IN THE DISTRICT COURT OF THE FIRST JUDICIAL DISTRICT OF THE STATE OF IDAHO, IN AND FOR THE COUNTY OF KOOTENAI

HARRY HARTMAN and PAMELA HARTMAN, individuals, as individuals and assignees of Jon Graf's rights set forth in Assignment Dated December, 2001, Plaintiffs, vs. STATE FARM FIRE AND CASUALTY COMPANY, a foreign corporation doing business in the State of Idaho, Defendants.	**CASE NO. CV-03-06793** MEMORANDUM OPINION AND ORDER IN RE: DEFENDANT'S MOTION FOR SUMMARY JUDGMENT

Plaintiffs pursued claims against an insurer pursuant to an assignment of rights from its insured. Upon refusal to make payment, Plaintiffs filed the instant case against the insurer. Defendant moved for Summary Judgment. Motion denied.

Joseph Jarzabek, ELSAESSER JARZABEK ANDERSON MARKS ELLIOTT & McHUGH, attorneys for Plaintiffs.

James D. LaRue, Jeffrey A. Thomson, and Jon M. Bauman, ELAM & BURKE, attorneys for Defendants.

I

FACTUAL AND PROCEDURAL BACKGROUND

A. Underlying Lawsuit

In order to understand this case, it is necessary to review the underlying facts and an underlying case based upon those facts. Harry and Pamela Hartman ("Hartmans") are the parents of Ty Hartman. On November 8, 1998, Ty disappeared after spending the evening with friends near Bonners Ferry. About a month later on December 9, 1998, Hartmans filed a wrongful death lawsuit in Boundary County against the three friends and their parents. One of those friends was Jon Graf.[1]

Eventually, the defendants in that lawsuit led police to the charred remains of Ty. They admitted that Ty had died early on the morning of November 9, 1998, and that some of them had burned his body.

State Farm Fire and Casualty Company ("State Farm") had issued a Homeowner's Policy identifying Dan Studer as the named insured. Under the terms of that policy, Dan and Jan Studer were insureds; Jan Studer's son, Jon Graf, was also an insured so long as Jon was a resident of the Studer household. That policy was in effect on November 8, 1998; Jon was a resident of the Studer household at that time.

The Studers and Jon Graf made claims against State Farm for defense and indemnity in the wrongful death case. State Farm provided them with a defense subject to a reservation of rights. Samuel Eismann was retained by State Farm to defend the Studers and Jon Graf ("Graf").

[1] ***See Hartman v. Keane, et al.***, Bonner County Case No. CV-98-22027. In the Complaint in that case, Plaintiffs Hartman alleged, among other things, the following causes of action: (1) Battery; (2) Wrongful Death; (3) Wrongful Death – Malicious Killing; and (4) Intentional Infliction of Emotional Distress.

At some point in time but apparently close to trial, State Farm retained Michael E. McNichols to represent it. Mr. McNichols filed a Motion to Intervene as a Matter of Right and Alternative Motion for Permissive Intervention. An Order Granting in Part and Denying in Part State Farm's Motion was entered. State Farm was permitted to intervene for the limited purpose of submitting jury instructions and special verdict questions and participating in the instruction conference.

During the underlying lawsuit, Hartmans offered to settle the case against Graf and his parents well within the policy limits. By letter dated April 24, 2001, Hartmans offered to settle the entire case against all defendants for $300,000.00, which would have required State Farm to pay $100,000.00 for its share. Hartmans met in two mediation sessions with counsel for two of the three defendants, including counsel for Graf. Near the end of the second session, counsel for defendants indicated that they would settle for a total of $25,000.00 between the two parties, or $12,500.00 each, and that was a final offer. At that point, Hartmans had agreed to settle for $150,000.00, or $75,000.00 each. No settlement was reached.

On January 16, 2001, Hartmans filed a Motion to Amend Complaint eliminating all claims against Studers and seeking dismissal of Studers from the wrongful death action. On February 28, 2001, an Order was entered dismissing Studers from the lawsuit.

Shortly before trial in the wrongful death action, Defendant Eric Dante agreed to pay $65,000.00 to Hartmans to settle his portion of the case. State Farm refused to eliminate Graf's liability, both for negligence and for intentional harm to Ty. At that point, Graf was subjected to liability beyond the policy limits.

After the case failed to settle through State Farm, Graf agreed to end the underlying lawsuit by allowing a judgment to be entered against him on December 18, 2001. Documents in the form of an Offer of Judgment by Graf and Notice of Acceptance of Offer of Judgment by Hartmans were executed. On the same day, a Judgment in favor of Hartmans was entered against Graf in the amount of $400,000.00. The Judgment was obtained without involvement or consent of the court or State Farm.

Graf's State Farm appointed attorney drafted an Assignment of Claims and Offer of Judgment whereby Hartmans agreed not to execute on the judgment against Graf in exchange for an assignment by Graf of any and all claims that Graf had against State Farm. That Assignment was executed later in the day on December 18, 2001.

The Assignment of Claims transferred to Hartmans all of Graf's rights, title, interest, and privileges, if any, in and to any claims and causes of action whatsoever that Graf may have had against State Farm. The Assignment of Claims acknowledged that Graf denied liability and that Graf did not have consent from State Farm to settle or submit the Offer of Judgment.

After State Farm was informed of the existence of the Judgment and Assignment, it advised Graf by letter that there was no coverage under the policy. On March 27, 2002, Hartmans' attorney, Joseph Jarzabek, demanded payment on the Judgment against Graf. Two days later on March 29, 2002, State Farm sent a letter informing Mr. Jarzabek that it would not pay the Judgment against Graf.

B. Present Lawsuit

On September 19, 2003, Hartmans filed this action claiming that State Farm had breached its contract and had acted in bad faith against Graf.[2] Hartmans seek to enforce the Judgment entered on December 18, 2001. State Farm filed an Answer.

Thereafter, State Farm moved for Summary Judgment. State Farm's Motion is supported by: a Statement of Undisputed Facts; an Affidavit of James D. LaRue, to which several exhibits, including letters and a copy of the policy, are attached; a Memorandum of Law; and a Reply Brief.

Hartmans have filed an Objection to State Farm's Motion for Summary Judgment. The Objection is supported by: a Memorandum in Support of Objection; an Affidavit of Joseph Jarzabek; and an Affidavit of William T. Tann.

State Farm filed a Motion to Strike the Affidavit of William T. Tann, which is dated July 1, 2004.

II

MOTION TO STRIKE

State Farm moved to strike the Affidavit of William T. Tann. Mr. Tann is a former claims representative. It is his opinion that State Farm breached its duty to settle the case for $75,000.00 and it was reasonable for the amount of damages in the Judgment to be $400,000.00.

State Farm brings its Motion to Strike pursuant to ***Rule 56(e), Idaho Rules of Civil Procedure***. Affidavits must be made on personal knowledge, must show that the

[2] In the First Amended Complaint, Hartmans allege "CAUSES OF ACTION – Bad Faith and Breach of Contract" and "CAUSE OF ACTION – Direct Claim."

affiant is competent to testify to the matters, and must set forth facts that would be admissible in evidence.

Basically, State Farm complains that (1) Mr. Tann did not make the Affidavit based on personal knowledge; (2) Mr. Tann did not show affirmatively that he was competent to testify; (3) Mr. Tann reviewed documents, but foundation is lacking because he does not specify or attach documents to which he referred, and (4) Mr. Tann states legal conclusions. Plaintiffs have now filed the Supplemental Affidavit of William T. Tann, dated July 21, 2004, to which is attached as exhibits the documents that he relied upon in reaching the opinions in his previously filed Affidavit.

The entire Affidavit of William T. Tann will not be stricken. Only those portions of the Affidavit that are admissible in evidence, however, will be considered in determining the Motion for Summary Judgment. To the extent that a legal conclusion might be stated, such will not be considered; Mr. Tann may, however, render an opinion.

III

STANDARDS FOR SUMMARY JUDGMENT

Summary judgment is provided for where there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. In order to make that determination, the court looks to "the pleadings, depositions, and admissions on file, together with the affidavits, if any . . . ." ***Rule 56(c), Idaho Rules of Civil Procedure***.

On a motion for summary judgment, the facts in the record are to be liberally construed in favor of the party opposing the motion. Where a jury has been requested, the party opposing the motion is to be given the benefit of all favorable inferences that might reasonably be drawn from the evidence. If the record contains conflicting

inferences or if reasonable minds might reach different conclusions, a summary judgment must be denied. ***Roell v. City of Boise***, 130 Idaho 199, 938 P.2d 1237 (1997); ***Bonz v. Sudweeks***, 119 Idaho 539, 808 P.2d 876 (1991).

If there are no genuine issues of material fact, the court will determine whether a party is entitled to judgment as a matter of law. ***Zumwalt v. Stephan, Balleisen & Slavin***, 113 Idaho 822, 748 P.2d 406 (Ct.App. 1987), ***rev. denied*** (1988).

According to ***Berg v. Fairman***, 107 Idaho 441, 444, 690 P.2d 896 (1984), the "purpose of summary judgment proceedings is to eliminate the necessity of trial where facts are not in dispute and where existent and undisputed facts lead to a conclusion of law which is certain."

IV

DISCUSSION

Basically, Hartmans assert three causes of action: (1) Claim of Breach of Contract; (2) Claim of Bad Faith; and (3) Direct Action upon the Judgment. State Farm maintains that Hartmans obtained no rights pursuant to the Assignment that would entitle them to pursue any claims against State Farm. As assignees, Hartmans stand in the shoes of Graf and take only those rights he had against State Farm. State Farm contends that, because Graf had no rights, Hartmans lack standing to pursue the instant lawsuit.

Hartmans, on the other hand, claim that (1) Graf did not need State Farm's consent to settle out of court after State Farm had refused to reasonably settle within the policy limits; and (2) Graf could assign his rights under the Homeowners Policy without State Farm's consent after a loss occurred.

A. Application of the Non-Assignment Provision of the Homeowners' Policy to Graf's Assignment of the Claim

The first issue to be addressed is the overall application of Idaho law to the Assignment in this case.[3] Hartmans and Graf entered into an Assignment of Claims. The Assignment of Claims stated as follows:

> [Jon Graf assigns] all of his right, title, interest and privileges, ***if any***, in and to any claims and causes of action whatsoever that he may have against State Farm Fire and Casualty Company, and its successors, if any, under Policy Number 12 27 5485-9, effective October 10, 1998 to October 10, 1999.
> . . .
> Nor does [Graf] have consent from State Farm Fire and Casualty Company to settle the above referenced action or to submit an offer of judgment therein.

(Emphasis added.) In consideration of the Assignment, Hartmans agreed not to execute on the judgment.

State Farm had issued a Homeowners ("HO") Policy insuring Studers and Graf. The Policy contained the following provision:

> The ***insured*** shall not, except at the ***insured's*** own cost, voluntarily make payments, assume obligations or incur expenses.
> . . .
> Assignment of ***this policy*** shall not be valid unless we give our written consent.

(Emphasis added.)

Insurance contracts are addressed in Chapter 18 of Title 41 of the Idaho Code. According to ***Idaho Code § 41-1826***, "[a] policy may be assignable or not assignable, as provided by its terms." No Idaho case has specifically interpreted that section.

State Farm argues that the non-assignment provision found in the HO Policy is valid and enforceable. In cases arising in other contexts, the Idaho Supreme Court has

[3] It appears that this is an issue of first impression and that, to date, the Idaho appellate courts have not directly addressed this particular question.

held that provisions in bilateral contracts, which restrict assignment without the consent of the obligor, are valid and enforceable. Also, the general rule is that a third party beneficiary has no greater rights than the named insured. ***Bantz v. Mutual of Enumclaw***, 124 Idaho 780, 864 P.2d 618 (1993).

Hartmans recognize that the Idaho law allows companies to limit the assignment of insurance policies. They draw a distinction, however, between limiting the assignment of "insurance policies" and prohibiting the assignment of "claims" under the policies, especially after a loss has occurred.

While the Idaho Supreme Court has not explicitly ruled on whether an assignment of rights after a loss is allowed, its opinions have implied that a party could assign its rights after a loss. ***See***, for example, ***Exterovich v. City of Kellogg***, 139 Idaho 439, 80 P.3d 1040 (2003); ***Simplot v. Western Heritage Insurance***, 132 Idaho 582, 977 P.2d 196 (1999).

Although there is a split, persuasive authority exists for the proposition that a provision in an insurance policy prohibiting assignments does not make the assignment of claims under the policy invalid where the assignment was made after the events giving rise to the liability had occurred. ***Public Utility District No. 1 of Klickitat County v. International Insurance Company***, 124 Wash.2d 789, 881 P.2d 1020 (1994). ***See also Conrad Brothers v. John Deere Ins. Co.***, 640 N.W.2d 231 (Iowa 2001).

There are good policy reasons for not permitting the assignment of an insurance policy itself. An individual with a good risk record is prohibited from assigning his or her policy to someone who is at greater risk, thus allowing the insurance companies to

determine their exposure when they issue a policy. The situation is different, however, after a claim has arisen under the policy.

Based on the wording of the Homeowners Policy, the Idaho statutes, the Idaho case law, and persuasive authority from other jurisdictions, a claim can be assigned even though there is a provision prohibiting the assignment of policies without the insurer's consent in the insurance policy after the events giving rise to the liability have occurred. Any loss had already occurred and any claims had already arisen when Graf executed the Assignment of Claims. A review of the language in the Assignment of Claims executed by Graf indicates that Graf was assigning all of his rights in and to any claims that arose under the HO Policy. He was not, however, assigning the policy; rather, he was assigning the claims. Therefore, it is concluded that Jon Graf could assign his claim to Hartmans.

B. Assignment of Claims to State a Breach of Contract Claim

The second issue is whether or not Jon Graf's assignment of his claims can be used as a means to state a breach of contract claim against State Farm. Hartmans contend that, by reason of Graf's assignment of claims, they are entitled to enforce any breach of contract claim that Graf might have had against State Farm. According to Hartmans, a breach occurred when State Farm failed to reasonably settle the wrongful death claim under the HO Policy and when that failure to settle resulted in liability to Graf in excess of the Policy's limits.[4]

The obligations owed by State Farm to Graf were stated in the HO Policy as follows:

[4] In the First Amended Complaint, Hartmans allege that the "failure to reasonably settle was also a breach of Insurance Company's obligations under the policy of insurance, and has resulted in liability to Jon Graf in excess of the policy's limits." ***See*** First Amended Complaint, p. 4.

> If a claim is made or a suit is brought against an ***insured*** for damages because of ***bodily injury or property damage*** to which this coverage applies, caused by an ***occurrence***, we will:
> 1. ***pay up to our limit of liability for the damages for which the insured is liable***; and
> 2. provide a defense at our expense by counsel of our choice. We may make any investigation and settle any claim or suit that we decide is appropriate. Our obligation to defend any claim or suit ends when the amount we pay for damages, to effect settlement or satisfy a judgment resulting from an ***occurrence*** equals our limit of liability. (Emphasis added.)

It is undisputed that State Farm provided Graf with a defense subject to a reservation of rights. In the Assignment of Claims, Graf acknowledged that he "has denied liability . . . and continues to do so." According to State Farm, it had no obligation to Graf to make payment to Hartmans because Graf's legal liability has never been determined. State Farm argues that, although Graf has denied liability, Hartmans' claim for breach of contract presumes liability to Graf in excess of the HO Policy's limits.

The duties owed by Graf to State Farm after a loss are described in the HO Policy as follows:

> In case of an accident or ***occurrence***, the ***insured*** shall perform the following duties that apply. You shall cooperate with us in seeing that these duties are performed.
> . . .
> e. the ***insured shall not***, except at the insured's own cost, ***voluntarily*** make payments, ***assume obligations*** or incur expenses. (Emphasis added.)

State Farm contends that, when Graf agreed to allow judgment to be entered against him, he assumed an obligation in violation of this condition of coverage so he could not thereafter have demanded that State Farm pay the judgment. Basically, State Farm argues that there is no breach of contract claim for Hartmans to pursue.

Hartmans, on the other hand, point out that it was not Graf's Offer of Judgment that gave rise to State Farm's liability under the HO Policy; rather, it was Graf's failure to

get timely care for Ty Hartman that gave rise to any liability that State Farm might have. Thus, according to Hartmans, State Farm breached its contract and acted in bad faith when it refused to settle the case against Graf for well under the HO Policy limits. Hartmans argue that State Farm's conduct released Graf from the contractual obligations that would have otherwise been binding.

The denial of a party's right to receive the benefits of an agreement that has been entered into breaches the duty of good faith that is implicit in every contract. ***Parker v. Boise Telco Federal Credit Union***, 129 Idaho 248, 923 P.2d 493 (Ct.App. 1996). A claim for breach of the implied covenant of good faith and fair dealing sounds in contract. ***Hoyle v. Utica Mutual Insurance Co.***, 137 Idaho 367, 48 P.3d 1256 (2002).

In ***Openshaw v. Allstate Insurance Company***, 94 Idaho 192, 484 P.2d 1032 (1971), the assignees of the insureds brought a lawsuit against the insurer seeking damages for the insurer's bad faith in failing to settle the plaintiffs' damage claim against the insureds. According to ***Openshaw***, 94 Idaho at 194,

> Generally it can be said that an insurance company which contracts to defend its insured following a claim by a third party against the insured, is under a duty either to exercise "good faith" or to exercise due care (be free from negligence) in defending the action against its insured, and in considering offers to compromise the claim for an amount with the policy limits. 14 Couch on Insurance 2d, § 51:130 et seq., p. 626. Annot: 40 A.L.R. 2d 168.

Thus, an insurer is under a duty to exercise good faith in considering offers to compromise an injured party's claim against the insured for an amount that is within the insured's policy limits.

Guidance can also be found in ***City of Idaho Falls v. Home Indemnity Co.***, 126 Idaho 604, 888 P.2d 383 (1995).[5] It is well established that the duty to defend and the duty to indemnify are separate and unrelated obligations. Where the insured executed a settlement, the insurer's duty to indemnify arose so long as a potential liability for the insured existed which resulted in a reasonable settlement in view of the size of a possible recovery and the probability of the claimant's success against the insured. ***See also Exterovich v. City of Kellogg***, 139 Idaho 439, 80 P.3d 1040 (2003).

Based on the case law, State Farm had a duty under the insurance contract to exercise good faith in considering Hartmans' offer to compromise their claim against Graf. At this point, a genuine issue of material fact exists as to whether State Farm failed to exercise good faith in considering Hartmans' offer to compromise their claim against Graf; *i.e.*, whether State Farm failed to reasonably settle Hartmans' claim.[6] All inferences must be drawn in favor of the non-moving parties on the Motion for Summary Judgment. When all inferences are drawn in the non-moving parties' favor, State Farm's bad faith conduct released Graf from any requirement prohibiting him from settling the case on his own.

There is a genuine issue of material fact as to whether, after Graf executed the settlement, State Farm had a duty to indemnify under the HO Policy; such a

[5] In ***City of Idaho Falls***, there were issues involving both the duty to defend and the duty to indemnify. In the instant case, State Farm provided a defense under a reservation of rights.

[6] At this point, attention is directed back to the facts of this case. State Farm had a duty to exercise good faith in considering offers to compromise Hartmans' claim against Graf for an amount within the policy limits. Although Graf has denied liability, the complaint in the underlying case contained allegations of what might be called shocking conduct on the part of Graf and others. There were attempts at settlement in the underlying case. Hartmans offered to settle the entire case within the policy limits. Initially, Hartmans offered to settle the case for a sum that would have required State Farm to pay $100,000.00. Hartmans eventually agreed to settle for $75,000.00, but State Farm refused to settle and refused to pay more than $12,500.00. Thereafter, Graf agreed to end the underlying lawsuit by allowing the judgment in the amount of $400,000.00 to be entered against him. According to Hartmans, State Farm breached its duty to settle the case within the policy limits and the amount of the Judgment entered against Graf was reasonable in light of a likely recovery in a wrongful death case like this. ***See*** Affidavit of William T. Tann.

determination depends upon whether a potential liability for Graf existed and whether the settlement was reasonable in view of the size of possible recovery and the probability of Hartmans' success against Graf. When all inferences are drawn in favor of the non-moving parties, State Farm had a duty to indemnify Graf for a reasonable settlement with Hartmans. Although Hartmans may be unable to prevail at a jury trial on such matters as bad faith on the part of State Farm or reasonableness of the settlement amount, the evidence in the record on the Motion for Summary Judgment creates a genuine issue of material fact.

In conclusion, Graf's assignment of claims could act to state a breach of contract claim by Hartmans against State Farm.[7] There are genuine issues of material fact regarding bad faith on the part of State Farm, State Farm's duty to indemnify, and the reasonableness of the settlement reached by Graf. Therefore, State Farm's Motion for Summary Judgment cannot be granted.

C. Assignment of Claims to State a Bad Faith Tort Claim

1. A Bad Faith Claim Can Be Assigned

State Farm contends that a claim for bad faith cannot be assigned under the Idaho law. State Farm argues that whether the cause of action is assignable depends upon the same principle as whether the cause of action would survive the death of the plaintiff. Thus, if it survives, it may be assigned; if it doesn't survive, it may not be assigned.

Idaho follows the common law on abatement and survival of claims. There is no "survival statute" in Idaho. For example, pain and suffering do not survive the death of the plaintiff. Although claims arising out of a contract survive, tort claims regarding a

[7] For clarification and because it can sometimes be confusing, the claim for a breach of contract must be distinguished from a tort claim for insurance bad faith. This section deals with the cause of action for breach of contract. To that extent, the determination here is limited to that issue.

contract sound in tort because such claims arise from a legal duty imposed as a result of the contractual relationship between the parties. ***See Evans v. Twin Falls County***, 118 Idaho 210, 796 P.2d 87 (1990); ***Chenery v. Agri-Lines Corp.***, 106 Idaho 687, 682 P.2d 640 (Ct.App. 1984). Thus, according to State Farm, a claim for bad faith cannot be assigned because it arises from a tort.

On the other hand, Hartmans note that the Idaho Supreme Court has not explicitly addressed the issue of assignability of bad faith claims against insurance companies nor has it explicitly ruled that bad faith claims against insurance companies cannot be assigned.[8] According to Hartmans, implied approval of the assignment by an insured party of its rights to a bad faith claim to a third party exists in ***Truck Insurance Exchange v. Bishara***, 128 Idaho 550, 916 P.2d 1275 (1996),[9] and ***Simplot v. Western Heritage***, 132 Idaho 582, 977 P.2d 196 (1999).[10]

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[8] This appears to be an issue of first impression since the Idaho appellate courts have not directly ruled upon this precise issue.

[9] Dotys purchased an automobile from Bisharas; when tires on the vehicle failed, the Dotys were injured. Bisharas were insured by Truck Insurance Exchange. Settlement negotiations between Dotys and Truck ensued, but settlement was never concluded. The case went to jury trial and Bisharas were found to be 100% at fault. Judgment was entered in favor of Dotys in the amount of $4,000,000. Thereafter, Dotys obtained an assignment of Bisharas' bad faith claim against Truck in exchange for Dotys' covenant not to execute upon the judgment. The concurring opinion authored by Justice Schroeder must be noted, however. In his concurring opinion in ***Bishara***, 128 Idaho at 559, Justice Schroeder writes as follows:

> I concur in the result in this case without implying that an assignment of an insured's bad faith claim to a third party is valid. A third party could not bring a bad faith claim directly against the insurer, and there are considerations which may make it bad policy to allow the third party to bring that claim by way of assignment – for example the incentive to present settlement offers that are questionable to create a rejection by the insurance company that may thereafter be challenged as bad faith, thus bootstrapping a very limited policy to an open-ended policy. However, this question has not been presented in this appeal, and the result should not be read as approving assignment of bad faith claims by an insured to a third party.

Any implication regarding assignment is based upon the majority opinion.

[10] Simplot hired Green to apply fertilizer to fields and Green agreed to indemnify Simplot for all claims arising from misapplication of the fertilizer. Green purchased a commercial liability insurance policy from Western. When Green misapplied the fertilizer and Western refused to pay the damages, Green assigned his interest to Simplot. In ***Simplot***, 132 Idaho at 585, the Idaho Supreme Court stated as follows: "When an insured assigns rights to recover proceeds under an insurance policy, the assignee, when attempting to recover from the insurer, should be in the same position as the named insured . . . ." and "Green effectively

There is a division of authority among the states. In ***Safeco Insurance v. Butler***, 118 Wash.2d 383, 397, 823 P.2d 499 (1992) (quoting ***Kagele v. Aetna Life & Casualty Co.***, 40 Wash.App. 194, 197, 698 P.2d 90 (1985)), the Washington Supreme Court expressly ruled that "a claim by an insured against his insurer may be assigned to the injured party."[11] A covenant not to execute, coupled with an assignment of rights and a settlement agreement, does not release the insurer from its obligation. The rationale for this rule is to protect the insured at a time when the insured's insurance company has essentially abandoned the insured. If, when their insurance coverage is in doubt, insureds are offered a settlement that would relieve them of personal liability, it cannot be said that it is not in their best interest to accept the offer. There is a strong public interest in protecting insureds and allowing them to reach settlements in their favor when they have been abandoned or neglected by their insurance company.

Other states allow insured parties to assign their interests under an insurance policy after a judgment has been entered against them in excess of policy limits. ***See*** discussion in ***Critz v. Farmers Insurance Group***, 230 Cal.App.2d 788, 795, 41 Cal.Rptr. 401 (1964).[12] The rationale for this rule is that (1) settlements will be encouraged, and (2) there is fairness or equalization of the contenders' strategic advantages. Therefore, insureds may assign their claims against insurers so that they can shield themselves from the danger to which the company has exposed them and so that the company will give

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assigned to Simplot his rights as an insured to collect the money due under the policy and to sue Western for breach . . . ."

[11] The ***Butler*** court also stated that an insurer who accepts the duty to defend under a reservation of rights, but who then performs the duty in bad faith, is estopped from denying coverage.

[12] The ***Critz*** court also recognized that bad faith is a question of fact and that, if plaintiff could not show bad faith, she would be unable to prevail regardless of the assignment.

greater consideration to the interests of the policyholders. ***See also Smith v. State Farm Mutual Auto Ins. Co.***, 5 Cal.App.4th 1104, 7 Cal.Rptr.2d 131 (1992).

The majority rule is that an insured tortfeasor may assign claims for bad faith against its insurance company to an injured third party. ***See Medical Mutual v. Evans***, 330 Md. 1, 29, 622 A.2d 103 (1993); ***Clearwater v. State Farm Mut. Auto. Ins. Co.***, 161 Ariz. 590, 780 P.2d 423, 426-27 (Ariz.App. 1989), *vacated in part on other grounds*, 164 Ariz. 256, 792 P.2d 719 (1990); ***Samson v. Transamerica Ins. Co.***, 30 Cal.3d 220, 178 Cal.Rptr. 343, 636 P.2d 32, 45 (1981); ***Aaron v. Allstate Ins. Co.***, 559 So.2d 275 (Fla.Dist.Ct.App.), *review denied*, 569 So.2d 1278 (Fla. 1990); ***Glenn v. Fleming***, 247 Kan. 296, 799 P.2d 79, 90-91 (1990); ***Ganaway v. Shelter Mut. Ins. Co.***, 795 S.W.2d 554 (Mo.App. 1990); ***Dumas v. State Farm Mut. Auto. Ins. Co.***, 111 N.H. 43, 275 A.2d 781 (1971); ***Gray v. Nationwide Mut. Ins. Co.***, 422 Pa. 500, 223 A.2d 8, 13 (1966); ***Mello v. General Ins. Co.***, 525 A.2d 1304, 1305-06 (R.I. 1987).

In some states, assignment is not allowed. In the states that don't allow assignment, one rationale is to prevent unscrupulous strangers to an occurrence from preying on the deprived circumstances of an injured person. There is an exception, however, to the minority rule in some jurisdictions when the assignment is made to the injured party. ***See Kimball Int. v. Northfield M. Prod.***, 334 N.J.Super 596, 612-14, 760 A.2d 794 (2000) (quoting ***Caldwell v. Ogden Sea Transp., Inc.***, 618 F.2d 1037 (4th Cir. 1980)).[13]

In the states that don't allow assignment, a second rationale is that the damages that arise from tort are personal to the individual and so an assignee can't suffer such

[13] This case did not arise in the context of an insurance case; it was, however, an assignment of a right to indemnification.

damages nor receive compensation for the damages as a matter of public policy. ***See Terrell v. Lawyers Mut. Liability Ins. Co. of North Carolina***, 507 S.E.2d 923 (N.C.App. 1998).

As argued by State Farm above, certain tort claims in Idaho do not survive the death of the plaintiff. In addition to the cases cited earlier, State Farm relies upon ***MacLeod v. Stelle***, 43 Idaho 64, 249 P. 254 (1926).[14] The Idaho legislature has not specifically adopted a "survival statute." ***But see Idaho Code § 6-1602(10)*** (providing that periodic payments in judgments exceeding $100,000 survive death and are assignable). At any rate, however, a person can assign his or her rights after a judgment has been entered. For example, ***see Federal Reserve Bank of San Francisco v. Hansbrough***, 49 Idaho 747, 292 P.222 (1930); ***Houtz v. Daniels***, 36 Idaho 544, 211 P. 1088 (1922). Therefore, it can be argued that they should be allowed to do so before a judgment. It can also be argued that the rule regarding survival should not apply to the more recently adopted tort of bad faith, but only to truly personal actions such as injury to persons, malicious prosecution, false imprisonment, or defamation; claims for damages that lessen the estate of the insured should survive.

The relative bargaining power of the insured and the insurer must be weighed. If the insurer refuses to deal in good faith knowing that the insured does not have the resources to fight against a large insurance company, the insured must have the ability to

[14] State Farm cited ***MacLeod v. Stelle*** for the proposition that the assignability of a cause of action is dependent on whether the cause of action would survive the death of the assignor. The ***MacLeod*** court stated that the "assignability of a cause of action is by the authorities intimately associated with, and in most cases held to depend upon, the same principle as the survival of a cause of action. Thus, if it survives, it may be assigned; if not, it may not." The ***MacLeod*** court went on to state, however, that the "later, and to me the better considered, cases have tended toward, and many of them have reached, the conclusion that the injuries of a personal nature which do not survive are such as injury to person, malicious prosecution, false imprisonment, libel, slander, and the like; and that an injury which lessens the estate of the injured party does survive, and thus is assignable." ***MacLeod v. Stelle***, 43 Idaho at 75.

limit his liability as Graf did in this case by allowing the judgment to be entered and assigning the claim for bad faith against State Farm to the injured third party. On the other hand, the assignees of the insured must still show that the insurer acted in bad faith in failing to settle the claim and that the settlement amount was reasonable before they can collect the amount reflected in the judgment; thus, Hartmans must show that State Farm acted in bad faith and that the amount of the Judgment against Graf was reasonable.

After considering the Idaho law and authority from other jurisdictions, this Court holds that a bad faith claim can be assigned. State Farm's argument with regard to survival of claims is a strong one. The better position, however, is that the survival rule applies only to injuries of a personal nature and does not apply to an injury, such as a bad faith claim, which lessens the estate of the injured party. Furthermore, it must be noted that the adoption of the common-law tort of insurance bad faith, distinct from an action on the contract, is relatively recent. ***See White v. Unigard Mutual Insurance Co.***, 112 Idaho 94, 730 P.2d 1014 (1986). To the extent that it was more recently recognized and based upon its nature, the assignability of such a claim should not be barred by the survival rule. Additionally, opinions from other jurisdictions, which apply the majority rule regarding the assignability of bad faith claims, provide persuasive guidance here. Finally, as a matter of policy, assignability affords the insured a vehicle by which to limit liability when an insurer has abandon or neglect him or her; at the same time, an assignee is required to show that the insurer acted in bad faith and, if the assignee can't, there is no case against the insurer.

As noted in footnote 6 above, there are genuine issues of material fact which preclude summary judgment for State Farm. Therefore, State Farm's Motion for

Summary Judgment must be denied. Any determination here is limited, however, to the facts of this case, including that the assignment occurred after an alleged loss and that the assignment was to injured parties.

2. Standing by a Third Party to Bring an Action in Bad Faith

State Farm contends that Hartmans, as third parties, have no standing to bring an action for bad faith because no first party claim has been asserted against it. As noted above, the tort of insurance bad faith was first recognized in ***White v. Unigard Mutual Insurance Co.***, 112 Idaho 94, 730 P.2d 1014 (1986). The scope of the claim has always been narrowly defined. The duty of good faith and fair dealing that gives rise to a bad faith action is the duty of the insurance company to act in good faith with regard to first-party insureds. In a number of bad faith insurance cases, the Idaho appellate courts have referred to the "first-party claims of the insured." ***See Robinson v. State Farm Mutual Auto Ins. Co.***, 137 Idaho 173, 45 P.3d 829 (2002); ***Idaho State Insurance Fund v. Van Tine***, 132 Idaho 902, 980 P.2d 566 (1999); ***Walston v. Monumental Life Ins. Co.***, 129 Idaho 211, 923 P.2d 456 (1996); ***Hettwer v. Farmers Insurance Company of Idaho***, 118 Idaho 373, 797 P.2d 81 (1990); ***White v. Unigard Mutual Insurance Co., supra; Linscott v. Rainier Nat. Life Ins. Co.***, 100 Idaho 854, 606 P.2d 958 (1980).

In ***Van Tine***, the Idaho Supreme Court stated as follows:

> We hold that there exists a common law tort action, distinct from an action on the contract, for an insurer's bad faith in settling the first party claims of its insured. . . .
>
> Pursuant to ***White***, there is no claim for bad faith unless it relates to an insurer intentionally and unreasonably failing to pay a claim or compensate the insured. ***Such a claim must relate to the failure to pay monies that the insured claims he is owed*** . . . .

Idaho State Insurance Fund v. Van Tine, 132 Idaho at 907.

Hartmans point out, however, that this claim for tortious bad faith is not a direct action by third parties against an insurer. There are two kinds of cases: (1) cases involving claims brought by a third party against the insurer alleging that the insurer acted in bad faith toward the third party; and (2) cases involving claims by an insured party alleging that the insurer acted in bad faith by refusing to settle a third party claim against the insured. Hartmans concede that the first kind of claim is a third-party claim that is not allowed under Idaho law. Even though it might sometimes be referred to as a third party claim, the second kind of claim is actually a first party claim. The second kind of claim is permitted.

This case falls within the second kind of claim based upon the assignment from Graf to Hartmans. Therefore, it is not barred as a third party claim. At this point, Graf has not asserted a bad faith claim against State Farm. However, since Graf could assign any first party bad faith claims that he might have to Hartmans as third parties, this kind of claim would be permitted. Hartmans have standing to bring an action for bad faith based upon the assignment of Graf's first party claims. Therefore, State Farm's Motion for Summary Judgment on this ground is denied.

D. Enforcement of the Consent Judgment

First, State Farm argues that Graf breached his duty under the HO Policy when he voluntarily assumed an obligation by consenting to the Judgment. This issue has been addressed above. At this point, however, it should be noted that, although Graf always denied liability, he also recognized that he had a continued risk of liability that his insurer was forcing him to take. The amount of the Judgment only exceeded the policy limits after State Farm refused to settle within the policy limits. If Graf had consented to the

Judgment and then attempted to collect it from State Farm himself, he could have done so subject to an issue of fact as to whether State Farm acted in bad faith. Likewise, based on the foregoing discussion regarding assignability, Hartmans could attempt to enforce the consent Judgment.

Second, State Farm argues that Hartmans were aware of the prohibition for assignability under the HO Policy at the time that they took the assignment. In the Assignment, Graf acknowledged that he did not have consent from State Farm. Hartmans dispute that they were aware of the provision in the HO Policy. Based on the foregoing discussion, Graf did not have to obtain consent to assign the claims to Hartmans. Therefore, it does not make any difference to the outcome here whether or not Hartmans were aware of the prohibition against assignability in the HO Policy.

Third, State Farm argues that Hartmans take no more rights under their assignment than were held by their assignor. ***Lithocraft, Inc. v. Rocky Mountain Marketing***, 108 Idaho 2247, 697 P.2d 1261 (Ct.App. 1985). Any defenses that could be asserted against the assignor can be asserted against the assignee. ***Anderton v. Waddell***, 86 Idaho 220, 384 P.2d 675 (1963). Such rules of law are well settled. Therefore, State Farm can assert any defenses against Hartmans that it could have asserted against Graf.

E. <u>Enforceability of the Consent Judgment and Assignment</u>

Hartmans are seeking to enforce the Judgment against Graf. State Farm contends that Hartmans cannot enforce the judgment obtained from Graf against it.

As with certain of the matters above, this is an issue that has not previously been directly addressed by the Idaho appellate courts. However, the Idaho Supreme Court has held that, where a judgment is entered in favor of an insured against an uninsured

motorist, the insured cannot bind his insurer to pay that judgment when the insurer was not a party to the litigation resulting in the judgment. Furthermore, the insurer is not bound by the judgment under either claim preclusion or issue preclusion. ***Vaught v. Dairyland Ins. Co.***, 131 Idaho 357, 956 P.2d 674 (1998); ***Anderson v. Farmers Insurance Co. of Idaho***, 130 Idaho 755, 947 P.2d 1003 (1997).

Courts in other jurisdictions have recognized that settlement agreements and stipulated judgments are subject to heightened scrutiny because such arrangements are inherently unfair to insurers, especially when the stipulated judgment against the insured is accompanied by an agreement not to execute against the insured. ***Pruyn v. Agricultural Ins. Co.***, 36 Cal.App.4th 500, 42 Cal.Rptr.2d 95 (1995). Courts do, however, uphold assignments coupled with covenants not to execute if there is sufficient judicial oversight to reduce the possibility of fraud and collusion. For example, in ***Glenbrook Homeowners Ass'n v. Scottsdale Ins. Co.***, 858 F.Supp. 986 (N.D.Cal. 1994), the court noted that assignments coupled with covenants not to execute are more likely to be upheld if the determination of liability and damages is made by a court, rather than by the parties themselves, after an independent adjudication of facts.

Claims that are assigned to third parties pursuant to a stipulated judgment which contains a covenant not to execute may be susceptible to fraud and collusion. It was explained as follows in ***Wright v. Fireman's Fund Ins. Co.***, 11 Cal.App.4th 998, 14 Cal.Rptr.2d 588, 603-04 (Cal.App. 1992):

> [W]here an insurer provided a defense to its insured in the underlying litigation, and the insured, without the participation or consent of the insurer, stipulated to a judgment without evidentiary support and with no potential for personal loss, such judgment is insufficient to impose liability on the insurer in a later action against the insurer . . . . To hold otherwise would create in the insured the ability to escape all liability for his or her

> own wrongdoing while imposing on the insurer totally unsupported liability. The potential for fraud and collusion is evident.

See also Mercado v. Allstate Ins. Co., 340 F.3d 824 (9th Cir. 2003); ***Rommstadt v. Allstate Ins. Co.***, 844 F.Supp. 361 (N.D. Ohio 1994); ***Hamilton v. Maryland Cas. Co.***, 27 Cal.4th 718, 117 Cal.Rptr.2d 318, 41 P.3d 128 (2002); ***First Gen. Realty Corp. v. Maryland Cas. Co.***, 981 S.W.2d 495 (Tex.App. 1998); ***Doser v. Middlesex Mut. Ins. Co.***, 101 Cal.App.3d 883, 162 Cal.Rptr. 115 (Cal.App. 1980).

It is undisputed that, in the instant case, Graf consented to Judgment against himself in the amount of $400,000 in favor of Hartmans. Graf assigned his rights, if any, against State Farm to Hartmans, who in turn provided Graf with an agreement not to execute on the consent Judgment. The amount of the consent Judgment was reached without any adjudication of the facts or judicial oversight. State Farm did not participate in the drafting of the agreement nor did State Farm consent to the Judgment or the Assignment.

Hartmans, on the other hand, contend that there is a split of authority as to whether or not a judgment based on consent and obtained without an actual trial is enforceable. Hartmans point to Idaho cases containing an out-of-court settlement procedure similar to the one utilized in this case. ***See Simplot v. Western Heritage Insurance***, 132 Idaho 582, 977 P.2d 196 (1999); ***Truck Insurance Exchange v. Bishara***, 128 Idaho 550, 916 P.2d 1275 (1996); ***City of Idaho Falls v. Home Indem. Co.***, 126 Idaho 604, 888 P.2d 383 (1995). From these cases, it would appear that Idaho has adopted the general rule that

> [i]n the absence of fraud and collusion, if a liability insurer who has a right to defend actions against the insured has timely notice of such an action and defends or elects not to defend, the judgment in such case is

> binding upon the insurer as to issues which were or might have been litigated therein, when the insurer is later sued by the injured person.

44 Am.Jur.2d, ***Insurance*** § 1445.

If an insurer defends under a reservation of rights, the injured party may enter into a settlement with the insured, take an assignment of the insured's rights against the insurer, and sue the insurer directly on the assigned claim. The settlement must, however, be reasonable[15] and there cannot have been fraud or collusion. Holmes, Appleman on Insurance 2d, Vol. 22, § 142.1.

In the instant case, it is undisputed that State Farm was defending Graf under a reservation of rights. It is further undisputed that State Farm intervened in the underlying action, although such intervention was limited. Finally, it is undisputed that Graf allowed Judgment to be entered against him in the amount of $400,000.00. Hartmans have filed an Affidavit of William T. Tann, in which Mr. Tann states that, in his opinion, State Farm breached its duty to settle the case for an amount within the policy limits and that the entry of Judgment in the amount of $400,000.00 by Graf and his State Farm attorney was reasonable.

Based upon the Idaho cases and the general rules, it is concluded that a stipulated or consent judgment coupled with an agreement not to execute without full adjudication is enforceable, but it is subject to heightened scrutiny. In particular, the judgment amount must be reasonable and there cannot have been any fraud or collusion between the insured and the injured party. At this point, there is a genuine issue of material fact as to whether the amount of the Judgment in this case was reasonable and whether there was

[15] This requires a showing that (1) the insured was indeed liable to the injured party; and (2) the amount of the settlement was reasonable. Judicial oversight in this manner provides protection for the insurer from unreasonable stipulated judgments.

fraud or collusion. Therefore, Summary Judgment cannot be granted to State Farm and State Farm's Motion for Summary Judgment on this issue must be denied.

F. Enforcement of the Consent Judgment Individually by Hartmans as Judgment Creditors in a Direct Action

In the Amended Complaint, Hartmans allege a cause of action for "direct claim." State Farm contends that Idaho bars a third party from bringing a direct action against an insurer.

An insurance carrier cannot be sued directly and cannot be joined as a defendant. This is the "no direct action" rule. ***Pocatello Industrial Park v. Steel West***, 101 Idaho 783, 621 P.2d 399 (1980). ***See also Graham v. State Farm***, 138 Idaho 611, 67 P.3d 90 (2003); ***Hettwer v. Farmers Ins.***, 118 Idaho 373, 797 P.2d 81 (1990). In ***Surplus Lines Ins. Co. v. Farmers Ins.***, 132 Idaho 318, 971 P.2d 1142 (1999), the Idaho Supreme Court rejected a direct action against a primary insurer by a third-party insurance carrier that asserted a subrogated claim for bad faith under the rule prohibiting direct actions.

Hartmans acknowledge that direct actions by injured parties against insurance companies are not generally allowed. They contend, however, that there are two exceptions to this rule: (1) where the insurance company consents to such suits, and (2) where the injured party has obtained a judgment against the insured and seeks to enforce the judgment. With regard to the second exception, ***see Downing v. Travelers Ins. Co.***, 107 Idaho 511, 691 P.2d 375 (1984). According to Hartmans, both exceptions apply in this case. Hartmans point to a provision in the HO Policy as consent to a direct action. The HO Policy contained the following provision:

> **Suit Against Us.** No action shall be brought against us unless there has been compliance with the policy provisions.
> No one shall have the right to join us as a party to an action against an insured. Further, no action with respect to Coverage L shall be brought against us ***until the***

> ***obligation of the insured has been determined by final judgment*** or agreement signed by us. (Emphasis added.)

Hartmans argue that this provision included consent to a direct action after the obligation of the insured was determined by final judgment and that a final judgment has been entered in this case. State Farm, however, denies that the provision constitutes consent.

It is unnecessary to reach a determination on the first exception since it is undisputed that Hartmans have obtained a judgment against Graf and that they are seeking to enforce that judgment. Therefore, based upon the second exception, Hartmans may bring their direct action to collect the Judgment against State Farm. It must be noted, however, that such a direct action is subject to the requirements set forth in Section E above regarding reasonableness and lack of fraud and collusion. Furthermore, the direct action is limited to the policy limits; Hartmans acknowledge that amounts in excess of the policy limits may be sought only under the bad faith claims.[16] State Farm's Motion for Summary Judgment on this ground must be denied.

[16] ***See*** Memorandum in Support of Objection to Defendant's Motion for Summary Judgment, p. 28.

V

CONCLUSION AND ORDER

There are genuine issues of material fact that preclude a grant of Summary Judgment and, as a matter of law, State Farm is not entitled to Summary Judgment. Therefore, the Motion for Summary Judgment by State Farm must be denied.

Based on the foregoing discussion, it is hereby ORDERED that the Motion for Summary Judgment by Defendant State Farm shall be and hereby is denied.

DATED this _____ day of October, 2004.

_____
John Patrick Luster
District Judge

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing MEMORANDUM OPINION AND ORDER IN RE: SUMMARY JUDGMENT was mailed, postage prepaid, sent by interoffice mail, or sent by facsimile transmission on the _____ day of October, 2004, to the following:

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ALL FIRST DISTRICT COURT JUDGES

DANIEL J. ENGLISH
Clerk of the Court

By: _____
Deputy Clerk