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### Bad Faith Damages Against Surplus Line Insurers Might Not Be Capped in Illinois

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I recently had occasion to read through the Illinois Surplus Line Law in detail when I noticed something interesting: surplus lines insurance companies may not be subject to the cap on bad faith damages usually applied to claims against insurers in Illinois. Allow me to explain.

In Illinois there is a statute, 215 ILCS 5/155 ("Section 155"), that governs bad faith claims against insurers. It states that:

*In any action by or against a company wherein there is in issue the liability of a company on a policy or policies of insurance or the amount of the loss payable thereunder, or for an unreasonable delay in settling a claim, and it appears to the court that such action or delay is vexatious and unreasonable, the court may allow as part of the taxable costs in the action reasonable attorney fees, other costs, plus an amount not to exceed any one of the following amounts:*

*(a) 60% of the amount which the court or jury finds such party is entitled to recover against the company, exclusive of all costs;*

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*(b) \$60,000;*

*(c) the excess of the amount which the court or jury finds such party is entitled to recover, exclusive of costs, over the amount, if any, which the company offered to pay in settlement of the claim prior to the action.*

In 1996, the Illinois Supreme Court held that Section 155 pre-empts common law tort claims for breach of the implied duty of good faith and fair dealing against insurers and provides the sole basis for policyholders to recover from insurers for breach of said duty. *See Cramer v. Ins. Exch. Agency*, 174 Ill.2d 513, 675 N.E.2d 897 (1996). As one can see, Section 155 limits recovery against an insurer to reasonable attorneys' fees, other costs, and the lesser of the amounts in (a), (b) and (c) above. The effect is to limit the policyholder's recovery to reasonable attorneys' fees, costs, and \$60,000 or less. No punitive damages or other tort damages, regardless of how egregious the insurer's conduct was. The Supreme Court in *Cramer* did state that Section 155 does not pre-empt a tort that has separate and independent elements and is based on something other than an insurer's failure to pay a claim, but policyholders can find it difficult to meet this test.

Understandably, not everyone is satisfied with this outcome. Don't get me wrong: Section 155 was enacted to benefit policyholders, and the fee-shifting aspect does help make lawsuits against insurers more economically feasible. Nevertheless, the feeling remains that the legislature could have gone further.

Enter the Illinois Surplus Line Law, 215 ILCS 5/445. This law governs when and how "surplus line insurance" may be procured for Illinois policyholders. "Surplus line insurance" means:

***insurance on a risk:***



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*(A) of the kinds specified in Classes 2 and 3 of Section 4 of this Code; and*

*(B) that is procured from an unauthorized insurer after the insurance producer representing the insured or the surplus line producer is unable, after diligent effort, to procure the insurance from authorized insurers; and*

*(C) where Illinois is the home state of the insured, for policies effective, renewed or extended on July 21, 2011 or later and for multiyear policies upon the policy anniversary that falls on or after July 21, 2011; and*

*(D) that is located in Illinois, for policies effective prior to July 21, 2011.*

215 ILCS 5/445(1) (definition of "surplus line insurance"). Section 4 of the Insurance Code states that Class 2 insurance is "Casualty, Fidelity and Surety" and Class 3 insurance is "Fire and Marine, etc." 215 ILCS 5/4. These are very broad categories that include accident and health, liability, vehicle, and property insurance. *Id.* The purpose of the Surplus Line Law "is to make it possible to secure protection against a risk when authorized companies will not provide that protection." *Corday's Dept. Store, Inc. v. NY Fire & Marine Underwriters, Inc.*, 442 F.2d 100, 103-04 (7th Cir. 1971). Consequently, surplus lines insurance is fairly common, particularly for unusual or hard to insure risks. For example, flood insurance is often procured through surplus line insurers. <https://www.investopedia.com/terms/s/surplus-lines-insurance.asp>.

Now for the interesting part. The Surplus Line Law states that:

***Surplus line insurance procured under this Section, including insurance procured from a domestic surplus line insurer, is not subject to the provisions of the Illinois Insurance Code other than Sections 123, 123.1, 401, 401.1, 402, 403, 403A, 408, and all of the provisions of Article XXXI to the extent that the provisions of Article XXXI are not inconsistent with the terms of this Act.***



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215 ILCS 5/445(12). Notice what is missing from the list: Section 155, which is part of the Insurance Code. If surplus line insurance is “not subject to” Section 155, that statute should not pre-empt common law tort claims for bad faith against surplus line insurers. These insurers have the benefit of not being subject to other parts of the Insurance Code, such as having to issue policies on forms approved by the Department of Insurance. See *Cordray's Dept. Store*, 442 F.2d at 104. Therefore, it makes sense that they should not have the benefit of Section 155. This means that policyholders that obtain surplus line insurance may be able to recover more than the limited amounts in Section 155 if they sue their insurers for bad faith, including punitive and other tort damages. See *Cramer*, 174 Ill.2d at 522-23, 675 N.E.2d at 901-02 (noting that some Illinois courts had held policyholders could recover tort damages, including punitive damages, from insurers that acted in bad faith). In an appropriate case, this could prove to be an unpleasant surprise for an unsuspecting surplus line insurer.