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STILLBORN PROTECTION AGAINST INSURERS’ BAD FAITH PRACTICES: THE FAILURE OF ILLINOIS’ PRIVATE ENFORCEMENT MECHANISM

William M. Shernoff
and
Marian Haycock Tully*

Both Illinois and California have strongly worded, specific statutes aimed at controlling unfair insurance practices. California has developed a sophisticated and effective method for private enforcement of the prohibited practices; Illinois has not. This article reviews Illinois law in light of California decisions, and determines that there is a pattern by which to predict the development of bad faith insurance law in Illinois. While the Illinois appellate courts have been active in this area, the Illinois Supreme Court has issued only one decision.¹ This article compares Illinois appellate decisions with California decisions, and focuses on the effect that Illinois Insurance Code section 767² has on the recovery of punitive damages and the causes of action that are potentially successful.

I. A PRIVATE REMEDY FOR AN INSURER’S VIOLATION OF ITS STATUTORY DUTY

A. The Illinois and California Unfair Practices Acts

Illinois’ Unfair Methods of Competition and Unfair and Deceptive Acts and Practices Act¹ and California’s Unfair Claims Settlement Practices

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1. Conway v. Country Cas. Ins. Co., 92 Ill. 2d 388, 442 N.E.2d 245 (1982). Conway was not a landmark decision and addressed only two narrow issues:

   whether the insurer’s payment to the extent of the liability limits of its policy to the claimant discharges its duty under the policy to defend its insured in the personal injury action; if not, whether the insured can recover the amount he pays in excess of the liability limits of the policy to settle a suit by the claimant; and, if the insurer’s duty to defend is part of the damages awarded.

Id. at 393, 442 N.E.2d at 246. When the court decided Conway, the intermediate appellate courts were split on several much broader questions.

2. ILL. REV. STAT. ch. 73, § 767 (1983).

3. ILL. REV. STAT. ch. 73, §§ 1028-1041 (1985).
Act are based on model legislation drafted by the National Association of Insurance Commissioners, entitled "An Act Relating to Unfair Methods of Competition and Unfair and Deceptive Acts and Practices in the Business of Insurance" (Model Act).

The Model Act was amended in 1972 to include fourteen different unfair claims settlement practices. California and Illinois adopted most of the model provisions. Both states added to the Model Act; however, Illinois has, literally, a more far-reaching statute than California.

Section 790.03(h) of the California Insurance Code lists thirteen prohibited practices from the Model Act. The California Code also prohibits insurers from "directly advising a claimant not to obtain the services of an attorney," and from "misleading a claimant as to the applicable statute of limitations." Section 766.6 of the Illinois Insurance Code, "Acts constituting improper claims practices," did not adopt two sections from the Model Act that California adopted. These two sections prohibit:

Making known to insureds or claimants a policy of appealing from arbitration awards in favor of insureds or claimants for the purpose of compelling them to accept settlements or compromises less than the amount awarded in arbitration; and

Failing to promptly settle claims, where liability has become reasonably clear, under one portion of the insurance policy coverage in order to influence settlements under other portions of the insurance policy coverage.

However, the Illinois Insurance Code includes sections that prohibit:

Engaging in activity which results in a disproportionate number of meritorious complaints against the insurer received by the insurance department;

Engaging in activity which results in a disproportionate number of lawsuits to be filed against the insurer or its insured by claimants;

... Failing to provide forms necessary to present claims promptly and with such explanations as are necessary to use them effectively.

These provisions impose broader duties than those described in the California Insurance Code. Illinois also has a "catch-all" provision that prohibits "[e]ngaging in other acts which are in substance equivalent to any of the foregoing."
Both Illinois and California authorize a remedy for unfair practices through the state insurance commissioner. The effectiveness of this remedy in the overall control of unfair practices is doubtful. Consequently, many states have adopted some form of private enforcement. Neither the California nor the Illinois Act expressly authorizes a private remedy. The California Supreme Court, however, recognizes a private cause of action available to both insureds and third-party claimants against insurers for conduct prohibited by the California Unfair Practices Act. The Illinois Supreme Court has not decided whether there is a cause of action for violation of its Unfair Practices Act. The Illinois appellate courts have refused to recognize a civil remedy available to either an insured or a third-party claimant for the insurer's violation of the Act.

B. The California Interpretation

California courts permit an insured to sue an insurance carrier, not only for breach of the insurance contract, but also for violations of the Unfair Practices Act. Since the Act governs the insurance industry for the benefit of citizens affected by unfair practices, California also permits a claimant who is not a named insured to bring an action against an insurance carrier. To further encourage compliance with the act, California permits recovery of compensatory and punitive damages from an insurance carrier that knowingly commits an unfair practice or commits a general business practice in violation of the Act.

14. The claims practices described and prohibited by the Model Act, with the additional prohibited practices of each state, will generally be referred to as unfair practices. The statutes will generally be referred to as the Unfair Practices Acts.


17. Id. at § 6.04(2)(a). See also S. Ashley, Bad Faith Actions: Liability and Damages § 9.03 (1984) (discusses private causes of action under various states' unfair claims settlement practices statutes).


23. Id.

24. Id.
In *Greenberg v. Equitable Life Assurance Society*, a California intermediate appellate court recognized that an insured has a civil remedy for violation of the California Unfair Practices Act. In *Greenberg*, the plaintiffs sought damages in a class action for the insurance company's alleged unfair practice of requiring a home loan borrower to purchase whole life insurance at a fixed rate. The court found that this "tie-in" agreement violated §790.03(c), which prohibits "unreasonable restraint of, or monopoly in, the business of insurance." The court held:

While the Insurance Code in sections 790.04 through 790.08 provides for administrative enforcement of statutes governing insurance companies, including section 790.03, Insurance Code section 790.09 states in pertinent part: "No order to cease and desist issued under this article directed to any person . . . shall in any way relieve or absolve such person from any civil liability . . ." Section 790.09 thus contemplates a private suit to impose civil liability irrespective of governmental action against the insurer for violation of a provision of the Insurance Code. The fair construction is that the person to whom the civil liability runs may enforce it by an appropriate action.

The separate nature of the civil remedy was reinforced in *Shernoff v. Superior Court*. In the lower court, the plaintiffs sought damages in a class action suit against title insurers, alleging a conspiracy to fix title insurance rates. The court ordered a stay intended to allow the insurance commissioner to investigate the plaintiffs’ allegations. The appellate court found that since the insurance commissioner’s disciplinary authority was limited to restraint of future illegal conduct, the plaintiffs’ civil remedy for damages from past acts was not precluded. The District Court of Appeal issued a writ of mandate to dissolve the stay order.

The California Supreme Court followed the reasoning of both *Greenberg* and *Shernoff* in its landmark decision in *Royal Globe Insurance Co. v. Superior Court*. The effect of *Royal Globe* has been felt nationwide.

26. CAL. INS. CODE § 790.03(c) (West 1972).
27. *Id.* The section prohibits "[e]ntering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance."
28. *Greenberg*, 34 Cal. App. 3d at 1000-01, 110 Cal. Rptr. at 475 (quoting CAL. INS. CODE § 790.09 (West 1972)).
30. "‘No rule of exhaustion of administrative remedies precludes processing of a civil claim without resort to an administrative procedure which is irrelevant to the claim.’ *Id.* at 410, 118 Cal. Rptr. at 682 (quoting *Greenberg*, 34 Cal. App. 3d at 1000-01, 110 Cal. Rptr. at 475).
33. 23 Cal. 3d 880, 592 P.2d 329, 153 Cal. Rptr. 842 (1979). The court reasoned that prior cases allowing private causes of action under § 790 should be followed to allow a private litigant to bring suit under § 790.09.
34. See *Shernoff*, supra note 16.
The plaintiff in *Royal Globe* filed an action for personal injuries incurred in a fall at a grocery. She joined the market's liability carrier, Royal Globe Insurance Company, and an independent adjuster, Robert E. Hunt Company, as defendants. The plaintiff sued for violations of subdivisions (h)(5) and (h)(14) of the Unfair Practices Act, specifically for "[n]ot attempting in good faith to effectuate prompt, fair and equitable settlement of claims in which liability has become reasonably clear, [and] . . . [d]irectly advising a claimant not to obtain the services of an attorney." Royal Globe held that a private litigant has standing to bring a civil action for violation of the Unfair Practices Act. The court looked first to the language of the Act:

Section 790.09 provides that a cease and desist order issued by the Commissioner under the provisions of the act shall not absolve an insurer from "civil liability or a criminal penalty under the laws of this state arising out of the methods, acts or practices found unfair or deceptive." This provision appears to afford to private litigants a cause of action against insurers which commit the unfair acts or practices defined in subdivision (h).

Civil liability under the Act accrues to both insureds and third-party claimants. "[A]n examination of the language of subdivision (h) demonstrates that it was intended to prohibit unfair settlement practices by insurers directed against both claimants and insureds." The California Supreme Court clearly recognized that claims practice regulation is designed to protect those affected by unfair practices. For example, the

35. CAL. INS. CODE § 790.03(h)(5), (14) (West Supp. 1986).
36. 23 Cal. 3d at 886, 592 P.2d at 333, 153 Cal. Rptr. at 846.
37. Id. at 885, 592 P.2d at 332, 153 Cal. Rptr. at 845 (emphasis in original). The court emphasized that § 790.09 differed from the Model Act, which provides that an insurer shall not be absolved of liability under any "other" state laws. The California statute omits the word "other." The California Supreme Court reasoned that this omission indicated the legislature's intent that civil liability on the part of the insurer would arise not only from other laws of the state, but also from the Unfair Practices Act itself. Id.
38. Id. at 888, 592 P.2d at 334, 153 Cal. Rptr. at 847. To clarify its analysis, Royal Globe distinguished a California appellate court ruling in Murphy v. Allstate Ins. Co., 17 Cal. 3d 937, 553 P.2d 546, 132 Cal. Rptr. 424 (1976). In that case, the court held that a third-party claimant who had recovered a judgment against the insured for an amount in excess of the policy limits could not sue an insurer for breach of the duty to settle without an assignment of the insured's cause of action. Id. The theory of recovery in Murphy was based on "contractual principles" and not statutory violations. In Royal Globe, the court stated:

In the present case, the plaintiff does not seek to rely upon the violation of the insurer's duty to its insured to settle plaintiff's claim. Rather, she relies upon the insurer's duty owed to her as a claimant under subdivisions (h)(5) and (h)(14) of § 790.03, a duty created by the statutory provisions and owed directly to plaintiff as a claimant.

23 Cal. 3d at 890, 542 P.2d at 334, 153 Cal. Rptr. at 848.
Department of Insurance investigates complaints from both insureds and third parties as part of its enforcement powers under the Act.\textsuperscript{39}

\textit{Royal Globe} also clarified the type of conduct that leads to statutory liability. The court rejected the defendant's argument that an action must be "committed with such frequency as to indicate a general business practice."\textsuperscript{40} The statute prohibits "knowingly committing or performing with such frequency as to indicate a general business practice,"\textsuperscript{41} any of a number of unfair claims settlement practices. The court followed a suggestion by the California Trial Lawyers Association in an amicus curiae brief:

\begin{quote}
[T]he language quoted provides for two alternative methods by which the prohibited acts may be shown, i.e., a violation of the subdivision occurs if the prohibited acts are knowingly committed on one occasion or, if knowledge cannot be established, then it will suffice if the acts were performed with such frequency as to indicate a general business practice.\textsuperscript{42}
\end{quote}

The statute itemizes unfair practices in both the singular and the plural.\textsuperscript{43} For example, subdivision (h)(5) proscribes misleading "a claimant as to the applicable statute of limitations."\textsuperscript{44} The California Supreme Court concluded that if a third-party claimant may sue an insurer under the statute, "it is inconceivable that the Legislature intended that such a litigant would be required to show that the insurer committed the acts prohibited by that provision 'with such frequency as to indicate a general business practice.'"\textsuperscript{45} The court concluded:

\begin{quote}
[T]o an aggrieved private litigant who can demonstrate that the insurer acted deliberately, the frequency of the insurer's misconduct and its application to others is irrelevant. Although the language of the statute is not clear, if the premise is accepted that a private party may bring an action for an insurer's violation of subdivision (h) under the rationale of \textit{Greenberg} and \textit{Shernoff}, then a single violation knowingly committed is a sufficient basis for such an action.\textsuperscript{46}
\end{quote}

\begin{itemize}
\item \textsuperscript{39} See \textit{Royal Globe}, 23 Cal. 3d at 889, 542 P.2d at 334, 153 Cal. Rptr. at 848. The court noted that the California Department of Insurance interpreted § 790.03(h) broadly enough to allow such private claims.
\item \textsuperscript{40} Id. at 890, 542 P.2d at 334, 153 Cal. Rptr. at 848.
\item \textsuperscript{41} \textit{CAL. INS. CODE} § 790.03(h) (West Supp. 1986).
\item \textsuperscript{42} \textit{Royal Globe}, 23 Cal. 3d at 890, 592 P.2d at 335, 153 Cal. Rptr. at 849.
\item \textsuperscript{43} See \textit{CAL. INS. CODE} § 790.03(h) (West Supp. 1986).
\item \textsuperscript{44} Id. at § 790.03(h)(5). This provision is one under which the \textit{Royal Globe} plaintiff sued.
\item \textsuperscript{45} \textit{Royal Globe}, 23 Cal. 3d at 891, 592 P.2d at 335, 153 Cal. Rptr. at 849 (quoting \textit{CAL. INS. CODE} § 790.03(h) (West Supp. 1986)).
\item \textsuperscript{46} Id. at 891, 592 P.2d at 335, 153 Cal. Rptr. at 849. The court ordered the trial court to enter judgment on the defendant's demurrer because the plaintiff had attempted to join both the insurer and the insured in the same lawsuit. The court held that an action against an insurer must be "concluded" before a bad faith action could arise. What constitutes a conclusion for the purpose of a \textit{Royal Globe} suit is still in conflict in the California appellate courts. See
\end{itemize}
C. The Illinois Interpretation

Unlike California, Illinois recognizes no cause of action for violation of the Unfair Practices Act to third-party claimants and severely limits actions brought by first-party insureds. Illinois courts specifically reject the California analysis.

In Scroggins v. Allstate Insurance Co., the plaintiff sued Allstate for "wrongful refusal to negotiate in good faith with plaintiffs, as claimants against Allstate's insureds." The Circuit Court of Cook County dismissed the allegation, and the First District Appellate Court affirmed. The appellate court held that "because the duty, though implied in law, arises out of the insurance contract relationship . . . it is clear that the duty is owed to the insured . . . ." The duty of good faith and fair dealing "is one which the insurer owes to its insured, not to third parties." Scroggins held that a third-party claimant has no standing to sue absent the insured's assignment of his cause of action against the insured.

Scroggins looked to the Illinois Unfair Practices Act and found that even under the statute, an insurer's duty runs only to its insureds. The

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48. 74 Ill. App. 3d 1027, 393 N.E.2d 718 (1st Dist. 1979).

49. Id. at 1029, 393 N.E.2d at 719. The underlying case involved an automobile collision.

50. Id. at 1030, 393 N.E.2d at 720 (citations omitted).

51. Id.

52. Id. But see Sheroff, supra note 16, at § 6.28:

In view of the general inadequacy of most administrative enforcement mechanisms to prevent statutory violations and the fact that such remedies provide no relief for the injured policyholder or claimant, the better view is that the insured or third party claimant should be permitted to maintain a private action for damages caused by such violations.

Id. (footnotes omitted).

53. Ill. Rev. Stat. ch. 73, §§ 766.5-766.6 (1983), provide:

Section 766.5. Improper claims practices.

It is an improper claims practice for any domestic, foreign, or alien company transacting business in this state to commit any of the acts contained in section [766.6] if:

(a) It is committed knowingly in violation of this act or any rules promulgated hereunder; or

(b) It has been committed with such frequency to indicate a persistent tendency to engage in that type of conduct.

Section 766.6. Acts constituting improper claims practices. Any of the following acts by a company, if committed without just cause and in violation of section [766.6], constitutes an improper claims practice:

(d) Not attempting in good faith to effectuate prompt, fair and equitable settlement of claims submitted in which liability has become reasonably clear.

Id.
court held that the plaintiffs failed to establish themselves as members of the "class of persons the statute is designed to protect."54 Although a similar contention had persuaded the California courts, Scroggins rejected the argument that a rule, promulgated by the Director of Insurance under the Unfair Practices Act, requiring insurance companies to "affirm or deny liability on first or third party claims within a reasonable time"55 demonstrated that the statute was designed to protect third-party claimants. The court stated:

While we agree that the statute and rule are apparently intended to cover third party as well as first party claims, plaintiffs' argument fails to recognize that the insurer's duty has always run to its insured in either context.56

Scroggins relied on the California decision in Murphy v. Allstate Insurance Co.,57 instead of Royal Globe.58 "The same court [which decided Royal Globe] unanimously held that the insurer's duty to settle runs to the insured and not to third party claimants."59 Scroggins cited another California appellate decision, which stated in dicta that "it would be 'rather a startling proposition' to hold that a statutory enactment of the duty to settle somehow extended to third party claimants."60 Reliance on Murphy v. Allstate Insurance Co.61 for this principle is unsound, because that case was not decided under the Unfair Practices Act; it was decided under a breach of contract theory.62

Although the Unfair Practices Act states that an insurer owes a duty to the third-party claimant, Illinois provides no civil remedy for the violation of this duty.63 To reach this conclusion, notwithstanding the plain words of the Act, Scroggins read one portion of the Act very narrowly.64 The Model Act and the act adopted by Illinois clearly apply to regulating the industry and not simply to governing the contract between the policyholder and the insurance company.65

54. Scroggins, 74 Ill. App. 3d at 1034, 393 N.E.2d at 723.
55. Id. at 1034, 393 N.E.2d at 723 (emphasis in original).
56. Id.
59. Scroggins, 74 Ill. App. 3d at 1036, 393 N.E.2d at 724 (emphasis in original).
60. Id. (quoting Scheuch v. Western World Ins. Co., 82 Cal. App. 3d 31, 145 Cal. Rptr. 294 (1978)).
62. Id. at 944, 553 P.2d at 588-89, 132 Cal. Rptr. at 428. See supra note 38 and accompanying text.
63. Scroggins, 74 Ill. App. 3d 1027, 393 N.E.2d 718 (1st Dist. 1979).
64. The Scroggins court distinguished Royal Globe in part because of the Illinois Act's retention of the word "other": "[t]he only comparable provision in our Insurance Code preserves 'other' and addresses itself only to 'liability under any other laws of this state.'" Id. at 1036, 393 N.E.2d at 724 (emphasis in original). See supra note 37 and accompanying text.
65. However, in Stamps v. Caldwell, 133 Ill. App. 2d 524, 273 N.E.2d 489 (1971), a third-
Scroggins noted that Royal Globe was a four-to-three decision, and cited Justice Richardson's dissent: "[If] the legislature had intended to change the course of [the] law 180 [degrees], and thereafter to impose upon carriers civil liability to injured third persons for failing to settle claims against their insured, then surely much more direct and precise language would have been selected." Scroggins never directly confronted the rationale of the Royal Globe majority opinion. Scroggins flatly stated that although both the California and Illinois Acts list unfair practices which refer to both insureds and third-party claimants, the duty of the insurer runs only to the insured. This reasoning overlooks the fact that few insureds will sue an insurer for breach of a statutory provision that relates to the claimant, thereby leaving third-party claimants without a remedy for an insurer's unfair practices.

Additionally, Illinois provides no civil remedy for a breach of statutory duties to insureds. However, since there is clearly a direct duty to insureds, the courts must rely on a different rationale to support this result. At least two districts have found that the Illinois Department of Insurance is the exclusive means to remedy violations of the Code.

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party claimant was denied attorney fees under § 767 in an action against an insurer to collect a judgment against its insured. The court stated that:

section [767] of the Illinois Insurance Code . . . is designed to protect insured parties who are forced to expend attorney fees where the insurer refuses to pay under the terms of the policy . . . and where such action on the part of the insurer was vexatious and without reasonable cause. The statute does not extend to third parties, such as plaintiff, and plaintiff cites no case law in support of his position. Id. (citing Keepes v. Doctors Convalescent Center, Inc., 89 Ill. App. 2d 36, 231 N.E.2d 274 (1967)). But see Sheroff, supra note 16, at § 6.04(2)(c)(i).

66. Scroggins, 74 Ill. App. 3d at 1036, 393 N.E.2d at 724 (1st Dist. 1979) (quoting Royal Globe, 23 Cal. 3d at 896, 592 P.2d at 339, 153 Cal. Rptr. at 853).

67. Id. at 1034, 393 N.E.2d at 723. But see McCarter v. State Farm Mut. Auto Ins. Co., 130 Ill. App. 3d 97, 473 N.E.2d 1015 (3d Dist. 1985), where the Third District Appellate Court held that an insurer's duty may run to third parties under special circumstances. In McCarter, both the injured third party and the negligent party in an automobile and motorcycle accident were insured by State Farm. State Farm allegedly "advised the plaintiff that he did not need to be represented during settlement negotiations and that [State Farm] would settle the plaintiff's claim . . . fairly and equitably because both vehicles were insured by [State Farm]." Id. at 101, 473 N.E.2d at 1018.

The McCarter court distinguished Scroggins' holding that "an insurance company's duty to negotiate in good faith is owed only to its insured and not to third parties." Id. The court held that "since State Farm had promised to represent and protect the interests of both the injured third party and the insured, it owed a duty of good faith to both parties." Id.


69. Tobolt v. Allstate Ins. Co., 75 Ill. App. 3d 57, 71, 393 N.E.2d 1171, 1181 (1st Dist. 1979) (§ 766.6 of the Code was merely "a definition section" which "provides no remedy"); Debolt v. Mutual of Omaha Ins. Co., 56 Ill. App. 3d 111, 115-16, 371 N.E.2d 373, 377 (3d Dist. 1978) (Insurance Code allows a private litigant to bring an action against an insurer for attorney fees only for withheld policy benefits or when the insurer's refusal to pay is "unreasonable and vexatious").
In *Hoffman v. Allstate Insurance Co.*, the Illinois Second District Appellate Court upheld the dismissal of a complaint that sought damages for Allstate's violation of Illinois Insurance Code section 766.6. Allstate towed Hoffman's car to an "unknown location" after it was damaged in an accident. Allstate's adjuster stated that Allstate considered the car a total loss and tendered a check to plaintiff in full payment of the claim. Included in the calculation for the check total was a $55.00 deduction for "dealer preparation and shampoo." When asked why this deduction was made on a "totalled" car, the adjuster said, "Allstate always does that."

Allstate also refused to inform Hoffman of the location of the car, which prevented him from having it appraised. The court held:

Plaintiff's reliance on paragraph 766.6 is unfounded. Paragraph 766.6 merely provides a list of acts which constitute improper claims practices. Paragraph 766.7 provides that penalties for violations of paragraph 766.6 are to be determined by the State Director of Insurance. Furthermore, in *Tobolt v. Allstate Insurance Co.*, the First District recently stated that paragraph 766.6 is merely a definition section which provides no remedies. Such remedies are provided in paragraph 767.

Hoffman was followed by the First District Appellate Court in *Hamilton v. Safeway Insurance Co.* The court affirmed the dismissal of a class action on behalf of all insureds allegedly entitled to uninsured motorist or hit and run benefits under insurance policies issued by Safeway. The complaint listed thirteen improper claims practices engaged in by Safeway that were prohibited by section 766.6. The court held that section 766.6 merely defined improper acts and provided no remedy. The plaintiffs' only available recovery was the money damages listed in section 767 for which the plaintiffs made no claim. "In enacting section [767], the Legislature preempted the field of remedies available to an insured who has difficulties with an unreasonable and vexatious insurance company."

The court relied on *Brooks v. Midas International Corp.*, reasoning that since the legislature had provided a remedy through the Director of Insurance, no civil remedy was available. *Brooks* had found that the

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70. 85 Ill. App. 3d 631, 407 N.E.2d 156 (2d Dist. 1980).
73. Id.
74. Id.
75. Id. at 635, 407 N.E.2d at 159.
76. 104 Ill. App. 3d 353, 432 N.E.2d 996 (1st Dist. 1982) (the First District, Fourth Division decided *Hamilton*; the First District, First Division decided *Tobolt v. Allstate Ins. Co.*, 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979)).
legislative intent precluded a private suit for injunctive relief under the Consumer Fraud and Deceptive Business Practice Act. The Hamilton court stated, "[T]he Legislature, had it intended to grant a private right of action for injunctive relief, would have explicitly done so . . . ." Hamilton, however, contradicts the Illinois Supreme Court case of Sawyer Realty Group v. Jarvis, which was decided only two days earlier.

Sawyer held that the plaintiffs had an implied private right of action under the Real Estate Brokers and Salesman Licensing Act.

It is clear that it is not necessary to show a special legislative intent to create a private right of action. If there is no indication that the remedies available are only those the Legislature expressed in the act, then where it is consistent with the underlying purpose of the act and necessary to achieve the aim of the legislation, a private right of action can be implied. Sawyer also found that the administrative remedy provided by the legislature does not preclude a private remedy.

We agree with the plaintiffs' assertion that the maxim expressio unius est exclusio alterius—the mention of one thing implies the exclusion of another thing—is only an aid and "should not be used to defeat the apparent intention of the Legislature." Because the Legislature provided for departmental enforcement does not necessarily mean that they must not have intended a private right of action.

The First District Appellate Court found Sawyer inapplicable to section 767 in Kinney v. St. Paul Mercury Insurance Co. The plaintiffs in Kinney alleged that snow had damaged their home in the amount of $10,000.00.

82. 89 Ill. 2d 379, 432 N.E.2d 849 (1982).
83. Sawyer Realty Group v. Jarvis was decided on February 2, 1982, and Hamilton was decided on February 4, 1982.
84. In Langendorf v. Travelers State Ins. Co., 625 F. Supp. 1103 (N.D. Ill. 1985), the Federal District Court for the Northern District of Illinois distinguished Sawyer on the flimsy basis that the Sawyer holding implies a private right of action only where necessary to achieve the aims of the statute. The Langendorf court said the aims of § 766.6 were adequately achieved through § 766.8, which empowers the Director of Insurance to issue a cease and desist order against the insurer that committed an act prohibited by § 766.6. The court felt it was irrelevant that the Director of Insurance had never brought such an order since the statute was enacted. Langendorf, 625 F. Supp. at 1106.
85. 89 Ill. 2d at 386, 432 N.E.2d at 852 (citing Kelsay v. Motorola, 74 Ill. 2d 172, 384 N.E.2d 353 (1978)).
86. Id.
87. Tobolt v. Allstate Ins. Co., 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979), was decided by the same court.
88. 120 Ill. App. 3d 294, 458 N.E.2d 79 (1st Dist. 1983).
The defendants' adjuster wrote an estimate of $3,950.70, but surreptitiously informed plaintiffs' contractor that his actual estimate was $9,500.00. The adjuster refused to accept the contractor's offer to repair the damage at that price. The defendants proposed $5,000 as their final offer in complete settlement of the claim. The plaintiffs sued for compensatory damages for breach of contract, and compensatory and punitive damages for breach of the implied covenant of good faith and fair dealing. The court rejected the plaintiffs' argument that Sawyer had effectively overruled Hamilton and Hamilton's predecessors.

The enactment involved in the case at bar differs from and is completely removed from the Brokers Licensing Act. The Brokers Licensing Act did not expressly deal with or consider allowance of damages for violation of the Act. The Legislature anticipated such general actions might well be brought. The fact that the Brokers Act did not expressly create a "private right of action for compensatory damages under any section of the Act [did not indicate] that the General Assembly rejected such a remedy . . . ." On the contrary, the Insurance Code provides explicitly for allowance of damages to private individuals resulting from violation of that Code and then places strong and express limitations on the amount of damages which may be recovered.

This superficial reasoning ignores the underlying issue. Section 767 does not provide a private cause of action, but merely provides a remedy of attorney fees and an additional limited amount of damages where an insurer has acted vexatiously or unreasonably. Even if section 767 limits a plaintiff's damages, the private cause of action still exists. The court also failed to consider that section 767 is not part of the Unfair Practices Act; it merely follows the Act. It seems logical that in determining whether the legislature had intended to provide a private remedy under the Unfair Practices Act, the court would consider the language of the Act. The Act itself provides an administrative remedy through the Director of Insurance. Although the Brokers Licensing Act provided an administrative remedy, Sawyer insisted that "[b]ecause the Legislature provided for departmental enforcement does not necessarily mean that they must not have intended to create a private right of action." Kinney also ignored the policy reasons articulated in Sawyer:

89. 104 Ill. App. 3d 353, 432 N.E.2d 996 (1st Dist. 1982).
91. Kinney, 120 Ill. App. 3d at 298-99, 458 N.E.2d at 82-83 (citations omitted).
92. ILL. REV. STAT. ch. 73, § 767 (1983).
93. See supra note 69 and accompanying text.
94. ILL. REV. STAT. ch. 73, §§ 766.7-766.8 (1983).
95. Sawyer, 89 Ill. 2d at 391, 432 N.E.2d at 854.
The public policy underlying certain statutes demands implication of a private remedy to compensate an aggrieved individual belonging to that class of persons whom the statute was designed to protect.*

_Sawyer_ enumerated two tests used by the United States Supreme Court in decisions concerning implied private rights of action. First:

(1) Is the plaintiff one of a class for whose special benefit the statute was enacted?
(2) Is there any indication of legislative intent to create or deny such a remedy?
(3) Is it consistent with the underlying purpose of the legislative scheme to impose such a remedy?
(4) Is the cause of action traditionally allocated to state law?*

Alternatively:

(1) Does the alleged violation contravene the public policy of the state?
(2) Are the plaintiffs within the class the statute was designed to protect?
(3) Is the injury one the statute was designed to prevent?
(4) Is the need for civil action under the statute clear?
(5) Is there any indication that remedies available are limited to those enumerated in the act?*

Application of either of these tests would lead to a private action for violation of the Unfair Practices Act. The statute was clearly designed to protect insureds. There is no express wording that creates or denies a private remedy. Although the statute creates an administrative remedy, a private remedy is not expressly excluded. Certainly a private remedy would be consistent with the underlying purpose of the legislative scheme to protect the public from deceptive practices. Additionally, although state law traditionally regulates insurance, state law does not regulate private causes of action against insurers.

Under the test stated in _Sherman v. Field Clinic_, insurance companies that engage in unfair practices contravene the state's public policy to protect the welfare of its citizens. The statute was clearly designed to prevent injuries to claimants. The best way to prevent injuries and compensate claimants would be to allow a private cause of action.

_Kinney's_ ineffectual attempt to distinguish _Sawyer_ is merely a disguised refusal to follow the holding of the Illinois Supreme Court. _Kinney_ ignored the Illinois Insurance Laws Commission Final Report regarding the passage of section 767:

96. _Id._ at 386-87, 432 N.E.2d at 852.
97. _Id._ at 388-89, 432 N.E.2d at 853 (citing _Cort v. Ash_, 422 U.S. 66 (1975)).
98. _Id._ at 388-89, 432 N.E.2d at 853 (citing _Sherman v. Field Clinic_, 74 Ill. App. 3d 21, 29, 392 N.E.2d 154, 160-61 (1st Dist. 1979)).
Traditionally, punitive damages have been seldom used. However, with its new prevalence as an integral element of litigation, the Commission thought that the insurance industry might have taken the opportunity to utilize the Senate Bill 517 [section 767] to establish statutory limits on the amount of punitive damages. This was not done.\textsuperscript{100}

The *Kinney* court refused to consider the Commission's report as evidence that the legislature intended the report to help interpret the statute: "[w]e find expressly that this section of the Insurance Code is not ambiguous and requires no statutory construction."\textsuperscript{101} The court disagreed with *Kelly v. Stratton*,\textsuperscript{102} in which a federal district court found that the Commission's report was sufficient evidence to indicate that the legislature did not intend to preempt the field by passing section 767. Without providing any further analysis, *Kinney* refused to follow the federal district court's decision because federal decisions are "certainly" not binding on state courts.\textsuperscript{103}

In reaching its decision in *Sawyer*, the Illinois Supreme Court cited *Kelsay v. Motorola, Inc.*\textsuperscript{104} *Kelsay* found an implied civil remedy under the Worker's Compensation Act where an employer discharged an employee for exercising her Worker's Compensation rights. The court found an implied private right of action even though the Worker's Compensation Act expressly preempts the field. The court reasoned that, because the legislature enacted the Worker's Compensation Act as a comprehensive scheme to protect employees, "[t]his scheme would be seriously undermined if employers were permitted to abuse their power to terminate by threatening to discharge employees for seeking compensation under the Act."\textsuperscript{105} Similarly, the Unfair Practices Act was passed to protect insureds, who are placed in a weak position and depend on insurance carriers in times of disaster. Limiting sanctions to an administrative slap on the hand of no more than $5,000.00 plus attorney fees would undercut this policy.\textsuperscript{106}

The Third Circuit Appellate Court, in *Van Vleck v. Ohio Casualty Insurance Co.*,\textsuperscript{107} also held that the legislature provided no private cause of action for violation of Illinois Insurance Code section 766.6.\textsuperscript{108} Van Vleck was an assignee of the insured's cause of action against Ohio

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\textsuperscript{100} *Kinney*, 120 Ill. App. 3d at 299, 458 N.E.2d at 83 (quoting Illinois Ins. Laws Study Comm'n, Final Report to the Governor and 80th General Assembly).

\textsuperscript{101} Id.

\textsuperscript{102} 552 F. Supp. 641 (N.D. Ill. 1982).

\textsuperscript{103} Id.

\textsuperscript{104} 74 Ill. 2d 172, 384 N.E.2d 353 (1978).

\textsuperscript{105} Id. at 182, 384 N.E.2d at 357.


\textsuperscript{107} 128 Ill. App. 3d 959, 471 N.E.2d 925 (3d Dist. 1984).

\textsuperscript{108} Ill. Rev. Stat. ch. 73, §766.6 (1983).
Casualty for failure to settle in good faith the claims brought by Van Vleck against the insured. The complaint alleged that Ohio Casualty failed to make any offer of settlement or to advise Van Vleck of the policy limits. The plaintiff particularly relied upon section 766.6(d), which prohibits "[n]ot attempting in good faith to effectuate prompt, fair and equitable settlement of claims submitted in which liability becomes reasonably clear." The court held that "paragraph 766.6 provides no private cause of action or remedy beyond those powers given to the State Director of Insurance in section 766.7 . . . ."

Since the Illinois courts have concluded that the Unfair Practices Act does not provide a civil remedy, the only causes of action available to insureds are based on common law theories. Even so, the possibility of getting a case to trial on available theories is severely limited.

II. PREEMPTION OF COMMON LAW CAUSES OF ACTION BY SECTION 767

The Illinois appellate courts do not follow California's lead in allowing a private cause of action for statutory violations. The Illinois courts are also divided on whether any extra-contractual damages are available in first-party actions against insurers. This division is based on disparate interpretations of Illinois Insurance Code section 767.

109. Van Vleck, 128 Ill. App. 3d at 960, 471 N.E.2d at 927. The court also dismissed Count 2 of the plaintiff's complaint, which alleged breach of the duty of good faith and fair dealing, because Van Vleck failed to allege that Ohio Casualty had an opportunity to settle the claim within the policy limits. Id. at 962, 471 N.E.2d at 928.

110. ILL. REV. STAT. ch. 73, § 766.7(d) (1983).

111. Van Vleck, 128 Ill. App. 3d at 961, 471 N.E.2d at 927.

112. Third-party claimants have no private remedy available except through the assignment of an insured's cause of action. See infra note 180.

113. ILL. REV. STAT. ch. 73, § 767 (1985). Section 767 provides for attorney fees. This provision immediately follows, but is not considered a part of, the Illinois Unfair Practices Act. The section provides:

(1) In any action by or against a company wherein there is in issue the liability of a company on a policy or policies of insurance or the amount of the loss payable thereunder, or for an unreasonable delay in settling a claim, and it appears to the court that such action or delay is vexatious and unreasonable, the court may allow as part of the taxable costs in the action reasonable attorney fees, other costs, plus an amount not to exceed any one of the following amounts:

(a) 25% of the amount which the court or jury finds such party is entitled to recover against the company, exclusive of all costs;
(b) $5,000;
(c) The excess of the amount which the court or jury finds such party is entitled to recover, exclusive of costs, over the amount, if any, which the company offered to pay in settlement of the claim prior to the action.

(2) Where there are several policies insuring the same insured against the same loss whether issued by the same or by different companies, the court may fix the amount of the allowance so that the total attorney fees on account of one loss shall not be increased by reason of the fact that the insured brings separate suits on such
A. The Fifth District

The leading Illinois case that recognizes a common law cause of action for an insurer's breach of the implied covenant of good faith and fair dealing is the Fifth District's decision in *Ledingham v. Blue Cross Plan for Hosp. Care*. *Ledingham* is a well-reasoned opinion that recognizes a cause of action in tort for breach of the duty of good faith and fair dealing implied in every insurance contract. A California Supreme Court case, *Fletcher v. Western National Life Insurance Co.*, influenced the *Ledingham* analysis. Fletcher found that an insurer's breach of a disability insurance contract could give rise to common law tort causes of action for intentional infliction of emotional harm and for tortious interference with a protected property interest, and that punitive damages could be recovered under either theory. *Ledingham* acknowledged that duties arise out of an insurance contract beyond the four corners of the policy.

*Ledingham* declared that Illinois courts should follow California and recognize the implied-in-law duty of good faith and fair dealing. The court discussed several important cases, including *Fletcher*, *Gruenberg v. Aetna Insurance Co.*, and *Eckenrode v. Life of America Insurance Co.* *Ledingham* stated the general rule excluding punitive damages in a contract action and approved California's adoption of a separate tort theory based on the relationship of the parties. The duty arises out of the relationship created by the insurance contract. Breach of the duty is both a breach of contract and a tort.

Having taken such a bold first step, the court then retreated:

Although in a proper case punitive damages may be awarded where the refusal to pay benefits is not made in good faith, and without fair dealing, that is not the case here. The decision to deny benefits was made in good faith on the basis of the insured's doctor's statement. The method of communicating that decision, and the behavior of the company was not "outrageous", nor was it in breach of the duty of good faith and fair dealing as that has been previously discussed. We find that the conduct of the insurer in this case does not rise to the level of a breach of either tort theory of sufficient gravity that punitive damages should be granted.
This conclusion is curious. The trial court's factual findings on the nature of the insurance company's conduct should not be disturbed on appeal unless an abuse of discretion is demonstrated on the record.\textsuperscript{121} \textit{Ledingham} found no abuse of discretion. The appellate court simply reassessed the culpability of the insurance company's conduct. The court could have reached this result without the extensive analysis of the covenant of good faith and fair dealing.

As a factual matter, the court found that the company's conduct was not outrageous, and thus refused to allow punitive damages for intentional infliction of emotional distress. However, instead of stopping with this factual finding, \textit{Ledingham} revived the Illinois Supreme Court case of \textit{Knierim v. Izzo}.\textsuperscript{122} \textit{Knierim} held that punitive damages are inappropriate for intentional infliction of emotional distress. Additionally, although \textit{Ledingham} seemed to announce a tendency in Illinois to follow the California analysis, it has been criticized or distinguished by each of the other Illinois Appellate Districts.

\textbf{B. The First District}

In \textit{Tobolt v. Allstate Insurance Co.},\textsuperscript{123} the First District Appellate Court criticized \textit{Ledingham} for its failure to consider section 767 of the Illinois Insurance Code. Plaintiffs claimed that Allstate refused, in bad faith, to pay the amount due under a homeowner's policy after a fire. The court affirmed the lower court's dismissal of plaintiffs' complaint for intentional infliction of severe emotional distress, and failure to act in good faith. The court permitted plaintiff to proceed only under a breach of contract theory. In order to dismiss plaintiffs' claim for intentional infliction of emotional distress, the court had to find that Allstate's conduct was not extreme and outrageous as a matter of law.\textsuperscript{124}

The court relied on the Third District's interpretation of \textit{Ledingham} in \textit{Debolt v. Mutual of Omaha Insurance Co.}:

\begin{quote}
We consider it to be of considerable import in the instant case that our State legislature has provided a remedy to insureds where an insurance company's refusal to pay or honor its contract is unreasonable and vexatious. Section 767 of the Illinois Insurance Code . . . permits an insured to recover attorney fees (25% of the amount the plaintiff is entitled to recover or $1,000 or whichever is the less) if it appears to the court that the insurer's refusal to pay is vexatious and without reasonable cause. This statutory provision has been the law in our state since 1967.
\end{quote}

\begin{itemize}
\item \textsuperscript{121} Fassola v. Montgomery Ward Ins. Co., 104 Ill. App. 3d 825, 433 N.E.2d 378 (3d Dist. 1982).
\item \textsuperscript{122} 22 Ill. 2d 73, 174 N.E.2d 157 (1961).
\item \textsuperscript{123} 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).
\item \textsuperscript{124} See infra notes 246-53 and accompanying text.
\end{itemize}
We are of the opinion that the legislature has intended to provide a remedy to an insured who encounters unnecessary difficulties with an unreasonable and vexatious insurance company. The insured can maintain an action on the contract for recovery of withheld policy benefits and upon proper finding by the court can be awarded attorney fees in addition to all other costs. Where the legislature has provided a remedy on a subject matter we are not only loath but in addition harbor serious doubts as to the desirability and wisdom of implementing or expanding the legislative remedy by judicial decree.  

Tobolt specifically recognized that California has no statute similar to Illinois' section 767. The court cited Urfer v. Country Mutual Insurance Co., which also criticized Ledingham and followed Debolt. Urfer held that section 767 preempts all other remedies. Interestingly, the Tobolt court commented, "We also note that in 1977 the legislature agreed that section 767 had preempted the field when it amended the section to increase the recovery for vexatious delay."

The court's comment follows a strange logic: because the reason for the remedy is broadened, access to other remedies is thereby limited. Further, section 767's title, "Attorney Fees," does not limit cause of action or remedy. Had the legislature intended to preempt tort theories of recovery or remedies, the section would refer to "Remedies" or "Amounts Recoverable in Addition to Contract Benefits." On this issue, Tobolt noted that, "in the interpretation of the meaning of a particular section the plain meaning of the substantive provisions of the section cannot be limited by its heading." A more likely reason for the statute's heading is that, since attorney fees are not generally available for breach of contract, the heading and the statutory remedy are specific in order to avoid the general rule which precludes recovery of attorney fees. Similarly, California Civil Code section 3294 is entitled "Punitive Damages." Section 3294 specifically permits punitive damages in causes of action where these damages have been historically unavailable. No one has ever argued that section 3294 limits the availability of compensatory damages in any way.

Illinois Insurance Code section 767 is a broadly worded statute that greatly affects the common law recovery of attorney fees for breach of

129. Tobolt, 75 Ill. App. 3d at 70-71, 393 N.E.2d at 1180 (citation omitted).
133. See supra notes 78-86 and accompanying text. For a discussion of recovery of attorney fees, see infra notes 134-40 and accompanying text.
insurance contract. Section 767 addresses a single additional item of damages recoverable for a particular activity: attorney fees may be recovered if the court finds the company's conduct vexatious or unreasonable.

_Tobolt_ also noted that "to the extent that _Eckenrode v. Life of America Insurance Co._,134 may be considered to hold to the contrary with reference to section [767], it is not binding upon Illinois courts."135 The court was referring to a footnote in _Eckenrode_:

Defendant argues that Illinois Rev. Stat. ch. 73, section 767, Attorney Fees, limits plaintiff's recovery to $1,000. However, defendant cites no decision for its position. And we think that the statute by its terms is limited to attorney fees and does not militate against our decision.136

The First District further distanced itself from the _Eckenrode/Ledingham_ line in _Kinney v. St. Paul Mercury Insurance Co._.137 The plaintiffs in _Kinney_ alleged that the defendant failed to make a good faith settlement offer on their homeowners insurance claim for snow damage. The court cited not only _Tobolt_,138 _Urfer_,139 and _Debolt_,140 but also _Hamilton_,141 and _Hoffman_,142 as standing for the proposition that Illinois Insurance Code section 767 preempts any common law cause of action for breach of the implied covenant of good faith and fair dealing.

### C. The Second District

In _Hoffman v. Allstate Insurance Co._,143 the Second District Appellate Court agreed with _Tobolt_,144 _Debolt_,145 and _Urfer_146 that section 767 precludes recovery of punitive damages. However, the court upheld plaintiff's claim for compensatory damages. The court observed that "paragraph 767, on its face, does not preempt a plaintiff's right to claim compensatory damages for a breach of good faith and fair dealing."147 This result indicates a significant split of opinion. The First District makes no dis-

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134. 470 F.2d 1 (7th Cir. 1972). _Eckenrode_ was cited in _Ledingham_ and decided prior to _Debolt_.
135. _Tobolt_, 75 Ill. App. 3d at 71, 393 N.E.2d at 1181.
136. _Eckenrode_ v. _Life of America Ins. Co._, 470 F.2d 1, 5 n.5 (7th Cir. 1972).
137. 120 Ill. App. 3d 294, 458 N.E.2d 79 (1st Dist. 1983). _See supra_ notes 87-106 and accompanying text.
138. 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).
139. 60 Ill. App. 3d 469, 376 N.E.2d 1073 (4th Dist. 1978).
141. 104 Ill. App. 3d 353, 432 N.E.2d 996 (1st Dist. 1982).
143. _Id._
144. 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).
146. 60 Ill. App. 3d 469, 376 N.E.2d 1073 (4th Dist. 1978).
147. _Hoffman_, 85 Ill. App. 3d at 635, 407 N.E.2d at 159.
tinction between compensatory and punitive damages. If section 767 preempts punitive damages, it must preempt extra-contractual compensatory damages as well, because section 767 offers the only remedy beyond contract benefits. 148

D. The Fourth District

In Lynch v. Mid-America Fire & Marine Insurance Co., 149 the Fourth District Appellate Court gingerly disagreed with the First District. Lynch determined whether or not section 767 preempted a common law tort action before the 1977 amendment. Tobolt 150 said that the 1977 amendment was merely a further indication of the legislative intent to preempt available remedies. Lynch held, however, that before its amendment, section 767 did not preempt the field. Significantly, the court reserved its opinion as to whether the present section 767 preempts a common law tort action. 151

The court reasoned correctly that even if section 767 limited the damages available, a cause of action could still be brought. The reasoning in Lynch leaves the Fourth District in a position to hold that the current section 767 does not preempt other remedies because the amendment simply added recovery for vexatious delay. This amendment would not substantively affect the preemption question.

Lynch favored the Second District’s holding in Hoffman:

The appellate court [in Hoffman] held the request for punitive damages to have been properly stricken but that a cause of action existed for compensatory damages. It noted the preemption theory expressed in Debolt, Tobolt and the Urfer concurrence, interpreted them as holding that section [767] preempted any claim by an insured for punitive damages and adopted that interpretation. The court then reasoned that nevertheless, section [767] did not, on its face, “preempt a plaintiff’s right to claim compensatory damages for a breach of good faith and fair dealing.” The opinion did not indicate that plaintiff’s claim for those compensatory damages was being made under section [767]. The opinion thus appears to disagree with Tobolt’s holding that no cause of action exists for compensatory damages for an insurer’s failure to deal in good faith with its insured. 152

Obviously, section 767 does not, on its face, preempt punitive damages. Lynch emphasized that section 767 merely granted discretionary authority to award attorney fees as costs. The court reasoned:

148. See Tobolt, 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979). The Tobolt court relied on Debolt and Urfer to conclude that § 766 preempted punitive and compensatory damages, although the section only addresses itself to attorney fees arising out of a vexatious lawsuit. Id. at 70-71, 393 N.E.2d at 1180-81.


150. 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).

151. Lynch, 94 Ill. App. 3d at 26, 418 N.E.2d at 426.

152. Id. at 25, 418 N.E.2d at 425 (citations omitted).
The fees were limited and even in this case could not have exceeded $1,000. The tenor of this section gives no indication that it was intended to cover the field of awarding compensation for bad faith or vexatious dealing by insurers. The Tobolt court reasoned that the amendment providing for a limited discretionary case award evidenced a prior intent to preempt the field. Even if the present section [767] indicates such a present intent, we do not see how that could relate to the prior legislative intent. Where legislation is amended to grant a power expressly, the amendment has been interpreted to indicate a legislative acknowledgment of a previous lack of that power. . . By analogy to that rule, legislative amendments to add provisions indicating a legislative intent to preempt a field could be deemed to be an acknowledgment that the provisions amended did not previously preempt. We express no opinion as to whether the present section [767] preempts the field, 1985

Lynch also cited the Illinois Supreme Court's reliance on Ledingham in Kelsay v. Motorola, Inc., 154 as standing for the rule that a separate tort action can arise from conduct that also involves a breach of contract. 155

Lynch, like Ledingham, broadly stated the law but refused to find the necessary supporting facts. In Lynch, the defendant insurer refused to settle plaintiff's fire insurance claim on a commercial building based on an "at best, uncertain" arson defense. 156 Lynch was unable to make payments on the building because of the insurer's refusal to pay. The same attorney who represented the insurer also represented the mortgagee of the building in foreclosure proceedings. Additionally, there was a dispute as to whether the insurer refused to provide or inform Lynch of the proof of loss form required for compensation. Accordingly, the jury found that defendant's conduct constituted bad faith, and the appellate court affirmed. However, the court reversed the jury award of $150,000.00 in compensatory damages as contrary to the manifest weight of the evidence and also reversed the jury's award of $100,000.00 in punitive damages, stating, "[n]o case has been called to our attention holding that evidence supporting an award of compensatory damages for an insurer's failure to settle the claim in good faith necessarily supports an award for punitive damages." 157

153. Id. at 25-26, 418 N.E.2d at 425 (citations omitted).
154. 74 Ill. 2d 172, 187, 384 N.E.2d 353, 360 (1978).
155. Based on this implied approval of Ledingham by the Illinois Supreme Court, Lynch held that, at least prior to the amendment of § 766, "[t]here existed a tort action for the refusal of an insurer to make payments due its insured, limited to those circumstances where the refusal was in bad faith." Lynch, 94 Ill. App. 3d at 26, 418 N.E.2d at 426.
156. Id. at 28, 418 N.E.2d at 427. The insurer also claimed the plaintiff had other existing insurance at the time of the fire, although plaintiff's other policy had terminated just before the issuance of the policy in suit. Id.
157. Id. at 29, 418 N.E.2d at 428. The court felt that the evidence presented as to plaintiff's compensatory damages was inadequate, although none of the evidence presented had been disputed by defense counsel. Id. The court reversed the punitive damages award, saying the insurer's conduct was not fraudulent. Id. The court failed to consider that other conduct besides
This statement is too simple. The factual finding of bad faith affirmed by the appellate court forms the basis for extra-contractual compensatory damages unless these damages are not proven. It is not the award of compensatory damages but the culpability of the defendant that forms the basis for punitive damages. By affirming the jury finding of bad faith, the appellate court has approved the factual foundation upon which to award punitive damages.

The Fourth District has also created a broad exception to preemption under section 767 where the defendant is a non-profit health care service. In McCall v. Health Care Service Corp., the court held that because non-profit health care services are exempt from the Insurance Code, they are also exempt from section 767 of the Insurance Code. Non-profit health care services are subject to a common law tort action for bad faith.

The plaintiff in McCall sued Blue Cross, alleging that Blue Cross breached its duty to deal fairly and in good faith by delaying payment on a claim. The appellate court reversed the lower court’s dismissal of plaintiff’s first amended complaint. McCall noted that Ledingham recognized a tort action for breach of the implied covenant of good faith and fair dealing. The court distinguished Debolt, Tobolt, and Hoffman as concerning stock or mutual companies subject to the Illinois Insurance Code.

No other Illinois decisions involving insurance companies regulated by the Insurance Code have distinguished Ledingham on this basis, even though Ledingham also involved an action against Blue Cross. Had Debolt, Tobolt and other decisions relied on this distinction, the preemption analysis would have been unnecessary. Arguably, many of the principles announced in Ledingham are too appealing to be discarded peremptorily.

McCall noted that “while all of these cases discuss preemption, it is noteworthy that such preemption did not change the nature of the tort...
but only the items of damage and the amount thereof." The court called bad faith the "semantic equivalent of vexatious and unreasonable delay."  

**E. Conclusion**

The First and Third District Appellate Courts have found that section 767 preempts both a common law tort action for breach of the implied covenant of good faith and fair dealing, and all remedies. The Fourth District has found that section 767 did not preempt other remedies before its amendment and has not reached the issue of post-amendment preemption. The Second District allows an action for extra-contractual compensatory damages, but not punitive damages. The Fifth District stands alone in allowing a cause of action for tortious breach of an insurance contract with both punitive and compensatory damages available.

**III. EXTRA-CONTRACTUAL DAMAGES UNDER SECTION 767**

The reasons for imposing greater duties upon an insurance carrier than those written into the insurance contract are rooted in a sound public policy that recognizes the quasi-fiduciary role of insurers in modern society. Punitive damages encourage insurance carriers to comply with public policy as declared in the Unfair Practices Act. Section 767 is merely an additional item of compensatory damages. If section 767 preempts recovery of extra-contractual damages, including punitive damages, it is ineffective as a sanction and actually undermines the intent of the Unfair Practices Act.

In California, the cause of action for tortious breach of contract stemmed from the courts' gradual recognition of situations in which one party to a contract owed a "special duty" to the other party. For example, early California decisions recognized that a plaintiff could recover extra-contractual damages when a common carrier breached the special duty of care owed to its passengers. As society becomes more complex, the special duty concept has expanded to include other situations in which a  

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162. 117 Ill. App. 3d at 111, 452 N.E.2d at 896.
167. Ledingham, 29 Ill. App. 3d 339, 330 N.E.2d 540 (5th Dist. 1975). Ledingham was the only one of these five cases to be heard by the Illinois Supreme Court, which reversed it on other grounds. 64 Ill. 2d 338, 356 N.E.2d 75 (1976).
special relationship is involved. Landlords, banks, and employers have been held subject to this special duty. Although the special duty arises out of the execution of a contract, its breach constitutes a tort, for which tort damages, including punitive damages, are available.

California courts have extended this special duty to insurance contracts. The courts have reasoned that insurers, like common carriers, have a special duty to their insureds. The breach of that duty may give rise to a cause of action sounding in tort.

The insurers' obligations are rooted in their status as purveyors of a vital service labeled quasi-public in nature. As a supplier of a public service rather than a manufactured product, the obligations of insurers go beyond meeting reasonable expectations of coverage. Insurers hold themselves out as fiduciaries, and with the public's trust must go private responsibility consonant with that trust. Furthermore, the relationship of insurer and insured is inherently unbalanced; the adhesive nature of insurance contracts places the insurer in a superior bargaining position. The availability of punitive damages is thus compatible with recognition of insurers' underlying public obligations and reflects an attempt to restore balance in the contractual relationship.

Illinois recognized a cause of action for a common carrier's tortious breach of contract in *Nevin v. Pullman Palace Car Co.* In *Nevin*, the plaintiff and his family were refused, without justification, a berth in a sleeping car. The Illinois Supreme Court noted that the plaintiff's contractual remedy was limited to recovery of the ticket fare, but held that an action on the tort would lie since the defendant was a common carrier with a special duty to its passengers.

*Debolt v. Mutual of Omaha Insurance Co.* refused to extend *Nevin* to an action seeking extra-contractual damages against an insurance carrier who refused to pay policy benefits. The court reasoned that although mere contractual recovery would be inadequate in a common carrier case because the recovery would be limited to the price of the ticket, contractual damages in a breach of insurance contract action would be sufficient because that was the extent of the insured's bargain. The *Debolt* reasoning ignores the primary reason for insurance. An insured buys insurance,

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173. 106 Ill. 222 (1883).
particularly liability insurance, in order to obtain peace of mind by reducing risk. In fact, Illinois courts have held that an insurer has a good faith obligation to its insured to make a reasonable attempt to settle a third party's claim within the policy limits, and have permitted extra-contractual damages for breach of this obligation.\textsuperscript{175}

Illinois appellate courts have declined to extend the preemptive effect of section 767 to third-party "duty to settle" cases. These cases involve an action by the insured against the insurer for the breach of the insurer's duty to reasonably negotiate a claim by a third party that results in a judgment in excess of the insured's policy limits.\textsuperscript{176} The excess verdict exposes the insured to an amount in excess of the contract benefits. This excess liability would be unrecoverable in a contract action, even if the plaintiff obtained the remedies provided in section 767. Section 767 was enacted as a cure for unreasonable and vexatious delay in paying contract benefits, and, therefore, is unrelated to an action based on an insurer's unreasonable failure to settle a third-party claim within policy limits. An excess judgment is a foreseeable result of a breach of the duty to settle under a liability policy. Both insurer and insured contract with precisely this risk in mind. Thus, section 767 does not affect these contract damages. Although the amount of the excess verdict may be recovered, extra-contractual and punitive damages are unavailable under this analysis because the action is considered purely a contract action for foreseeable contract damages.\textsuperscript{177}

\textit{Debolt} distinguishes the "duty to settle" cases upon which \textit{Ledingham} relied. \textit{Debolt} found third-party cases inapplicable:

Where the insurer ignores the interest of its insured and judgment in excess of policy limits is awarded the insurer will be compelled to pay the excess. We do not deem the "duty to settle" cases pertinent to the instant case since the insurer's discretion and control is not absolute.\textsuperscript{178}

\textsuperscript{175} LaRotunda v. Royal Globe Ins. Co., 87 Ill. App. 3d 446, 408 N.E.2d 928 (1st Dist. 1980) (insurer's breach of its duty to defend insureds against suit rendered insurer liable for costs of defense and for maximum amount of policy coverage).

\textsuperscript{176} See Debolt, 56 Ill. App. 3d at 115, 371 N.E.2d at 377.

\textsuperscript{177} See infra text accompanying notes 282-83. California considers an insurer's bad faith failure to settle a third-party claim to be a breach of a different aspect of the insurer's common law duty of good faith and fair dealing. Gruenberg v. Actna Ins. Co., 9 Cal. 3d 566, 574, 510 P.2d 1032, 1038, 108 Cal. Rptr. 480, 485 (1973). The insured may bring a tort action for both the excess verdict and noncontractual damages (e.g., emotional distress, punitive damages). However, only the claim for the excess verdict is assignable. Murphy v. Allstate Ins. Co., 17 Cal. 3d 937, 553 P.2d 584, 132 Cal. Rptr. 424 (1976). Because the claim in Illinois is only for the excess verdict, the entire claim may be assigned. See Phelan v. State Farm Mut. Auto. Ins. Co., 114 Ill. App. 3d 96, 448 N.E.2d 579 (1st Dist. 1983); LaRotunda v. Royal Globe Ins. Co., 87 Ill. App. 3d 446, 408 N.E.2d 928 (1st Dist. 1980).

\textsuperscript{178} Debolt, 56 Ill. App. 3d at 115, 371 N.E.2d at 377. However, the insurer's discretion is never absolute; it is always subject to the implied covenant of good faith and fair dealing, regardless of the type of claim or policy, and it is always governed by the standards set out in the Unfair Practices Act.
Debolt views the insurance contract relationship too narrowly. The courts have generally allowed extra-contractual damages where contractual damages would be inadequate for a party to a quasi-fiduciary relationship who depended on the other party to uphold a contract. For example, a plaintiff who buys a ticket from a common carrier places his entitlement to safe travel in the hands of the carrier. If he suffers while captive on his journey he may recover more than the refunded ticket. Similarly, a person who contracts with an innkeeper expects to be provided with a safe bed away from home. Recovery of the price of the room, leaving the traveler stranded, would be inadequate. In the same way, a party who contracts with an insurance company, does not seek "by the contract . . . to obtain a commercial advantage but to protect against the risk of accidental losses, including the mental distress which might follow from the losses."

"An insurer's breach of its duty to an insured creates just the sort of damage the insured sought to protect against by entering into the contract." Debolt held that since the insured could recover attorney fees over and above section 767 contractual damages, extra-contractual damages, including punitive damages, are precluded because there is no cause of action in tort. The court found it to be of "considerable import" that section 767 of the Illinois Insurance Code was enacted by the state legislature to provide a remedy to insureds "where an insurance company's refusal to pay or honor its contract is unreasonable and vexatious."

The court confuses "remedy" and "cause of action," and, thus, its reasoning is circular. If section 767 is a remedy, it would not necessarily prohibit a cause of action. The confusion lies partially in the significance Debolt attaches to a finding of vexatious and unreasonable conduct under the statute. These factual findings are the underpinnings of additional contract damages and not an independent cause of action. If the insurer breaches the insurance contract, the insured is entitled to the benefits under the contract. If, in addition, this breach is unreasonable and vexatious, the insured may recover limited attorney fees. This is simply a two-step analysis of a single cause of action. Separate causes of action sounding in tort could still be brought and traditional

180. Even if the special duty concept were not extended to insurance contracts, some breach of contract cases permit recovery of emotional distress if that type of damage is foreseeable. Historically, a party breaching a contract that involves a corpse (e.g., a mortuary/cemetery contract) must pay the other party damages for emotional distress. The cause of action does not sound in tort and is not based upon a special duty. Rather, the cause of action is for breach of contract, and damages for emotional distress are recoverable not as extra-contractual damages, but as damages foreseeable under the contract. Similarly, damages for emotional distress for an insurer's breach of an insurance contract are foreseeable and should be recoverable.
182. Id.
BAD FAITH PRACTICES

1985]

tort remedies recovered. Such separate actions could be based on the insurer's breach of the implied covenant of good faith and fair dealing, for intentional infliction of emotional distress, conversion of policy benefits, etc. No disservice is done to section 767, because plaintiffs would be fully compensated, and fair claims practices would be encouraged.

Debolt notes Ledingham's reliance on California cases but reasons that California does not have a statutory provision that permits an insured to recover attorney fees.\(^{183}\) In fact, punitive damages are statutory in California.\(^{184}\) The missing link in Debolt's analysis is that attorney fees are compensatory and not punitive.

According to Debolt:

It could well be argued that the rationale of the California courts is that absent a statutory remedy punitive damages will be allowed to an aggrieved party who has been mistreated by an insurer . . . We believe the remedy provided in [section 767 of the Illinois Insurance Code] is highly significant in that it provides a remedy for an insured and thereby attempts to keep him harmless resulting from the misconduct of his insurer.\(^{185}\)

Punitive damages may be characterized as a remedy in that they serve a remedial purpose by affecting future conduct. In contrast, attorney fees are compensation for a past loss. California has allowed punitive damages because the cause of action sounds in tort. Historically, both compensatory and punitive damages are permitted in tort actions. Public policy has long supported compensatory damages for tort victims and sanctions against sufficiently culpable tortfeasors.\(^{186}\) Although section 767 provides for attorney fees, such fees should be awarded in addition to the compensatory and punitive damages available as a remedy for a tort cause of action. Punitive damages should be available for conduct exceeding vexatious and unreasonable delay, such as malice, fraud or oppression.

Debolt,\(^{187}\) Urfer\(^{188}\) and Tobolt\(^{189}\) fail to recognize three obstacles. First, even if section 767 were an exclusive remedy for an insurer's vexatious and unreasonable conduct, both Illinois and California require something more than vexatious and unreasonable conduct to award punitive damages against a defendant. Second, the purpose of punitive damages is to deter

\(^{183}\) Id. at 115-16, 371 N.E.2d at 378. But see Brandt v. Superior Court, 37 Cal. 3d 813, 693 P.2d 796, 210 Cal. Rptr. 211 (1985) (attorney fees are recoverable to the extent that they relate to fees incurred in attempting to recover benefits due under contract of insurance; punitive damages are available in addition to attorney fees in such cases).

\(^{184}\) CAL. CIV. CODE § 3294 (West 1972).

\(^{185}\) 56 Ill. App. 3d at 111, 371 N.E.2d at 378.


\(^{188}\) 60 Ill. App. 3d 469, 376 N.E.2d 1073 (4th Dist. 1978).

\(^{189}\) 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).
and set an example, not to compensate the plaintiff. Third, as a practical matter, section 767 fails as an economic disincentive to unfair claims practices.

For example, Deboli\textsuperscript{10} found that section 767 provides "a remedy for an insured and thereby attempts to keep him harmless resulting from the misconduct of his insurer."\textsuperscript{11} Punitive damages are not awarded to keep a plaintiff "harmless," but to punish the defendant. The conduct of the defendant, not the damages of the insured, is at issue.

California Civil Code section 3294(a) allows punitive damages only "where the defendant has been guilty of oppression, fraud, or malice . . . ." It defines such conduct as:

1. "Malice" means conduct which is intended by the defendant to cause injury to the plaintiff or conduct which is carried on by the defendant with a conscious disregard of the rights or safety of others.
2. "Oppression" means subjecting a person to cruel and unjust hardship in conscious disregard of that person's rights.
3. "Fraud" means an intentional misrepresentation, deceit, or a concealment of a material fact known to the defendant with the intention on the part of the defendant of thereby depriving a person of property or legal rights or otherwise causing injury.\textsuperscript{12}

The California courts have only allowed punitive damages where the insurer's conduct exceeds "vexatious or unreasonable."\textsuperscript{13} Under Illinois common law, punitive damages may be awarded only where the defendant has acted with fraud, actual malice, violence, oppression, or with such gross negligence as to indicate a wanton disregard of the rights of others.\textsuperscript{14}

Attorney fees can be recovered under section 767 even without the showing of actual injury necessary to justify an award of compensatory damages in tort.\textsuperscript{15} The statute creates a standard for recovery that is easier to satisfy than the common law standard for punitive damages. Where the insurer's conduct is more than vexatious and unreasonable, punitive damages should be available in Illinois.\textsuperscript{16}

Illinois has no statute similar to California Civil Code section 3294, and therefore follows the common law. The Restatement (Second) of Torts, section 908, provides:

\begin{itemize}
  \item \textsuperscript{10} 56 Ill. App. 3d 111, 371 N.E.2d 373 (3d Dist. 1978).
  \item \textsuperscript{11} \textit{Id.} at 117, 371 N.E.2d at 378 (emphasis added).
  \item \textsuperscript{12} Cal. Civ. Code § 3294 (West 1972).
  \item \textsuperscript{14} Roberts v. Western-Southern Life Ins. Co., 568 F. Supp. 536 (N.D. Ill. 1983).
  \item \textsuperscript{15} \textit{Id.}
  \item \textsuperscript{16} \textit{Id.}
\end{itemize}
BAD FAITH PRACTICES

(1) Punitive damages are damages, other than compensatory or nominal damages, awarded against a person to punish him for his outrageous conduct and to deter him and others like him from similar conduct in the future.

(2) Punitive damages may be awarded for conduct that is outrageous, because of the defendant's evil motive or his reckless indifference to the rights of others. In assessing punitive damages, the trier of fact can properly consider the character of the defendant's act, the nature and extent of the harm to the plaintiff that the defendant caused or intended to cause and the wealth of the defendant.

. . . . . [T]he purpose of punitive damages is not compensation of the plaintiff but the punishment of the defendant and deterrence . . . [P]unitive damages may be awarded because of, and measured by, [the defendant's] wrongful purpose or intent . . . .

. . . . . Whether to award punitive damages and the determination of the amount, are within the sound discretion of the trier of fact, whether judge or jury.197

Illinois courts have overlooked the deterrent purpose of punitive damages by holding that section 767 fully compensates plaintiffs:

The wealth of the defendant is also relevant since the purposes of exemplary damages are to punish for a past event and to prevent future offenses, and the degree of punishment for deterrence resulting from a judgment is to some extent in proportion to the means of the guilty person.198

California courts examine four factors to assess the amount of punitive damages:

(a) The reprehensibility of the defendant's conduct.
(b) The defendant's wealth.
(c) The amount of compensatory damages.
(d) The amount necessary to deter future conduct.199

The reprehensibility of the defendant's conduct is relevant to the amount of punitive damages, and irrelevant to the amount that the plaintiff has been awarded in compensatory damages. Compensatory damages are in issue to determine the ratio of punitive to compensatory damages, not to determine if the plaintiff has been properly compensated. The defendant's wealth is frequently critical in determining the amount necessary to deter and punish the defendant and to remove any financial incentive for similar conduct by others.

The Illinois courts have generally agreed that section 767's legislatively mandated limit on damages for an insurer's vexatious and unreasonable

197. Restatement (Second) of Torts § 908 (1979) (emphasis added).
198. Id. § 908(e).
delay is the equivalent of punitive damages. This acknowledgment disregards the common law policy behind punitive damages and denies any opportunity to deter the unfair practices of insurers. A statutory limit of $5,000.00 is insufficient to deter most insurance carriers from engaging in unfair practices. Only the possibility of punitive damages can create a sufficient deterrent.

Punitive damages have traditionally been available in an intentional tort action. Thus, punitive damages should be available against an insurance company for common law fraud, conversion and intentional infliction of emotional distress. However, when the Illinois Supreme Court first recognized the tort of intentional infliction of emotional distress in *Knierim v. Izzo*, it held that punitive damages are not recoverable for this tort in Illinois.

In *Knierim*, the defendant threatened to kill the plaintiff’s husband and subsequently followed through with the murder. The plaintiff alleged no physical injury except that the defendant’s conduct caused an “oppressive and undesirable disturbance of her mental tranquility.” In settling the propriety of a request for punitive damages, the court held:

> Generally, [punitive] damages may be recovered in cases where the wrongful act complained of is characterized by wantonness, malice, oppression or circumstances of aggravation ... The alleged conduct of the defendant in intentionally causing the severe emotional disturbance is characterized by these elements. Indeed it is the outrageous nature of his conduct that forms the basis for the action.

We believe, nevertheless, that punitive damages cannot be sanctioned as an additional recovery in such an action. Since the outrageous quality of the defendant’s conduct forms the basis of the action, the rendition of compensatory damages will be sufficiently punitive.

Since an action for the tort lies only when the defendant’s conduct comes under the category in which punitive damages are recoverable, the court reasoned that a punitive damage award would constitute double recovery.

This reasoning is problematic. Compensatory damages are awarded to compensate the plaintiff for emotional distress caused by the defendant’s conduct. The actual amount of compensation may or may not influence a defendant’s future conduct because the plaintiff may not prove damages of an amount sufficient to reach and “sting” the defendant. Particularly in the corporate setting, the defendant’s wealth must be considered both to reach that defendant and to remove the profitability of unfair practices in the market place. There is no double recovery, because punitive damages are over and above compensation.

Although the defendant’s conduct might always constitute conduct for which punitive damages could be awarded, punitive damages are never

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201. *Id.* at 83, 174 N.E.2d at 163.
202. *Id.* at 87-88, 174 N.E.2d at 165 (citations omitted).
allowed as a matter of right. If the full compensation of the plaintiff also constitutes a significant amount of the defendant's wealth, punitive damages are unnecessary because their purpose will already have been served. It is always within the discretion of the trier of fact to award punitive damages.

Punitive damages are not considered compensatory, but rather exemplary. Thus, a second and ever-present challenge arises in the argument that the plaintiff is the recipient of a "windfall" that exceeds his compensatory or actual damages. In California, active insurance litigators have been promoting efforts to form a "victims' fund," or a charitable organization into which defendant insurers would pay punitive damage awards. The insurance industry is the most vehement opponent of this and similar plans. As long as a carrier can argue that a plaintiff is getting more than he deserves, the carrier can sway sympathetic jurors and lawmakers. However, if defendant insurers would deposit punitive damages into such a fund, the insurers could no longer rely on juror sympathy. Rather, insurers would be forced to defend themselves solely on their conduct. Naturally, the insurance industry opposes such plans.

The insurance industry also has considerable influence in Illinois.\(^\text{203}\) In \textit{Roberts v. Western-Southern Life Insurance Co.},\(^\text{204}\) the United States District Court discussed the legislative history of section 767. The court reviewed testimony by Bernard E. Epton, a former state representative and Chairman of the Insurance Laws Study Commission from 1971-1983. Epton testified that the Commission believed that section 767 "provided the sole source of recovery in Illinois by a first party insurance claimant."\(^\text{205}\) Epton said the insurance industry supported the bill, "as evidenced by the nearly unanimous votes of both houses of the legislature."\(^\text{206}\) In a footnote, the court found "interesting the implication that the bill would not have done so well had the industry not backed it."\(^\text{207}\)

In fact, twenty-eight of the two hundred largest property-casualty insurance companies in America are based in Illinois, including the three largest: State Farm Mutual Automobile Insurance Company, Allstate Insurance Company, and State Farm Fire & Casualty Insurance Company.\(^\text{208}\) There are more property/casualty carriers in Illinois than in any other state, and Illinois ranks fourth among states in the number of life insurance companies.\(^\text{209}\)

\(^{203}\) One commentator has declared, "Illinois has long been considered one of the more hospitable states from which to operate an insurance company," basing his conclusion on the regulatory and legislative climate of the state. A. Tobias, \textit{The Invisible Bankers} 30 (1982).

\(^{204}\) 568 F. Supp. 536 (N.D. Ill. 1983).

\(^{205}\) Id. at 550.

\(^{206}\) Id.

\(^{207}\) Id. at 550 n.34.


\(^{209}\) Id. at 30.
A final challenge is that punitive damages raise premium rates. In California, insurance companies may not pass on to consumers losses resulting from punitive damages. Department of Insurance Accounting Statement 84-1 provides, in part:

The accrual of punitive or monetary damage loss contingencies . . . may be charged to the underwriting loss or expense account in the annual statement; however, these amounts must be deducted from losses or expenses prior to determining any underwriting or rating calculations.\footnote{State of California Department of Insurance Accounting Statement 84-1 (Nov. 26, 1984).}

In California, underwriting losses form the basis for calculating the rates that are regulated by the Department of Insurance. Since punitive damage amounts must be deducted from underwriting losses before rates are calculated, these losses cannot be passed on to the consumer in the form of increased rates.\footnote{See generally Cal. Ins. Code § 1850-1860 (West 1972).}

Insurance companies in Illinois could conceivably pass on the cost of punitive damage awards to consumers. However, raising rates would affect competition with foreign carriers having lower rates. Illinois is an "open competition" state because insurance rates are unregulated. The remedy for potentially inflated rates is not to prohibit punitive damages, but to enact legislation that would prevent insurers from passing on the costs of their unlawful conduct to the innocent consumer.

IV. The Plaintiff's Burdens of Pleading and Proof

A. Ledingham v. Blue Cross

\textit{Ledingham v. Blue Cross Plan for Hosp. Care}\footnote{29 III. App. 3d 339, 330 N.E.2d 540 (5th Dist. 1975).} sets forth the circumstances under which a plaintiff may recover punitive damages for an insurer's breach of the duty of good faith and fair dealing. In \textit{Ledingham}, the insurers refused benefits to the insured based on her doctor's uncertainty as to whether her illness developed before or after the health insurance policy was issued.\footnote{Id. at 341, 330 N.E.2d at 542.} In determining whether the conduct of the insurer was sufficiently outrageous to support the award of punitive damages, the court relied on the California case of \textit{Fletcher v. Western National Life Insurance Co.}\footnote{Fletcher v. Western Nat'l Life Ins. Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970).} \footnote{Fletcher framed the issue this way: Whether threatened and actual bad faith refusals to make payments under a}
Ledingham agreed with Fletcher that punitive damages are recoverable in an action for interference with a protected property interest. However, the court relied on the Illinois Supreme Court case of Knierim v. Izzo, and rejected recovery of punitive damages for intentional infliction of emotional distress. Ledingham concluded that punitive damages were recoverable where the insurer's conduct included any of the following elements: (1) falsely accusing the insured of misrepresentation, (2) attempting to settle based on untrue defenses, (3) causing excessive delay, and (4) engaging in other arguably "outrageous" conduct.

V. Illinois' Strict Pleading Requirements

Both California and Illinois are "fact pleading" jurisdictions. However, California interprets pleadings much more liberally. Gruenberg v. Aetna Insurance Co. defined the appellate standard for reviewing a sustained demurrer in California:

[The rule is that if, upon consideration of all the facts stated, it appears that the plaintiff is entitled to any relief at the hands of the court against the defendants, the complaint will be held good . In other words, "plaintiff need only plead facts showing that he may be entitled to some relief."]

Debolt discussed the Illinois standard:

We are well aware of the fundamental rule that a motion to dismiss such as we had in the instant case admits all facts well pleaded together with all reasonable inferences which could be drawn from those facts . . . [I]t is also well established that a motion to dismiss or strike a pleading admits facts well pleaded, but not conclusions of fact unsupported by allegations of specific facts upon which such conclusions rest.

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disability insurance policy, maliciously employed by the insurer in concert with false and threatening communications, for the purpose of causing the insured to surrender his policy or disadvantageously settle a nonexistent dispute, may legally give rise to a cause of action for intentional infliction of emotional distress or some other cause of action sounding in tort.

Id. at 400, 89 Cal. Rptr. at 92.


216. Fletcher rejected the argument accepted in Knierim that "[because] the basis of the tort of intentional infliction of emotional distress is outrageous conduct, compensatory damages assuage the outrage and punitive damages should not be allowed in addition thereto." Fletcher, 10 Cal. App. 3d at 404, 89 Cal. Rptr. at 95. Fletcher said such a contention was "not meritorious." Id. (citing State Rubbish Collectors Assoc. v. Siliznoff, 38 Cal. 2d 330, 240 P.2d 282 (1952)).

217. Ledingham, 29 Ill. App. 3d at 350-51, 330 N.E.2d at 549.

218. CAL. CIV. PROC. CODE § 425.10 (West Supp. 1985); ILL. ANN. STAT. ch. 110, § 2-603 (Smith-Hurd 1983).


220. 56 Ill. App. 3d at 113, 371 N.E.2d at 375 (citation omitted).
Out of the thirteen appeals from preliminary pleading stages reviewed for this article, nine were affirmed at least partially because the facts alleged were "conclusory."\textsuperscript{221}

The standard of review stated by the Fourth District Appellate Court in \textit{Perschall v. Metropolitan Life Insurance Co.}\textsuperscript{222} is similar to the California standard. The court affirmed the trial court's finding of vexatious and unreasonable conduct by the insurer. "Although we agree that the question is a close one, we find no justification for reversal. The applicable standard of review would permit reversal only if we find that the trial court abused its discretion."\textsuperscript{222} However, most Illinois courts do not follow the standard articulated by the Fourth District.

\textit{Urfer v. Country Mutual Insurance Co.}\textsuperscript{224} followed \textit{Ledingham}'s reliance on \textit{Fletcher} to determine bad faith:

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 the policyholder for the purposes of causing him to surrender his policy or disadvantageously settle a nonexistent dispute, constitutes a tortious interference with a protected property interest of its insured for which damages may be recovered.\textsuperscript{225}

The \textit{Urfer} court found that the complaint contained:

no allegations of fact purporting to show willful, vexatious or unreasonable conduct within the context of \textit{[Fletcher]} . . . It is well established that an actionable wrong cannot be made out by the vituperous and profuse interpolation of adjectives characterizing an act as having been wrongfully done. The pleading of conclusions alone will not suffice for factual allegations upon which a cause of action must be based.\textsuperscript{226}

\begin{footnotesize}
\begin{itemize}
    \item 222. 113 Ill. App. 3d 233, 446 N.E.2d 570 (4th Dist. 1983).
    \item 224. 60 Ill. App. 3d 469, 376 N.E.2d 1073 (4th Dist. 1978).
    \item 225. \textit{id.} at 472, 376 N.E.2d at 1075 (quoting \textit{Fletcher}).
    \item 226. \textit{id.} at 473, 376 N.E.2d at 1075-76 (quoting Alswang v. Claybon, 40 Ill. App. 3d 147, 351 N.E.2d 285 (1st Dist. 1976)).
\end{itemize}
\end{footnotesize}
Urfer seems to require conduct substantially the same as the defendant’s conduct in Fletcher. In Urfer, the defendant insurer, Country Mutual, failed to pay Delmar Urfer’s hospital and medical bills and failed to make income continuation payments.\textsuperscript{227} The third amended complaint did not seek recovery for breach of contract, but “sounded only in tort for compensatory and punitive damages alleging a willful refusal to pay.”\textsuperscript{228}

Urfer claimed that he was obliged to sell portions of his farm business because of Country Mutual’s refusal to pay on the policy.\textsuperscript{229} However, since the complaint did not allege that Country Mutual had been advised of the sale, the court found that Urfer failed to allege poverty.\textsuperscript{230}

The court discussed what would constitute a prima facie case for tortious breach of an insurance contract under Fletcher:

\begin{quote}
[In Fletcher] a \textit{prima facie} case for an action in tort arose where the defendant had numerous medical reports establishing the fact of disability; a medical report on a surgical fusion of a vertebra with the medical opinion that it would interfere with employment; defendant knew that plaintiff was unable to work and its investigative report showed that plaintiff was impoverished as the result of such denial of payments while he was unable to work; that defendant misrepresented the fact as to a pre-existing defect in discontinuing payment and defendant’s offer to compromise plaintiff’s claim was conditioned upon a complete release of that claim.\textsuperscript{231}
\end{quote}

In Fletcher, the plaintiff was injured at work while lifting a heavy object. He was surgically treated for a hernia, returned to work, but was eventually placed on disability for continued problems with his back. There was “virtually unanimous” agreement that the plaintiff was disabled because of the back injury.\textsuperscript{232} Fletcher subsequently was hospitalized for a myelogram. His consulting physicians recommended surgical fusion of a spinal disc. The defendant insurer, Western National, received a letter from one of the physicians that stated:

\begin{quote}
I am sure that you are well aware of the fact that Mr. Fletcher has a large family and if such surgery were performed subsequently his employment outlook would be very poor to say the least.\textsuperscript{233}
\end{quote}

\begin{footnotes}
\item[227] 60 Ill. App. 3d at 470, 376 N.E.2d at 1073. Urfer, who was hit by a school bus, previously received $50,000 from the school district in a settlement. His first two complaints were dismissed, because they were based on the defendant’s breach of a “no fault” insurance contract under the Illinois “no fault” insurance statute, which had been held unconstitutional. 60 Ill. App. 3d at 470, 376 N.E.2d at 1074.
\item[228] \textit{Id.} The third amended complaint was mistakenly referred to as the second amended complaint in the trial court’s order of dismissal.
\item[229] \textit{Id.} at 474, 376 N.E.2d at 1076.
\item[230] \textit{Id.} The court also noted that the first medical report to establish disability was delivered to Country Mutual more than three years after the injury. \textit{Id.}
\item[231] \textit{Id.}
\item[232] \textit{Fletcher}, 10 Cal. App. 3d at 387, 89 Cal. Rptr. at 83.
\item[233] \textit{Id.} at 387, 89 Cal. Rptr. at 83.
\end{footnotes}
While Fletcher was not working after the hernia surgery, Western National paid him $150.00 per month under the sickness portion of his disability insurance policy. After being notified of the surgical fusion of the disc, Western National's claims supervisor elected to treat the claim under the "sickness" provision of the policy, which exposed the company to liability for only two years. The "injury" provision would have exposed the company to liability for thirty years, a difference in exposure of more than $50,000.00.

Western National refused to make any payment to Fletcher. It accused Fletcher of misrepresenting his condition by failing to reveal a congenital condition when he applied for insurance, "[n]otwithstanding the complete absence of any investigation concerning a congenital defect." Initially, Western National demanded that Fletcher pay $2,250.00, less the amount of his premiums, for benefits received under the policy. Finally, Western National offered to allow Fletcher to keep the payments already made to him, in consideration for cancellation of his policy.

Urfer stated that defendant Country Mutual did not act in bad faith because its conduct was unlike Western National's conduct in Fletcher. This emphasis on the malicious conduct in Fletcher should not go to the plaintiff's ability to state a cause of action. Such ability should be based on an objective standard of what constitutes a breach of the covenant of good faith and fair dealing or a violation of the Unfair Practices Act. The degree of maliciousness goes to whether punitive damages are properly assessed.

It is peculiar that the Illinois courts rely almost exclusively on the malicious conduct in Fletcher to determine if a complaint states a cause of action for bad faith. The more liberal standard adopted by most California courts is whether or not benefits were unreasonably withheld. The applicable California standard jury instruction reads:

An insurance company which fails to deal fairly and in good faith with its insured by refusing unreasonably to pay the insured for a valid claim covered by the policy is subject to liability for all damages proximately caused thereby.

In Debolt, and Tobolt, two additional Illinois Appellate Courts relied on Fletcher to hold that plaintiffs failed to state a sufficient cause of action for intentional infliction of emotional distress. In Debolt, James Debolt purchased a disability income policy from Mutual of Omaha. Debolt injured his back and became totally disabled as defined by his

234. Id. at 389, 89 Cal. Rptr. at 85.
235. Urfer, 60 Ill. App. 3d at 473, 376 N.E.2d at 1075.
238. 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).
insurance policy. In Count One of his complaint, Debolt alleged that Mutual of Omaha, cognizant of his physical incapacity and financial problems, delayed and ultimately ceased payments, and "shuffled" his claim file between Illinois and its home office in Nebraska. When the disability benefits were substantially in arrears, Mutual of Omaha offered to re-purchase the contract of insurance at "an unconscionably low figure." In Count Two, Debolt sought $5,000,000 in punitive damages for Mutual of Omaha's breach of the duty of good faith and fair dealing. Count Three sought $250,000.00 in compensatory damages for intentional infliction of emotional distress.

The trial court granted defendant's motion to dismiss Counts Two and Three with prejudice. The Third District Appellate Court affirmed. The court based its rejection of the action for intentional infliction of emotional distress on the plaintiff's failure to meet the standard pleading rules:

[W]e find that [plaintiff's complaint] . . . is fraught with conclusions of fact unsupported by allegations of specific facts, i.e., that defendant instilled in plaintiff a fear for his life and that defendant instituted a policy designed to coerce the plaintiff into surrendering his policy.

The court concluded that the "specific facts" pled by plaintiff were not enough to show "outrageous conduct" by the insurer. Debolt relied on the Illinois Supreme Court's refusal to find sufficient facts to state a cause of action based on far more "abusive conduct" in Public Finance Corp. v. Davis.

In Tobolt, the plaintiffs' home was extensively damaged by fire. The home was insured for up to $40,000.00 under an Allstate homeowner's policy. The plaintiffs alleged that Allstate failed to meet its obligation to pay for repairs to their home, clothing, personal property loss, and additional living expenses. They further alleged that Allstate's failure to meet this obligation caused plaintiffs indigence and great financial distress. Plaintiffs alleged that Allstate thus left them unable to make a "balloon note" payment of over $5,000.00 on their home, and compelled them to borrow money, accept gifts, and seek assistance of the American Red Cross to pay their bills. They alleged that their credit was damaged, and that they suffered extreme emotional distress as a result of Allstate's failure to meet its obligation.

240. Debolt, 56 Ill. App. 3d at 112, 371 N.E.2d at 375.
241. Id. at 117, 371 N.E.2d at 378. The plaintiff voluntarily dismissed Count One of the complaint in order to take the appeal.
242. Id. at 113, 371 N.E.2d at 375.
243. Id.
244. Id. at 114, 371 N.E.2d at 376.
245. 66 Ill. 2d 85, 360 N.E.2d 765 (1976).
246. 75 Ill. App. 3d 57, 393 N.E.2d 1171 (1st Dist. 1979).
247. Id. at 59-60, 393 N.E.2d at 1172-73.
In addition, the plaintiffs alleged that:

Allstate had notice and knew, or had reason to know full well, that its deliberate and unwarranted refusal to honor numerous demands during a time when plaintiffs were in dire need of the insurance proceeds would be and was in reckless disregard of and harmful to the interest of plaintiffs.248

As in Debolt, the Tobolt court relied on Public Finance Corp. v. Davis.249 The court found that a defendant's conduct must be extreme and outrageous; a tortious, criminal, or a malicious intent is not enough. "Liability has been found only where the conduct has been so outrageous in character, and so extreme in degree, as to go beyond all possible bounds of decency . . . ."250 The emotional distress suffered must be severe, and the conduct must be conduct from which "the actor knows severe emotional distress is certain or substantially certain to result."251 The court found that plaintiffs had failed to sufficiently allege these elements:

The allegations of count two and the correspondence incorporated in it show that the only dispute between plaintiffs and Allstate was the amount of the adjustment and the amount owing them. No facts are alleged showing Allstate's adjustment of the fire loss constituted outrageous conduct by Allstate.252

The "correspondence" discussed the Tobolts' assignment of Worldwide Public Adjusters to represent their interest in the loss. Worldwide Public Adjusters had hired its subsidiary, Worldwide Construction Company, to repair the Tobolts' dwelling. Allstate insisted that any repairs completed improperly were the responsibility of Worldwide Adjusters and Worldwide Construction:

In the present case, defendant adjusted the loss based upon its own investigation and the independent investigation of plaintiffs' public adjuster. In addition, plaintiffs' complaint contains no allegations of bad faith "settlement" negotiations or outrageous conversations with plaintiffs.253

Both Debolt and Tobolt distinguished Eckenrode v. Life of America Insurance Co.,254 in which a federal district court upheld a plaintiff's cause of action for intentional infliction of emotional distress. In Eckenrode, the plaintiff's husband was a homicide victim. The plaintiff met all conditions of her husband's life insurance policy and repeatedly demanded

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248. *Id.* at 60, 393 N.E.2d at 1173.
249. 66 Ill. 2d 85, 360 N.E.2d 765 (1976).
250. *Tobolt*, 75 Ill. App. 3d at 63, 393 N.E.2d at 1175 (quoting *RESTATEMENT (SECOND) OF TORTS* § 46 comment d (1965).
252. *Tobolt*, 75 Ill. App. 3d at 64, 393 N.E.2d at 1176.
253. *Id.* at 65, 393 N.E.2d at 1177.
254. 470 F.2d 1 (7th Cir. 1972).
payment, but the defendant refused to pay. "Denied payment by insurer, [plaintiff] was required to borrow money to support her family, while her financial condition worsened. The family was required to live with, and accept charity from a relative." 255

The plaintiff alleged that the insurer knew or should have known of her dire need of the policy proceeds, but that it repeatedly and deliberately refused her demands for payment. "Insurer, knowing full well that plaintiff needed the proceeds of the policy to provide necessaries for her children, applied 'economic coercion' in refusing to make payment on the policy, and in 'inviting' plaintiff to 'compromise' her claim by implying it [insurer] had a valid defense to the claim." 256

Tobolt said of Eckenrode:

[D]efendant's refusal to pay accidental death benefits was based on a bad faith insistence on a non-existent defense. The court held that refusal to pay, under circumstances where plaintiff's need for the proceeds was great and defendant's duty to pay was clear, could constitute extreme and outrageous conduct and entitle plaintiff to recover for severe emotional distress. 257

Tobolt emphasized that Eckenrode "was careful to point out that 'settlement tactics may be privileged under circumstances where an insurer has done no more than insist upon his legal rights in a permissible way' . . . From the correspondence attached to plaintiffs' amended complaint, it is apparent that Allstate was only 'insisting upon its legal rights in a permissible way.' " 258 However, Tobolt ignored Fletcher's declaration about an insurer's "privilege" to conduct settlement negotiations:

Undoubtedly an insurance company is privileged, in pursuing its own economic interests, to assert in a permissible way its legal rights and to communicate its position in good faith to its insured even though it is substantially certain that in so doing emotional distress will be caused. The social utility served by recognition of this privilege is obviously enhanced when the privilege is exercised in connection with settlement negotiations, which are certainly to be encouraged.

Nevertheless, the exercise of the privilege to assert one's legal rights must be done in a permissible way and with a good faith belief in the existence of the rights asserted . . . Even if it could be said that defendants were asserting their legal rights in good faith, they were not privileged to do so in an outrageous manner . . . Settlement implies the existence of a good faith dispute, and there is no public policy in favor of an attempt to coerce settlement of a nonexistent dispute by outrageous means." 259

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255. Id. at 2.
256. Id.
257. Tobolt, 75 Ill. App. 3d at 66, 393 N.E.2d at 1177.
258. Id.
259. Fletcher, 10 Cal. App. 3d at 395-96, 89 Cal. Rptr. at 89 (citations omitted).
C. Relaxed Pleading Requirements for Emotional Distress

Tobolt distinguished the California case of *Crisci v. Security Insurance Co. of New Haven, Conn.* The Tobolt court held that:

[where other interests have been involved, mental distress may be an element of damages not requiring “outrageous” conduct or “severe” mental distress, but that where the claim is for the independent tort of intentional infliction of emotional distress that conduct must be “outrageous” and the emotional distress “severe.” In *Crisci*, other interests were invaded.]

However, *Crisci* is indistinguishable: both Debolt and Tobolt sued not only for intentional infliction of emotional distress, but also for breach of the implied covenant of good faith and fair dealing. Under *Fletcher*, this breach would constitute interference with a protected property interest, and all damages proximately flowing from the breach, including emotional distress, would be recoverable.

*Tobolt* and *Debolt* did not mention *Gruenberg v. Aetna Insurance Co.*, another California case, which held that plaintiffs could recover damages for mental distress incurred in connection with other injuries. Jerome Gruenberg owned a restaurant that was insured against fire loss by the three defendant insurers. Gruenberg was charged with arson after the restaurant burned down. A claims adjuster for an independent adjusting agency testified at the preliminary hearing that Gruenberg had excessive fire insurance coverage. The magistrate eventually dismissed the charges for lack of probable cause. During the pendency of the criminal proceedings, defendants requested that Gruenberg submit to an exam under oath in compliance with his policy provisions. Gruenberg refused to submit to the exam while the criminal charges were pending. After the charges were dismissed, Gruenberg’s attorney advised defendants that he would submit to an examination.

The insurers denied liability based on Gruenberg’s failure to appear for the exam. The court held that Gruenberg could recover for emotional distress although he failed to allege that defendants’ conduct was extreme and outrageous. Gruenberg did not sue for the independent tort of intentional infliction of emotional distress; he sued for mental distress associated with his failure to obtain benefits under his insurance policy. The California Supreme Court cited *Crisci*, in which it upheld recovery for “mental suffering.” The court stated, “We are satisfied that a plaintiff who as a result of a defendant’s tortious conduct loses his property and suffers mental distress may recover not only pecuniary loss but also for his mental distress.”

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261. 75 Ill. App. 3d at 66, 393 N.E.2d at 1177.
263. *Id.* at 579, 510 P.2d at 1042, 108 Cal. Rptr. at 489 (citing *Crisci*, 66 Cal. 2d at 433-34, 426 P.2d at 179, 58 Cal. Rptr. at 19) (emphasis added by *Gruenberg* court).
The court distinguished the Restatement (Second) of Torts, section 46, which applies only "to the independent tort of intentional infliction of emotional distress." The court relied on comment (b) to that section, which discusses emotional distress as an element of damages where other interests have been invaded. "[I]n the instant case we are concerned with mental distress resulting from a substantial invasion of property interests of the insured and not with the independent tort of intentional infliction of emotional distress . . . ." Gruenberg also distinguished Fletcher, since the theory of recovery in Fletcher was "predicated on the tort of intentional infliction of emotional distress alone," as opposed to Gruenberg, in which "recovery is sought on a totally distinct theory."

The only Illinois appellate court case to hold that a plaintiff's claim for intentional infliction of emotional distress was sufficient is Robertson v. Travelers Insurance Co. In Robertson, the Fifth District Appellate Court held that an employee stated a sufficient cause of action for "outrage" against his employer's workers compensation insurer. Robertson slipped and fell while employed as a carpenter. Travelers Insurance Company was his employer's workers compensation insurer. Robertson was required to file his claim for workers compensation no later than one year after the date upon which he last received direct benefits, which would have been March 30, 1973. A Travelers claims representative interviewed Robertson on March 26, but did not remind him of the running of the limitations period. On March 29, Travelers wrote Robertson a letter denying his claim. Robertson received the letter on April 2. A memo written by a claims representative stated: "On 4-3-73, this writer discussed the above case with supervisor Balsiger and claims attorney Knobbe and both of these individuals agree with this writer that the statute of limitations has expired . . . The Travelers Insurance Company should be 'home free'."

Robertson filed a workers compensation claim on April 2, 1973. The Supreme Court of Illinois held that Travelers was estopped from asserting the statute of limitations as a defense. During the pendency of the suit, plaintiff was recovering from surgery and could not work:

He was forced to borrow from relatives, go on public aid, and accept charity from the volunteer fire department of which he was a long-

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264. RESTATEMENT (SECOND) OF TORTS § 46 (1965).
265. Gruenberg, 9 Cal. 3d at 580, 510 P.2d at 1042, 108 Cal. Rptr. at 489.
266. Id.
267. Id. at 580, 510 P.2d at 1042, 108 Cal. Rptr. at 490.
268. Id.
269. 100 Ill. App. 3d 845, 427 N.E.2d 302 (5th Dist. 1981) (same court that decided Ledingham).
270. Id. at 855, 427 N.E.2d at 312.
271. Id. at 846, 427 N.E.2d at 305 (the insurer was under the impression that the statute of limitations ran on March 27, 1973).
272. Id. at 848, 427 N.E.2d at 306.
standing member, in order to provide for his family. This financial
strain upset the plaintiff and caused him to become, in his own words,
"highly nervous and forgetful."

The court held that these facts were sufficient to allege the tort of
"outrage." The court cited its own decision in Ledingham, holding that
an insurer could be sued under either of two tort theories: intentional
infliction of emotional distress, and interference with a protected property
interest for an insurer's threatened or actual bad faith refusal to pay
benefits under a policy.

The court approved Debolt as properly affirming the dismissal of a
complaint that "failed to allege specific facts which could be interpreted
as outrageous conduct by the defendant." The court also agreed with
Tobolt's holding that Allstate had only differed with its insured on the
amount of the loss and had insisted upon its legal rights in a permissible
way.

The court favorably compared the facts of Robertson's claim with
Eckenrode v. Life of America Insurance Co. The court found that the
conduct of Travelers Insurance Company was:

[Erroneously repeated at least as outrageous as the conduct held actionable by the Seventh Circuit. In some respects, the deviousness of Travelers' employees renders their action even more reprehensible. Furthermore, the plaintiff here suffered injury comparable to that suffered by Mrs. Eckenrode... All of these facts, alleged by the plaintiff, show conduct significantly more outrageous than that in Ledingham, Debolt, and Tobolt. This complaint resembles that in Eckenrode, and thus states a cause of action in outrage under Illinois law.

D. California Cases

California courts base their decisions on the common law principle found in Crisci v. Security Insurance Co., and Communale v. Traders & General Insurance Co. In every insurance contract there is an implied

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273. Id.
276. 470 F.2d 1 (7th Cir. 1972).
277. Robertson, 100 Ill. App. 3d at 853, 427 N.E.2d at 309. The court remanded the case for a new trial on the issue of damages, ruling that the trial court had erred in allowing punitive damages against the defendant.
280. 50 Cal. 2d 654, 328 P.2d 198 (1958).
BAD FAITH PRACTICES

1985] 433
covenant of good faith and fair dealing. It is the obligation, deemed to be imposed by the law, under which the insurer must act fairly and in good faith in discharging its contractual duties. When the insurer fails to deal \textit{fairly and in good faith} with its insured by refusing, without proper cause, to compensate for a loss covered by the policy, such conduct may give rise to a cause of action in tort for breach of the implied covenant of good faith and fair dealing.\footnote{California courts do not distinguish between the duty owed to the insured to settle his own claim or to settle a third-party claim against the insured:}^{282}

California courts do not distinguish between the duty owed to the insured to settle his own claim or to settle a third-party claim against the insured:

\textbf{[I]n \textit{Communale} and \textit{Crisci} we made it clear that [liability is imposed on the insurer] not for a bad faith breach of contract but for failure to meet the duty to accept reasonable settlements, a duty included within the implied covenant of good faith and fair dealing . . . In those two cases, we considered the duty of the insurer to act in good faith and fairly in handling the claims of third persons against the insured, described as a "duty to accept reasonable settlements"; in the case before us we consider the duty of an insurer to act in good faith and fairly in handling the claim of an insured, namely a duty not to withhold unreasonably payments due under a policy. \textit{These are merely two different aspects of the same duty}.}^{283}

California courts have also held that "the insurer's duty is unconditional and independent of the performance of plaintiff's contractual obligations."\footnote{284}^{284}

\textit{Fletcher} listed the elements of a prima facie case for the tort of intentional infliction of emotional distress:

\begin{enumerate}
\item outrageous conduct by the defendant;
\item the defendant's intention of causing, or reckless disregard of the probability of causing, emotional distress;
\item the plaintiff suffering severe or extreme emotional distress; and
\item actual and proximate causation of the emotional distress by the defendant's outrageous conduct.\footnote{The \textit{Fletcher} court held that the defendant's conduct met these requirements:}
\end{enumerate}

\textit{Viewed most favorably to plaintiff, the foregoing facts and inferences to be drawn therefrom established that defendants, without probable}\footnote{285}^{285}
cause for believing that plaintiff had made an intentional material misrepresentation or that his disability was due to anything other than his injury in January 1965, embarked upon a concerted course of conduct to induce plaintiff to surrender his insurance policy or enter into a disadvantageous "settlement" of a nonexistent dispute by means of false and threatening letters and the employment of economic pressure based upon his disabled and, therefore impecunious, condition (the very thing insured against) exacerbated by Western National's malicious and bad faith refusal to pay plaintiff's legitimate claim. Defendants concede that their conduct was deplorable and outrageous.\textsuperscript{286}

The \textit{Fletcher} court then discussed "severe" emotional distress:

\begin{quote}
It is for the court to determine whether, on the evidence, severe emotional distress can be found; it is for the jury to determine whether, on the evidence, it has in fact existed. It is our conclusion that there is sufficient evidence from which emotional distress of the requisite severity can be found and that there is substantial evidence to support the jury's determination that it in fact existed . . . .

It is true that plaintiff's testimony did not indicate that he suffered any traumatic emotional distress of the character of shock, horror or nausea, but the requisite emotional distress may consist of any highly unpleasant mental reaction such as fright, grief, shame, humiliation, embarrassment, anger, chagrin, disappointment or worry . . . Susceptibility of the plaintiff to emotional distress and a defendant's awareness thereof, have often been mentioned as significant in determining liability.\textsuperscript{287}
\end{quote}

The court also noted that the duration of the emotional distress is a factor to be considered in determining its severity. Although a number of "woeful occurrences"\textsuperscript{288} had befallen the plaintiff, a substantial part of plaintiff's emotional distress was a result of the "threatened and actual discontinuance of payments by defendants and the resulting economic consequences."\textsuperscript{289}

The court allowed punitive damages because plaintiff's case sounded in tort, not in contract. The court rejected defendant's contention that section 10111 of the California Insurance Code bars punitive damages.\textsuperscript{290}

Instead of following the California approach to bad faith actions, Illinois courts have tended to cite only those aspects of California cases which bolster their own very different analysis. By using only pieces of the larger California framework, the different Illinois districts have become divisive.

\begin{footnotes}
\item[286.] \textit{Id.} at 392, 89 Cal. Rptr. at 87.
\item[287.] \textit{Id.} at 397-98, 89 Cal. Rptr. at 99 (quoting \textsc{Restatement (Second) of Torts} § 46, comment j (1965)).
\item[288.] \textit{Id.} at 398, 89 Cal. Rptr. at 91.
\item[289.] \textit{Id.} at 399, 89 Cal. Rptr. at 91.
\item[290.] The California Insurance Code provides: "In life or disability insurance, the only measure of liability and damage is the sum or sums payable in the manner and at the times as provided in the policy to the person entitled thereto." \textsc{Cal. Ins. Code} § 10111 (West 1972). No California court has held that this section prohibits private causes of action or limits damage awards.
\end{footnotes}
BAD FAITH PRACTICES

in their fragmented approach to insurance law. Still, this fragmentation

291. The United States District Court for the Northern District of Illinois followed this pattern in Langendorf v. Travelers State Ins. Co., 625 F. Supp. 1103 (N.D. Ill. 1985). In Langendorf, the district court granted defendant Travelers' motion to dismiss Count V of the plaintiffs' complaint, which the court interpreted as a claim for consequential damages resulting from Travelers' breach of the implied duty of good faith and fair dealing. The Langendorf court recognized that "[the Illinois appellate] courts have not been particularly clear about what is required to state a claim for the breach of the duty of good faith dealing." Id. at 1108. However, it ignored this acknowledgment and narrowly defined the two elements necessary to plead such a claim, relying on another federal district court case, Barr v. Safeco Ins. Co. of America, 583 F. Supp. 248 (N.D. Ill. 1984), and on the very strict holding of the Fourth District Appellate Court in Urfer v. Country Mut. Ins. Co., 376 N.E.2d 1073 (1978).

The Langendorf court held that the plaintiffs failed to plead two necessary elements: (1) that "the insurer must have known it was liable on the contract but nonetheless refused to pay"; and (2) that "the insurer must also know that if it did not pay on its policy, substantial damage and injury would likely befall the insured." Id. at 1108-09. In Langendorf, the plaintiffs alleged that plaintiff Sheri Langendorf was hospitalized due to severe complications after giving birth, and incurred approximately $115,000 in medical bills. Although the Langendorfs' group insurance policy provided for "unlimited medical and hospital care benefits," Travelers claimed there was a $50,000 limit on the benefits payable, and refused to pay any amount over the $50,000 limit. Id. at 1104. Even though these facts were alleged, the court dismissed a construction of Count V of the complaint for consequential damages caused by Travelers' breach of the implied duty of good faith and fair dealing, finding that the plaintiffs failed to allege facts meeting the court's self-initiated determination of very strict requirements of a bad faith cause of action.

The court also found that Count V could not be interpreted as a claim for intentional infliction of emotional distress, following the reasoning of Anderson v. Mutual of Omaha Ins. Co., 594 F. Supp. 726 (S.D. Ill. 1984), in which the Federal District Court for the Southern District of Illinois held that § 767 preempts a claim under that theory for an insurer's outrageous delay in settling a claim.

The court did uphold one narrow interpretation of Count V: it held that a claim for the "contract-based consequential injury of emotional distress" had been "well pled" by the plaintiffs, but it did not rule on the issue of whether such consequential injuries are compensable in a claim for breach of insurance contract because the parties had not addressed that issue on appeal. The court strongly implied that such a claim would be dismissed once it had been properly addressed. Id. at 1106.

The court also dismissed the construction of Count VI of the plaintiffs' complaint as a claim for consequential damages for Travelers' breach of the duty of good faith and fair dealing. The court again found that the plaintiffs had failed to plead the two necessary elements to overcome dismissal. It interpreted Count VI as a claim for another consequential damage resulting from the alleged breach of contract, but refused to rule on whether such damages are recoverable. Id. at 1109.

This decision is one more example of the Illinois courts' insistence on dismissing actions for breach of the implied covenant of good faith and fair dealing at the pleading stage, without giving the plaintiffs the opportunity to be heard on the merits. This unwillingness to address bad faith issues head-on has apparently infected the federal courts located in Illinois as well.

The federal court in Langendorf failed to follow its own statement of its duty that "when the highest state court has not yet spoken on an issue, a federal district court is obligated to predict what that court would do if presented with the issue." Id. at 1105. Instead of examining what the Illinois Supreme Court would do when confronted with the conflicting appellate court decisions, Langendorf capriciously chose the strictest requirements it could for pleading the
seems to be overridden by an almost universal reluctance to find adequately stated causes of action, unless unusually strict pleading requirements are met. Although some districts have theoretically approved bad faith actions, such requirements have made actions difficult to maintain and large damage awards a virtual impossibility.

CONCLUSION

Illinois needs to clarify the interpretation of Insurance Code section 767. As currently applied by intermediate appellate courts, section 767 needlessly limits compensatory damages and emasculates Insurance Code section 766.6. Conflicting decisions of the various appellate districts can be resolved by looking to history, public policy, and the laws of other jurisdictions. Specifically, section 767 should not preempt common law remedies. The attorney fees provision adds an element of compensatory damages not ordinarily available in a contract setting. The availability of an additional compensatory remedy does not affect the general practices of insurance companies. Punitive damages have a therapeutic effect on the type of conduct prohibited by the statute. Punitive damages have traditionally been available for malice, oppression and fraud and can be adequately controlled by judges at both the trial and appellate levels. Illinois should and can make its Unfair Practices Act protect against predatory practices.

tort of bad faith.

The Langendorf court also found that no private cause of action could be brought under § 766.6 of the Illinois Insurance Code, following the consensus of the appellate courts. For a further discussion of this, see text accompanying footnotes 64-112.