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Insurance—Disability Insurer's Refusal to Pay Gives Rise to Action in Tort—Fletcher v. Western National Life Insurance Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970)

anon

RECENT DEVELOPMENTS

INSURANCE—DISABILITY INSURER'S REFUSAL TO PAY GIVES RISE TO ACTION IN TORT—*Fletcher v. Western National Life Insurance Co.*, 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970).

Plaintiff suffered a totally disabling back injury in an industrial accident. His insurance policy with the defendant company provided for benefits of $150 per month for thirty years for total disability due to injury. But if the disability were due to sickness, the benefits were to continue for only two years. The defendant had received extensive medical information confirming the accidental cause of the disablement. To avoid full payment, however, it attempted to pay under the limited two-year sickness provision, then stopped payments altogether, fabricated a story about a previously existing condition and demanded return of the payments it had made. Later, the company offered to permit the plaintiff to retain the past payments in return for his surrender of the policy. While the payments were withheld the plaintiff's family subsisted on macaroni, beans, and potatoes; their utilities were shut off; a daughter had to leave school; and they lost property in which they had invested.

Plaintiff brought suit to obtain a declaration of the defendant's liability under the policy and to recover damages for emotional injuries caused by the defendant's conduct. The defendant stipulated its liability under the policy, and a cause of action for intentional infliction of emotional distress was submitted to the jury. Following a jury award of $60,000 compensatory and $650,000 punitive damages, the trial judge reduced the punitive damages to $190,000. A primary issue on appeal was whether the action was one at contract rather than tort. Only a tort theory would allow plaintiff to recover damages for mental suffering or punitive damages. The appellate court affirmed. *Held:* Despite the contractual nature of the insurance policy, the action was one at tort. *Fletcher v. Western National Life Insurance Co.*, 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970).

I. THE BORDERLAND OF TORT AND CONTRACT

Classification of a cause of action as tort or contract is important because of the different rules of jurisdiction, statutes of limitation,

wrongful death, and damages.[1] In *Fletcher,* a contract measure of damages would probably have permitted only an award of the stipulated policy benefits, while the tort measure of damages permitted an additional award of $250,000.[2]

Often a plaintiff will attempt to plead his action as either tort or contract to gain the most favorable rule.[3] However, there never has been complete freedom to classify an action according to the plaintiff's desire. Generally accepted broad definitions of tort and breach of contract do exist.[4] Contractual duties are owed only to parties to a contract and are created by the consent of the parties to the terms of the contract. Duties that sound in tort are owed to persons at large and are created by the law to promote social policy, regardless of the parties' consent.[5]

Often, though, a contract will create a relationship that gives rise to duties imposed by law in addition to those duties arising out of the contract. For example, a doctor may voluntarily accept a contractual duty, for breach of which a contract action will lie, and the law will add a duty of due care for breach of which a tort action will lie.[6] Such cases fall between the categories in a gray area called the "borderland of tort and contract."[7] Unfortunately, there is no generally accepted

1. Thornton, *The Elastic Concept of Tort and Contract as Applied by the Courts of New York,* 14 BROOK. L. REV. 196 (1948).

2. The measure of contract damages is usually narrower than tort damages, since contract damages are limited to those reasonably foreseeable at the time of contract. Hadley v. Baxendale, 156 Eng. Rep. 145 (1845); C. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES 560-81 (1935). Damages for mental suffering generally are not recoverable. Westwater v. Rector of Grace Church, 140 Cal. 339, 73 P. 1055 (1903). Punitive damages are also precluded. Crogan v. Metz, 47 Cal. 2d 328, 303 P.2d 1029 (1956). In tort, both compensatory and punitive damages are recoverable. Arcadia, Cal., Ltd. v. Herbert, 54 Cal. 2d 328, 5 Cal. Rptr. 686, 353 P.2d 294 (1960). Washington is one of only four states that does not allow punitive damages. W. PROSSER, LAW OF TORTS § 2 (4th ed. 1971).

The difference between tort and contract damages is of great importance in *Fletcher.* In the instant case $190,000 of the $250,000 were punitive damages and the remaining $60,000 compensatory damages were for mental suffering. Opening Brief for Appellant at 2, Fletcher v. Western Nat'l Life Ins. Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 788 (1970). Both of these amounts would have been precluded if the action had been categorized as a breach of contract.

3. Addis v. Gramophone Co. Ltd., [1909] A.C. 488, 492.

4. Estep v. Budger Mfg. Co., 164 Cal. App. 2d 119, 330 P.2d 298 (1958).

5. P. WINFIELD, THE PROVINCE OF THE LAW OF TORT 40 (1931).

6. Brown v. Moore, 247 F.2d 711 (3rd Cir.), *cert. denied,* 355 U.S. 882 (1957). For a good discussion of the tort-contract question in a variety of areas see Comment, *Exemplary Damages in Contract Cases,* 7 WILLAMETTE L. J. 137 (1971).

7. W. PROSSER, SELECTED TOPICS ON THE LAW OF TORTS 380 (1954).

rule for determining the classification of these borderland actions.[8] A case may be classified as a contract action for one purpose and as a tort action for another.[9] This flexibility leads to a greater probability of differing results on an issue such as the classification of an action for the nonpayment of insurance benefits.

Although there has been no special historical development in the area of insurer-insured relationships, the majority of jurisdictions that have considered the classification of nonpayment of benefits have classified it as a breach of contract action for traditional contract damages.[10] Although classifying the action as one for breach of contract, the Washington Supreme Court is one of only a few courts which nevertheless have taken an expansive view of foreseeable damages in allowing recovery for such elements as pain and suffering.[11] However,

8. *Id.* at 430-36. Prosser suggests a misfeasance-tort, nonfeasance-contract dichotomy, with numerous exceptions. *Id.* at 387-442. Some courts have held that if the action cannot be maintained without pleading and proving the contract, then the action is one for breach of contract. *See, e.g.,* Phillips v. Wick, 288 S.W.2d 899 (Tex. Ct. App. 1956). Other courts look for the gravamen of the complaint. *See, e.g.,* Quitmeyer v. Theroux, 144 Mont. 302, 395 P.2d 965 (1964). Still others permit the plaintiff to make a choice. *See, e.g.,* Eads v. Marks, 39 Cal. 2d 807, 249 P.2d 257 (1952). Many classifications are made on the basis of particular historical developments, such as the special duties of common carriers. P. WINFIELD, THE PROVINCE OF THE LAW OF TORT 60-62 (1931).

9. W. PROSSER, LAW OF TORTS § 92, at 621-22 (4th ed. 1971); Guest, *Tort or Contract?*, 3 U. MALAYA L. REV. 191, 222 (1961); Thornton, *The Elastic Concept of Tort and Contract as Applied by the Courts of New York,* 14 BROOK. L. REV. 196 (1948).

10. The traditional measure of contract damages limits recovery to policy benefits plus interest. Comment, *Damages Assessed Against Insurers for Wrongful Failure to Pay,* 10 WM. & MARY L. REV. 466, 467 (1968). Of factual similarity to *Fletcher* was Hass v. Pacific Mut. Life Ins. Co., 70 Ohio App. 322, 41 N.E.2d 263 (1941), where the plaintiff sued for mental suffering and related economic loss following nonpayment on a disability policy. The action was found to be at contract, and damages were limited to the policy benefits plus interest. Other cases considering the nonpayment of benefits all make the same classification. Blackman v. Independent Life & Accident Ins. Co., 299 S.C. 54, 91 S.E.2d 709 (1956) (life insurance); Scottish Union & Nat'l Ins. Co. v. Bejcy, 201 F.2d 163 (6th Cir. 1953) (fire insurance); Liberty Nat'l Life Ins. Co. v. Stringfellow, 38 Ala. App. 594, 92 So.2d 924 (1956) (burial insurance).

11. In effect, the Washington court has closed the hiatus between proximate results and foreseeable results. In Wilkins v. Grays Harbor Community Hosp., 71 Wn.2d 178, 427 P.2d 716 (1967), the plaintiff brought a breach of contract action on a medical service contract. The defendant insurer had refused to permit exploratory surgery covered by the contract. A nine-month delay in surgery resulted in added damage from stomach cancer and additional pain and suffering. Rather than limit the damages to the proven medical expense of $3,734 that was owed on the contract, the court permitted an additional $40,000 for pain and suffering and other general damages. The court reasoned that such damages were foreseeable at the time of contracting.

A few other courts have reached the same result with a liberal application of foreseeability. Miholevich v. Mid-West Mut. Auto. Ins. Co., 216 Mich. 495, 246 N.W. 202 (1933). Pennslyvania Threshermen & Farmers' Mut. Cas. Ins. Co. v. Messenger, 29 A.2d 653 (Md. Ct. App. 1943). The California courts have taken tentative steps toward a more liberal application of the foreseeability rule, although not in the nonpayment of

punitive damages are not available in Washington.[12] Some states have classified it as a breach of contract but have used statutes to supplement damages with attorney's fees and a percentage penalty.[13] None of these authorities was presented to the court,[14] and *Fletcher* became the first case in which such an action was classified as a tort.[15]

II. THE COURT'S RATIONALE

The court's conclusion that the action sounded in tort[16] seems to

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benefits area. Comment, *Recovery for Mental Anguish from Breach of Contract: The Need for an Enabling Statute*, 5 CALIF. WESTERN L. REV. 88 (1968).

12. *See* note 2, *supra*.

13. 3 J. APPLEMAN, INSURANCE LAW AND PRACTICE §§ 1601-05 (1967). California's only statute in the area limits liability to the amount stated in the policy. CAL. INS. CODE § 10111 (West 1955). There is no indication that this applies to tort actions involving an insurance policy. Wetherbee v. United Ins. Co., 265 Cal. App. 2d 921, 71 Cal. Rptr. 764 (1968).

14. Opening Brief for Appellant, Brief for Respondent, and Reply Brief for Appellant, Fletcher v. Western Nat'l Life Ins. Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970).

15. One other decision may have considered this a tort action. Federal Life Ins. Co. v. Frazer, 192 Ind. 565, 137 N.E. 273 (1922). The court did not discuss the borderland issue, but added 5% damages to the award. This might have been a penal sum indicative of a tort. However, the court's holding that the judgment was affirmed *as of the date of submission of the case* suggests a contract action with 5% interest. A statute permitting up to 8% interest on judgments supports such an analysis. IND. ANN. STAT. § 19-12-102 (1964).

The California courts previously had not directly considered the tort-contract issue in the context of an action for nonpayment of benefits. In Reichert v. General Ins. Co., 68 Cal. 2d 882, 69 Cal. Rptr. 321, 442 P.2d 377 (1968), the plaintiff had originally pleaded tort elements to his suit for damages caused by nonpayment of fire insurance. His amended complaint, however, dropped those elements. As *Fletcher* noted, the majority and dissent in *Reichert* seemed to assume the action was for breach of contract, but never directly considered the issue. *Fletcher*, 10 Cal. App. 3d at 402, 89 Cal. Rptr. at 94.

Wetherbee v. United Ins. Co., 265 Cal. App. 2d 921, 71 Cal. Rptr. 764 (1968), had considered the defense that nonpayment of insurance benefits was a breach of contract action with damages limited to policy benefits. The court permitted tort damages for *fraudulent inducement* of the plaintiff to enter into the contract, thereby avoiding the nonpayment problem.

16. The court considered this the most troublesome aspect of the case. *Fletcher*, 10 Cal. App. 3d at 400, 89 Cal. Rptr. at 92. However, the issue was neither identified as a borderland question nor analyzed with borderland principles, probably because none of the briefs presented such an approach.

The issue was further obscured because the defendant presented it as a question of causation, asking the court to consider two aspects of its conduct separately when determining actual causation. The defendant asked that two threatening letters be considered as one aspect of its conduct and the non-payment of benefits as a separate aspect.

The defense was willing to concede that the *letters* were potentially tortious conduct, but argued that they caused no actual injury. It then contended that the *nonpayment of benefits* was the only conduct that might have caused harm. But this conduct, they argued, was a breach of contract and could not be the basis of a tort.

depend entirely on an extension of *Crisci v. Security Insurance Co.*[17] In *Crisci,* the California Supreme Court held that an insurer owes its insured an implied-in-law duty of good faith and fair dealing to do nothing to deprive the insured of the benefits of the policy.[18] In the case of a liability insurer this includes the duty to act reasonably and in good faith to settle claims against the insured by third parties. Violation of that duty sounds in tort.[19] After discussing *Crisci,* the *Fletcher* court extended these principles to the disability insurance case before it.[20] In meeting the contract argument the court applied the rule that when conduct clearly constitutes a breach of contract the court will not be precluded from further inquiry into the defendant's conduct. If that conduct was tortious a tort action will lie.[21] The court in *Fletcher* had little difficulty finding the familiar tort of "intentional infliction of emotional distress."[22]

It has been suggested that the court held that a tort of intentional infliction of emotional distress was not applicable.[23] However, on close analysis it appears that the court did apply such a tort.[24] This

17. 66 Cal. 2d 425, 58 Cal. Rptr. 13, 426 P.2d 173 (1967).
18. *Id.,* 58 Cal. Rptr, at 16-17, 426 P.2d at 176-77.
19. *Id.,* 58 Cal. Rptr. at 16, 18, 426 P.2d at 176, 178.
20. *Fletcher,* 10 Cal. App. 3d at 401-02, 89 Cal. Rptr. at 93-94:
> We think that, similarly, 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. We think that, as in *Crisci,* the violation of that duty sounds in tort notwithstanding that it also constitutes a breach of contract.

21. Although such a rule has not been articulated, it seems implicit in the basic analysis of borderland cases. *See* Eads v. Marks, 39 Cal. 2d 807, 249 P.2d 257 (1952). *See also* note 6 and accompanying text, *supra.*
22. *Fletcher,* 10 Cal. App. 3d at 401-02, 89 Cal. Rptr. at 93-94:
> We hold, therefore, that defendants' threatened and actual bad faith refusals to make payments under the policy, maliciously employed by defendants in concert with false and threatening communications directed to plaintiff for the purpose of causing him to surrender his policy or disadvantageously settle a nonexistent dispute is essentially tortious in nature and is conduct that may legally be the basis for an action for damages for intentional infliction of emotional distress.

23. *See* 4 Loyola (L.A.) L. REV. 208, 215 (1971). Apparently this analysis is based on the belief that the court used "may" in a sense of probability rather than in a permissive sense when it said: "[D]efendants' threatened and actual bad faith refusals to make payments . . . is conduct that *may* legally be the basis for an action for damages for intentional infliction of emotional distress." *Fletcher,* 10 Cal. App. 3d at 401, 89 Cal. Rptr. at 93 (emphasis added).
24. In context it is likely that the court made a positive holding rather than an equivocation. The defense had argued that even if there was a prima facie case of intentional infliction of emotional distress, the breach of contract element would preclude finding a tort. *See* note 16, *supra.* In essence they were saying, "This conduct *may not* be

tort had not previously been used for nonpayment of benefits,[25] but *Fletcher's* extreme facts made it a likely setting for an extension. The tort has been a growing protection for peace of mind in various fields;[26] *Fletcher* simply extended it into a new area.

Rather than base its decision solely on the intentional infliction of emotional distress, the court identified a second tort of "interference with a protected property interest."[27] A tort of this name was neither presented at trial nor discussed in the briefs. It has been suggested that *Fletcher* developed a new, unlitigated tort which was not argued on appeal.[28]

A better analysis is that "interference with a protected property interest" was used as a generic name covering a wide class of injuries to property,[29] just as "interference with the person" covers a wide class of injuries to people.[30] Although never identified, the specific tort in *Fletcher* which falls within the general class seems to be a breach of an implied-in-law duty of good faith and fair dealing identified in *Crisci*.

The *Fletcher* court had laid the groundwork for such an extension

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the basis for a tort." The court resolved the matter by saying that indeed it *may* be the basis for a tort.

The key sentence began: "We *hold* therefore . . . ." *Fletcher*, 10 Cal. App. 3d at 401, 89 Cal. Rptr. at 93 (emphasis added). If the court had simply meant to discuss probabilities, it would have included its remarks in general discussion rather than in the holding. Further support for this analysis comes from the extensive space devoted to a discussion of this tort both before and after the holding. *Id.* at 394-401, 403, 89 Cal. Rptr. at 88-92, 95.

25. Intentional infliction of emotional distress has been applied in the area of settlement practices, but never for simple nonpayment of benefits. *See* Annot., 39 A.L.R.3d 739,767-73 (1971).

26. W. PROSSER, LAW OF TORTS § 12 (4th ed. 1971).

27. We further hold that, independent of the tort of intentional infliction of emotional distress, such conduct on the part of a disability insurer constitutes a tortious interference with a protected property interest of its insured for which damages may be recovered to compensate for all detriment . . . .

Fletcher, 10 Cal. App. 3d at 401, 89 Cal. Rptr. at 93. It is not clear why the court went on to make this dual holding. It may have done this out of uncertainty over the validity of finding intentional infliction of emotional distress. *See* note 23, *supra*. Or it may have done this out of a desire to extend greater protection to insureds. *See* note 58 and accompanying text, *infra*. The court suggested that it did this to gain greater respect for the law and the judicial process by emphasizing economic rather than emotional injury. *Fletcher*, 10 Cal. App. 3d at 402, 89 Cal. Rptr. at 94.

28. *See* 4 LOYOLA (L.A.) L. REV. 208, 225 (1971).

29. Prosser classifies various torts, including trespass to land, trespass to chattels, and conversion, as "interference with property." W. PROSSER, LAW OF TORTS §§ 13-15 (4th ed. 1971). Such a broad category might also include torts involving intangible economic property such as injurious falsehood and interference with contractual relations.

30. *Id.* §§ 7-12.

of *Crisci* when it reasoned that the duty of good faith and fair dealing extended to disability insurers in general.[31] An analysis of the probable elements of the "new" tort suggests that they are similar to the elements in *Crisci*.[32] The only explanation for this tort was that it appropriately placed the emphasis on economic loss, which is consistent with the emphasis in *Crisci*.[33] If such an analysis is correct, this "new" tort is not new after all.

Two lines of reasoning were employed in *Fletcher* to support an extension of this "new" tort into the disability insurance field. The first was based on the similarity of *Crisci* to the present case.[34] The second was based on an analogy to the interference with contractual relations.[35] Both of these are weak support for such an extension.

The belief that the situation in a liability settlement dispute is similar to the situation in a disability payment dispute fails to recognize a fundamental difference in the relationships involved. There is an implied duty of good faith and fair dealing in *Crisci* and other settlement dispute cases only because the insurer has complete control of the insured's rights and therefore stands in an almost fiduciary role.[36] A disability insurer has control of no such rights; he stands more in an adversary role. An extension of the duty may be sound policy, but it is a far-reaching extension to make without consideration of such a fundamental difference.

The second rationale, that of an analogy to intentional interference

31. *Fletcher*, 10 Cal. App. 3d at 401, 89 Cal. Rptr. at 93.

32. In *Crisci*, as in *Fletcher*, it was the insurance company's failure to give the insured the protection for which he contracted that constituted tortious conduct. One difference was that there had to be a bad faith refusal in *Fletcher*, while in *Crisci* the standard was reasonableness. *Crisci*, 58 Cal. Rptr. at 16-17, 426 P.2d 176-77. *See* text accompanying note 60, *infra*.

33. *Fletcher*, 10 Cal. App. 3d at 402, 89 Cal. Rptr. at 94. The primary injury emphasized in *Crisci* was the loss of the benfits of the policy. *Crisci*, 58 Cal. Rptr. at 16, 426 P.2d at 176. *Fletcher* extended this to the disability insurer: "[T]he 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*." *Fletcher*, 10 Cal. App. 3d at 401, 89 Cal. Rptr. at 93 (emphasis added).

34. *Fletcher*, 10 Cal. App. 3d at 401, 89 Cal. Rptr. at 93.

35. *Id.* at 402-03, 89 Cal. Rptr. at 94-95.

36. The *Crisci* line of authority goes back to Keeton, *Liability Insurance and Responsibility for Settlement*, 67 HARV. L. REV. 1136 (1954), which noted that the duty is based on the special relationship involving exclusive control by the insurer. *Crisci*, 58 Cal. Rptr. at 18, 426 P.2d at 178. Other jurisdictions have noted that the special duty of a liability insurer is based on a fiduciary or agent role. Tyler v. Grange Ins. Ass'n, 3 Wn. App. 167, 473 P.2d 193 (1970). Aetna Cas. & Sur. Co. v. Kornbluth, 28 Colo. App. 194, 471 P.2d 609 (1970).

with contractual relations, is also weak. It is true that a stranger to the contract would have been liable in tort for interfering with the contractual relations of the insured, and at first glance it does seem persuasive that a party to a contract should not be held to a lesser standard of conduct than a stranger. But application of such reasoning would make a party to any contract a potential defendant at tort for breach of the contract.[37] To the contrary, the law has drawn a valid distinction between a breach of contract by one of the contracting parties and a breach induced by a third party.[38]

Although the court's rationale for the *Crisci* extension is weak, the extension is partially justified by an analysis of the special insurer-insured relationship that the court discussed in another context.[39] An implied covenant of good faith and fair dealing may be applicable due to the great disparity in the economic situations and bargaining abilities of the parties. The *Fletcher* court noted that:[40]

> These considerations are particularly cogent in disability insurance. The very risks insured against presuppose that if and when a claim is made, the insured will be disabled and in strait financial circumstances and, therefore, particularly vulnerable to oppressive tactics on the part of an economically powerful entity.

Such factors suggest the judicial implication of a covenant of good faith and fair dealing even without a fiduciary relationship.[41]

37. 4 LOYOLA (L.A.) L. REV. 208, 227 (1971).

38. A party to a contract cannot be a defendant for interference with contractual relations. W. PROSSER, LAW OF TORTS § 129 (4th ed. 1971). To change that rule would eradicate the rule of damages unique to contract law. Canister Co. v. National Can Corp., 96 F. Supp. 273 (D. Del. 1951).

There are significant differences between the insured-insurer and insured-stranger relationships. If the insured cannot set the contractual rights and liabilities, at least he can choose the insurer with whom he deals. There is no such control over the insured's relationship with a stranger. The insured already has a breach of contract remedy against the insurer; a tort action is needed for protection against a stranger.

39. The court noted the rule that a special relationship of parties may be significant in finding a tort of intentional infliction of emotional distress and that insurance companies stand in such a relationship to their insureds. *Fletcher*, 10 Cal. App. 3d at 403-04, 89 Cal. Rptr. at 95.

40. *Id.* at 404, 89 Cal. Rptr. at 95.

41. The quasi-public nature of the insurance industry has led to creation of a special duty owed to third parties injured by insureds holding liability policies. Barrera v. State Farm Mut., 71 Cal. 2d 659, 79 Cal. Rptr. 106, 456 P.2d 674 (1969).

III. THE NEW RULE AND PUBLIC POLICY

Although the court did not touch upon them, there are strong policy reasons to hold an insurance company liable at tort for a bad faith refusal to pay an insured. The insured public benefits from the greater capability of a tort measure of damages both to compensate the insured and to deter companies from denying future claims. Contract damages are inadequate in both respects.

The insured who has been injured by a wrongful failure to pay is inadequately compensated when limited to a contract action due to the requirement that damages be reasonably foreseeable at time of contract.[42] The usual application of this rule means that there can be no recovery for the very losses the insured hoped to avoid.[43] One solution is a reasonable expansion of contract damages as is the situation in Washington.[44] The more comprehensive solution is to use the tort measure of damages allowing compensation for all injuries.[45]

A further policy advantage of tort damages is their ability to deter future bad faith nonpayments through the use of punitive damages in those jurisdictions which permit them. Without compensatory or punitive damages the insurer has little to lose by denying claims of persons whom it believes can be overcome by pressure.[46] The defendant's employee in *Fletcher* claimed that he would do the same thing again with similar facts.[47] Punitive damages would remedy such practices.[48]

42. *See* note 2, *supra*.

43. *See* note 10, *supra*. The injustice of applying the rule by limiting damages to policy benefits is seen in Scottish Union & Nat'l Life Ins. Co. v. Benjcy, 201 F.2d 163 (6th Cir. 1953). There was evidence that following the nonpayment of benefits the insured became ill, suffered loss of time and money, incurred medical expenses, and suffered mental anguish. The court reversed a jury verdict awarding special damages, ruling that damages must be limited to the policy benefits plus interest.

44. *See* note 11, *supra*.

45. Use of the tort measure of damages would compensate for all the injuries proximately caused by the defendant's conduct, including those injuries that could not reasonably be called foreseeable. This would avoid tortured extensions of the concept of foreseeability.

46. If the insured fails to act after denial of payment, the company pays nothing. If the insured goes to court and wins a contract action, the company will only have to pay the policy benefits. To save trial costs it can always admit its liability at the last minute, as the company tried to do in *Fletcher*. *Fletcher*, 10 Cal. App. 3d at 385, 89 Cal. Rptr. at 82. An insurer would not be concerned about extraneous factors such as losing a renewal on someone like Mr. Fletcher.

47. *Fletcher*, 10 Cal. App. 3d at 408-09, 89 Cal. Rptr. at 99.

48. The *Fletcher* decision itself had an impact within the insurance industry. Letter from Corporate Headquarters, Uniguard Insurance Group, to Claims Managers, Nov.

The experience of at least one state with a statute governing bad faith nonpayments suggests that there is significant abuse.[49] It is logical to expect more abuse in those states which permit companies to employ such practices with impunity. New solutions such as *Fletcher* are necessary to aid those who are injured and to deter those who injure them.

If adopted elsewhere, *Fletcher's* impact would be greatest in those states that currently restrict damages to the policy limits in cases of nonpayment.[50] States like Washington which permit a wide measure of contract damages would be less affected,[51] as would those states that supplement contract damages by statute.[52] Analysis of the elements of the two *Fletcher* torts suggests that each has potential application in particular kinds of cases.

Presumably the tort of *intentional infliction of emotional distress* could apply whenever the prima facie case was met. This would require: outrageous conduct, intention or recklessness, extreme emotional distress, and actual and proximate causation.[53] The fact pattern of each instance of nonpayment should be examined to determine if it has these elements. The principle limitations of this tort are the requirements of outrageous conduct and extreme emotional harm. Wrongful failures to pay are often less than outrageous and result in economic rather than emotional harm.[54] Beyond the nonpayment of benefits cases, it seems likely that this tort could be used by third parties injured by liability policy holders.[55] However, an insurer might

25, 1970, a copy of which is on file with the *Washington Law Review*. The letter discusses *Fletcher* and points out the need for continued vigilance to avoid acts of bad faith that might lead to compensatory or punitive damages.

49. Clark Center, Inc. v. National Life & Accident Ins. Co., 245 Ark. 567, 433 S.W.2d 151 (1968).

50. *See* note 10, *supra*.

51. *See* notes 11 and 45, *supra*.

52. *See* note 13, *supra*.

53. *Fletcher*, 10 Cal. App. 3d at 394, 89 Cal. Rptr. at 88. A fifth element, privilege, is best viewed as a defense. It permits the insurer to deny or attempt to settle questionable claims. A company is privileged to perform acts that will cause emotional distress as long as it acts in good faith and in a reasonable manner. Privilege will not arise if there is not a good faith dispute, since the law does not encourage settlement of nonexistent disputes. *Id.* at 396, 89 Cal. Rptr. at 89-90.

54. One of the losses in *Fletcher* was real estate on which payments could not be maintained. *Fletcher*, 10 Cal. App. 3d at 393, 89 Cal. Rptr. at 88. If this were the only injury, intentional infliction of *emotional* distress would not be available as an action.

55. The determinative factor should be whether or not the prima facie case was met. Third parties suing because of nonpayment on liability policies would often be unsuccessful due to the defense of privilege, which arises when a claim is in legitimate dispute. The courts favor settlement negotiations in such cases. *Id.* at 395, 89 Cal. Rptr. at 89.

not be held to as high a standard of care as when dealing directly with an insured.[56]

The tort of *interference with a protected property interest* will be applicable only for an insured's actions for nonpayment of benefits, since it is based on the duty of good faith and fair dealing that arises out of the contract.[57] Within that area, however, it has potential for much broader application than the tort of intentional infliction of emotional distress because it requires neither extreme conduct nor severe emotional harm.[58] Based on its use in *Fletcher,* the required pattern probably is an intentional or reckless, bad faith refusal to pay insurance benefits when such refusal proximately causes injury to the insured.[59] The requirement of bad faith will exclude the great majority of wrongful nonpayments.[60] However, such a requirement might eventually be dropped, as it has been by some statutes.[61] It is likely that this tort will be adopted in other jurisdictions. A majority of states currently recognize a duty of good faith and fair dealing in the settlement area of liability insurance and most classify violation of that duty as a tort.[62] Just as *Fletcher* extended *Crisci,* other courts can make an extension to cover nonpayment of insurance benefits.[63]

Neither intentional infliction of emotional distress nor interference with a protected property interest should be limited to the *disability*

56. The standard of care in the nonpayment of benefits cases is based directly on the insurer-insured relationship. *Id.* at 403, 89 Cal. Rptr. at 95. A third party lacks such special consideration.

57. A similar duty of good faith and fair dealing does not arise without a contract. Consequently, third parties negotiating on a liability policy could not use this tort.

58. Indeed, the reason the court gave for using this tort was to place emphasis on *economic* injury. *Fletcher,* 10 Cal. App. 3d at 402, 89 Cal. Rptr. at 94.

59. *Id.* at 401-02, 89 Cal. Rptr. at 93-94. Since bad faith is an element, the defense of privilege is unnecessary. A company only has a privilege to engage in settlement practices when there is a good faith dispute. *Id.* at 395-96, 89 Cal. Rptr. at 89-90.

60. 3 J. APPLEMAN, INSURANCE LAW AND PRACTICE § 1612 (1967).

61. In the settlement of liability claims a standard of reasonableness is now used, but eventually it may be replaced by a strict liability standard. *Crisci,* 58 Cal. Rptr. 17, 426 P.2d 177. Comment, *Crisci's Dicta of Strict Liability for Insurer's Failure to Settle: A More Rational Settlement Behavior,* 43 WASH. L. REV. 799 (1968). Already three states do not require bad faith as a condition precedent to applying punitive statutes in the nonpayment of benefits area. 3 J. APPLEMAN, INSURANCE LAW AND PRACTICE § 1612 (1967).

62. *See Annot.,* 40 A.L.R. 2d 168 (1955).

63. It is clearly established in Washington that liability insurers have a duty of good faith to settle claims against insureds. Violation of that duty sounds in tort. Murray v. Mossman, 56 Wn.2d 909, 355 P.2d 985 (1960). Tyler v. Grange Ins. Ass'n, 3 Wn. App. 167, 473 P.2d 193 (1970). These cases could be the basis for a Washington decision similar to *Fletcher.*

insurance area. The special relationship and position of the parties is the same in most kinds of insurance. Almost by definition, insurance of any sort is purchased in recognition of the weakened position that a particular type of misfortune may create.

With the development of "no fault" systems many more people will soon be dealing with their own insurance companies in an adversary relationship. Inevitably a few insurers will use their excessive power to force unfair settlements on their insureds. The tort remedies of *Fletcher* will provide aid for those injured by such practices and also deter such practices in the future.