Assignable Rights Under a Liability Insurance Policy

Introduction

A policyholder's rights against a liability insurer and its dependent counsel are assets that can be sold, like anything else of value. A policyholder may properly sell these assets to a plaintiff in return for a covenant not to execute against the personal assets of the policyholder. Such sales usually take two form: 1) an assignment of assignable rights; and 2) a grant of a lien on rights that are not assignable. However, the sale must be handled carefully.

The full amount of judgment, costs of defense, economic loss, Brandt fees, another insurer's equitable contribution, and a post assignment duty of good faith are assignable. Claims for emotional distress, punitive damages, bodily injury, and legal malpractice are not assignable. Insurers often assert defenses to an assignment, some of which are valid and others of which are not. A policyholder is not required to give notice of an assignment. Insurer consent to an assignment is not required. An assignment does not violate the cooperation clause. An assignment may validly be made prior to judgment. Insurers may have several valid defenses: 1) that they adequately reserved rights to deny coverage; 2) that the language of the assignment released the policyholder of liability to the plaintiff; 3) that no judgment against the policyholder was entered; 4) that the assignment is part of a collusive settlement; and 5) that the policyholder and the plaintiff have improperly split a cause of action.

There are substantial advantages to the plaintiff getting a judgment, rather than a settlement and for the plaintiff and policyholder to join as co-plaintiffs in a single action against a defaulting insurer and dependent counsel.

Principles of Assignment

"A thing in action, arising out of the violation of a right of property, or out of an obligation, may be transferred by the owner."[1] "Under this section it is clear that the insured's cause of action is assignable if it is based upon contract. However, it is nevertheless assignable even if based upon tort. [T]he only causes or rights of action which are not transferable or assignable in any sense are those which are founded upon wrongs of a purely personal nature, such as slander, assault and battery, negligent personal injuries, criminal conversation, seduction, breach of marriage promise, malicious prosecution, and others of like nature. All other demands, claims and rights of action whatever are generally held to be transferable. [T]he following demands, claims, and rights of action have been held to be assignable: causes of action arising from the breach of a contract of any kind (except the breach of a promise to marry); causes of action arising from torts which affect the estate rather than the person of the individual who is injured. Under the latter head are claims arising from the carrying away or conversion, of personal property, from the fraudulent misapplication of funds by the officer of a bank, from negligent or intentional injury done to personal property or upon real estate. ¶ Assignability of things in action is now the rule; non-assignability, the exception; and this exception is confined to wrongs done to the person, the reputation, or the feelings of the injured party, and to contracts of a purely personal nature, like promises of marriage. [Civil Code §§ 953, 954] were intended to the common-law rule. [T]he insurer's wrongful act strikes the insured in his pocketbook and diminishes his estate; it does not harm his person or his personality. If the act is a tort, it is a tort affecting the insured's property and is not personal to him. The modern trend in favor of

[1] Civ. Code § 954.

assignability dispels any remaining doubts concerning the transferability of the insured's claim."[2]

"[C]ircumstances under which an assignment without the insurer's consent has been upheld [are]: (1) when at the time of the assignment the benefit has been reduced to a claim for money due or to become due, or (2) when at the time of the assignment the insurer has breached a duty to the insured, and the assignment is of a cause of action to recover damages for that breach."[3]

Assignable Claims

1. The Full Amount of a Judgment

"An insurer who denies coverage does so at its own risk, and, although its position may not have been entirely groundless, if the denial is found to be wrongful it is liable for the full amount which will compensate the insured for all the detriment caused by the insurer's breach of the express and implied obligations of the contract. . . . The insurer should not be permitted to profit by its own wrong. . . . An action for damages in excess of the policy limits based on an insurer's wrongful failure to settle is assignable whether the action is considered as sounding in tort or in contract."[4]

2. Policyholder Defense Costs

An insurer that breaches its duty to defend is "liable for all costs and attorneys' fees expended by [its insured] for this purpose."[5] "[T]he courts have held that, by its refusal to participate, the recalcitrant [insurer] waives the right to challenge the reasonableness of defense costs."[6] "[The] wrongdoer shall bear the risk of the uncertainty which his own wrong has created."[7] "Nonetheless, where one insurer fully protects the insured by providing a defense and full coverage for a claim, a second insurer's refusal to defend generally cannot support a tort action for breach of the covenant of good faith and fair dealing because the latter's conduct will not enhance the insured's cost of defending itself or its exposure to liability."[8]

3. Policyholders' Economic Loss

"When the carrier does breach its duty to settle, the insured has been allowed to recover economic loss."[9] "We are satisfied that a plaintiff who as a result of a defendant's tortious conduct loses his property may recover for the pecuniary loss."[10]

4. Brandt Fees

"When an insurer's tortious conduct reasonably compels the insured to retain an attorney to obtain the benefits due under a policy, it follows that the insurer should be liable in a tort action for that expense in the same way that medical fees would be part of the damages in a

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[2] *Brown v. Guarantee Ins. Co.* (1957) 155 Cal. App. 2d 679, 693-95 (*Brown*) (ellipses omitted).

[3] *Henkel Corp v. Hartford Acc. & Indem. Co.* (2003) 29 Cal.4th 934, 129 Cal.Rptr.2d 828, 836.

[4] *Comunale v. Traders & General Ins. Co.* (1958) 50 Cal.2d 654, 660-61 (*Comunale*).

[5] *Hogan v. Midland National Ins. Co.* (1970) 3 Cal.3d 553, 558.

[6] *Safeco Ins. Co. of America v. Superior Court* (2006) 140 Cal. App. 4th 874, 878-79.

[7] *Arenson v. National Auto. & Cas. Ins. Co.* (1957) 48 Cal.2d 528, 539; see also, *Amato, supra*, 53 Cal.App.4th at 839.

[8] *Emerald Bay Community Assn v. Golden Eagle Ins. Corp.* (2005) 130 Cal.App.4th 1078, 1093.

[9] *Murphy v. Allstate Ins. Co.* (1976) 17 Cal.3d 937, 941 (*Murphy*) (ellipsis omitted).

[10] *Crisci v. Security Ins. Co.* (1967) 66 Cal.2d 425, 433 (ellipses omitted).

personal injury action. [T]he plaintiff [is] entitled to an award for attorney's fees incurred to obtain the policy benefits, which award must not include attorney's fees incurred to recover any other portion of the verdict."[11] This right has be given the eponymous name, Brandt fees.

"[A]n insured's assignment of a cause of action against an insurance company for tortious breach of the covenant of good faith and fair dealing by wrongfully denying benefits due under an insurance policy carries with it the right to recover Brandt fees."[12]

5. Another Insurer's Equitable Contribution

When a defendant has multiple policies of insurance, a performing insurer may sue a non-performing insurer for equitable contribution. In one reported opinion, a plaintiff took and assignment of a performing insurer's rights, and as assignee sued a non-performing insurer for breach of contract and bad faith. However, the claim failed on technical pleading grounds since the assignee pled breach of contact and bad faith, not equitable contribution.

6. Continuing Duty of Good Faith

"[T]he duty not to withhold in bad faith payment of adjudicated claims runs not only in favor of the insured but also in favor of a judgment creditor. Accordingly, the plaintiff becomes a third party beneficiary of the policy [and] a beneficiary of the covenant of good faith, the duty to exercise good faith in not withholding adjudicated damages necessarily is owing to the plaintiff also. [W]ith respect to the specific good faith duty to pay adjudicated claims, a judgment creditor enjoys the contractual status, rights, and posture that vest such a cause of action.[13]

Non-Assignable Claims

1. Emotional Distress

"When the carrier does breach, the insured has been allowed to recover. However, part of the damage arises from the personal tort aspect of the bad faith cause of action. And because a purely personal tort cause of action is not assignable in California, it must be concluded that damage for emotional distress is not assignable."[14]

However, when the policyholder files a petition in bankruptcy, claims against the insurer for unreasonable refusal to settle a third party action pass to the bankruptcy trustee,[15] including claims nonassignable under state law such as claims for emotional distress.[16]

2. Punitive Damages

"The courts have barred assignment only of claims for punitive damages."[17] "[B]ecause a purely personal tort cause of action is not assignable in California, it must be concluded that [punitive] damage [are] not assignable."[18]

3. Bodily Injury

Although it is unlikely that an insurer's breach may cause a bleeding injury,

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[11] *Brandt v. Superior Court* (1985) 37 Cal.3d 813, 817, 802 (ellipses omitted)

[12] *Essex Ins. Co. V. Five Star Dye House, Inc.* (2006) 38 Cal.4th 1252, 1265.

[13] *Hand v. Farmers Ins. Exchange* (1994) 23 Cal.App.4th 1847, 1858, 1861 (citations and ellipses omitted).

[14] *Murphy, supra*, 17 Cal.3d at 942 (citations and ellipsis omitted).

[15] *Brown, supra*, 155 Cal.App.2d at 695-696.

[16] *Sierra Switchboard Co. v. Westinghouse Elec. Corp.* (9th Cir. 1986) 789 F.2d 705, 708-709.

[17] *Smith v. State Farm Mut. Auto. Ins. Co.* (1992) 5 Cal. App. 4th 1104, 1111 (*Smith*).

[18] *Murphy, supra*, 17 Cal.3d at 942 (citations and ellipsis omitted).

nonassignable claims include "personal injury damage."[19]

Insurer Defenses

Insurers have resisted the validity of assignments on numerous grounds that have been consistently rejected by the courts. Still valid defenses exist.

1. Invalid Defenses

A. Insurer Consent Not Required

"The insured may assign his cause of action for breach of the duty to settle without consent of the insurance carrier, even when the policy provisions provide the contrary."[20] "[A] clause in the policy which provides that an assignment of an interest under the policy shall be binding only if [the insurer] consents . . . does not preclude the transfer of a cause of action for damages for breach of a contract."[21]

B. Cooperation Clause Not Violated

"The requirement of cooperation by the policyholder assumes that the insurer has complied in good faith with the conditions of the policy. An insurer may be estopped to claim breach of a cooperation clause which has been induced by its own action. The insurer's breach so narrows the policyholder's duty of cooperation that the self-protective assignment does not violate it."[22] "[A]n acute change in the relationship between policyholder and insurer [resulting from an assignment] does not or should not affect the policyholder's obligation to appear as defendant and to testify to the truth."[23]

C. No Notice to the Insurer Is Required

In one case, an insurer rejected a settlement offer within its policy limit whereupon the policyholder assigned his rights to the plaintiff without notifying the insurer of the assignment. Upon learning of the assignment, the insurer offered its policy limit, which the plaintiff rejected. Thereafter, judgment was entered in excess of the policy limit. "In our opinion, the present assignment is not violative of public policy."[24] However, giving notice to the insurer may be important to resist the defense of collusion.

D. An Assignment May Precede Judgment

"The insured's remedy to protect himself from an excess judgment is to assign to the claimant his cause of action for bad faith refusal to settle in exchange for a covenant not to enforce the judgment against the insured's personal assets. This assignment, however, is not immediately assertable, and it does not settle the third party's claim. As long as the insurer is providing a defense, the insurer is allowed to proceed through trial to judgment. The assignment of the bad faith cause of action becomes operative after the excess judgment has been rendered."[25] "That [the policyholder's] claim against the insurer was incomplete at the time of the attempted transfer to [the plaintiff] is not crucial, in our view. Common law and statutory rules against assignment of expectations may prevent the transferee from immediate assertion of his

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[19] *Id*. at 946-47.

[20] *Id*. at 942 (citations omitted); see also, *Smith, supra*, 5 Cal.App.4th at 1110.

[21] *Comunale, supra*, 50 Cal.2d at 661-62 (citations and ellipses omitted).

[22] *Critz v. Farmers Ins. Group* (1964) 230 Cal.App.2d 788, 801-802 (*Critz*) (citations and ellipses omitted).

[23] *Id*. at 801 (ellipsis omitted).

[24] *Id*. at 803.

[25] *Hamilton, supra*, 27 Cal.4th at 732, quoting *Safeco Ins. Co. v. Superior Court* (1999) 71 Cal. App. 4th 782, 788-89 (citation omitted).

claim. The attempted transfer of a future right may operate as an equitable assignment or contract to assign, which becomes operative as soon as the right comes into existence. The modern tendency is to recognize assignment of a prospective right to arise under an existing contract. [T]he principle is designed to give effect to the mutual intent of assignor and assignee. The real limits on assignability of future rights are those fixed by public policy, enunciated either by Legislature or court."[26]

2. Valid Defenses

A. Reserved Coverage Defenses

"[The assignee] had no greater right to collect on the policy than did [the assignor]. And the coverage question was already at issue in [the assignee]'s complaint against [the insurer. At trial, the insurer] will be afforded a full opportunity to demonstrate that the defendants were not covered by insurance for the underlying claim."[27]

B. Release

The terms of an assignment should not include a release of the policyholder by the plaintiff. If the policyholder's liability to the plaintiff is extinguished, damages may also be extinguished, or reduced. Some insurers argue that a covenant not to execute prevents the policyholder from "suffering any damage by reason of the personal judgment against him. [A] covenant not to execute is not a release. It did not blot out the personal judgment against [the policyholder] or extinguish his claim for breach of contract against the carrier."[28]

"The covenant not to execute is similar to the covenant not to sue. Whatever the legal effect of such covenants may be, and the law is not too clear on this subject, it can at least be said that such a covenant does not amount to a release or satisfaction of the debt. It does not extinguish the cause of action or the judgment. The judgment against [the policyholder] personally still exists."[29]

C. A Judgment Is Required to Establish a Breach of Duty to Settle

So long as the insurer is providing a defense, an adjudication on the merits resulting in a judgment is essential to ripen a cause of action against an insurer for bad faith failure to settle. "An essential element of a cause of action for breach of the implied covenant based on the refusal to settle is resulting damages. Damages ordinarily include the entire amount of a judgment after trial, including the amount in excess of policy limits but excluding any punitive damages. Until a judgment has been entered against the insured after a trial, there is no assurance that the insured will suffer any damage from the insurer's breach of its implied obligation to accept a reasonable settlement offer. As Hamilton put it, 'where the insurer has accepted defense of the action, no trial has been held to determine the insured's liability, and a covenant not to execute excuses the insured from bearing any actual liability from [a] stipulated judgment, the entry of a stipulated judgment is insufficient to show, even rebuttably, that the insured has been injured to any extent by the failure to settle, much less in the amount of the stipulated judgment.'"[30]

"We conclude that a judgment against the insured is a condition to the insured's right to

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[26] *Critz, supra*, 230 Cal.App.2d at 799-800.

[27] *Ceresino v. Fire Ins. Exch.* (1989) 215 Cal.App.3d 814, 823-24 (ellipses omitted).

[28] *Critz, supra*, 230 Cal.App.2d at 803 (ellipsis omitted).

[29] *Ivy v. Pacific Automobile Ins. Co.* (1958) 156 Cal.App.2d 652, 662 (citation and ellipsis omitted).

[30] *Wolkowitz v. Redland Ins. Co.* (2003) 112 Cal.App.4th 154, 163 quoting *Hamilton, supra*, 27 Cal.4th at 726.

assign to the claimant a cause of action for bad faith against the insurer."[31]

D. Collusion

Collusion is a valid defense to a bad faith claim. Because an assignment coupled with covenants to limit execution tends to alter the the policyholder's motivation to conduct a vigorous defense, assignments consistently draw claims of collusion. "The principles of fraud and collusion are self-evident and require no extended discussion. The facts and circumstances which will lead a court to conclude that either are present are limited only by the imagination of those who would cheat and deceive."[32] However, the insurer must prove collusion. "A related contention is that the assignment and covenant not to execute upon the judgment violate public policy by imparting a collusive character to the personal injury suit. [S]uch an agreement might lead to a fraud upon the court by concealing the position of a party who is an important witness in the action. There is no claim that [the policyholder] actually said or did anything which jeopardized defense of the lawsuit. Nothing in the assignment agreement impelled him toward false testimony. The alliance between these motivating forces did not result in a collusive lawsuit, either in terms of natural tendencies or actual results."[33]

E. Splitting a Cause of Action

"Every action must be prosecuted in the name of the real party in interest."[34] "While the general rule is that causes of action for injuries to person and property are separate, all damages for a single breach of contract must be recovered in one action. [An] entire claim arising either upon a contract of from a wrong cannot be divided and made the subject of several suits. A rule placing the emphasis where it belongs and permitting recovery of all proximately caused detriment in a single cause of action is more likely to engender public respect for and confidence in the judicial process. [A policyholder] possessed of a single and indivisible cause of action against [an insurer. When h]e assigned that cause of action [he] simply waived any claim for purely personal damages that he might have been able to recover had he brought the action himself. He could not split the cause of action. If [the policyholder] desired to retain his claim for emotional distress he could very easily have contracted with the [the plaintiffs] to pay to them all or any part of a judgment that he might recover, a procedure similar to a contingency fee contract between an attorney and his client. Thus he could have recovered all proper damages without submitting the defendant to a multiplicity of lawsuits such as has been done here. [The policyholder] did not do that, he assigned his cause of action. An action must be prosecuted in the name of the real party in interest. That person, by virtue of the assignment, was the [assignee] and not the [assignor]."[35]

"[T]he terms of the assignment explicitly reserved to [the policyholder] any cause of action which he might have against [the insurer] for physical injuries. [T]his was not a blanket assignment of all causes of action against [the insurer]. More significantly, procedurally [the plaintiff] and [the policyholder] are joined as parties plaintiff in a single suit against [the insurer that] is clearly in accord with the modern rules governing partial assignments, and comports with

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[31] *Smith v. State Farm Mut. Auto. Ins. Co.* (1992) 5 Cal.App.4th 1104, 1114 (ellipsis omitted).

[32] *Pruyn v. Agricultural Ins. Co.* (1995) 36 Cal.App.4th 500, 530.

[33] *Critz, supra*, 230 Cal.App.2d at 802.

[34] Code Civ. Proc. § 367.

[35] *Purcell v. Colonial Ins. Co.* (1971) 20 Cal App 3d 807, 813-14 (citations, quotation marks, and ellipses omitted.)

the ‘primary right’ theory. Because the partial assignor and the partial assignee are joined as parties plaintiff in the same lawsuit, the judgment is binding upon both plaintiffs, and [the insurer] is protected from future litigation arising out of the same facts under the doctrine of res judicata. By the terms of the assignment, [the policyholder] reserved to himself ‘that cause of action for physical injuries’ sustained as a result of [the insurer]’s failure to settle within the policy limits.”[36]

[36] *Cain v. State Farm Mut. Auto. Ins. Co.* (1975) 47 Cal.App.3d 783, 796 (ellipses omitted).