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NJM Insurance Group

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March 31, 2016

Chief Justice Stuart Rabner and Associate
Justices of the Supreme Court of New Jersey
Hughes Justice Complex
25 W. Market Street
P.O. Box 970
Trenton, NJ 08625-0970

Re: Response to the Civil Practice Committee's recommendations for Court Rule modifications in response to the referrals described in Wadeer v. New Jersey Manufacturers Ins. Co.

Honorable Justice Rabner and Associate Justices:

In the Wadeer v. New Jersey Manufacturers Ins. Co., 220 N.J. 591 (2015) opinion, the Supreme Court of New Jersey referred issues regarding three Court Rules to the Civil Practice Committee ("the Committee") for consideration of possible amendments. The Civil Practice Committee's 2016 Report includes its recommendations and comments in response to this referral.

For the reasons set forth below, New Jersey Manufacturers Insurance Company ("NJM") recommends adoption of the Committee's proposed modification to the Entire Controversy Rule. In addition, consistent with public policy and the purpose of each Rule, NJM respectfully urges the Supreme Court of New Jersey not to amend the Court Rules relating to the Offer of Judgment Rule and the award of attorney's fees.

I. Entire Controversy Doctrine

New Jersey's Entire Controversy Doctrine is set forth in R. 4:30A, which states:

> *Non-joinder of claims required to be joined by the entire controversy doctrine shall result in the preclusion of the omitted claims to the extent required by the entire controversy doctrine, except as otherwise provided by R. 4:64-5 (foreclosure actions) and R. 4:67-4(a) (leave required for counterclaims or cross-claims in summary actions).*

We concur with this Court's analysis of the reasons for modifying application of the entire controversy doctrine to UM/UIM bad faith claims as set forth below.

> *We agree that barring such bad faith claims on the basis of the entire controversy doctrine is inappropriate in the UM context.*

> *While we acknowledge and reiterate the underlying goals of the entire controversy doctrine ... we find that the nature of first-party bad faith claims warrants exemption from a harsh application of this rigid doctrine. Acts of first-party bad faith in the UM context can, and often will, continue throughout the course of the underlying legal proceedings; that is, an insurance carrier's acts of bad faith may often not cease until a verdict is returned, and this is only after the plaintiff has been forced to fully litigate the matter through arbitration and trial. Rather than forcing a plaintiff to amend the initial complaint to add and reflect each incident of bad faith, we believe that viewing bad faith claims as separate and distinct actions promotes judicial efficiency and economy. We also note the difficulties that will be encountered in the discovery process by seeking information as to bad faith acts which may be prohibited in the UM cause of action.*
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> *The question remains, however, whether fairness requires that our court rules be modified to permit an insured to bring a bad faith cause of action against an insurer after the underlying UM claim is resolved. In our view, the goals of the entire controversy doctrine are not served by mandating that the plaintiff simultaneously file a first-party bad faith claim with the underlying breach of contract/UM lawsuit. However, to foster debate about whether our courts should allow first-party bad faith claims to be asserted and decided after resolution of the underlying, interrelated UM action, we refer Rule 4:30A to our Civil Practice Committee for review.*
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> Wadeer, 220 N.J. at 609-610 (2015)

As this Court clearly recognized, the application of the entire controversy doctrine in the UM/UIM context could lead to issues that are not supported by the doctrine's goals, forcing plaintiffs to expend time and money to litigate a bad faith case before a verdict is reached that may trigger a bad faith cause of action. Similarly, insurance company defendants may be pressed to produce a copy of their UM/UIM claim file during active defense of the litigation, thus revealing their defense strategies. Wadeer, 220 N.J. at 609-610 (2015)

Since the Appellate Division's decision in Taddei v. State Farm Indem. Co., 401 N.J. Super. 449, 465 (App. Div. 2008), in which the Court clarified that the entire controversy doctrine bars a bad faith claim in the UM/UIM context unless it is raised in the underlying UM/UIM claim, NJM has received a substantial number of Superior Court Complaints that included counts for bad faith in UM/UIM cases. But for the Taddei ruling, it is doubtful that these bad faith counts would have been alleged, because the underlying cases have not resulted in viable bad faith claims. In some instances the first notice of a UM/UIM claim was the complaint that contained the bad faith Count. Rather than providing for greater efficiency, forcing UM/UIM claimants to assert bad faith claims results in less efficient litigation of UM/UIM claims. For these reasons, during oral argument of the Wadeer

matter, attorneys for both parties agreed that applying the entire controversy doctrine should not be applied to UM/UIM claims.

Therefore, NJM concurs with the following recommendation of the Civil Practice Committee to amend R. 4:30A:

> *Non-joinder of claims required to be joined by the entire controversy doctrine shall result in the preclusion of the omitted claims to the extent required by the entire controversy doctrine, except as otherwise provided by R. 4:64-5 (foreclosure actions) and R. 4:67-4(a) (leave required for counterclaims or cross-claims in summary actions). Claims of bad faith, which are asserted against an insurer after an underlying uninsured/underinsured motorist claim is resolved in a Superior Court action, are not precluded by the entire controversy doctrine.*

II. Offer of Judgment Rule

New Jersey's Offer of Judgment Rule, R. 4:58-1, permits a party to make an offer to take a monetary judgment. According to R. 4:58-2(a), the consequences of non-acceptance are as follows:

> *If the offer of a claimant is not accepted and the claimant obtains a money judgment, in an amount that is 120% of the offer or more, excluding allowable prejudgment interest and counsel fees, the claimant shall be allowed, in addition to costs of suit: (1) all reasonable litigation expenses incurred following non-acceptance; (2) prejudgment interest of eight percent on the amount of any money recovery from the date of the offer or the date of completion of discovery, whichever is later, but only to the extent that such prejudgment interest exceeds the interest prescribed by R. 4:42-11(b), which also shall be allowable; and (3) a reasonable attorney's fee for such subsequent services as are compelled by the non-acceptance.*

An insurance carrier defendant is currently subject to Offer of Judgment expenses in underinsured/uninsured motorist ("UM/UIM") cases and is responsible for the payment of Offer of Judgment damages, even if those expenses result in a payment in excess of an insurance policy's UM/UIM limit. McMahon v. NJM, 364 N.J. Super. 188 (App. Div. 2003). In the Rule's current form, when a jury enters a verdict in excess of an insurance carrier's UM/UIM policy limit, a trial court will mold the verdict to the available limits of the UM/UIM policy. Taddei v. State Farm Indem. Co., 401 N.J. Super. 449 (App. Div. 2008). Thus, if a Plaintiff files an Offer of Judgment for the total limit of a UM/UIM policy, then it is not possible for a money judgment to be entered for more than 120% of the Offer of Judgment.

In referring this issue to the Civil Practice Committee for consideration the Supreme Court suggested that the Rule should be modified to achieve its purpose in the context of UM/UIM cases as follows:

> *We find that the molding of a monetary jury award is appropriate when done to conform with and reflect allocation of liability. However, in the UM/UIM context, where reduction is based not on a tortfeasor's comparative negligence but instead on the policy limits of a given carrier, we find that the current construction of Rule 4:58–2 provides no incentive for such carriers to settle. Rather, under the current rule, carriers are prone to take their chances at trial where the offer of judgment is somewhat near their policy limits because they have relatively little to lose in doing so. Thus, the rule's required reduction of a monetary jury award artificially to the policy limits renders moot any reasonable offer of settlement by the insured below the 120% threshold; unless an insured makes an offer of judgment that is unreasonably below its policy limits, it is unlikely that an insurance carrier will choose to settle the respective claim. In light of this, we conclude that the aims of Rule 4:58–2, "to encourage, promote and stimulate early out-of-court settlement," Crudup v. Marrero, 57 N.J. 353, 357, 273 A.2d 16 (1971), are ill-achieved in the UM/UIM context under the rule's current construction.*
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> *Accordingly, we refer Rule 4:58–2 to the Civil Practice Committee to consider and recommend an appropriate amendment addressing this infirmity.*
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> Wadeer v. New Jersey Mfrs. Ins. Co., 220 N.J. 591, 611 (2015)

In contrast with the Court's view, an insurance carrier has multiple incentives to settle a UM/UIM claim that may be worth more than the balance of its insured's policy limit. Insurance carriers benefit by the early resolution of claims by reducing investigation and litigation costs. Furthermore, by properly evaluating a UM/UIM claim, an insurance carrier is satisfying the interests of two classes of policyholders:

- The insurance carrier has a duty to make a good faith evaluation of a claim for the benefit of the individual policyholder who purchased coverage and relied upon the insurance carrier to provide first party UM/UIM benefits. This duty is not satisfied if an insurance carrier recklessly or purposefully denies, delays or underpays a claim.
- The insurance carrier also has a duty to all of its policyholders to make a good faith evaluation of every claim so as to be a good steward of the financial interests of premiums previously paid, and premiums to be assessed in the future. An insurance carrier fails to satisfy this duty if it does not properly investigate a claim or if it pays claimants more than the actual value of a claim.

Further, in a competitive automobile insurance market as exists in this State, an insurer's reputation and its ability to attract and retain business are strong motivators to ensure its meritorious resolution of the claims of its policyholders.

Although the Civil Practice Committee has recommended that, for UM/UIM matters, the Offer of Judgment Rule should be triggered by the amount of a jury or non-jury verdict rather than the amount of a money judgment, NJM urges the Supreme Court to reject this recommendation. The goals of the Offer of Judgment Rule should be kept in mind before making any decision to alter the Rule. The comments and annotations to New Jersey's Court Rules, confirm that "Inducement to settlement has remained the fundamental purpose of the rule as it has evolved. [citations omitted]." Pressler & Verniero, Current N.J. COURT RULES, Comment R. 4:58 (GANN). Arguably, the incentive for the proposed change to this Rule is to shift fees rather than to encourage settlement. When, for example, a party submits an Offer of Judgment prior to providing any discovery responses, the offering party is most likely seeking to set-up a shift in fees rather than seeking a quick settlement. The comments and annotations to New Jersey's Court Rules point out that, over the years, revisions to the Rule have been viewed with a "growing concern that the rule was being used not primarily as a settlement device but rather to effect fee-shifting in cases where neither a rule nor a statute provided for attorney-fee allowances, that is, to move away from the American rule towards the English rule...." For this reason the Rule should not be altered for UM/UIM matters.

However, if the Supreme Court is inclined to adopt the Committee's recommendation to modify the Rule, then clarification regarding the calculation of Offer of Judgment damages is warranted. Calculation of Offer of Judgment damages should be based upon the amount of the verdict reduced by the net UM/UIM policy limit and any appropriate offsets including comparative negligence, a credit for the tortfeasor's available insurance coverage and payments that are available from any collateral sources.

III. Attorney's Fees

In general, New Jersey follows the American Rule whereby each party bears responsibility for payment of its own legal fees. While contracting parties may include fee-shifting provisions in their contracts, there is no fee-shifting provision in the UM/UIM endorsement. With respect to actions involving an insurance carrier, R. 4:42-9 states:

> *(a) Actions in Which Fee is Allowable. No fee for legal services shall be allowed in the taxed costs or otherwise, except...*
> *(6) In an action upon a liability or indemnity policy of insurance, in favor of a successful claimant.*

This Rule is limited to actions that are related to an attempt to require an insurance carrier to indemnify or defend a third party liability claim. The attorney fee Rule has not been extended to successful claimants seeking first party coverage from their insurance carrier. "An action to collect under the underinsured motorist coverage of a New Jersey automobile policy is not within the category of suits in which R. 4:42-9(a)(6) permits an attorney's fee to be awarded." New Jersey Manufacturers Ins. Co. v. Breen, 297 N.J. Super. 503, 516 (App. Div. 1997) aff'd as modified, 153 N.J. 424 (1998)

In Wadeer this Court stated the following regarding attorney's fees:

> *Lastly, we note that New Jersey Court Rules allow for counsel fees to be awarded "in an action upon a liability or indemnity policy of insurance, in favor of a successful claimant." R. 4:42–9(a)(6). However, with respect to first-party insurance, such as UM/UIM coverage, the statutory prescription for attorney's fees is inapplicable. Rule 4:42–9(a)(6) has not been extended to authorize a fee award to an insured who brings direct suit against his insurer to enforce any direct coverage, including UM/UIM coverage. We refer this issue to the Civil Practice Committee for comments and recommendations addressing the issue.*
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> Wadeer v. New Jersey Mfrs. Ins. Co., 220 N.J. at 611 (2015).

The Civil Practice Committee Report (at page 44) states that a "majority of the Committee opposed amending *Rule* 4:42-9 to provide for the collection of counsel fees for a prevailing claimant in a UM/UIM matter, assuming that the Court adopts the recommendation to amend *Rule* 4:58...." NJM recommends that the Supreme Court of New Jersey should not amend the Attorney Fee Rule regardless of whether the Offer of Judgment Rule is amended because fee shifting in UM/UIM cases will inevitably lead to an increase in costs to the public and to policyholders.

In addition, the Civil Practice Committee Report (at pages 44-45) requested "clarification from the Court as to whether it should consider the broader and controversial question of amending *Rule* 4:42-9 to address direct actions by insureds for first party insurance coverage." For the reasons set forth in this letter, the Attorney Fee Rule should not be altered for UM/UIM matters or for other actions involving first party insurance coverage.

In particular, sufficient rationale has not been provided to justify movement away from the American Rule for attorney fees. Changing the current rule will undoubtedly lead to unintended, negative consequences, such as discouraging an insurance carrier from invoking its right to defend a case with a meritorious defense argument, ultimately increasing costs to all of its policyholders. As previously noted, an insurance carrier owes a duty to all of its policyholders to defend claims that, after a good faith evaluation, it determines are worth less than the amount of claimant's demand. To

do otherwise effectively raises rates on all policyholders - running directly counter to the cost-control efforts the State Legislature has undertaken over the last decade in an effort to produce a competitive and efficient private passenger automobile insurance system.

Another unintended, negative consequence of amending the attorney fee Rule would be the resultant increase in litigation. The addition of attorney's fees for UM/UIM claimants' damages would serve as a financial incentive for UM/UIM claimants' attorneys to file suit rather than resolve a claim pre-suit even if the insurance carrier made a reasonable and significant offer. By encouraging attorneys to proceed through litigation rather than resolving matters through pre-suit negotiations, the New Jersey Superior Court would receive an influx of cases that would not otherwise need to be filed. Although the total number of UM/UIM claims would remain steady, the number of cases in the courts can be expected to increase.

A typical third party auto negligence claim that is filed against an at-fault driver (and indemnified by the at-fault driver's insurance carrier) does not give rise to an attorney fee award. Changing the attorney fee Rule for UM/UIM claims would result in UM/UIM claimants receiving monetary judgments that are greater than the monetary judgments rendered for third party claimants.

Finally, in its current form, the Offer of Judgment Rule already allows a UM/UIM claimant to recover attorney's fees, enhanced interest and costs when a judgment is entered for 120% or more than an offer rejected by a Defendant/insurance carrier. It should be noted that the fees, interest and costs under the Offer of Judgment Rule are recoverable from the insurance carrier even if those amounts result in an award in excess of the UM/UIM policy limit. McMahon v. New Jersey Manufacturers Ins. Co., 364 N.J. Super. 188 (App. Div. 2003). Thus, if the consequences for failing to accept an Offer of Judgment are triggered, then a claimant may collect attorney's fees from the insurance carrier, regardless of the amount of the insurance carrier's UM/UIM limit.

CONCLUSION

For the reasons set forth above, NJM concurs with the Civil Practice Committee that the Entire Controversy Rule should be modified to relieve parties from the requirement to plead a bad faith claim prior to completion of litigation related to the underlying UM/UIM claim. Modifying the Entire Controversy Rule for UM/UIM matters will provide for more efficient litigation of such matters without restricting the rights of any of the litigants.

On the other hand, the Offer of Judgment Rule and the attorney fee Rule should remain unchanged. The Offer of Judgment Rule currently offers an attorney fee remedy for plaintiffs who receive a verdict for 120% more than their Offer of Judgment. Insurance carriers already have incentives to offer the limits of their UM/UIM policy, prior to trial, for a claim that is worth more than the balance of its insured's policy limit. There is insufficient rationale to alter the current

American Rule regarding attorney's fees. Allowing fee-shifting for UM/UIM cases would result in negative consequences that would overcome any perceived benefit.

New Jersey Manufacturers Insurance Company appreciates the opportunity to present you with the information that is contained in this letter. We welcome the opportunity to appear before you to further explain the rationale supporting the information that is set forth in this letter.

Respectfully submitted,

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New Jersey Manufacturers Insurance Company