Indiana Adopts Restatement to Address Insurer “Safe Harbor” for Insufficient Policy Limits Scenarios

Gregory Michael Gotwald

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Summary

- The Indiana Supreme Court recently held that Indiana follows Section 26 of the Restatement of the Law of Liability Insurance.
- It governs how insurers should handle situations where there are insufficient limits to resolve multiple claims. .
- This includes a “safe harbor” from claims of bad faith or breach of good faith and fair dealing.

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Having insufficient insurance policy limits to settle with all claimants is a common situation and presents difficult circumstances for insurers. Using up limits to settle with some claimants (but not all) reduces the policyholder's liability, but it exposes the policyholder to any remaining claims—claims the policyholder will have to defend on its own. Conversely, refusing to settle with a claimant in hopes of resolving all claims with limited policy proceeds exposes the policyholder to a judgment in excess of the policy's limits if any one claimant secures it.

This situation can put insurers in difficult positions. They may face extra-contractual claims no matter what they do. In a case of first impression for Indiana, the Indiana Supreme Court recently addressed this and adopted Section 26 of the Restatement of the Law of Liability Insurance in *Baldwin v. Standard Fire Ins. Co.*, 269 N.E.3d 1197 (Ind. 2025). In doing so, the court surveyed various cases and treatises, ultimately landing on Section 26, which "requires insurers to try to limit [a policyholder's] overall liability exposure and provides insurers with a 'safe harbor' for limiting their own liability through an interpleader action." *Id.* at 1204.

Baldwin notes that insurers have "wide discretion" to settle cases for policyholders in some jurisdictions. *Id.* at 1205 (citing Texas Farmers Ins. Co. v. Soriano, 881 S.W.2d 312, 315 (Tex. 1994).) Some courts allow settlement on a "first come, first served" basis. *Baldwin*, 269 N.E.3d at 1205 (citing Voccio v. Reliance Ins. Cos., 703 F.2d 1, 3 (1st Cir. 1983).) With this approach, however, insurers risk bad-faith claims from policyholders that the insurer "hastily made excessive settlements that deplete the policy limits." *Baldwin*, 269 N.E.3d at 1205.

Other jurisdictions take a minimize-the-liability approach. "Under this approach, 'the insurer's goal should be to try to effect settlement of all or some of the multiple claims so as to relieve its insured of so much of his potential liability as reasonably possible, considering the paucity of the policy limits.'" (quoting Peckham v. Cont'l Cas. Ins. Co., 895 F.2d 830, 835 (1st Cir. 1990).) The court noted the struggles with this approach as well: This "places an insurer at the mercy of a jury's later decision (aided by self-serving testimony from the claimants) that it could have eliminated more liability by a different settlement strategy." *Baldwin*, 269 N.E.3d at 1205 (quotations omitted).

Having acknowledged the difficulties of these situations, the court then addressed interpleader actions. "Interpleader allows for the joinder of multiple claimants to a common fund into a single action to divide proceeds among them equitably." With its interpleader discussion, the court noted that interpleaders can also provide a "safe harbor" for insurers against extra-contractual claims. *Id.* at 1206.

As to what insurers should do in these situations, the court ultimately adopted the Restatement's two-part approach. First, "'[i]f multiple legal actions that would count toward a single policy limit are brought against an insured, the insurer has a duty to the insured to make a good-faith effort to settle the actions in a manner that minimizes the insured's overall exposure.'" (quoting Restatement of the Law of Liability Insurance § 26(1)). The second section provides the insurer a safe harbor from bad-faith actions:

> The insurer may, but need not, satisfy this duty by interpleading the policy limits to the court, naming all known claimants, and, if the insurer has a duty to defend or a duty to pay defense costs on an ongoing basis, continuing to defend or pay the defense costs of its insured until:
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> (a) Settlement of the legal actions;
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> (b) Final adjudication of the actions; or
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> (c) Adjudication that the insurer does not have a duty to defend or to pay the defense costs of the actions.

Baldwin, 269 N.E.3d at 1206-07 (quoting § 26(2)).

But the court went on to note the limitations of the Restatement's interpleader immunity. Quoting Comment c., it highlighted that the safe-harbor provision "'is principally directed at simple liability-insurance-coverage situations'" "In other words, the more complex a liability insurance arrangement is, the more likely the safe harbor provided in subsection (2) may not be practicable." (quotations omitted).

The court then applied this standard, finding that Standard Fire had satisfied the requirements for immunity from the claims of bad faith and a breach of the duty of good faith and fair dealing.

Practitioners should also be aware of Reporter's Note (b). It may limit the application of Section 26(2)'s safe-harbor provision. Note (b) cites *McReynolds v. Am. Commerce Ins. Co.*, 235 P.3d 278, 284 (Ariz. Ct. App. 2010) as "a recent example of a court creating a 'safe harbor' for the insurer similar to that created by subsection (2)[.]" And in describing

McReynolds, the Restatement notes that the insurer "satisfied its duty to settle when it promptly *and in good faith* interpleaded its policy limits into court, naming all known claimants, and continued to provide a defense to its insured[.]" Section 26 *n.* (b) (emphasis added).)

This language in the Restatement likely imposes a good-faith requirement when an insurer files an interpleader, if it wants "safe-harbor" protections. And although *Baldwin* did not expressly address this, it cited to *McReynolds* favorably. Furthermore, it noted the long-standing rule that "Indiana law imposes a duty of good faith and fair dealing on insurers to discharge their contractual obligations towards a policyholder." *Baldwin*, 269 N.E.3d at 1210. Thus, if an insurer nefariously seeks interpleader, it will not likely obtain bad-faith protection.

While practitioners will need to consider any existing law in the governing jurisdiction, Section 26 and *Baldwin* may give additional support for whether the insurer acted properly when faced with multiple claimants and insufficient limits.

Additionally, questions remain about whether courts will apply the same law to other circumstances. For example, will the same rules apply to situations when there are multiple insureds and insufficient limits? Or, how will courts treat a first-party property loss where there are multiple insureds and insufficient limits?

Author

Gregory Michael Gotwald

Plews Shadley Racher & Braun LLP

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