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Insurer's Liability for Prejudgment Interest: A Modern Approach

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INSURER'S LIABILITY FOR PREJUDGMENT INTEREST: A MODERN APPROACH

I. INTRODUCTION

The term "prejudgment interest" denotes the interest on a judgment computed from the time of the actual injury to the date of the final judgment.[1] It is interest[2] on a sum of money which, until the rendering of final judgment, has not been declared to be damages for the plaintiff. Prejudgment interest is not punitive.[3] It is better viewed as compensatory in nature because its purpose is to indemnify a claimant for the loss of the money which presumably could have been earned had payment of damages not been delayed.[4] Once a cause of action accrues, the injured party becomes entitled to be made whole.[5] Prejudgment interest may be viewed as an essential element of fair and just compensation.[6]

The Christian components of the medieval world viewed interest as an evil and oppressive device of the rich.[7] This attitude has long since disappeared from modern commercial life; however, it is still reflected in the reluctance of some courts to award prejudgment interest as a matter of course. Legal scholars gradually began to realize that money has a "use value," and interest, reflecting this "use" by the defendant, is a legitimate element in providing a plaintiff with full compensation. Courts have demonstrated an increasing willingness to award prejudgment interest in recent times; however, a substantial degree of conflict remains in the decisions. This conflict, combined with the influence and diversity of local statutes and cases, makes it virtually impossible to state any single rule or set of rules regarding the award of prejudgment interest. However, through an analysis of historical and modern court decisions, the particular statutes involved, and public policies promulgated, one can gain an understanding about the guiding principles in this area of the law.

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1. D. DOBBS, HANDBOOK ON THE LAW OF REMEDIES § 3.5 (1973).

2. Interest awards, other than those based upon contract provisions, are awards of simple interest. Thus, prejudgment and judgment interest is ordinarily not compounded. Hamilton v. Netherton, 194 Kan. 683, 401 P.2d 657 (1965).

3. Busik v. Levine, 63 N.J. 351, ___, 307 A.2d 571, 575, *appeal dismissed*, 414 U.S. 1106 (1973).

4. *See* Comment, *The Availability of Prejudgment Interest in Personal Injury and Wrongful Death Cases*, 16 U.S.F.L. REV. 325, 326-27 (1982).

5. *See* State v. Phillips, 470 P.2d 266, 274 (Alaska 1970) (wrongful death action in which prejudgment interest was held to accrue from time of death).

6. For a detailed analysis of formulas used to compute the exact amount of interest to be paid, see Comment, *Prejudgment Interest as an Element of Damages: Proposed Solutions for a Colorado Problem*, 49 U. COLO. L. REV. 335 (1978).

7. Comment, *Interest Damages in Virginia*, 28 VA. L. REV. 1138, 1141 (1942).

Through such an analysis, this article discusses the insurer's liability for prejudgment interest, specifically focusing upon whether and to what extent an insurer is liable for prejudgment interest when the verdict exceeds the policy limits. The scope of this analysis deals primarily with automobile liability insurance; however, the principles discussed herein are generally applicable to other forms of liability insurance as well.

II. The Standard Liability Insurance Policy

A. *Definition*

A liability policy is a contract of insurance which undertakes to pay on behalf of the insured all sums which he becomes legally obligated to pay as damages.[8] Thus, the purpose of automobile liability insurance is to protect the owner of a motor vehicle against losses arising out of claims due to injuries to third persons for which he, as owner of the vehicle, is responsible.[9] The coverage afforded an insured, as well as the liability of an insurer, is determined by the insuring clauses, exceptions, and exclusions contained in the policy.[10]

Under such a policy the insured is normally required to notify the insurer within a reasonable time of any accident which might result in a claim under the policy. The insured must also cooperate with the insurer in the defense of any action under the policy, and he is further precluded from taking any action toward the settlement of a claim on his own. A failure to comply substantially with any of these requirements will result in the release of the insurer from liability under the policy.[11]

B. *The Postjudgment Interest Clause*

The standard liability insurance policy contains a postjudgment interest[12] clause providing that the insurer shall pay "all interest accruing after entry of judgment until the company has paid or tendered or deposited in court such part of such judgment as does not exceed the limits of the company's liability thereon."[13] This contract provision was the first

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8. 2 R. Long, The Law of Liability Insurance § 9.01 (1981).

9. C. Hulvey & W. Wandel, Workmen's Compensation and Automobile Liability Insurance in Virginia 103 (1930).

10. Long, *supra* note 8, at § 9.01.

11. It becomes apparent that the insurance company exercises total control over the policy and the litigation process. The insured is largely at the mercy of the insurer, and it thus becomes necessary for the courts to protect the rights of the insured. *See* Wilkerson v. Maryland Casualty Co., 119 F. Supp. 383 (E.D. Va. 1953), *aff'd*, 210 F.2d 245 (4th Cir. 1954).

12. Postjudgment interest refers to interest to be paid on a judgment from the time the judgment is rendered by the court to the time of the payment by the insurance company.

13. Annot., 76 A.L.R.2d 983, 987 (1961). "While the annotation concerns liability for interest on judgments, it equally applies where prejudgment interest is concerned." Michigan Milk Producers Ass'n v. Commercial Union Ins. Co., 493 F. Supp. 66, 70 n.5 (W.D. Mich.

form of judgment interest to be allowed by the courts.[14] The courts were at one time split as to the exact meaning of this clause; however, there is now a consensus that this provision requires the insurer to pay interest on the entire amount of damages until it either pays the amount of its liability under the policy limits to the plaintiff or tenders such amount to the court.[15] Thus, an insurer may be obligated to pay postjudgment interest on a judgment recovered against the insured in excess of the policy limits, even though the payment of such interest may cause the insurer's total liability to exceed the limits of the policy.[16] In *United Services Automobile Association v. Russom*,[17] the court stated that the payment of interest is by its nature an undertaking to pay a sum over and above the policy limits, frequently in substantial amounts. The courts have also noted that since the insurer maintains exclusive direction and control of the defense and settlement of a claim, it seems only fair that he be required to assume full responsibility for the accrual of any interest necessarily resulting from a delay in payment following the rendering of judgment.[18]

The court's acceptance of postjudgment interest, as well as the insurer's liability for interest on an amount exceeding the policy limits, laid the groundwork for the award of prejudgment interest and the liability of the insurer for such interest on awards which exceed its policy limits.

III. The Insurer's Liability for Prejudgment Interest

A. *The Liquidated-Unliquidated Debate*

Historically, prejudgment interest was allowed only on liquidated claims.[19] The original distinction between liquidated and unliquidated damages was based on the theory that the defendant should be penalized for not promptly paying the set amount owed, but it was considered unfair to impose a penalty for not paying an obligation of an uncertain amount.[20] The modern rule is to recognize prejudgment interest as an or-

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1980).

14. 76 A.L.R.2d at 986.

15. *See* Security Ins. Co. v. Houser, 191 Colo. 189, 552 P.2d 308 (1976). *See also* Powell v. T.A. & C. Taxi, Inc., 104 N.H. 428, 188 A.2d 654 (1963) (automobile liability insurer held liable for postjudgment interest on full amount of award, even where such award was in excess of the stated policy limits); McPhee v. American Motorists Ins. Co., 57 Wis. 2d 689, 205 N.W.2d 152 (1973) (reasonable to impose the entire expense of accrual of postjudgment interest upon the insurer in view of company's right to control the litigation process).

16. *See* United Servs. Auto. Ass'n v. Russom, 241 F.2d 296 (5th Cir. 1957); Crook v. State Farm Mut. Auto. Ins. Co., 235 S.C. 452, 112 S.E.2d 241 (1960).

17. 241 F.2d at 303. *See also* Long, *supra* note 8, at § 9.01.

18. Wilkerson v. Maryland Casualty Co., 119 F. Supp. 383, 388 (E.D. Va. 1953).

19. A liquidated amount is one which is made certain or fixed by agreement of the parties or by operation of law. *See* Comment, *supra* note 7, at 1141.

20. *See* Zorn v. Britton, 120 Fla. 304, ___, 162 So. 879, 880 (1935) (interest is allowed on damages to property from date of accrual of cause of action, but is not allowable on unliqui-

dinary element of compensatory damages present in all cases.[21] If such interest is not allowed, the plaintiff will often be less than fully compensated for the actual loss or injury he has suffered.[22] The liquidated-unliquidated distinction has taken on considerably less significance in modern litigation and has been largely repudiated or ignored in many jurisdictions.[23] In general, there is now a willingness by courts to allow interest on unliquidated claims as justice may dictate.[24] To the extent that the liquidated-unliquidated distinction survives today, it must be subordinated to the more fundamental principle that damages in a given case must give full compensation for the plaintiff's losses.[25]

B. *Protecting the Rights of the Insurer: A Limited Liability View*

There are two schools of thought concerning an insurer's liability for prejudgment interest in excess of the policy limits. The first school holds that the insurer's liability for interest is strictly limited by its policy limits clause.[26] In *Guin v. Ha*,[27] the Supreme Court of Alaska held that a

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dated damages for personal injuries).

21. LONG, *supra* note 8, at § 9.01. This stems from the recognition that money has a use value. Therefore, while the defendant retains possession of the money which he will eventually have to pay to the plaintiff, assuming a future judgment against him, the plaintiff is deprived of the use and earning power of his own money, and should thus be compensated for the loss. *See* Comment, *supra* note 7, at 1142.

22. Interest is allowed as damages from the time when the principal debt became due, or when the right to damages for the breach of contract or tort first accrued. C. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES § 58 (1935).

23. *See* Comment, *Prejudgment Interest: An Element of Damages Not to be Overlooked*, 8 CUM. L. REV. 521, 535 (1977).

24. 22 Am. Jur. 2d *Damages* § 181 (1965).

25. If the plaintiff has been deprived of the use of his property, he should be compensated for that loss whether the exact sum due him as principal is ascertainable.

> The fact remains in both situations the defendant has had the use, and the plaintiff has not, of moneys which the judgment finds was the damage plaintiff suffered. This is true whether the contested liability is for a liquidated or for an unliquidated sum. For that reason, the concept of a "liquidated" sum has often been strained to find a basis for an award of interest.

Busik v. Levine, 63 N.J. 351, ___, 307 A.2d 571, 575 (1973). Upon a recognition of the use value of money and the compensatory nature of interest, the liquidated-unliquidated distinction breaks down.

26. *See* Guin v. Ha, 591 P.2d 1281 (Alaska 1979). *See also* Dittus v. Geyman, 68 Mich. App. 433, 242 N.W.2d 800 (1976) (automobile liability insurer held liable for prejudgment interest from date of complaint, but only to extent that amount of interest did not exceed policy limits); Factory Mut. Liab. Ins. Co. v. Cooper, 106 R.I. 632, 262 A.2d 370 (1970) (insurer under automobile liability insurance policy was not obligated to pay prejudgment interest in excess of its policy limits merely because it exercised exclusive control over the litigation process and thus the running of interest). *But see* Michigan Milk Producers Ass'n v. Commercial Union Ins. Co., 493 F. Supp. 66 (W.D. Mich. 1980) (where automobile liability insurer exercised full control over litigation process, he was held liable for prejudgment interest on full amount of award, including excess of policy limits).

27. 591 P.2d 1281 (Alaska 1979).

medical malpractice liability insurer was liable for prejudgment interest to the extent that the sum paid by the insurer did not exceed the policy limits set by the insurer. The court found that under Alaskan law, prejudgment interest was properly classified as compensatory damages, and thus such interest was damages within the meaning of the insurer's liability limits clause.[28] Thus, the insurer was not obligated to pay interest in excess of its designated policy limits. It was felt that in order to hold the insurer liable for prejudgment interest exceeding the policy limits, the company must have assumed such an obligation in the contract, or public policy must intervene and impose the obligation despite the terms of the contract.[29]

1. The Insurance Contract[30]

"The liability of an insurer and the extent of the loss under a policy of

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28. *Id.* at 1285. The provisions of the insurance policy, insofar as they were relevant to the issue of prejudgment interest, provided:

> MALPRACTICE LIABILITY
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> 2. NOW WE THE UNDERWRITERS hereby agree, subject to the terms, limitations, exclusions and conditions of this Insurance, to pay on behalf of the Assured all sums which the Assured shall by law be held liable to pay for damages arising out of bodily injury or mental injury to or death of any patient caused by or alleged to have been caused by error, omission or negligence in professional services rendered or which should have been rendered (hereinafter referred to as Malpractice)
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> . . . .
>
> 3. As respects the coverage afforded by this Insurance, the Underwriters will defend any claim or suit in the name of and on behalf of the Assured and will pay the costs and expenses incurred in such defence . . . .
>
> 4. Irrespective of the number of persons or entities named as Assured in the Schedule or added by endorsement, the liability of the Underwriters hereunder for damages shall not exceed the limit of liability set out in the Schedule in respect of any one patient, nor the limit of liability set out in the Schedule in respect of all claims made against the Assured during the currency of this Insurance . . . , except that, subject to the provisions contained in Paragraph 3, the Underwriters will pay the costs and expenses incurred in the defence of any claim or suit.

Id.

29. *Id.* at 1287. "[T]he interpretation of the words of the contract is treated in the same manner as questions of law." National Bank v. J.B.L. & K., Inc., 546 P.2d 579, 586 (Alaska 1976).

> [W]hen the language of an insurance policy admits to two reasonable constructions, the fault must be charged to the insurer who selected the language, and the language is interpreted in favor of the insureds. But, in seeking to ascertain the intent of the parties, [the] insurance policy must be examined in its entirety and the language used must be given its plain, ordinary, and usual meaning.

Factory Mut. Liab. Ins. Co. v. Cooper, 106 R.I. 632, ___, 262 A.2d 370, 372 (1970).

30. The purpose of contract interpretation is to ascertain and effectuate the reasonable expectations of the parties. However, due to the inequality in bargaining power and the need for certainty in ascertaining rates, somewhat different standards are applied to the interpretation of insurance contracts. An insurance contract may be considered a contract of adhesion and thus should be construed to provide the coverage which a lay person would reasonably have expected. However this approach is not to be used as an instrument for

liability or indemnity insurance[31] must be determined, measured and limited by the terms of the contract."[32] By the terms of its contract, the insurer in *Guin*[33] agreed to pay the liability of the insured for damages up to $25,000, to defend the insured, and to pay "costs and expenses incurred in such defense."[34] The agreement to pay costs and expenses is considered a standard supplementary payments clause and is not subject to limitation by the policy.[35]

The insurer's promise to pay all costs and expenses incurred in the defense of the suit would not, in common understanding, include prejudgment interest.[36] Costs include those items that a court is authorized to tax against the losing party, and Alaska does not include prejudgment interest among the items allowed as costs.[37] Nothing in the supplemental payments clause could be construed as imposing upon the insurer the obligation to pay prejudgment interest, as such interest is an item of compensatory damages and is thus limited by the damages clause in the contract. Thus, when an insurer pays the limits of liability coverage to an injured third party on behalf of its insured, it discharges its obligation under the policy.

Alaska's general interest statute[38] provides that the rate of interest in the state is eight percent per year on any money *after it is due.* Under this statute, money is due when the cause of action accrues.[39] Thus, Alaska's interest statute imposes on defendants in tort actions the obligation to pay prejudgment interest computed from the date of the injury.[40] In *Guin*, the insured argued, based on this statute, that the policy limits were due from the insurer on the date of injury rather than the date of settlement. The court disagreed with this contention.[41] Pursuant to the policy, the insurer had agreed to pay on behalf of the insured all sums which the "assured shall by law be held liable to pay for damages."[42] Until a valid judgment was rendered or settlement reached, the insured was

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rewriting the contract. Guin v. Ha, 591 P.2d 1281, 1284-85 (Alaska 1979) (citing Stordahl v. Government Employees Ins. Co., 564 P.2d 63, 65-66 (Alaska 1977)).

31. Under a policy of indemnity insurance, the insurer does not become obligated to the insured until the insured has suffered an actual "out of pocket" loss (actually paid the award to the plaintiff).

32. 15 G. COUCH, CYCLOPEDIA OF INSURANCE LAW § 56:1 (2d ed. 1966).

33. 591 P.2d 1281 (Alaska 1979).

34. *Id.* at 1285.

35. *Id.*

36. *Id.*

37. Thus, an analysis of the applicable statutory law is of extreme importance when attempting to ascertain the meaning of an insurance policy.

38. ALASKA STAT. § 45.45010 (1976).

39. State v. Phillips, 470 P.2d 266, 274 (Alaska 1976).

40. *Id.*

41. 591 P.2d at 1290.

42. *Id.*

not liable by law to pay damages to the injured party. Thus, the sum that the insurance company might eventually pay on behalf of the insured was not due until the time of settlement. In this way, the court held that the language of the contract itself in no way obligated the insurer to pay prejudgment interest in excess of the policy limits.[43]

2. Public Policy Considerations

The "limited liability school" fears that holding the insurer liable for prejudgment interest in excess of the policy limits will put unfair pressure on the insurer to settle early. It is argued that such excess liability could force an insurance company to acquiesce to a plaintiff's demands at an early stage of the proceeding, regardless of any meritorious defenses it may have. It would do so rather than run the risk of paying a large amount of interest caused by court delays, should the plaintiff eventually recover.[44] In addition, the insurer is responsible for the costs of defending the litigation, which increase substantially in the advanced stages of trial preparation, thus providing added impetus for early acquiescence.

It is also argued that holding insurers liable for prejudgment interest in excess of the policy limits denies insurers the right to limit their risks contractually.[45] Aside from altering the insurer's assumed contractual duties, the excess liability injects an unwarranted element of uncertainty into the area of liability insurance and thus presents considerable problems in the accurate computation of premiums.

In *Guin*,[46] the court recognized the fact that under liability insurance policies the insurer maintains exclusive control of the litigation process and retains the use of, and presumably earns interest on, the funds for which it will eventually be held liable. However, it held that notions of economic fairness are not sufficient grounds for restricting the contractual rights of the insurer.[47]

Recognizing the possibility that increasing an insurer's liability to include interest in excess of the policy limits might facilitate the early settlement of claims in cases where liability was clear, the court in *Guin* stated that "[e]ncouraging early settlement where liability is clear is a salutary goal, but it does not require the insurer to bear the burden of risk it has not assumed."[48] The court further noted that in every contract

43. *Id.* at 1291.

44. Comment, *supra* note 4, at 352-53.

45. *See* Michigan Milk Producers Ass'n v. Commercial Union Ins. Co., 493 F. Supp. 66, 71 (W.D. Mich. 1980).

46. Guin v. Ha, 591 P.2d 1281 (Alaska 1979).

47. *Id.* at 1284. For a full discussion of public policy considerations favoring holding the insurer liable for prejudgment interest beyond the policy limits, see *infra* text accompanying notes 60-71.

48. 591 P.2d at 1291.

there exists an implied covenant of good faith and fair dealing which obligates the insurer to act promptly in response to reasonable offers of settlement[49] or to bring the case to trial.

Thus, an insured will not suffer at the hands of an uncooperative insurance company because any undue delay on its part could be seen as a breach of this implied covenant of good faith.[50] The insured is entitled to recover from his insurer any prejudgment interest attributable to such bad faith, regardless of the policy limits.[51]

Thus, the limited liability school of thought acknowledges the existence of public policy considerations on either side of the issue but adheres to the position that no compelling reason exists to hold the insurer liable for prejudgment interest in excess of its stated policy limits.

C. *The Insurer's Liability for Interest in Excess of the Policy Limits: A Modern Approach*

The second school of thought adheres to the view that insurers should be held liable for prejudgment interest, including an amount which exceeds the specific policy limits.[52] Policy considerations concerning the very nature and purpose of awarding interest support such a view.

1. Prejudgment Interest Statutes and Their Effect on the Liability Insurance Policy

Prejudgment interest statutes[53] vary drastically as to their provisions

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49. A thorough discussion of the issue of insurer's duty to make a good faith effort to settle the claim within the policy limits is beyond the scope of this article. For a discussion of the modern view regarding this issue, see Comment, *Insurers' Liability for Excess Judgments in Virginia: Negligence or Bad Faith?*, 15 U. RICH. L. REV. 153 (1980) (modern trend is toward holding insurer liable for excess judgment based on mere negligence standard rather than on requirement of bad faith).

50. 591 P.2d at 1291. *See* Rova Farms Resort, Inc. v. Investors Ins. Co., 65 N.J. 474, 323 A.2d 495 (1974) (in making decision on whether to go to trial, insurer must weigh the conflicting interest as if it had full coverage for whatever verdict might be received, regardless of the policy limits). For a discussion concerning the bad faith issue see Koesterer, *Liability in Excess of Policy Limits*, 1977 FED'N INS. COUNS. Q. 287.

51. Note that if the courts recognize and follow the modern trend of holding the insurer liable for excess judgments based on a negligence standard, this would have important effects on the insurer's liability for prejudgment interest. A lowering of the good faith standard would necessarily mean a concomitant increase in the insurer's liability for prejudgment interest, resulting in increased premiums to spread this additional expense.

52. The following states apparently follow this school: Arkansas, Colorado, Florida, Illinois, Kansas, Louisiana, Maryland, Nebraska, New Hampshire, New Jersey, North Carolina, Tennessee, Texas, Virginia, Washington, and Wisconsin (Ohio and Pennsylvania have decisions holding each way). Michigan Milk Producers Ass'n v. Commercial Union Ins. Co., 493 F. Supp. 66, 70 n.7 (W.D. Mich. 1980).

53. There are a number of states that provide for the payment of prejudgment interest by statute. Such states include Colorado, Louisiana, Michigan, New Hampshire, New York,

for the awarding of prejudgment interest; however, all have a decided impact on the nature and extent of the insurer's liability. The basic aim of such statutes is to insure that the plaintiff is fully compensated for his injuries by awarding him the "use value" of the money to which he was entitled, and at the same time, to alleviate delay in the disposition of cases, thereby lessening congestion in the courts by providing an incentive for the early settlement of claims.[54]

In Michigan, prejudgment interest is awarded under section 6013 of the Revised Judicature Act.[55] This section of the act *requires* the addition of prejudgment interest to all judgments in civil actions unless there has been a bona fide offer of settlement by the losing party which is as large as or larger than the amount ultimately awarded.[56] The statute does not specifically mention insurers; however, if the statute is to accomplish its purpose, the insurer must be held liable for prejudgment interest in excess of its policy limits.[57] If the insurer is insulated from liability beyond its policy limits, he will have far less incentive to seek early settlements of claims approaching or exceeding policy limits than he would were he cog-

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North Dakota, Oklahoma, and Rhode Island. Busik v. Levine, 63 N.J. 351, ___, 307 A.2d 571, 576 (1973).

54. *See* Laudenberger v. Port Auth., 496 Pa. 52, 436 A.2d 147 (1981), *appeal dismissed*, ___ U.S. ___, 102 S. Ct. 2002 (1982); Comment, *Denham v. Bedford: Statutory Prejudgment Interest and Its Effect on Third Party Insurers*, 1979 DET. C.L. REV. 345, 347.

55. MICH. COMP. LAWS ANN. § 600.6013 (Supp. 1982-1983). By enacting this statute, Michigan has adopted the theory that all civil judgments become due at the time plaintiff files his complaint, rather than at the time of judgment. This statute is in line with the abandonment of the liquidated-unliquidated distinction because the defendant is liable for interest on the total amount of the judgment, even though he may have no way of knowing in advance what that amount will be.

56. The text of this statute is as follows:

> If a bona fide written offer of settlement in a civil action based on tort is made by the party against whom the judgment is subsequently rendered and the offer of settlement is substantially identical or substantially more favorable to the prevailing party than the judgment, the court may order that interest shall not be allowed beyond the date the written offer of settlement is made.

MICH. COMP. LAWS ANN. § 600.6013(5) (Supp. 1982-1983). The author feels that mandatory prejudgment interest statutes should include such a protective clause relieving defendant of the interest obligation when plaintiff unreasonably refuses a bona fide settlement offer.

57. As the Supreme Court of Pennsylvania recently noted,

> The judicial system has long been vexed by the problem of congestion and delay in the disposition of civil actions for bodily injury, death or property damages pending in the trial courts. . . .
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> [B]ut in too many cases meaningful negotiations commence only after a trial date is fixed or on the courthouse steps or in the courtroom, thus leading to delay in the disposition of cases and congestion in the courts.

Laudenberger v. Port Auth., 496 Pa. 52, ___, 436 A.2d 147, 150-51 (1981) (quoting Civil Procedure Rules Committee, *Proposed Rule 238 Comment, reprinted in* 8 PA. BULL. 2668 (1978)), *appeal dismissed*, ___ U.S. ___, 102 S. Ct. 2002 (1982). Tort litigation places a major demand upon the judicial system, and it is a generally accepted principle that most tort judgments are covered by liability insurance. Comment, *supra* note 4, at 352.

nizant of the fact that his liability for prejudgment interest would not be limited by his policy limits. Secure in the belief that his liability is limited by his policy limits, the insurer may cause undue delay in an attempt to wear the plaintiff down. In *Denham v. Bedford*,[58] the Michigan Court of Appeals recognized the existence of this problem and held that public policy dictated that the prejudgment interest statute be incorporated into the insurance policy. The policy had contained the standard postjudgment interest clause, but had made no mention of prejudgment interest. The court held that the existence of the statute, and the public policy considerations inherent in it, mandated that the postjudgment interest clause be modified to provide for the calculating of interest from the filing of the complaint. The court then held the insurer liable for prejudgment interest on its portion of the judgment, even where the inclusion of such interest required the insurer to pay an amount in excess of its policy limits.[59] Thus, due to the existence of the Michigan prejudgment interest statute, the insurer was held liable for prejudgment interest in an amount exceeding its policy limits despite the absence of such an explicit agreement in the insurance policy.

2. Public Policy Considerations

In *Busik v. Levine*,[60] the New Jersey Supreme Court viewed its prejudgment interest rule as an attempt to induce prompt defense consideration of settlement possibilities,[61] demonstrating that the award of prejudgment interest bears directly upon the judicial machinery and the policies of judicial management.[62] As recognized by the Michigan court in *Denham*,[63] effective enforcement of such a rule and the policy considerations behind it require holding the insurer liable for prejudgment interest in an amount which exceeds the policy limits. In *Denham*, the court

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58. 82 Mich. App. 107, 266 N.W.2d 682 (1978), *aff'd*, 407 Mich. 517, 287 N.W.2d 168 (1980).

59. *Id.* at ___, 266 N.W.2d at 685. The court based its holding on an earlier decision, Cosby v. Pool, 36 Mich. App. 571, 194 N.W.2d 142 (1971), which held that an insurance contract made prior to enactment of the prejudgment interest statute was effectively amended by the statute and required payment of interest from the date of the filing of the complaint, not merely from the date of judgment as the actual contract provided. The court discussed the constitutionality of altering an insurance contract in such a manner and determined that the statute did not change the substance of the contractual duties and obligations and applied it retroactively. *Id.* at ___, 194 N.W.2d at 145. *See* Ballog v. Knight Newspapers, Inc., 381 Mich. 527, 164 N.W.2d 19 (1969).

The Supreme Court of New Jersey approved retroactive application of a prejudgment interest statute in cases where the accident involved occured before the rule was adopted, but the cases come to trial after the effective date of the rule. Busik v. Levine, 63 N.J. 351, 307 A.2d 571 (1973).

60. 63 N.J. 351, 307 A.2d 571 (1973).

61. *Id.* at ___, 307 A.2d at 575.

62. *Id.* at ___, 307 A.2d at 576.

63. Denham v. Bedford, 82 Mich. App. 107, ___, 266 N.W.2d 682, 686 (1978).

stated:

> For us to hold otherwise, an insurer would have no motivation to settle a meritorious claim. By refusing to settle, the insurer not only has a chance to wear a plaintiff down, thereby possibly settling a meritorious claim for less than its actual value, but it also knows that even if plaintiff is successful in litigation, it [the insurance company] will still be able to retain all the income made from the use of a plaintiff's money. Such a policy is contrary to the sound administration of the judicial system and repugnant to the public policy behind the insurance laws of this state.[64]

In holding an insurer liable for prejudgment interest on the amount of its policy limits, even where payment of such interest would force the insurer's total liability beyond its stated policy limits, the insurer is only paying that which it presumably earned by holding the money. Thus, it is both just and rational to hold the insurer liable to the plaintiff for such an amount. Accordingly, the majority of jurisdictions have resolved that the insurer is liable for all prejudgment interest on its policy limits, even where the payment of such interest forces the insurer's total liability beyond its stated policy limits.[65]

In *Michigan Milk Producers Association v. Commercial Union Insurance Co.*,[66] it was stated that,

> The only issue . . . which remains unresolved at common law is not whether an insurer is liable for interest on the policy limits but whether the insurer is liable for interest on the whole judgment. The courts have split on this issue although the majority and modern trend is in favor of holding the insurers liable for interest on the whole judgment.[67]

It is argued that insurers should be held liable for prejudgment interest on the entire judgment rather than merely on their policy limits because they exercise full control over the entire litigation process.[68] By the very terms of the insurance policy, the liability insurer retains full control over any investigation process, settlement, or litigation. The insured has no control over the process; and if he attempts to settle of his own volition, he runs the risk of forfeiture of any rights under the policy. It hardly seems fair to allow the insurance company to litigate the entire case in an effort to save its policy coverage and then force the insured to pay the prejudgment interest on the excess verdict when he exercised no control over the litigation process. The insurer is in a position to control the litigation process and is better able to absorb the costs of delay by spreading the expenses over a large number of policy holders. Thus, the equities

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64. *Id.* at ___, 266 N.W.2d at 686.

65. Michigan Milk Producers Ass'n v. Commercial Union Ins. Co., 493 F. Supp. 66, 71 (W.D. Mich. 1980).

66. *Id.* at 66.

67. *Id.* at 70 (citing Denham v. Bedford, 407 Mich. 517, 533, 287 N.W.2d 168, 173 (1980)).

68. 493 F. Supp. at 71.

would seem to weigh in favor of the insurer being held liable for the full amount of prejudgment interest.

An additional rationale for requiring an insurer to pay prejudgment interest in excess of the policy limits can be found in the terms of the contract itself. In *Michigan Milk Producers Association*,[69] the insurance policy contained a standard postjudgment interest clause that had been included within a supplementary payments provision.[70] Payments specified in the supplementary payments section of an insurance policy are supplementary in so far as they are in addition to the damages payment to which the policy limits refer. Thus, the agreement to pay interest was by its nature an agreement to pay an amount beyond the policy limits. The court held that the postjudgment interest clause was modified by the Michigan prejudgment interest statute to include the payment of interest from the time of the filing of the complaint. The insurer was then held liable for prejudgment interest on the full amount of the judgment.[71] Thus, due to the Michigan interest statute and the policy considerations inherent in it and the terms of the insurance contract itself, the insurer became liable for interest on the entire judgment.

IV. Insurer's Liability for Prejudgment Interest in Virginia: A Possible Stance

The Supreme Court of Virginia has not yet dealt directly with the issue of an insurer's liability for prejudgment interest. However, an analysis of the Virginia decisions regarding postjudgment interest, coupled with a careful reading of the Virginia statute providing for the payment of interest on judgments,[72] yields a sound basis for a rational prediction of Virginia's position on the issue.

In analyzing the state of the law regarding the payment of prejudgment interest in Virginia, one author noted:

> Here is only a trifling subdivision of the small segment of the law, but even here many difficulties have arisen. The efforts of the legislature to clarify the uncertainties have not been entirely effective, and a review of judicial decisions on the point leaves several questions unanswered. The fact that

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69. *Id.*

70. The supplemental payments provision of the contract obligated the insurer to defend the insured against any suit seeking damages payable under the policy and to pay in addition to the applicable limits of liability

> all costs taxed against the insured in any such suit or arbitration proceeding and all interest on the entire amount of any judgment and before the company has paid or tendered or deposited in court that amount of the judgment which does not exceed the limits of the company's liability thereon.

Id. at 67.

71. *Id.* at 69.

72. Va. Code Ann. § 8.01-382 (Cum. Supp. 1982).

> the issue has been passed on in only a relatively few cases (compared with the innumerable adjudications in which a claim for interest might have been made and disputed) fosters the suspicion that counsel may have often shied away from a precarious path which might have led to a substantial benefit for a client.[73]

Virginia provides for the allowance of prejudgment interest by statute.[74] The statute is purely discretionary, clothing the judge or jury with the power to provide for interest on the full award or only a part thereof and to fix the period from which the interest will run. The interest is deemed to run until the judgment is paid. The statute further provides that if the judge or jury does not provide for interest, the award shall bear interest from the time the judgment was entered, thereby making the payment of postjudgment interest mandatory.[75]

The existence of the statute serves to support the proposition that the Virginia legislature, and thus the desires of the public, support the award of prejudgment interest in Virginia. The statute applies to all actions and suits, and the jury is given broad discretion both as to the allowance of the interest and to the fixing of the date at which it shall commence. There is nothing in the statute to indicate that interest is not to be awarded on unliquidated claims. "The fact that the provisions of the statute are to be applied in a tort action, which is usually an unliquidated claim, clearly indicates a legislative intent that an unliquidated claim is within its purview."[76] The purpose of the statute is to allow for the full compensation of a plaintiff by awarding him the "use value" of money.[77] The statute is discretionary, thus allowing for the award of interest where the equities so dictate and the denial of it where they do not. Thus, in a case where the plaintiff unreasonably refuses a good faith offer by the

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73. Comment, *supra* note 7, at 1138-39.

74. The text of the statute is as follows:

> Except as otherwise provided in § 8.3-122, in any action at law or suit in equity, the verdict of the jury, or if no jury the judgment or decree of the court, may provide for interest on any principal sum awarded, or any part thereof, and fix the period at which the interest shall commence. The judgment or decree entered shall provide for such interest until such principal sum be paid. If a judgment or decree be rendered which does not provide for interest, the judgment or decree awarded shall bear interest from its date of entry, at the rate so provided in § 6.1-330.10, and judgment or decree entered accordingly; provided, if the judgment entered in accordance with the verdict of a jury does not provide for interest, interest shall commence from the date that the verdict was rendered.

VA. CODE ANN. § 8.01-382 (Cum. Supp. 1982).

75. The statute thus provides for the payment of both prejudgment and postjudgment interest.

76. Beale v. King, 204 Va. 443, 448, 132 S.E.2d 476, 480 (1963). Section 8.01-382 of the Virginia Code which now applies to all actions and suits, expanded the section to which the court refers in *Beale*, which was limited to actions in contract or tort and suits in equity. VA. CODE ANN. § 8.01-382 (Cum. Supp. 1982).

77. City of Danville v. Chesapeake & Ohio Ry., 34 F. Supp. 620, 638-39 (W.D. Va. 1940).

insurer, the jury may refuse to award interest or may award only partial interest as justice dictates.

The federal decisions applying this statute have continually adhered to the view that the insurer is liable for the payment of interest even though such payment makes the total amount due exceed the stated policy limits.[78] In *American Automobile Insurance Co. v. Fulcher*,[79] the court found it clear "that the liability stipulated in the policy is a contractual one relating solely to the risks insured against, and that it in no way affects the payment of interest on the judgment, which is a liability imposed by law."[80] Thus, the payment of interest is not to be limited by the terms of the insurance policy.

In *Wilkerson v. Maryland Casualty Co.*,[81] the court recognized that the insurer controls the entire litigation process and that the policy holder is powerless to effect a settlement of his own volition. The court stated:

> Not infrequently judgment is obtained against an insured for an amount in excess of the coverage of the policy and it would seem a harsh rule to permit the insurer to litigate the entire case in an effort to save the amount of its coverage while interest on the excess accumulates against the insured. . . . With the company in control of the conduct of the case the policy holder is powerless should he desire to effect a settlement unless the company consents.[82]

While this rationale was employed in holding the insurer liable for postjudgment interest in excess of its policy limits, the same rationale has been used by other courts to hold the insurer liable for prejudgment interest beyond its policy limits.[83]

The provision for the award of interest on unliquidated claims in Virginia as early as 1849[84] reflects a longstanding permissive attitude towards the awarding of interest as damages. In recognition of this attitude and the public policy of providing for full and fair compensation to plaintiffs and protecting the interests of the insured,[85] as well as the federal decisions applying the Virginia interest statutes in holding the insurer liable

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78. *See* American Auto. Ins. Co. v. Fulcher, 201 F.2d 751, 757 (4th Cir. 1953) (insurer held liable under automobile liability insurance policy for postjudgment interest exceeding policy limits).

79. *Id.*

80. *Id.*

81. 119 F. Supp. 383 (E.D. Va. 1953), *aff'd*, 210 F.2d 245 (4th Cir. 1954) (automobile liability insurer held liable for full amount of postjudgment interest even where such amount exceeded the stated policy limits).

82. *Id.* at 388.

83. *See* Michigan Milk Producers Ass'n v. Commercial Union Ins. Co., 493 F. Supp. 66 (W.D. Mich. 1980); Denham v. Bedford, 82 Mich. App. 107, 266 N.W.2d 682 (1978), *aff'd*, 407 Mich. 517, 287 N.W.2d 168 (1980).

84. Comment, *supra* note 7, at 1149.

85. *See supra* notes 76-77 and accompanying text.

for postjudgment interest in excess of the predetermined policy limits,[86] one can reasonably predict that if faced with the issue today, Virginia would follow the apparent modern trend and hold the insurer liable for prejudgment interest in an amount exceeding the policy limits, including possibly the amount of the entire judgment as well.[87]

V. Conclusion

It is often necessary to award prejudgment interest to achieve full and just compensation for an injured plaintiff due to the delay in payment of funds owed him as a result of injuries inflicted by the defendant. Both the ultimate liability for the payment of such interest and the extent of it are extremely important to both the liability insurer and the insured. Whether the insurer is liable for prejudgment interest in excess of the policy limits is a function of the particular policy's language, the existing case and statutory law in a given jurisdiction, and the weight which the court chooses to attach to competing policy considerations.

In numerous jurisdictions the postjudgment interest clause has been used as a vehicle for the expansion of the liability of the insurer for prejudgment interest. Whether done through a particular statute, or based purely on analogy to precedent, or on reasons of public policy, or a combination of these, the courts have evidenced an increased willingness to hold the insurer liable for prejudgment interest. To the extent that a modern trend exists, it would appear to be in favor of increasing the insurer's liability for prejudgment interest to include the payment of interest on the full award in situations where the verdict exceeds the policy limits.

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86. *See supra* notes 78-83 and accompanying text.

87. While in some cases a request for interest might be refused, it should nonetheless be requested in all cases. The plaintiff takes no risk in asking for an instruction informing the jury that they may give interest on the verdict, for such a request is not likely to result in a lower award. On the otherhand, it is virtually certain that the jury will award interest in at least some cases. It is also likely that while a jury might not award interest, it will take such a request into consideration when considering the amount to be awarded and thereby be influenced to render a higher award. The legislature considered prejudgment interest important enough to provide for it by statute. Plaintiff's attorneys should be aware of their client's entitlement to prejudgment interest under the statute and make a timely request for its award.