“[A]n insurer’s and an insured’s interests are not aligned when the insured is claiming on his own behalf as they are or should be in third-party cases—in a first-party case, an insurer’s interest in challenging the claim directly conflicts with the insured’s interest in making the claim.”).
32 See id.
33 See American Med. Int'l, Inc. v Giurintano, 821 S.W.2d 331, 339 (Tex. Civ. App. 1991) (“[A] fiduciary relationship is an extraordinary one and will not be lightly created; the mere fact that one subjectively trusts another does not, alone, indicate that he placed confidence in another in the sense demanded by fiduciary relationships, because something apart from the transaction between the parties is required.”).
34 See Rajala v. Allied Corp., 919 F.2d 610, 623 (10th Cir. 1990) (applying Kansas law).
35 See Farmers Ins. Co. v McCarthy, 871 S.W.2d 82, 87 (Mo. Ct. App. 1994).
fiduciary duties are "serious and many," an agreement to assume them is never presumed. The relationship of seller to buyer is not ordinarily characterized as fiduciary, even though a seller typically has far superior knowledge of its position, product, and capabilities. Nor does the fact that one party to a transaction has greater bargaining power, superior knowledge, or the ability to exploit the weaker party support the imposition of fiduciary duties. The ability to exploit disparate bargaining power is not a useful test for a fiduciary relationship as evidenced by a typical agency relationship; that is, an agent owes his principal fiduciary duties even though the principal possesses superior bargaining strength. In the buyer-seller context, the duty of utmost good faith and single-minded loyalty that characterize fiduciary relationships simply are not present no matter how disparate the parties' resources. The confidence that contracting parties place in one another is based on economic self-interest capable of at least some individual protection.

The fact that the weaker party to a bargain cannot seek protection under fiduciary law does not mean that it is at the stronger party's mercy, or that it must endure overreaching. What it does mean, however, is that the aggrieved party must seek relief under other doctrines.

C. The Inapplicability of Fiduciary Theory to the Insurer-Insured Relationship

The insurer-insured relationship is not fiduciary, regardless of whether the insurance policy at issue is a liability policy or some variety of first-party coverage. In both contexts insurers have the ability and obligation to scrutinize the claims presented, to investigate claims, to value claims, to limit or condition the circumstances in which they will pay, to simply deny claims, to litigate their insureds' liability, and to otherwise serve their own interests and those of other insureds. Such discretion, calculated

36 Rajala, 919 F.2d at 623.
37 See id.
38 See id. at 624; Committee on Children's Television, Inc. v. General Foods Corp., 673 P.2d 660, 676 (Cal. 1983).
39 See Committee on Children's Television, 673 P.2d at 675.
40 See id. at 675 n.21.
41 See id. at 676.
42 See Rajala, 919 F.2d at 624.
43 See Barker et al., supra note 9, at 7-8.
judgment, and allocation or weighing of interests would not be possible were the insurer-insured relationship fiduciary in nature.\footnote{See id. at 8 (observing that were the insurer-insured relationship fiduciary, "[e]very decision of an insurer adverse to an insured would be actionable in tort. But that is not the law.").} Those who advocate a fiduciary relationship between insurers and their insureds often look to insurers' descriptions of themselves and other carriers as fiduciaries in pleadings for support.\footnote{See, e.g., Anderson \& Fourmer, Why Courts Enforce, supra note 14, at 385-89.} More particularly:

\begin{quote}
[I]nsurance companies tell courts that other insurance companies are fiduciaries. Typically, insurance companies make these statements when seeking insurance coverage for themselves, when seeking reinsurance, or in trying to shift responsibility to another insurance company.

The best evidence that insurance companies are fiduciaries is the fact that they frequently represent in court that they are fiduciaries. Indeed, perhaps most damning is the fact that insurance companies take this position when seeking insurance coverage, and reject it when insurance coverage is sought from them.\footnote{Eugene R. Anderson \& Susannah Crego, Trust Me: Insurance Companies Are Fiduciaries 12-13 (May 6, 1999) (unpublished manuscript on file with the author).} This argument warrants immediate rejection.

The fact that an insurer enmeshed in litigation with another insurance company describes its adversary as owing it a fiduciary duty evidences little or nothing,\footnote{Insurance companies probably would be wise to avoid describing themselves or other carriers as fiduciaries or as owing fiduciary duties, and to demand that their counsel not do so, precisely to foreclose this sort of argument.} and it certainly does not amount to the acknowledgment or assumption of fiduciary duties in unrelated cases or other situations. For example, if the forum state's law holds that insurers are fiduciaries in the context of potential settlements with third-parties, how can an insurer's argument for judicial application of that law when litigating a dispute with another carrier constitute the assumption of a duty or a judicial admission?\footnote{"Judicial admissions are formal concessions in pleadings, or stipulations by a party or its counsel, that are binding upon the party making them." Keller v United States, 58 F.3d 1194, 1198-99 n.8 (7th Cir. 1995). Judicial admissions must be statements of \textit{fact} made to a court, as opposed to legal arguments. See New York State Nat’l Org. for Women v Terry, 159 F.3d 86, 97 n.7 (2d Cir. 1998).} It simply does not and cannot. Propositions of law cannot be
the subject of judicial admissions, and arguments made in support of a litigant's theory or position do not constitute either a judicial admission or a "party admission." The most that can be said is that the insurance company is arguing controlling law to support its position in a single case, as is any litigant's right. The insurer may think the law wrong generally, or the proposition unsound in theory, but that does not prevent it from using it to its benefit, even if it wants to take a different position in a different jurisdiction. Such alternative argument is neither improper nor duplicitous.

1. Liability Insurance

Claims or pronouncements that an insurer is a fiduciary to its insured typically are made in the liability insurance context. In Prosser v. Leuck, for example, the Supreme Court of Wisconsin stated that "[b]y entering into an insurance contract and taking control of settlement or litigation the insurer assumes a fiduciary duty on behalf of the insured." A Pennsylvania court recently observed that a liability insurer "assumes a fiduciary responsibility" to its insured "when handling, inter alia, all third party claims brought against the insured." In Asermely v. Allstate Insurance Co., the Rhode Island Supreme Court declared that "[i]t is not sufficient that the insurance company act in good faith when considering a plaintiff's reasonable offer to settle a case against the insured" when considering a plaintiff's reasonable offer to settle a case against the insured for an amount within the insurer's liability limits. Rather, the insurer's duty in

49 See Guidry v. Sheet Metal Workers Int'l Ass'n, Local No. 9, 10 F.3d 700, 716 (1993), on reh'g, 39 F.3d 1078 (10th Cir. 1994), cert. denied, 514 U.S. 1063 (1995).
50 See Terry, 159 F.3d at 97 n.7
51 See In re San Juan DuPont Plaza Hotel Fire Litig., 802 F. Supp. 624, 639 n.39 (D.P.R. 1992) (holding that insurers' admission that definition of "advertising liability" was ambiguous during argument did "not constitute a party admission"), aff'd, 989 F.2d 36 (1st Cir. 1993).
53 Prosser v. Leuck, 592 N.W.2d 178 (Wis. 1999).
54 Id. at 182.
57 Id. at 464.
such a situation "is a fiduciary obligation to act in the best interests of the
insured." 58

It can thus be said that some courts make a liability insurer a fiduciary
to its insured by blending the insurer's contractual duty to defend with its
implied duty to settle claims within policy limits. This insurance cocktail
is equal parts bad law and bad reasoning.

A fiduciary owes his beneficiary undivided loyalty, and he "must treat
the [beneficiary's] interests as paramount when exercising powers or
discretion arising from the relationship." 59 A liability insurer's duties to its
insureds are fundamentally different. Looking first at an insurer's defense
obligation, a liability insurer has a right to defend its insured as well as a
duty to do so. 60 An insurer has this right because in the overwhelming
majority of cases only the insurer's assets are at risk; the insured has no
personal exposure because any judgment or verdict will fall within the
insurer's policy limits. The insurer accordingly has the right to select
defense counsel, to make strategic or tactical decisions, to weigh the cost
of defense against any potential verdict and offer to settle on that basis, and
the like. In most instances, the insurer is free to settle or litigate an action
without fear of liability to its insured for decisions with which the insured
disagrees. 61 Even where an insured may have important interests (e.g.,
reputation) that he wants to vindicate by way of a trial, the insurer typically
has the contractual right to settle as it deems expedient and can protect its
economic interests by settling to avoid additional defense costs or any
possible verdict. 62 The insurer's interests thus trump the insured's interests.
That would not be possible were the insurer-insured relationship truly
fiduciary. For that matter, the mere fact that an insurer can defend its
insured under a reservation of rights indicates that the duty to defend is a
poor basis for the recognition of a fiduciary duty. 63

58 Id.
59 Barker et al., supra note 9, at 2.
1997); Sherwood Brands, Inc. v. Hartford Accident & Indem. Co., 698 A.2d 1078,
1083-84 (Md. 1997); Moeller v. American Guar. & Liab. Ins. Co., 707 So. 2d
1062, 1068-70 (Miss. 1996).
absence of bad faith, a liability insurer generally is free to settle or to litigate at its
own discretion, without liability to its insured for a judgment in excess of the policy
limits.").
62 See, e.g., Miller v. Sloan, Listrom, Eisenbarth, Sloan & Glassman, 978 P.2d
922, 928-29 (Kan. 1999).
Moreover, it cannot be that an insurer’s control of litigation against its insured amounts to a degree of control over the insured that would spawn a fiduciary relationship. An insured can always have a voice in its defense by hiring independent counsel to monitor the insurer’s litigation conduct. The insured also has some say in his defense because he shares an attorney-client relationship with the attorney hired by the insurer to defend him, and the defense attorney has ethical obligations to him that exist independent of the insurance policy. The insurer’s control of the insured’s defense is therefore exclusive only if the insured chooses to make it so. The insured’s ability to retain at least some control over its defense is inconsistent with a fiduciary relationship based on the surrender of personal control to another.

Turning next to liability insurers’ implied duty to settle, it is important to recognize that the duty is not absolute. An insurer’s duty to settle on the insured’s behalf does not translate into a unilateral requirement that it pay policy limits on demand, nor is an insurer required “to engage in unproductive and irrelevant [settlement negotiations] solely for sake of form.” An insurer can have no implied duty to settle unless the plaintiff makes a settlement offer within policy limits. And, even then, an insurer may opt for a vigorous defense over settlement if it reasonably believes that

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64 See Bernhard v. Farmers Ins. Exch., 915 P.2d 1285, 1289 (Colo. 1996) ("The determination of whether a true fiduciary relationship exists depends upon the degree of control exercised by the fiduciary over the affairs of the other person.").

65 See id.

66 See Finley v. Home Ins. Co., 975 P.2d 1145, 1154 (Haw. 1998); Rogers v. Robson, Masters, Ryan, Brumund & Belom, 407 N.E.2d 47, 49 (Ill. 1980); Hartford Accident & Indem. Co. v. Foster, 528 So. 2d 255, 269 (Miss. 1988); see also Prevratil v. Mohr, 678 A.2d 243, 250 (N.J. 1996) (stating that “in any litigation, counsel for an insurer must put the insured’s interests ahead of the insurer’s”); State Farm Fire & Cas. Co. v. Mabry, 497 S.E.2d 844, 847 (Va. 1998) ("The attorney employed by the insurer to defend the insured is bound by the same high standards which govern all attorneys, and owes the insured the same duty as if he were privately retained by the insured.").

67 See Bernhard, 915 P.2d at 1289.


69 Rhie v. Wisconsin County Mut. Ins. Corp., 568 N.W.2d 4, 8 (Wis. Ct. App.), review dismissed, 568 N.W.2d 301 (Wis. 1997).

70 If the plaintiff’s settlement offer exceeds the applicable policy limits, the insurer cannot later be held liable for refusing to settle. See, e.g., Texas Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 314-15 (Tex. 1994); McLaughlin v. National Union Fire Ins. Co., 29 Cal. Rptr. 2d 559, 566-67 (Ct. App. 1994).
the insured is not liable, or that the plaintiff’s demand exceeds a probable jury award. Courts do not presuppose that settlement is always the preferred means of protecting the insured’s interests.

There are, of course, reasonable limits on an insurer’s discretion when presented with a choice of a policy limits settlement versus continued litigation. The insurer cannot subordinate the insured’s interests to its own. In weighing whether to accept or reject a policy limits settlement offer, the insurer must give the insured’s interests the same consideration that it gives its own interests. What this means, as a practical matter, is that when presented with a settlement offer an insurer should seriously and carefully evaluate the possibility that a judgment might be entered against the insured that exceeds policy limits. As the Smith v Audubon Insurance Co. court explained, “a liability insurer is the representative of the interests of its insured, and the insurer, when handling claims, must carefully consider not only its own self-interest, but also its insured’s interest so as to protect the insured from exposure to excess liability.”

The established principle that an insurer weighing settlement need only give its insured’s interests consideration equal to its own in order to satisfy its duty of good faith and fair dealing is inconsistent with the existence of a fiduciary relationship. A fiduciary must give his beneficiary’s interests paramount consideration, not equal consideration. Were the insurer-insured relationship a true fiduciary relationship, the insurer would always be

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73 See Medical Malpractice Joint Underwriting Ass’n of R.I. v Rhode Island Insurers’ Insolvency Fund, 703 A.2d 1097, 1102 (R.I. 1997) (“[A]n insurer must refrain from acts that demonstrate greater concern for the insurer’s monetary interest than the financial risk attendant to the insured’s situation.”) (citing Allstate Ins. Co. v Campbell, 639 A.2d 652, 656-57 (Md. 1994)).


76 Id. at 376.

77 But see Rawlings v. Apodaca, 726 P.2d 565, 571 (Ariz. 1986) (stating that an insurer’s duty to give its insured’s interests equal consideration is “of a fiduciary nature”).
required to place the insured’s interests above its own. An insurer’s good faith duty of equal consideration is much more constrained. Indeed, the recognition of a fiduciary duty to settle cases within policy limits would render the duty of good faith and fair dealing meaningless. This is because any breach of an insurer’s implied duty of good faith and fair dealing in the settlement context would necessarily be a breach of the insurer’s fiduciary duty.

The fact that a liability insurer has no duty to disregard its own interests when they conflict with the insured’s interests clearly evidences the lack of a fiduciary relationship. The Delaware Supreme Court explained how this clash of interests is incompatible with a fiduciary relationship in *Corrado Brothers, Inc. v. Twin City Fire Insurance Co.* The insured in *Corrado Brothers* argued that the insurer had not settled a workers’ compensation claim in good faith because, in doing so, it caused the insured to be charged an additional retrospective premium of nearly $50,000. More particularly, the insured argued “that an insurer’s duty in handling a claim, having a potential for the imposition of a retrospective premium, is to be measured by the standards of a fiduciary.”

Although persuaded that “an insurer may not settle a claim in which a retrospective premium will be imposed on the insured unless the settlement is both in good faith and reasonable,” the *Corrado Brothers* court

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79 See Bernhard v. Farmers Ins. Exch., 915 P.2d 1285, 1289 (Colo. 1996) (“One who is acting as a fiduciary for another has the duty to act with the utmost good faith and loyalty on behalf of, and for the benefit of, the other person. The duty required of an insurer towards the insured is much more constrained.”) (citations omitted).
80 See Barker et al., supra note 9, at 9-10.
83 See id. at 1190-91. A retrospective premium is determined annually based on the insured’s losses the previous year, best known as “claim experience.” The insurer and the insured establish an annual premium at the inception of the policy period based on estimated losses for the ensuing year. If the actual losses during the policy period are lower than estimated, the insured receives a partial premium rebate. If actual losses are greater than estimated, the insurer charges the insured an additional premium. See Douglas R. Richmond, *Self-Insurance and the Decision to Settle*, 30 TORT & INS. L.J. 987, 989 (1995).
84 Corrado Bros., 562 A.2d at 1192.
85 Id. at 1191.
concluded "that the term 'fiduciary' overstates the essential relationship" between an insurer and its insured.\textsuperscript{66}

The concept of a fiduciary relationship, which derives from the law of trusts, is more aptly applied in legal relationships where the interests of the fiduciary and the beneficiary incline toward a common goal and in which the fiduciary is required to pursue solely the interests of the beneficiary. The relationship of insurer and insured, however, arises contractually with each party reserving certain rights under the contract, the resolution of which often leads to litigation. Thus, the settlement of a claim may benefit the insurer to the extent that it eliminates or reduces the cost of contesting the claim through litigation. The settlement may, however, prejudice the interests of the insured to the extent that settlement may result in an increase in future premiums or represent a tacit admission of liability. This expected clash of interests is clearly not compatible with the concept of a fiduciary.\textsuperscript{87}

Were the insurer-insured relationship ever to be fairly characterized as fiduciary, \textit{Corrado Brothers} was the platform. The insured's retrospective premium obligation arguably should have heightened the insurer's duty to consider and accommodate its insured's interests. Even in that situation, however, the insurer was not required to ignore its own legitimate interests in order to benefit the insured.

Courts occasionally assert that an insurer's equal consideration of its insured's interests in the settlement context will not satisfy the insurer's duty of good faith. Instead, "the insurer must conduct itself as though it alone were liable for the entire amount of the judgment."\textsuperscript{88} This would appear to express a fiduciary duty, inasmuch as the insurer is being required to make its policyholder's interests paramount. Such courts would seem to compel an insurer to elevate the insured's interests above its own. That is, of course, what the law requires of a fiduciary when his interests and his beneficiary's interests do not align. An examination of representative cases reveals, however, that the duty being announced is simply one of good faith and fair dealing.

In \textit{Egan v. Mutual of Omaha Insurance Co.},\textsuperscript{89} for example, the California Supreme Court stated the rule that an insurer "when determining

\textsuperscript{66} \textit{Id.} at 1192.
\textsuperscript{67} \textit{Id.} (citations omitted).
\textsuperscript{89} \textit{Egan v. Mutual of Omaha Ins. Co.}, 620 P.2d 141 (Cal. 1979).
whether to settle a claim, must give at least as much consideration to the welfare of its insured as it gives its own interests.\textsuperscript{90} Having announced an insurer’s duty to settle a claim within policy limits, the court went on to express that the “governing standard” for measuring an insurer’s good faith “is whether a prudent insurer would have accepted the settlement offer if it alone were to be liable for the entire judgment.”\textsuperscript{91} In other words, a prudent insurer must carefully and accurately evaluate a case’s verdict value, just as any reasonable litigant should. The \textit{Egan} court’s ordered statement of an insurer’s implied duty to settle within policy limits and the measure of its good faith relative to that duty makes clear that metaphorically placing the insurer in the insured’s shoes is not the expression of a fiduciary standard.

In \textit{Dairyland Insurance Co. v. Herman},\textsuperscript{92} the New Mexico Supreme Court stated that an insurer “should place itself in the shoes of the insured”\textsuperscript{93} and act as though it alone would bear any judgment.\textsuperscript{94} Were another court to read only that passage, it might conclude that an insurer must act as a fiduciary when evaluating settlement. What the \textit{Dairyland} court actually held, however, was that while an insurer’s good faith evaluation of the risks and benefits attending settlement offers is generally accorded judicial deference, the insurer’s judgment should receive less deference where “there is a substantial likelihood of a recovery that exceeds policy limits.”\textsuperscript{95} When a third-party claimant makes a firm and reasonable offer to settle what is clearly an excess claim within policy limits, the insurer’s duty of good faith and fair dealing may well require it to settle.\textsuperscript{96} If the insurer breaches its duty of good faith by refusing to accept a reasonable settlement offer within policy limits when there is a substantial likelihood of an excess verdict, the insurer will be liable for the entire amount of any subsequent judgment.\textsuperscript{97}

The \textit{Dairyland} court did not state that an insurer must always accept a third-party claimant’s settlement offer,\textsuperscript{98} or that it is forbidden to consider

\textsuperscript{90} \textit{Id.} at 145.
\textsuperscript{91} \textit{Id.}
\textsuperscript{92} \textit{Dairyland Ins. Co. v. Herman}, 954 P.2d 56 (N.M. 1997).
\textsuperscript{93} \textit{Id.} at 61.
\textsuperscript{94} \textit{Id.}
\textsuperscript{95} \textit{Id.}
\textsuperscript{96} \textit{Id.}
\textsuperscript{97} \textit{Id.}
\textsuperscript{98} The court expressly noted that “there is no presupposition that settlement is always the preferred means of protecting the policyholder’s interests.” \textit{Id.}
its own interests when weighing settlement. The court held only that an insurer cannot gamble with the insured’s money. An insurer that is willing to bet against an excess verdict must back its play with its own money.

In short, an insurer’s obligation to pay an excess verdict when it rejects a policy limits settlement offer is not linked to a fiduciary duty. An insurer that gives its insured’s interests equal consideration before rejecting a policy limits offer in what is clearly an excess liability case realistically bears the same liability if that decision was made without any regard for the insured’s interests. An insurer may incur liability in excess of its policy limits without acting in bad faith. Prioritizing the insured’s interests will seldom change the ultimate outcome. Given that a failure to settle will typically leave the insurer liable for the full amount of any subsequent excess verdict, it is in all likelihood an insurer’s consideration of its own interests that causes it to settle within policy limits when faced with probable excess liability. To behave otherwise is to render meaningless the policy limits for which it bargained. An insurer’s decision to accept a

99 See id. (stating that a liability insurer’s duty of good faith and fair dealing “means that ‘an insurer cannot be partial to its own interests, but must give its interests and the interests of its insured equal consideration’ ”) (quoting Lujan v. Gonzales, 501 P.2d 673, 680 (N.M. Ct. App. 1972)).

100 See id. (stating that “[t]he courts of this state will not permit insurers to profit by their own wrongs”).

101 This is generally so because an insurer that declines or fails to settle a case within policy limits may breach its contract with its insured without committing an act of bad faith. The insured would thus be entitled to recover all consequential damages flowing from the insurer’s breach, including any excess judgment. As one noted insurance law scholar explains:

Contract remedies applied flexibly could go far toward fully compensating the aggrieved insured. If an insurer unjustifiably refuses to accept a reasonable settlement offer, it is a foreseeable consequence of the insurer’s conduct that a judgment might be entered in excess of the policy limits. If the duty to settle is treated as a subsidiary element of the contractually based duty to defend, the excess judgment would still be the insurer’s responsibility under contract law’s remedial scheme.


policy limits settlement offer is more an act of economic self-interest than an attempt to protect the insured.

2. First-Party Insurance

An insured may depend on his first-party insurer to provide a cushion in times of hardship, or security and peace of mind in the face of calamity. There are many examples of such dependence: a life insurance policy may support a family for years after the policyholder dies, health insurance may spare a seriously ill person runous medical expenses, uninsured motorist insurance may make an accident victim whole when a tortfeasor cannot, and business interruption coverage may save an enterprise from bankruptcy. Be that as it may, and just as with liability insurance, a first-party insurer has no obligation to pay claims that its policy does not cover, or to take any other action inconsistent with the terms of its policy.

When presented with a claim by its insured, a first-party insurer need not pay automatically. An insurer is free to verify the existence of a claimed loss, to investigate the facts and circumstances of the loss to determine the existence and scope of coverage, and to determine the amount payable for a covered loss. An insurance company may challenge or dispute a claim that is "fairly debatable" without breaching its duty of good faith to the insured.

The law vests insurers with the right and obligation to scrutinize the legitimacy or validity of claims presented, and to limit their payment to those claims that pass muster. Insurers may even have a duty to their other policyholders to contest illegitimate claims. The recognition of a duty to dispute questionable claims rests on the assumption that an insurer's payment of illegitimate claims raises the cost of insurance for all of the

103 See Lucas v. State Farm Fire & Cas. Co., 963 P.2d 357, 360 (Idaho 1998) ("Good faith and fair dealing with an insured does not include the payment of sums that are reasonably in dispute, but only the payment of legitimate damages.").


company's policyholders. An insurer's ability to contest illegitimate claims is important, for insurance fraud is a significant problem. Of course, an insurance company's careful analysis of claims submitted to it is contrary to the interests of any given insured making a claim, for the insured is interested in the most generous possible payment made hastily and with no questions being asked.

The relationship between a first-party insurer and its policyholder is ill-suited for fiduciary controls. Indeed, fiduciary theory simply does not work here for at least two reasons. First and foremost, an insurer's interests and an insured's interests are not aligned when the insured is claiming on his own behalf, as they are in third-party cases where insurer and insured face a common adversary. The insurer is never cast as the insured's agent. The insurer and insured do not deal in trust when a first-party claim is made; here they are adversaries. Even when a claim is clearly covered, the insurer and insured may disagree over the amount due or the nature of the benefits to be paid. This inherent conflict, which is well-recognized in insurance law, cannot be reconciled with the existence of a fiduciary relationship.

Second, there is no conceivable set of circumstances in which the insured surrenders control of litigation in which it is a party to the insurer. In the first-party context, any litigation is the product of either the insured or the insurer suing the other. Regardless, the insured controls the litigation.

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106 See id. (stating that an insurer's "[p]ayment of illegitimate claims raises the costs of insurance for all policyholders"); see also Universe Life Ins. Co. v. Giles, 950 S.W.2d 48, 60 (Tex. 1997) (Hecht, J., concurring) ("Indeed, from a competitive viewpoint, an insurer must pay only valid claims and must deny invalid claims to keep premiums to customers to a minimum.").
107 See Giles, 950 S.W.2d at 61 (Hecht, J., concurring) (discussing several studies on the frequency or prevalence of insurance fraud).
108 See id. at 60.
109 See Beck v Farmers Ins. Exch., 701 P.2d 795, 799-800 (Utah 1985) (distinguishing between third-party and first-party insurance and holding that in a first-party relationship the insurer's duties are contractual rather than fiduciary).
111 See, e.g., McCauley v. Suls, 716 A.2d 1129, 1134 (Md. Ct. Spec. App. 1998) (stating that "an insurance company owes no fiduciary duty in a first-party claim because the insured controls the litigation and a fiduciary duty need not be imposed").
The inapplicability of a fiduciary duty to the first-party insurance relationship was explained in *Kanne v. Connecticut General Life Insurance Co.* The *Kanne* plaintiffs sued their health insurer for breach of contract, bad faith, breach of fiduciary duty, fraud, and the breach of certain statutory duties in connection with the delayed payment of various medical bills. The *Kanne* court found for the plaintiffs on their breach of contract and bad faith claims, but rejected their breach of fiduciary duty claim. It reasoned that while an insurer’s duty of good faith and fair dealing may be “fiduciary in nature, it does not create a fiduciary relationship.” The *Kanne* court further stated:

In the insurance context, the implied covenant of good faith and fair dealing requires no more than “that each party is prevented from interfering with the other’s right to benefit from the contract.” It does not further require that the insurer place the insured’s interests above its own as would be the case were the insured a fiduciary.

Beyond the principle that an insurer need only give its insured’s interests equal consideration, the *Kanne* court observed an insurer “is privileged, in pursuing its own economic interests, to assert its legal rights.” An insurer is not required to pay every claim presented. The company has a duty to its other policyholders and to the public “not to dissipate its reserves through payment of meritless claims.”

Recognizing the inherent conflict of interest between a first-party insurer and its insured, the *Kanne* court applied strict rules of construction against the insurer to remedy the unfairness and lack of reason evident in its conduct. The court also enforced the insurer’s duty of good faith and fair dealing. The court declined to go farther, however, observing that

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113 See id. at 902-04.

114 See id. at 908-10.

115 Id. at 908.

116 Id. (citation omitted).

117 Id. (citing Fletcher v. Western Nat’l Life Ins. Co., 89 Cal. Rptr. 78 (Ct. App. 1970)).


119 See id.

120 See id. at 907-08.
while Connecticut General [was] obliged to act in good faith and deal fairly, this is not a fiduciary duty.”

D. Insurers’ Duty of Good Faith and Fair Dealing, and the Insurer-Insured Relationship

An insurer who breaches its duty of good faith and fair dealing may be sued in tort for bad faith. In the case of a liability insurer charged with bad faith for not settling a claim within policy limits, the determination of whether the insurer acted in bad faith will require a weighing of such factors as: (1) the probability of the insured’s liability; (2) the amount of the policy limits; (3) the extent of the claimant’s damages; (4) the adequacy of the insurer’s investigation; (5) whether the insurer followed its own defense attorney’s advice regarding settlement; (6) whether any misrepresentations were made by the insured which may have misled the insurer in settlement negotiations; and (7) the openness of the communications between the insurer and the insured. And, of course, there must be a judgment in excess of policy limits.

In the first-party context, an aggrieved insured generally must establish (1) that the insurer’s conduct was unreasonable and (2) that the insurer knew or should have known it was being unreasonable in order to prevail on a bad faith claim.

“Bad faith” cannot be uniformly defined or described. The majority rule appears to be that there must be some level of intentional wrongdoing by an insurer in order to support a bad faith claim. The insurer must do more than simply breach its contract with the insured. As the Arkansas Supreme Court observed in State Auto Property & Casualty Insurance Co. v. Swaim, 991 S.W.2d 555 (Ark. 1999): “An insurance company commits the tort of bad faith when it affirmatively engages in dishonest, malicious or oppressive conduct in order to avoid a just obligation to its insured.” Id. at 559. “Mere negligence or bad judgment is insufficient so long as the insurer is acting in good faith.” Id. This sort of high standard is not universal, however. Some states allow bad faith recovery for an insurer’s negligence. See Richmond, supra note 21, at 98.


unreasonableness of the insurer’s conduct is the essence of the first-party tort.126

Courts have fashioned a tort duty of good faith and fair dealing specifically for the insurer-insured relationship.127 An insurer's duty of good faith and fair dealing protects a policyholder against an insurer’s exploitation of its superior bargaining power and exclusive control over claim processing.128 It compels an insurer to communicate with its insured and to repeatedly weigh the insured’s best interests in light of shifting circumstances. If an insurer breaches its duty, the insured may recover a range of compensatory damages intended to restore the insured to the position he would have enjoyed but for the insurer’s bad faith. An insurer that unreasonably refuses to settle a third-party claim within its policy limits becomes liable for any judgment exceeding its policy limits.129 Insureds may also recover damages for emotional distress or mental anguish, interest, lost income, and other related economic losses. In addition, most jurisdictions allow punitive damages in bad faith actions.130

Assuming that insureds need a tort remedy for reckless or unscrupulous behavior by insurers, the duty of good faith and fair dealing implied in all insurance policies affords all the relief and shelter necessary. The compensatory and punitive damages available to insureds in bad faith actions deter reckless or unscrupulous conduct by insurers. If an insurer is undeterred, a bad faith action is a powerful weapon for righting the wrong.


127 See Richmond, supra note 21, at 76-80 (discussing the history of bad faith in insurance law).


129 See Richmond, supra note 21, at 79.

130 See id. at 79-80.
The tort of bad faith provides for all of those damages that an insured might recover for an insurer’s breach of fiduciary duty, and perhaps more. The threat of a bad faith claim forces insurers to protect insureds’ best interests in ways that allow insureds to enjoy the peace of mind and security for which they bargained.

Although heightening insurers’ duties to those of fiduciaries would afford insureds greater protection still, extending such protection would be inconsistent with the public and private interests that permeate insurance. If insurers were made to be true fiduciaries, they would lose their ability to hold down premiums by weeding out illegitimate claims, contesting an insured’s liability, or disputing a third-party claimant’s damages. The cure might then be worse than the illness because insurers would then surely have to fund their new duty through significantly increased premiums.

Try though some courts might, it is not possible to make insurers fiduciaries to their insureds for some claim-related purposes, but not for others. For example, a first-party insurer cannot be a fiduciary to its insured when it comes to communicating claim information or facts learned during an investigation, but share some lesser relationship when it comes time to deny the claim as invalid, or pay less than the full amount requested by the insured. At all times the insurer and the insured are bound by the terms of their contract, and the resolution of any claim involves more than the simple act of payment. Accordingly, consistent judicial enforcement of insurers’ duty of good faith and fair dealing in all aspects of their relationships with their insureds is the most reasonable approach to preventing and remedying unreasonable or oppressive conduct by insurers.

But if the insurer-insured relationship is not fiduciary, how should it be characterized? Courts often characterize it as “special.” That is not a bad description, for the insurer-insured relationship seems protective by nature and tort law treats some protective relationships as “special” for duty purposes. At the same time, characterizing the insurer-insured relationship as a “special relationship” paints with too broad a brush. The insurer-

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Insurers are not fiduciaries. The insured relationship is made "special" by the same factors that require a cause of action for bad faith, all of which are linked to the underlying insurance policy. An insurer's duty of good faith and fair dealing is implied in support of the policy, it would not exist otherwise. The precise nature of an insurer's duty of good faith and fair dealing—and thus the contours of its relationship with its insured—depend on the nature and purpose of the underlying policy. No policy, no relationship, no duty. Accordingly, the insurer-insured relationship is best described as a special kind of contractual relationship.

Certainly, the insurer-insured relationship is contractual. But it differs from other contractual relationships. It merits recognition as a special kind of contractual relationship because the insurance policy out of which the relationship arises and around which it centers "represents a unique type of legally enforceable contract." An insurance policy is different from other contracts because in both first-party and third-party arrangements it gives "the insurer almost adjudicatory responsibility." The insurer determines coverage, the validity of claims, the value of claims, whether and how much to pay, and the like. Although the insured has the power to enforce the contract, invoking his rights or remedies detracts significantly from the peace of mind and security that he thought he purchased with the policy. The contractual relationship between an insurer and its insured is built on more than the carrier's bare promise to pay covered claims.

The idea that the insurer-insured relationship is a special kind of contractual relationship finds support in the courts' treatment of insurers'...
duty of good faith and fair dealing. The implied duty of good faith and fair dealing clearly is a contract law principle. But while that duty is found in all contracts, it became a tort duty in insurance and is enforced almost exclusively in connection with insurance policies. For example, courts routinely reject the argument that an employment agreement includes an implied duty of good faith and fair dealing sounding in tort. This is even though an employment contract is of great economic significance to an employee because it provides the means for an employee to meet his basic needs.

And why does it matter how the insurer-insured relationship is classified or described? Is it important for any reason other than the law’s love of precision? Correctly describing the insurer-insured relationship is important because the nature of the relationship determines the parties’ duties and rights. Altering the relationship between insurer and insured upsets their bargain. Even minor misstatements, such as describing the insurer-insured relationship as “akin” or “analogous” to a fiduciary relationship, can lead to uncertain results. Treating the insurer-insured relationship as a special kind of contractual relationship provides a predictable basis for deciding disputes.

III. THE FLAWED RISE OF FIDUCIARY DUTY IN INSURANCE LAW

The principle that an insurer is a fiduciary to its insured is arguably attributable to language found in the dissenting opinion in Gruenberg v. Aetna Insurance Co. In Gruenberg, the California Supreme Court held that first-party insurers owe their insureds a duty of good faith and fair dealing, and that the breach of that duty is actionable in tort. Indeed, Gruenberg is widely recognized as the landmark first-party bad faith case.

In his dissent, Justice Roth wrote that in the third-party context an insurer’s right to control litigation against an insured and the insured’s duty to cooperate in his defense “creates a fiduciary agency between the [insurer

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142 See generally Restatement (Second) of Contracts § 205 (1979).
145 See id. at 1038.
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and the insured]." He further observed that a liability insurer that fails to
give its insured's interests paramount consideration when presented with
a policy limits settlement offer in a potential excess liability case acts in
bad faith and "renders the insurer liable for breach of its fiduciary duty." Continu
ing, but equivocating, he observed that a liability insurer's implied
duty to settle "equates with a fiduciary duty on the insurer."

Justice Roth's point was that liability insurers and first-party insurers
do not share the same relationships with their insureds. In the liability
insurance context, most covered claims are settled short of trial, and that
is one of the usual means by which the insured is protected. A first-party
insurance policy does not create a situation whereby an insurer effectively
can gamble with the insured's money. For that reason, he did not believe
that the court should recognize bad faith as a tort in the first-party
insurance context.

Justice Roth's comments about a liability insurer's supposed fiduciary
duties ought not be seen as having precedential value—or even persuasive
value—for several reasons. First, Justice Roth misinterpreted the California
precedent he cited to support his statement that a liability insurer's duty to
settle certain claims within policy limits "equates with a fiduciary duty". The cases on which he chiefly relied—Comunale v. Traders & General
Insurance Co. and Crisci v. Security Insurance Co.—do not stand for
that principle. In both Comunale and Crisci the California Supreme Court
held only that an insurer must give its insured's interests at least as much
consideration as it gives its own. That is not the expression of a fiduciary
duty.

Second, to the extent Justice Roth wanted to make the point that a
liability insurer has a duty to settle clear excess claims within policy limits,
he never needed to brand the insurer-insured relationship "fiduciary." An
insurer's duty of good faith compels it to settle in a case of clear excess

147 Gruenberg, 510 P.2d at 1043 (Roth, J., dissenting).
148 Id.
149 Id.
150 See id.
151 See id. at 1049.
152 Id. at 1043.
155 See Comunale, 328 P.2d at 201 ("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 consideration as it does to its own interest."); Crisci, 426 P.2d
at 176-78 (citing Comunale.)
liability. In fact, Justice Roth twice appeared to confuse fiduciary duty with the lesser duty of good faith and fair dealing. Third, California courts have long rejected Justice Roth’s position that a liability insurer has a duty “to handle all claims with the interest of the insured uppermost,” which expresses a fiduciary standard. Ignoring Comunale and Crisci, for at least twenty years California courts have held only that insurers must protect their insureds’ interests equally with their own.

Judicial or scholarly reliance on Gruenberg for the recognition of a fiduciary relationship between insurers and insureds is at best careless. Sloppy language amounting to dicta in a dissenting opinion resting on an obligation that has been squarely rejected by courts of that same state is an infirm doctrinal foundation.

Another California case sometimes cited for the proposition that an insurer is a fiduciary to its insured is Egan v. Mutual of Omaha Insurance Co. As noted earlier, Egan clearly stated the general rule that an insurer’s duty of good faith is one of equal consideration. Later in the opinion, the court explained why an insured could recover punitive damages for an insurer’s bad faith despite a California statute limiting the award of punitive damages to those actions “for the breach of an obligation not arising from contract.” In doing so it quoted a law review article:

“Suppliers of services affected with a public interest must take the public’s interest seriously, where necessary placing it before their interest in maximizing gains and limiting disbursements [A]s a supplier of a public service rather than a manufactured product, the obligations of insurers go beyond meeting reasonable expectations of coverage. The obligations of good faith and fair dealing encompass qualities of decency and humanity inherent in the responsibilities of a fiduciary. Insurers hold

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156 See Gruenberg, 510 P.2d at 1043 (stating that an insurer’s failure to settle within policy limits “is bad faith and renders the insured liable for breach of its fiduciary duty”); see id. (stating that an insurer’s good faith duty to settle “equates with a fiduciary duty”).

157 Id.


159 Egan, 620 P.2d at 141.

160 See id. at 145. See supra text accompanying notes 89-91.

161 Egan, 620 P.2d at 146 (emphasis added) (quoting CAL. CIV CODE § 3294 (West 1997)).
themselves out as fiduciaries, and with the public's trust must go private responsibility consonant with that trust."\textsuperscript{162}

The *Egan* court's point was not that insurers are fiduciaries, but rather that the insurer-insured relationship is not adversarial and is similar to a fiduciary relationship insofar as an insurer sometimes must consider its insured's interests rather than attending solely to its own interests. This view of *Egan* is confirmed by the court's description of the insurer-insured relationship as a "special relationship."\textsuperscript{163} Had the *Egan* court meant to brand the insurer-insured relationship fiduciary it surely would have done so.

No one should now rely on any California case as authority for the existence of a fiduciary relationship between insurers and their insureds. California courts have made clear that the insurer-insured relationship is not fiduciary.\textsuperscript{164}

Beyond California's borders, the Idaho Supreme Court's decision in *White v. Unigard Mutual Insurance Co.*\textsuperscript{165} is commonly viewed as supporting the existence of a fiduciary relationship between insurers and insureds. This view is simply inaccurate.

The *White* court held "that there exists a common law tort action, distinct from an action on the contract, for an insurer's bad faith in settling the first party claims of its insured."\textsuperscript{166} In deciding to apply tort principles to first-party insurance, the *White* court had to distinguish insurance policies from other contracts in order to expand the damages available to an aggrieved insured.\textsuperscript{167} Continuing, the court reasoned that there exists a "special relationship" between insurers and insureds that justifies the recognition of a tort cause of action for bad faith in the first-party context.\textsuperscript{168}

In explaining its reasoning, the *White* court quoted the California Supreme Court's decision in *Seaman's Direct Buying Service v. Standard*
in which that court stated the insurer-insured relationship is characterized by elements of "public interest, adhesion and fiduciary responsibility." But the White court expressly rejected the principle that an insurer is a fiduciary to its insured, limiting its fiduciary analogy to a recognition that an insured sometimes has the right to trust his insurer to look out for his best interests, thus justifying the recognition of a covenant of good faith and fair dealing premised on the "special relationship" between insurer and insured.

The term "fiduciary" next appears in a passage dealing with the defending insurance company's attempt to distinguish liability insurance from first-party insurance, and thus halt the spread of the bad faith tort into the first-party realm. The court observed that the defendant "concedes that while an action sounding in tort may be applicable in third party situations due to the fiduciary relationship established when the insurer assumes control of the litigation it has no merit when the insured is bringing the action himself." In rejecting the defendant's argument against first-party bad faith, the court observed that the simple filing of a lawsuit by a first-party insured "does not necessarily create an adversarial relationship between himself and the insurer which abrogates the special relationship imposed by the insurance contract."

The White court did not recognize the existence of a fiduciary duty in this portion of its opinion, either. Rather, the court sought to explain that the differing first-party relationship—where an insurer and insured generally are seen as having opposing interests as soon as the insured seeks benefits under the policy—is of a nature that a bad faith tort is required to protect insureds from overreaching by insurers. While there may be a tort action for the willful breach of an insurance contract and an insurer's bad faith in failing to promptly settle a valid claim, the outcome of any such action will depend on the facts of the particular case. An insurer is not

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170 Id. at 1166; see also White, 730 P.2d at 1019.
172 See id.
173 Id. at 1019-20 (emphasis added).
174 Id. at 1020 (citing Sullivan v. Allstate Ins. Co., 723 P.2d 848, 850 (Idaho 1986)).
175 See id.
176 See id.
guilty of bad faith if “it challenges the validity of a fairly debatable claim, or when its delay [of payment] results from an honest mistake.”\textsuperscript{177}

In conclusion, the cases from the 1970s and 1980s that are most often cited as supporting the existence of a fiduciary relationship between an insurer and its insureds are not persuasive. They can be said to support the existence of fiduciary duties only if the proponent misunderstands their explanatory language. Other courts have senselessly confused and blended bad faith with breach of fiduciary duty.\textsuperscript{178} Fiduciary duty has crept into the insurer-insured relationship as a result of careless explanation, misunderstanding, and artless language.

CONCLUSION

The duty of a fiduciary is to act with utmost loyalty to his beneficiary. A fiduciary must give unyielding priority to his beneficiary’s best interests whenever he acts on his beneficiary’s behalf. In contrast, neither party to a contract has an obligation to take care of the other. Contracting parties are free to pursue their own interests without regard for the interests of the other. A contractual relationship is essentially adversarial, within certain bounds of commercial honesty.

Insurance policies are a special kind of contract because of their almost adjudicatory nature and the insured’s special reliance on the insurer. An insurance policy embodies more than a carrier’s bare promise to pay covered claims. Accordingly, the relationship between an insurer and an insured is a special kind of contractual relationship. Courts protect insureds’ interests in this relationship by enforcing insurers’ implied duty of good faith and fair dealing.

No matter how else it might be described, the insurer-insured relationship is not a fiduciary one. Altering the special contractual relationship between insurer and insured by branding it fiduciary upsets the parties’ bargain. To impose fiduciary duties on insurers would prevent them from acting to protect their own interests and those of other policyholders. To routinely make insurers fiduciaries would also prevent them from contesting excessive or fraudulent claims, thus harming the insurance-buying public. Even minor indiscretions, such as describing the insurer-insured relationship as “akin” or “analogous” to a fiduciary relationship, can lead to uncertain results. Judicial enforcement of insurers’ implied duty

\textsuperscript{177} Id. (citing Rawlings v. Apodaca, 726 P.2d 565, 572-73 (Ariz. 1986)).

of good faith and fair dealing affords insureds all the protection they need against overreaching and abuse by insurers, while avoiding the many problems posed by making the insurer-insured relationship a fiduciary one.