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Insurance Bad Faith

Mediation
(Resolving Cases With Extra-Contractual Exposure)

by
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Commentary

Mediation (Resolving Cases With Extra-Contractual Exposure)

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me • di • a • tion

The act or process of mediating; *especially*: intervention between conflicting parties to promote reconciliation, settlement or compromise.[1]

I. Introduction

By definition, mediation begins with "me." Once conflicting parties have resorted to litigation, they naturally act purely in their own respective self-interest. When a mediation involves allegations of insurer "bad faith," this is especially so. The parties are initially polarized. One party (the claimant) is hoping for complete recompense for his or her loss, irrespective of policy limits. The other party (the insurer) has negotiated a premium based on the risk of exposure within policy limits, so it wants to limit or avoid any exposure it may have beyond policy limits. The interests of these two parties seem irreconcilable. However, when self-interested parties are given an opportunity to resolve their dispute without protracted litigation, they will do so if a negotiated settlement is their best option.

Mediation is perhaps the most efficient and effective way to resolve legal disputes. Control ultimately rests with the parties, instead of leaving the outcome to chance before a judge and jury. The mediator facilitates a resolution by assisting the parties in identifying issues, fostering joint problem solving, and exploring settlement alternatives.[2] While the decision-making authority rests solely with the parties, the role of the mediator is to reduce obstacles to communication and to facilitate the parties' ability to voluntarily enter into an agreement resolving their dispute.[3] In a case involving possible extra-contractual exposure for the insurer, the key is simply (1) to illuminate both sides about the alternatives to settlement, and (2) to focus the parties on the benefits of a mediated resolution.

II. The Benefits of Mediation

The benefits to all mediations include the following: (1) the possibility of a quick resolution in lieu of protracted litigation; (2) assistance from an impartial intermediary to guide the parties through the process; (3) confidentiality, which promotes open communications between the parties; (4) averting the distraction of discovery and trial; (5) savings on litigation expenses; (6) self-determination in negotiating an outcome while avoiding the risk of a less favorable resolution through litigation; (7) finality and closure.

Public policy also favors settlement as a means to preserve judicial resources.[4] Since mediation is designed to promote settlement, it necessarily benefits the courts by reducing docket loads.[5]

With respect specifically to insurance disputes, mediation benefits the insureds by resolving claims without the time and emotional resources of litigating the case to trial.[6] Third-party claimants benefit from settlement at mediation because money is available more quickly

and the emotional expenditure of taking a case to trial is averted.[7] The insurance company benefits from settlement at mediation by limiting litigation expenses and allowing the claim to be "closed."[8] In "bad faith" cases, a mediated settlement is especially beneficial to an insurance company faced with the alternative of defending its conduct before a jury that may have a preconceived bias against it.[9]

III. Selecting The Mediator

It has been said that "the most important step to ensuring mediation success is selecting the right mediator for the job."[10] The mediator's style and experience are imperative to the success of any conflict resolution involving issues of extra-contractual liability. Indeed, insurer "bad faith" mediations are not appropriate for every mediator available to attempt settlement of your case.

A. The Mediator's Conflict-Resolution Style

Mediator styles typically fall into one of four basic categories: (1) evaluative; (2) facilitative; (3) transformative; and (4) hybrid.[11]

1. The Evaluative Approach

The evaluative mediator is like a judge, hearing arguments and formulating opinions about the strengths and weaknesses of the parties' positions.[12] Without the power to adjudicate the controversy, the evaluative mediator will nonetheless offer an opinion and predict the likely outcome of litigation if the case does not settle.[13] For cases involving extra-contractual liability exposure for the insurance company, the successful evaluative mediator will require some expertise in the law of "bad faith" to properly assess the relative strengths and weaknesses of the parties' positions. With the requisite experience, an evaluative mediator will have the power to persuade one or both of the parties (and their legal counsel) to move from their original position toward a compromise with the other party.[14] By far, this is the mediation style most favorably suited for cases involving an insurer's possible extra-contractual liability; provided that the mediator has sufficient expertise in the field.

The evaluative approach is somewhat at odds, however, with some basic tenets of mediation. Remember, mediation is a process that fosters self-determination. The mediator is neither judge, nor jury. One of the most important rules is that mediator be impartial.[15] Mediators may even be prohibited from offering a personal or professional opinion that could unduly influence the parties.[16] However, the experienced evaluative mediator knows how to ask pressing questions of the parties to get them to re-evaluate the strength of their own case. The mediator is also permitted to point out possible outcomes of the case based on the merits of a claim or defense, so long as it does not rise to the level of a professional opinion on the likely outcome of the dispute.[17] Experienced evaluative mediators know how to apply pressure, without extinguishing the parties' sense of self-determination.

2. The Facilitative Approach

The facilitative mediator looks for creative solutions to find a win-win for the parties. The goal is to obtain a mutually beneficial agreement that provides a "value added" scenario rather than a compromise by both parties to effectuate a settlement. The facilitative mediator engages in "shuttle diplomacy," moving from one room to the next, speaking with each party about their interests and looking for creative solutions to design a resolution that does "more than merely divide a fixed pie."[18] This approach is effective for commercial disputes involving business partners or competitors that may have an ongoing business relationship beyond the instant dispute, but is rarely useful in insurance disputes involving extra-contractual liability exposure. "Bad faith" cases are almost always a "one-off" controversy, with no continuing business relationship to build upon after the instant dispute is resolved.

3. The Transformative Approach

The transformative mediator focuses on interpersonal relationships between or among the parties, instead of the merits or likely outcome of the dispute to be resolved. The transformative mediator facilitates the parties' recognition that the relationship itself is of greater value than a favorable resolution of the controversy at hand for either party. Because this approach also finds its foundation in a relationship that is ongoing beyond the instant dispute, it is unlikely that a purely transformative approach would be effective in an extra-contractual insurance dispute.

4. The Hybrid Approach

The "hybrid" approach to mediation is merely a flexible approach that borrows from more than one of the foregoing styles to fit the mediation at hand.[19] The best mediators are able to employ the most effective

techniques based on the particular facts, type of dispute, interests of the respective parties, interpersonal relations, emotional intensity, and other factors that may have an effect on the outcome of the mediation.[20]

As noted above, the evaluative approach is the single best individual style for an insurance case involving extra-contractual liability. However, the transformative approach, which focuses on relationships and emotional involvement of the parties in the dispute, may be helpful (or perhaps even critical) to resolve a "bad faith" claim. For the claimant who is genuinely dismayed by an insurer's handling of the underlying insurance claim, the idea of settling with the insurer may evoke an adverse visceral reaction. A pure evaluative mediator may not be able to recognize the recalcitrance of a party to accept the mediator's "expert" evaluation of the case. A "hybrid" evaluative-transformative approach may be the most effective.

For example, in a third-party liability scenario where a claimant suffers a life-altering loss and the insurer was not timely in effectuating a settlement, it is often essential that the insured tortfeasor and the insurer both express sincere regret for the claimant's loss. Moreover, a rift in interpersonal communications between the insurer and the claimant that might otherwise be an obstacle to resolution at mediation may be overcome if the insurer offers a genuine apology for its imperfections in the claim handling. With proper finesse, these concessions can be made without any actual admission of wrongdoing.[21]

B. The Mediator's Qualifications and Experience

A mediator's proficiency is based in equal parts on natural talent, superior interpersonal skills, actual mediation experience, and real life expertise in the area of law upon which the controversy is founded. Natural talent and superior interpersonal skills are the hallmarks of any gifted mediator. For commercial disputes involving common contract or business tort claims, any seasoned mediator could rise to the challenge. However, extensive experience with extra-contractual insurance litigation is essential for a successful global or "bad faith" mediation. A mediator intricately familiar with the law will be able to identify the strengths and weakness of each argument.[22] With pertinent expertise in the subject matter, the mediator will be able to communicate effectively with the parties and their legal counsel, and wield significantly more clout when coercing concessions from both sides. Therefore, pertinent experience in insurance issues and the law of insurer bad faith in the applicable jurisdiction is imperative to a successful mediation.

IV. The Mediation Process

A. Timeliness of Mediation

Cost-saving is one of the most prominent benefits of mediation. It stands to reason that the sooner the mediation, the better, to minimize the litigation expense before settling the case. However, a mediation attempted too early may be nothing more than a lesson in futility. Meaningful discovery is necessary for a successful mediation in most instances.[23] The parties need to be fully prepared to address not just the merits of the issues surrounding liability, but also the value of the claim based on recoverable damages. If damages are known from the outset and the amount does not justify protracted litigation, then early "preemptive" mediation is appropriate.[24] Similarly, if liability is clear and damages are capped by statute, early mediation may be productive.[25] However, if the damages may be significant, then discovery before mediation is the best course.

B. Pre-Mediation Exchange of Information

Pre-mediation statements or summaries describing the parties, the basis of the dispute, and the merits of the claim (both facts and law) are essential to maximize the chances of a successful mediation. A mediator should not be first learning on the day of mediation, in open session, in front of the parties and their legal counsel, of the contested facts surrounding a claim of "bad faith" by the insurer that allegedly entitles the claimant to recover extra-contractual damages.

The pre-mediation statement should include a discussion of both: (1) the underlying dispute giving rise to the insurance claim, and (2) the claim of entitlement to extra-contractual damages against the insurer. All pertinent facts and a statement of the applicable law should be shared with the mediator. If there are pending motions or rulings already in place that impact the respective positions taken by the parties in litigation, the statement should address them as well. Both sides should identify any prior negotiations to date, their goals in mediation (whether it is to procure a global settlement or otherwise), and how they believe

the mediator can be most effective in facilitating a resolution at mediation. Based on the pre-mediation exchange of information, the mediator should be prepared, in advance, to begin bringing the parties closer to a resolution from the moment the mediation conference begins.

C. Opening Statement by the Mediator

Mediations traditionally begin with an "orientation session." The mediator will explain the mediation process and role of the mediator.[26] The mediator will describe mediation as a consensual process, wherein the mediator is an impartial facilitator without authority to impose a settlement or adjudicate any aspect of the dispute.[27] The mediator will also let the parties know that they are encouraged to share information freely, as all communications will be kept confidential.[28] Often the mediator will explain to parties unfamiliar with the process the benefits of mediation, as opposed to litigation.

The experienced mediator will then attempt to reach immediate consensus on something. The consensus may be nothing more than agreement to the procedural format of the mediation. Or, perhaps, the mediator will have the parties sign a confidentiality agreement. A charismatic mediator may even attempt a commitment from all parties to throw out all preconceptions about their case and promise work together in an effort to resolve their dispute at mediation. Any mutual agreement at the outset will set the stage for further concord, rather than deadlock, as the mediation progresses.

D. Opening Statement by the Parties

Most mediators next offer the opportunity for each side to present opening statements. This is typically given by the parties' respective legal counsel. If the mediator is not already informed by pre-mediation statements, then the mediator will rely heavily on this opening statement to understand the case. Attorneys on both sides will attempt to educate the mediator, so that the "impartial" intermediary has sufficient information to challenge the other side on the merits of the case.

Experienced negotiators will be savvy to the impact the opening statement will have on the opposing party, and the reaction it will induce from the opposing lawyer. Many attorneys, however, are so accustomed to presenting argument in court that they lose sight of the audience, and of the ultimate objective of mediation. While the opening statement should be informative, it should not necessarily focus solely on the merits of the case.

Of course, if the party on other side of the table is unfamiliar with the reasons they need to modify their expectations regarding the outcome of the case, a bit of advocacy based on a detailed opening statement of facts and applicable law may be appropriate. Nonetheless, the tone in which it is presented is of equal importance. In a case involving assertions of "bad faith," emotions can run high. An opening statement that is too aggressive may do more harm than good to the mediation process. The parties enter the mediation conference as adversaries. Their positions are diametrically opposed. The goal of mediation is to provide a forum where issues can be aired in an informative, but non-combatant, way.

Based either on pre-mediation summaries or a discussion with counsel for the parties in advance of the mediation, an experienced mediator will know before the mediation conference begins whether the opening statements of each side are likely to polarize the parties or engage them in the mediation process. The mediator should consider whether to set parameters for the lawyers' opening statements to ensure the statements are productive. How much of the law and details of the facts is necessary to be informative? Each party's presentation should also be somewhat conciliatory to pave a path for mutual concessions as the negotiations ensue. Counsel for the parties and the mediator are equally responsible for building trust, establishing a relationship that will foster productive negotiations, and facilitating cooperation in the mediation process.

E. Open Session and Caucuses

Once the opening statements are concluded, most mediators will immediately move the parties into separate rooms for private caucuses. Other mediators will encourage continued discussion in an open forum, so long as that process is fruitful. The continued open session approach is often a matter of mediator style, but the efficacy of this approach is largely driven by the type of case being mediated and the comfort level of the parties themselves. The benefit of continued open discussions is that it builds trust, repairs relations, and encourages cooperation toward the common goal of dispute resolution. Typically, however, the

interpersonal dynamic between or among the parties in a case involving allegations of "bad faith" will usually preclude continued "open" discussions immediately after opening statements.

Private caucuses give the mediator an opportunity to press the parties for more information and to test the strengths and weakness of the parties' positions. The seasoned mediator will not simply convey numbers or messages back and forth between the rooms (known as "shuttle diplomacy"), but rather use the time with each party to identify common ground, pressure points, and tolerances. Ultimately, the mediator should be pressing both sides for concessions, obtaining valuable information from one party to use when talking with the other, and planning how to move the parties into a range that could settle the case.

F. Settling or Impasse

Settlements reached should be immediately documented in a written agreement signed by the parties and counsel of record. If the parties do not reach an agreement, the mediator will have to decide whether to declare an impasse. The best mediators recognize that the first day of a mediation conference is likely not the last opportunity to settle. Insurance company representatives who attend mediation will likely report back to management and confer about whether the next step is continued negotiations or litigation. Mediators more often than not leave the mediation process open for a period of time before declaring an impasse. Particularly where the case involves bad faith allegations, the insurance company will want to reevaluate settlement strategy based on the feedback received following mediation. If the parties see an opportunity for further negotiations, most experienced mediators will be happy to assist in further discussions by telephone, or schedule a second mediation conference.

V. Special Considerations for "Bad Faith" Mediations

A. Building Trust

"Bad faith" assertions come in many forms: intentional delay, misrepresentations, strong-arming (*e.g.*, refusing to settle under one coverage to force settlement of another coverage), wrongful denial of a claim, arbitrary claim determinations, low balling, failure to communicate promptly in response to claim inquiries, failure to properly investigate, failure to settle, failure to inform an insured of exposure to an excess judgment in favor of third-party claimants, failure to defend, unduly aggressive investigations, unduly aggressive litigation tactics, failure to implement proper standards for handling of claims, etc.

The "bad faith" lawsuit begins with the allegation that the insurer has acted in a manner which wrongfully prefers its own interests over the interests of its insureds. One of the mediator's first challenges is "to evoke in each negotiator at the table the will, despite circumstances, to persevere in a serious but difficult settlement initiative."[29] In the earliest stage of the mediation process, trust building is essential.[30] Bad faith cases involve perceived breaches of faith leading to doubt that replaces whatever trust once existed between the contractually interlinked insurer and insured.[31] Even if the mediator cannot restore the parties' confidence in one another, the mediator must build confidence of the parties to trust in the mediator.[32]

To secure this confidence, it is essential that the mediator is able to properly evaluate the strengths and weaknesses of the parties' positions. Thus, the mediator must be familiar with prevailing law, potential exposure to extra-contractual liability, and the dynamics of both the underlying coverage dispute and the insurer's potential exposure to extra-contractual liability. There is no substitute for practical experience in the handling such claims as an advocate when assessing the value thereof as the mediator.

B. Evaluating the Merits of a Bad Faith Claim

One of the most significant considerations in evaluating the merits of the extra-contractual allegations against the insurer is to apply the proper standard for determining whether the insurer has acted in bad faith. For example, the Florida Courts had once applied a "fairly debatable" standard to determine if an insurer acted in bad faith. Under that standard, an insurer has not acted in bad faith if it had a reasonable basis to deny policy benefits.[33] Florida law today, however, applies a "totality of the circumstances" test.[34] As a result, the issue of whether an insurer in Florida has committed bad faith is less frequently determined as a matter of law, but rather most often now goes to a jury.[35] This is but one example of how an experienced mediator can press the parties on their positions.

C. Valuation of the Bad Faith Claim

The "value" of a first-party bad faith lawsuit is governed by compensatory damages, interest, costs and attorneys fees. However, the insurer may also be exposed to punitive damages, which could be substantial. It is critical that a mediator know the applicable laws in the jurisdiction where the litigation is pending to set a value on the potential extra-contractual exposure. In Florida, for example, a first-party bad faith action can be brought against the insurer only after the claimant satisfies certain statutory prerequisites.[36] Moreover, no punitive damages may be sought in a first party bad faith claim in Florida unless the bad faith conduct occurred with such frequency as to indicate a general business practice.[37] Only a mediator with particular experience handling first-party insurance litigation in Florida would be able to identify these issues if not specifically addressed by the parties.

In the context of a third-party bad faith lawsuit, a mediator with the proper litigation experience would have knowledge of the likely jury outcome in various venues throughout the state. This would assist the mediator in quantifying the likely excess exposure to the insured as a result of the alleged bad faith. Of course, any mediator could simply ask the parties what they value the case to be worth. However, the values may be widely divergent. The evaluative mediator would need to apply his own substantive expertise to most effectively test the parties' respective valuation of the insurer's monetary exposure.

D. The Risk to Each Party of Not Settling

From the insurer's point of view, bad faith claims come with extra-contractual exposure, litigation costs, and distraction of employees responsible for responding to discovery and trial demands. In addition, bad faith claims give rise to the possibility of regulatory scrutiny and negative publicity.[38] The insurer's best alternative to settlement is to proceed to trial and be vindicated of any wrongdoing, but still incur legal expenses which are likely not recoverable, and endure the distraction of years of litigation. This "win/lose" scenario still results in an unfavorable outcome for the insurer. Therefore, the insurer has every incentive to settle during the mediation process.

From the insured's point of view, the loss giving rise the underlying insurance claim has financial ramifications. If the claim was based on a loss suffered by a third-party claimant, the insured could be exposed to liability far in excess of policy limits for medical expenses, lost earnings, and pain and suffering damages. The insured's personal economic survival may be threatened.[39] Additionally, the psychological costs associated with the insured enduring litigation as the defendant, rehashing a traumatic life event, may be significant. Being forced to sit through testimony of the insured's accountability and the extent of the claimant's suffering may be overwhelming for the insured. At the same time, the insured is faced with the uncertainty of the outcome, and the economic impact the trial will have on the insured's life thereafter. Until the underlying third-party claim is resolved, the insured will have no closure. The insured's best alternative to a negotiated settlement is to win the underlying liability trial, but only after months (if not years) of enduring the emotional strain of litigation discovery and trial, and the lingering fear of the unknown outcome to follow. This "win/lose" scenario still results in an unfavorable outcome for the insured. Therefore, the insured also has an incentive to settle during the mediation process.

VI. Conclusion

The benefits of settling claims with extra-contractual exposure through the mediation process far outweigh the alternatives. This is true for all parties concerned. The key elements to a successful mediation are (1) making an informed selection of the mediator, (2) properly timing the mediation, (3) adequately preparing in advance for the mediation conference, and (4) committing to a good-natured approach in negotiations. If properly planned and executed, the parties have the power to maximize the likelihood of settlement at mediation.

Endnotes

1. Merriam-Webster Incorporated, © 2012, Retrieved November 15, 2012, from http://www.merriam-webster.com/dictionary/mediation.

2. Fla. Stat. § 44.1011(2) (2012).

3. Florida Rules for Certified and Court-Appointed Mediators 10.220.

4. Robbie v. City of Miami, 469 So. 2d 1384 (Fla. 1985) (holding "settlements are highly favored and will be

enforced whenever possible"); Feldman v. Kritch, 824 So. 2d 274, 277 (Fla. 4th DCA 2002) ("Settlements are highly favored as a means to conserve judicial resources, and will be enforced when it is possible to do so.").

5. Daniel Marley and Dana Harbin, "Mediating The Coverage / Bad Faith Dispute," 18th Annual Insurance Symposium (April 1, 2010).

6. Id.

7. Id.

8. Id.

9. Id.

10. Anthony Rospert and Martin Mackowski, "Selecting the Right Mediator," For The Defense (June 2012).

11. Id.

12. Id.

13. Id.

14. Id.

15. See, e.g., Florida Rules for Certified and Court-Appointed Mediators 10.330.

16. See, e.g., Florida Rules for Certified and Court-Appointed Mediators 10.370(c).

17. See, e.g., Florida Rules for Certified and Court-Appointed Mediators 10.370(c).

18. Id.

19. Id.

20. Id.

21. The insured and the insurer should take care not to over-emphasize their accountability for the claimant's loss, which could potentially jeopardize a party's negotiating strength by suggesting that the likely outcome of the case clearly favors the other side.

22. Daniel Marley and Dana Harbin, "Mediating The Coverage / Bad Faith Dispute," 18th Annual Insurance Symposium (April 1, 2010).

23. Id.

24. Id.

25. Id.

26. See, e.g., Florida Rules for Certified and Court-Appointed Mediators 10.420(a).

27. Id.

28. Id.

29. Id.

30. Id.

31. Id.

32. Id.

33. Imhof v. Nationwide Mut. Ins. Co., 643 So. 2d 617, 619 (Fla. 1994).

34. In determining whether an insurer has "acted fairly and honestly toward its insured and with due regard for his interests" the Supreme Court of Florida applies the "totality-of-the-circumstances" standard in § 624.155, and not a "fairly debatable" standard. - State Farm Mutual v. Laforet, 658 So. 2d 55, 62–63 (Fla. 1995) (requiring evaluation of insurer's promptness and diligence in resolving coverage dispute in a first-party cause of action), receding from Imhof v. Nationwide Mutual Ins. Co., 643 So. 2d 617, 619 (Fla. 1994) (dicta adopting "fairly debatable" standard).

35. Alan J. Nisberg, "Florida's Bad Faith Quagmire: Is Summary Judgment Ever Available?," Mealey's Litigation Report: Insurance Bad Faith, Vol. 22, #22 (March 26, 2009).

36. See Fla. Stat. § 624.155(3)(a)("As a condition precedent to bringing an action under this section, the department and the authorized insurer must have

been given 60 days' written notice of the violation. If the department returns a notice for lack of specificity, the 60-day time period shall not begin until a proper notice is filed.")

37. Fla. Stat. § 624.155(5) provides:

    No punitive damages shall be awarded under this section unless the acts giving rise to the violation occur with such frequency as to indicate a general business practice and these acts are:

    (a) Willful, wanton, and malicious;
    (b) In reckless disregard for the rights of any insured; or
    (c) In reckless disregard for the rights of a beneficiary under a life insurance contract.

    Any person who pursues a claim under this subsection shall post in advance the costs of discovery. Such costs shall be awarded to the authorized insurer if no punitive damages are awarded to the plaintiff.

38. James Laflin, "Mediation of Insurance Bad Faith Cases," © California Insurance Law & Regulation Reporter, West Group (1998).

39. Id. ■

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