Under What Circumstances May an Insured Enter Into a Consent Agreement?

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I. What is a Consent Agreement?

In most instances, the Agreement will contain:

1. a stipulated judgment against the insured establishing liability and identifying a specific amount of damages;

2. a covenant for the claimant not to execute the stipulated judgment against the insured (meaning the insured has no obligation for the judgment amount and the claimant may only enforce it against the insurance company); and

3. an assignment of the insured's rights under the policy to the claimant.

II. What are Consent Judgments Called?

These types of agreements largely spawned from the Nebraska Supreme Court's decision in *Metcalf v. Hartford Acc. & Indem. Co.*, 176 Neb. 468, 476, 126 N.W.2d 471, 476 (Neb. 1964) (citing *Fullerton v. U.S. Cas. Co.*, 184 Iowa 219, 167 N.W. 700, 705 (Iowa 1918); *Griggs v. Bertram*, 88 N.J. 347, 364, 443 A.2d 163, 171-72 (1982).

1. Consent Judgments go by many different names:

   a. Florida: *Coblentz* Agreements
      - *Coblentz v. Am. Sur. Co. of New York*, 416 F.2d 1059 (5th Cir. 1969) (applying Florida law).

   b. Arizona: *Damron* Agreement or *Morris* Agreement
      - *Damron v. Sledge*, 460 P.2d 997 (Ariz. 1969); *USAA v. Morris*, 741 P.2d 246 (Ariz. 1987).

   c. Missouri: "065 Agreements"
      - § 537.065, Mo. Stat.

   d. Minnesota & North Dakota: *Miller-Shugart* Agreements

- *Miller v. Shugart*, 316 N.W.2d 729 (Minn. 1982).

e. Colorado: *Basher* Agreements
   - *Northland Ins. Co. v. Bashor*, 177 Colo. 463, 494 P.2d 1292 (Colo. 1972).

f. Other states, like Washington and Texas, simply refer to these as "Covenant Judgments" or "Consent Judgments."
   - *e.g. Bird v. Best Plumbing Grp., LLC*, 766, 287 P.3d 551, 556 (Wash. 2012); *Transportation Ins. Co. v. Heiman*, 1999 WL 239917, at *4 (Tex. App.—Dallas Apr. 26, 1999, no pet.).

III. Under What Circumstances Can an Insured Enter Into a Consent Agreement?

Majority:

1. Consent Agreement is permitted when:

   a. The claim or insured is covered under the policy

and ...

   b. The insurer wrongfully refuses to defend.

Or...

   c. the policy is an indemnity only policy

IV. Insured Can Enter Into a Consent Agreement when a defense is being afforded under a Reservation of Rights

1. **Arizona:** *USAA v. Morris*, 154 Ariz. 113, 741 P.2d 246, 249 (Ariz. 1987).

> An insurer with a coverage defense must defend its insured under a properly communicated reservation of rights or it will lose its right to later litigate coverage. . . . [I]f the company was defending Waltz unconditionally, the cooperation clause of the policy would have prohibited Waltz from settling the claim without the insurer's consent. This is so because the purpose of a cooperation clause is to prevent insureds from compromising a claim for which the insurer unconditionally has assumed liability under the policy, thus obviating, at least to the extent of the policy limit bargained for, the insured's exposure to personal liability.
> 249-50

The question in this case is whether an insurer may assert the policy's cooperation clause to prevent insureds being defended under a reservation of rights from protecting themselves by settling.
251

A majority of courts resolve this type of conflict by permitting an insured to reject a defense offered under a reservation of rights. The insured thus forces the insurer to elect either to defend unconditionally or to refuse to defend at its peril.
251

An insurer that performs the duty to defend but reserves the right to deny the duty to pay should not be allowed to control the conditions of payment. The insurer's insertion of a policy defense by way of reservation or nonwaiver agreement narrows the reach of the cooperation clause and permits the insured to take reasonable measures to protect himself against the danger of personal liability. Accordingly, we hold that the cooperation clause prohibition against settling without the insurer's consent forbids an insured from settling only claims for which the insurer unconditionally assumes liability under the policy. Thus, an insured being defended under a reservation of rights may enter into a *Damron* agreement without breaching the cooperation clause. Such agreements must be made fairly, with notice to the insurer, and without fraud or collusion on the insurer. The insurer's reservation of the privilege to deny the duty to pay relinquishes to the insured control of the litigation, almost as if the insured had objected to being defended under a reservation.
252

2. **Maine:** *Patrons Oxford Insurance Co. v. Harris*, 905 A.2d 819 (Me. 2006).

[A]n insurer does not breach the insurance agreement by electing to defend its insured under a reservation of rights. Furthermore, we agree with those courts that have held that "an insurer who reserves the right to deny coverage cannot control the defense of a lawsuit brought against its insured by an injured party." This position strikes a fair balance between the insurer and the insured. If the insurer could continue to control the insured's defense despite reserving its rights to later deny coverage, it could assert a liability defense and insist on fully litigating the insured's case, thus exposing the insured to personal liability if there is a verdict favorable to the claimant. If the verdict is favorable to the claimant, the insurer still has another opportunity to avoid liability by doing exactly as Patrons did here, litigating coverage in a declaratory judgment action. Thus, we agree with the Arizona Supreme Court that the insured "risks financial catastrophe if he is held liable, while the insurer may save itself by litigating both issues-the insured's liability and the coverage defense-and winning either."
825-26

By allowing the insured to control his own case when the insurer issues a reservation of rights, the insured can protect himself "from the sharp thrust of personal liability," *id*. (quotation marks omitted), and the insurer still has a meaningful opportunity to protect its own interests in a declaratory judgment action where it may assert, among other things, a coverage defense. Because Patrons chose to defend Harris under a reservation of rights, it gave up the ability to control Harris's defense. Therefore, Patrons cannot now assert that it was denied the opportunity in the personal injury action to litigate Harris's liability to Luce because it was an opportunity Patrons possessed and relinquished when it proceeded under the reservation of rights
826

In conclusion, an insured being defended under a reservation of rights is entitled to enter into a reasonable, noncollusive, nonfraudulent settlement with a claimant, after notice to, but without the consent of, the insurer.
828

3. **Washington:** *Martin v. Johnson*, 141 Wash. App. 611, 170 P.3d 1198 (Wash. 2007).

If an insurance company refuses in bad faith to settle a claim, the insured may independently negotiate a settlement; the insurance company is then liable for the settlement to the extent that it is reasonable and paid in good faith. . . . [A]t a time when insurance coverage is in doubt, it is in an insured's best interest to accept a settlement offer that effectively relieves him or her of personal liability. An insurer that is disputing coverage cannot compel an insured to forego a settlement that is in his or her best interests.
1202

Here, Metropolitan had informed the Estate that it was denying coverage for the Martins' claims and was providing a defense under a reservation of rights. Facing potential liability for the clean-up costs and general damages, it was in the Estate's best interest to accept a settlement offer that relieved it of liability; Metropolitan cannot compel the Estate to forego this opportunity.
1202

4. **Wyoming:** *Insurance Co. of North America v. Spangler*, 881 F. Supp. 539 (D. Wyo. 1995).

[T]his court concludes that were it faced with this question, the Wyoming Supreme Court would adopt the rationale of those cases holding that an insurer who reserves the right to deny coverage loses the right to control the litigation.
544

[T]his court concludes that where the insurer was defending under a reservation of rights and had filed a declaratory judgment action contesting coverage, the insured's assignee is not barred from recovery from the insurer for a stipulated liability to which the insurer did not consent and the insured is not personally liable.
544

The Supreme Court of Arizona was faced with this issue in *Morris, supra*. That court surveyed the case law holding generally that an insurer disputing coverage could not invoke "its duty to cooperate clause to prevent the insured from taking reasonable measures to protect himself from the hazards of his position." . . . This court believes that were the issue before the Wyoming Supreme Court, it would follow the *Morris* and *Miller* line of cases.
545

5. *BUT SEE Gainsco Ins. v. Amoco Product*, 53 P.3d 1051 (Wyo. 2002)

   May require more than just serving a reservation of rights letter before an insured may enter into a Consent Agreement. (More to Come Later in Outline).

6. *But see* **Texas:** *Motiva Enterprises, LLC v. St. Paul Fire and Marine Ins. Co.*, 445 F.3d 381 (5th Cir. 2006) (applying Texas law).

   Motiva argues that when National Union's tender of a defense was subject to its reservation of rights to later deny coverage, Motiva was entitled to settle the [underlying] claim without consulting National Union.
   384

   We conclude . . . an insurer which tenders a defense with a reservation of rights is entitled to enforce a consent-to settle clause . . . . The district court therefore did not err in holding that Motiva breached its insurance policy by settling without National Union's consent, even though National Union reserved its right to contest coverage and therefore did not tender to Motiva an unqualified defense.
   385

   Compare with:

   a. *Evanston Ins. Co. v. Atofina Petrochemicals, Inc.* 256 S.W.3d 660, 671-73 (Tex. 2008)

      In this case, the plaintiffs sued Atofina, Atofina requested coverage from Evanston, and Evanston wrongfully denied coverage . . . . Atofina then settled with the underlying plaintiffs and litigated the remaining coverage issues against Evanston. Evanston argued that Atofina failed to meet its burden of showing that the settlement amount was reasonable.

671

The Court discussed *Employers Casualty Co. v. Block*, which held that if an insurer wrongfully denies coverage and its insured then enters into an agreed judgment, the insurer is barred from challenging the reasonableness of the settlement amount. 744 S.W.2d 940, 943 (Tex. 1988). Noting that although the facts in *Atofina* differed from those in *Block*, the Court held that none of those differences justified departing from the central holding of *Block*. Evanston's wrongful denial of coverage barred it from challenging the reasonableness of Atofina's settlement.

b. Lennar Corp. v. Markel American Ins. Co., 413 S.W.3d 750, 754-57 (Tex. 2013)

Though Markel did not consent to Lennar's settlements with homeowners, it concedes . . . that [the consent-to-settle] provision does not excuse its liability under the policy unless it was prejudiced by the settlements.
754

An insurer establishes prejudice from a settlement to which it did not agree by showing that the insured's unilateral settlement was a material breach of the policy—that is, that it significantly impaired the insurer's position. . . . Markel failed to prove that it was prejudiced in any way by Lennar's settlements.
756

V. When Can an Insurer Retain Right to Determine if Insured Can Enter Into a Consent Agreement after a ROR?

1. When an insurer tenders a defense subject to a reservation of rights, the **insurer** retains its full authority under a consent to settlement provision.

    a. *Motiva Enterprises, LLC v. St. Paul Fire & Marine Ins. Co.*, 445 F.3d 381 (5th Cir. 2006) (applying Texas law).

    b. *Danrik Const. Inc. v. Am. Cas. Co. of Reading Pennsylvania*, 314 F. App'x 720 (5th Cir. 2009) (applying Louisiana law) (unpublished).

    c. *First Bank of Turley v. Fid. & Deposit Ins. Co. of Maryland*, 1996 OK 105, 928 P.2d 298 (Okla. 1996).

    d. *Vincent Soybean & Grain Co. v. Lloyd's Underwriters of London*, 246 F.3d 1129 (8th Cir. 2001) (applying Arkansas law).

    e. *L & S Roofing Supply Co. v. St. Paul Fire & Marine Ins. Co.*, 521 So. 2d 1298, 1304 (Ala. 1987) ("The mere fact that the insurer chooses to defend

its insured under a reservation of rights does not *ipso facto* constitute such a conflict of interest that the insured is entitled at the outset to engage defense counsel of its choice at the expense of the insurer.").

VI. Can an Insured Enter Into a Consent Agreement after a ROR AND the Filing of a Dec Action?

1. YES!

    a. **Minnesota:** *Miller v. Shugart*, 316 N.W.2d 729 (Minn. 1982).

While Milbank Mutual Insurance Company was litigating whether it had coverage for both the insured car owner and the driver, the insured owner and the driver settled with the injured plaintiff and confessed judgment for a stipulated sum.
731

Milbank argues the indemnity agreement of its policy has been voided because the insureds breached their duty under the policy to cooperate. We disagree.

Under the auto liability policy, Milbank has a duty to defend and indemnify its insureds, and the insureds have a reciprocal duty to cooperate with their insurer in the management of the claim. Plaintiff contends that defendants were relieved from their duty to cooperate because Milbank breached its duty to defend. We would put the issue differently. Milbank has never abandoned its insureds nor, by seeking a determination of its coverage, has it repudiated its policy obligations.[2] Milbank had a right to determine if its policy afforded coverage for the accident claim, and here Milbank did exactly as we suggested.
733

On the other hand, while Milbank did not abandon its insureds neither did it accept responsibility for the insureds' liability exposure. What we have, then, is a question of how should the respective rights and duties of the parties to an insurance contract be enforced during the time period that application of the insurance contract itself is being questioned. . . . Did the insureds breach their duty to cooperate by not waiting to settle until after the policy coverage had been decided? In our view, the insureds did not have to wait and, therefore, did not breach their duty to cooperate.

While the defendant insureds have a duty to cooperate with the insurer, they also have a right to protect themselves against plaintiff's claim. . . . If, as here, the insureds are offered a settlement that effectively relieves them of any personal liability, at a time when their insurance coverage is in doubt, surely it cannot be said that it is not in their best interest to accept the offer. Nor, do we think, can

the insurer who is disputing coverage compel the insureds to forego a settlement which is in their best interests.

On the facts of this case we hold, therefore, that the insureds did not breach their duty to cooperate with the insurer, which was then contesting coverage, by settling directly with the plaintiff.
733-34

b. **Texas:** *Motiva Enterprises, LLC v. St. Paul Fire and Marine Ins. Co.*, 445 F.3d 381 (5th Cir. 2006) (applying Texas law).

Motiva notified its insurer, National Union, of two lawsuits that had been filed against it. National Union initially disclaimed coverage, and Motiva filed suit seeking a declaratory judgment regarding its coverage. National Union later tendered its offer to defend the lawsuits subject to a reservation of rights. Motiva settled one of the underlying lawsuits without National Union's consent, arguing that because National Union tendered its defense subject to a reservation of rights, Motiva was entitled to settle the lawsuit without consulting National Union.
383-84

As discussed in Section IV above, the Court in *Motiva* held that the lower court did not err in holding that Motiva breached its insurance policy by settling without National Union's consent, even though National Union reserved its right to contest coverage and therefore did not tender to Motiva an unqualified defense. Neither the parties nor the Court addressed the impact, if any, of the pending declaratory judgment action between Motiva and National Union on Motiva's ability settle the underlying lawsuits.

VII. Can an Insured Enter Into a Consent Agreement After a ROR and a Demand Within Policy Limits?

1. YES!

a. **Iowa:** *Kelly v. Iowa Mutual*, 620 N.W. 2d 637 (Iowa 2000).

The estate appears to argue that Iowa Mutual's defense of McCarthy pursuant to a reservation of rights violated the contract. An insurer does not breach the policy simply because the defense it provides is under a reservation of rights. Nevertheless, some courts have held that an insured may settle without the insurer's consent where the insurer provides a defense to the insured but reserves its right to deny liability for any ultimate judgment. We think the reasoning of these cases is flawed because they permit an insured to breach his duties under the policy without losing coverage, even though there has not been a breach of the contract by the insurance company. Therefore, we decline to follow them.

642

We have not had an occasion to consider the insurer's duty to settle under circumstances such as those before us, where the insurer has reserved its right to deny coverage for any judgment entered against the insured. Certainly under these circumstances, where the insured may ultimately be responsible for a judgment if coverage is found not to exist, it is extremely important that the insurance company, who is controlling the defense, fulfill its contractual obligation to settle where appropriate. One commentator has observed that an insurer may breach the contract by failing to settle an appropriate case, even though its failure to settle is attributable solely to the company's negligence. This commentator suggests that, "recognizing that the company has, despite the absence of bad faith, breached the insurance contract, the company should be precluded from enforcing the provisions in the policy inuring to its benefit, such as the one prohibiting unauthorized settlements by the insured."

We agree. An insurance company cannot use its erroneous belief that it has no coverage to justify a refusal to settle. At the point in time that the insurer is faced with a fair and reasonable settlement demand that a reasonable and prudent insurer would pay, the insurer must either abandon its coverage defense and pay the demand or lose its right to control the conditions of settlement.[6] If the insurer prefers to debate coverage and, accordingly, refuses to pay the settlement demand, the insured is free to either pay the settlement demand or stipulate to the entry of judgment in the amount of the demand. The insurer, if found to have coverage, will be liable for the insured's settlement if the settlement is found to be fair and reasonable.
644-45

b. **Texas:** *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116 (5th Cir. 1983)

If the insurer properly reserved its rights and the insured elected to pursue his own defense, the insurer is bound to pay damages which resulted from covered conduct and which were reasonable and prudent, up to the policy limits.
121

Rhodes has been called into doubt by *Motiva*, discussed in Sections IV and VI. The Court in *Motiva*, however, seemed to take issue with the insured's argument that *Rhodes* broadly stands for the proposition that an insurer who defends an insured subject to reservation of rights is bound by the insured's settlement.

c. **Wyoming:** *Gainsco Ins. v. Amoco Product*, 53 P.3d 1051 (Wyo. 2002).

Amoco refers us first to *Insurance Co. of North America v. Spangler,* 881 F.Supp. 539 (D.Wyo.1995). In *Spangler,* the insurer defended a wrongful death action under a reservation of rights as to coverage, and also brought a separate declaratory judgment action to test coverage. The claimant and the insured then

settled the wrongful death action for an amount within policy limits, and the claimant covenanted not to execute against the insured. The insurer then amended its complaint in the declaratory judgment action to raise the issue of the enforceability against it of the stipulated judgment. *Id.* at 541–42. The specific issue addressed in *Spangler* is similar to the issue now before this Court:

> Is the assignee of the insured barred from recovery from the insurer for a stipulated liability to which the insurer did not consent and the insured is not personally liable?

Id. at 543. Because this question had not previously been answered by this Court, the federal court made its "best estimate" as to how this Court would rule on the question. *Id.* at 544. In answering the question in the negative, the federal court emphasized two facts: (1) an insurer defending under a reservation of rights "loses the right to control the litigation;" and (2) a covenant not to execute is not a complete release of all liability. *Id.*
1060

We agree with the rationale of *Spangler* and those cases that find that the inclusion of a covenant not to execute in the settlement agreement between an insured and a claimant, under the circumstances of the case now before us, does not act to negate the fact that a judgment has been entered against the insured and, therefore, does not bar the claimant, as assignee of the insured, from pursuing a claim against the insurer for third-party bad faith. The existence of the judgment, with or without a covenant not to execute, is a detriment to the insured sufficient to support an assignable tort claim. Public policy favors this result in that it allows an insured to reach a reasonable settlement of a case being defended under a reservation of rights and it discourages an insurer from rejecting a reasonable settlement offer. The insurer is adequately protected by the requirement that such settlements be reasonable and by its ability to raise the issues of fraud and collusion.
1061

Because Gainsco defended Andrews under a reservation of rights, Andrews obtained separate counsel. After considerable negotiation, Amoco and Andrews reached a settlement. . . . Gainsco declined to participate in the settlement.
1067

Gainsco concedes that an insured does not violate the cooperation clause of an insurance policy by settling a claim being defended under a reservation of rights, so long as such settlement is preceded by adequate notice to the insurer. 1067

VIII. Can an Insured Enter Into a Consent Agreement After a ROR and the Rejection of the Defense by the Insured?

1. YES if the Insured actually rejects the defense—silence is acquiescence to the qualified defense.

a. **Florida:** *Taylor v. Safeco Insurance Co*., 361 So. 2d 743 (Fla. 1st DCA 1978).

We conceive that the insurer's potential obligation to pay also subsists when, as a result of the parties' failure to agree upon a conditional defense, the putative insured chooses to control the litigation and to effect a reasonable settlement.
746

Aguero v. First American, 927 So. 2d 894 (Fla. 3d DCA 2005).

"[W]hen an insurer offers to defend under a reservation of rights, Florida law provides that the insured may, at its own election, reject the defense and retain its own attorneys without jeopardizing his right to seek indemnification from the insurer for liability." However, the insured must actually reject that defense.

In the instant case, Ryder's May 20, 1999 letter could be construed as a rejection of First American's defense under a reservation of rights. If it is determined that Ryder's letter constituted a rejection of First American's defense under a reservation of rights, Ryder would have been entitled to retain its own attorney to defend against Iglesias' claim without jeopardizing its right to seek indemnification from First American.
898

However: an insured cannot reject a defense that has been previously accepted and then enter into a consent judgment, unless there is a material change in the conditional defense. *Mid-Continent v. Am. Pride Bldg. Co.,* 601 F.3d 1143 (11th Cir. 2010); *Western Heritage Ins. Co. v. Montana*, 30 F. Supp. 3d 1366 (M.D. Fla. 2014).

b. **Pennsylvania:** *Babcock & Wilcox Co. v. Am. Nuclear Insurers*, 2013 PA Super 174, 76 A.3d 1, 18 (2013) *appeal granted in part,* 84 A.3d 699 (Pa. 2014).

We find that the *Taylor* approach, in providing an insured the option to decline a defense tendered subject to a reservation of rights, but protecting an insurer's right to control the defense when it is accepted by the insured, best balances the interests of insurer and insured, and better honors the binding nature of the insurance contract.
20

We reject the *Morris* approach not only because it contravenes fundamental precepts of contract law, but also because we believe that it is founded on an unrealistic diminution of the risks facing an insurer defending subject to a reservation. . . . We also note that application of the *Morris* standard would appear to reduce an insurer's incentive to undertake the defense at all, if it

anticipates that a viable coverage defense will be available after trial on the underlying suit. If the insurer is to lose control of the terms of settlement simply for reserving its rights until continuing discovery and fact-finding illuminate whether a viable coverage defense exists, subject only to a jury's determination as to what sort of settlement is "fair and reasonable," the insurer reasonably might choose to decline to defend entirely. If it does so, and coverage is found, it is exposed at most for the reimbursement of the insured's costs of defense[13] and either the verdict or that portion of the amount of settlement that is deemed fair and reasonable. While the insurer may expose itself to an excess verdict by declining to defend, the same is true in the event that it defends subject to a reservation and exercises its right to control settlement in a manner indicating bad faith.
21-22

For the reasons set forth above, we hold that, when an insurer tenders a defense subject to a reservation, the insured may choose either of two options. It may accept the defense, in which event it remains unqualifiedly bound to the terms of the consent to settlement provision of the underlying policy. Should the insured choose this option, the insurer retains full control of the litigation, consistently with the policy's terms. In that event, the insured's sole protection against any injuries arising from the insurer's conduct of the defense lies in the bad faith standard articulated in *Cowden*.

Alternatively, the insured may decline the insurer's tender of a qualified defense and furnish its own defense, either *pro se* or through independent counsel retained at the insured's expense. In this event, the insured retains full control of its defense, including the option of settling the underlying claim under terms it believes best. Should the insured select this path, and should coverage be found, the insured may recover from the insurer the insured's defense costs and the costs of settlement, to the extent that these costs are deemed fair, reasonable, and non-collusive.
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[W]e believe *Taylor* provides the standard most consistent with Pennsylvania law
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(NOTE: On January 24, 2014, the Supreme Court of Pennsylvania accepted appeal as to one issue: "Does a policy holder forfeit its right to insurance coverage by settling an underlying and covered claim without its insurer's consent, where the insurer is defending subject to a reservation of rights to disclaim coverage, the settlement is at arm's length, is fair and is reasonable, and the insurer has failed to offer any amounts in settlement?" No opinion has been issued).

c. **Missouri:** *Central Bank v. St. Paul Fire & Marine Ins.*, 929 F.2d 431 (8th Cir. 1991) (applying Missouri law).

Under Missouri law, an insurer may undertake the defense of its insured and reserve its right to later disclaim coverage, provided it gives the insured notice of a reservation of rights. . . . "Upon such notification the insured may either accept the reservation of rights and allow the company to defend or it may reject the reservation of rights and take over the defense itself." This is what happened in the instant case.

Although it was under no obligation to do so, Central Bank agreed to St. Paul's assumption of the defense of the Boyd suit under a reservation of rights, and Central Bank never attempted to disclaim the reservation of those rights.
433

Butters v. City of Independence, 513 S.W.2d 418 (Mo. 1974).

[G]arnishee did not offer a full, non-reservation of rights defense to the City, so that the City, following garnishee's denials of coverage, had no further obligation to cooperate with Royal Indemnity Company which had breached the policy and the City was, therefore, free to defend itself as it saw fit, including entering into the statutory covenant with plaintiffs. Further refusal of the City to agree to the tendered reservation defense was not a failure to co-operate.
423

d. **Massachusetts:** *Three Sons, Inc. v. Phoenix Ins. Co.*, 357 Mass. 271, 257 N.E.2d 774 (Mass. 1970).

The question, therefore, is whether under the insured's duty to cooperate it may refuse to allow the insurer to defend and control a suit under a reservation of rights. The defendant argues that the insured has no such right. We disagree.
776

A reservation of rights in such circumstances notifies the insured that the insurer's defense is subject to the later right to disclaim liability. The insured thus can take the necessary steps to protect his rights, and has no basis for claiming an estoppel. A reservation of rights and insistence on retaining control of the defence is another matter. As we stated in the Salonen case, 'We are not to be understood as holding that an insurer may reserve its rights to disclaim liability in a case and at the same time insist on retaining control of its defense.'

The judge, therefore, rightly ruled that the defendant had a duty to defend the plaintiff in the actions at law without a reservation of rights or claim of nonwaiver, so long as it insisted on retaining control of the defense.
777

e. **Kentucky:** *Medical Protective Co. of Fort Wayne, Indiana v. Davis*, 581 S.W.2d 25 (Ky. Ct. App. 1979) (applying Kentucky law).

> [W]hen the insurer reserves a right to assert its nonliability for payment there is little or no reason to require the insured to surrender defense of the claim to a company which asserts that it has no obligation to satisfy the claim. Under such conditions the insured has the right to refuse the proffered defense and conduct his own defense.
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>
> That an insured may seek to defend himself without counsel after refusing to accept a defense offered under a reservation of rights is one of the risks an insurer must take when it elects to offer a defense under a reservation of rights. If it is correct in its position that the policy does not afford coverage or has been breached in some way, then it prevails regardless of whether the insured accepts the defense but it offers such a defense at its peril, because if the insured refuses to accept it and elects to defend himself, the company is found by the result, in the absence of fraud or collusion, unless it can establish that the policy did not afford coverage or was breached by the insured.
>
> In this case the insured refused to accept the qualified defense, he elected to defend himself, and the insurer did not establish noncoverage or that the insured had breached some duty it owed to the company. The company therefore became obligated to the extent of the policy limits of its liability and appellees were entitled to a directed verdict.
> 26-27

f. **Idaho:** *Boise Motor Car Co. v. St. Paul Mercury Indem. Co., 62 Idaho 438, 112 P.2d 1011 (Idaho 1941)*

> Respondent elected to go forward with defense of the Heard suit after having notice appellant would not consent to reservation of respondent's right to withdraw, and its continued assertion of such right of withdrawal thereafter was a breach of its insurance contract and created a hazard, to protect itself from which appellant was justified in employing attorneys. 1016

g. **Alaska:** *Cont'l Ins. Co. v. Bayless & Roberts, Inc.*, 608 P.2d 281 (Alaska 1980)

> This appeal presents issues arising from an insurance company's refusal to unconditionally defend its insured and the insured's subsequent decision to settle the case. . . . Continental informed B & R that it would continue to defend only if B & R would agree to a reservation of Continental's right to later deny liability on the ground of the alleged breach. B & R refused to accept such a conditioned defense and, therefore, Continental withdrew from the case.
> 283

While Continental was willing to proceed with B & R's defense, it insisted on reserving its right to later challenge B & R's right to claim the protection of the policy, by asserting the insured's alleged breach as a defense in a later action to enforce the policy.
288

In reaching our decision, therefore, we consider only the policy defense situation. We leave open the question whether the insurer has the same obligations and liabilities in the coverage defense situation.
289

The Boise approach requires the insurer to make a clear choice between defending and withdrawing, and, in the policy defense situation, we believe that approach is necessary to protect the interests of the insured. Thus, we decline to adopt in full the position of either party. It may be that, where the insurance company wishes to contest coverage, the insured is obligated to accept a defense under a reservation of rights. We hold, however, that where, as here, the insurance company challenges the insured's right to enforce the policy on the ground the insured has breached a condition thereof, the insured has a right to demand an unconditional defense. Thus, the insurance company must either affirm the policy and defend unconditionally or repudiate the policy and withdraw from the defense. The insurer may not reserve its right to repudiate the policy, unless the insured consents to a reservation of that right.

In the case at bar, therefore, B & R was fully within its rights and did not breach the policy when it insisted that Continental either defend unconditionally or withdraw from the defense.
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h. **Texas:** *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116 (5th Cir. 1983)

When a reservation of rights is made . . . the insured may properly refuse the tender of defense and pursue his own defense. The insurer remains liable for attorneys' fees incurred by the insured and may not insist on conducting the defense. Refusal of the tender of defense is particularly appropriate where . . . the insurer's interests conflict with those of the insured.
120-121

If the insurer properly reserved its rights and the insured elected to pursue his own defense, the insurer is bound to pay damages which resulted from covered conduct and which were reasonable and prudent, up to the policy limits.
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IX. Can an Insured Enter Into a Consent Agreement After a ROR and After Giving the Ins. Co. the Opportunity to Agree to the Consent Judgment?

1. Yes: Insured is prohibited from entering into a Consent Agreement when the insurer is providing the insured with a defense (which may even be conditional) UNLESS the insurer given chance to agree to the judgment.

   a. *Wright v. Fireman's Fund Ins. Companies*, 11 Cal. App. 4th 998, 14 Cal. Rptr. 2d 588 (Cal. App. 1992).

   b. *Romstadt v. Allstate Ins. Co.*, 844 F. Supp. 361 (N.D. Ohio 1994) *aff'd,* 59 F.3d 608 (6th Cir. 1995) (applying Ohio law).

   c. *Motiva Enterprises, LLC v. St. Paul Fire and Marine Ins. Co.*, 445 F.3d 381 (5th Cir. 2006)

   An insurer's right to participate in the settlement process is an essential prerequisite to its obligation to pay a settlement.

X. Can an Insured Enter Into a Consent Agreement Obligating the Excess Coverage While Being Defended by an Underlying Policy?

1. NO: Where an insured is covered by both a primary policy and a true excess or umbrella policy, an excess carrier's duty to defend is generally secondary to the primary insurer's duty to defend.

   a. Arizona: *Regal Homes, Inc. v. CNA Ins.*, 217 Ariz. 159, 167-68, 171 P.3d 610, 618-19 (Arizona Ct. App. 2007) ("Until a primary insurer offers its policy limit, the excess insurer does not have a duty to evaluate a settlement offer, to participate in the defense, or to act at all.")

   b. Florida: *U.S. Fire Ins. Co. v. Mikes*, 576 F. Supp. 2d 1303, 1325 (M.D. Fla. 2007) *aff'd sub nom. U.S. Fire Ins. Co. v. Freedom Vill. of Sun City Ctr., Ltd.*, 279 Fed. Appx. 879 (11th Cir. 2008) ("Once an insurer assumes the defense of the insured pursuant to its duty to defend, other insurers, including an excess insurer, that provide coverage and have a duty to defend are ordinarily no longer obligated to provide a defense to the insured.").

   c. Washington: *Rees v. Viking Ins. Co.*, 77 Wash. App. 716, 719, 892 P.2d 1128, 1130 (Wash App. Ct. 1995) ("An excess carrier's obligation to pay and defend begins when, and only when, the limits of the primary insurance policy are exhausted.").

d. California: *Travelers Cas. & Sur. Co. v. Am. Int'l Surplus Lines Ins. Co.*, 465 F. Supp. 2d 1005, 1028 (S.D. Cal. 2006) ("Unless the excess policy provides otherwise (and Travelers' does not), the primary insurer owes the *exclusive* duty to defend the insured against third party claims until the primary coverage is exhausted or otherwise not on the risk.").

e. Kansas: *Associated Wholesale Grocers, Inc. v. Americold Corp.*, 261 Kan. 806, 829, 934 P.2d 65, 81 (Kan. 1997) ("Simply stated, the primary policy provides 'first dollar' liability coverage up to the limits of the policy…Before [primary insurer] tendered its policy limits, [excess carrier] was not obligated to defend [the insured] or take charge of settlement efforts on behalf of [the insured]. [Primary insurer] had assumed [the insured]'s defense.")

f. Louisiana: *XL Specialty Ins. Co. v. Bollinger Shipyards, Inc.*, 954 F. Supp. 2d 440, 445 (E.D. La. 2013) ("The terms of the policies indicate that as an excess provider, Continental is not liable to pay claims until the primary insurance has been exhausted and does not owe a duty to defend.").

g. Texas: *Keck v. National Union Fire Ins. Co.*, 20 S.W.3d 692, 700 (Tex. 2000) ("An excess insurer owes its insured a duty to accept reasonable settlements, but that duty is also not typically invoked until the primary insurer has tendered its policy limits." National Union (the excess carrier) had no duty to evaluate a settlement demand until after the primary carrier's tender of its policy limits.)

XI. However, if The Primary Coverage is ONLY an Indemnity Policy (No Duty To Defend), Then:

1. Yes: *Perera v. U.S. Fid. & Guar. Co.*, 35 So. 3d 893 (Fla. 2010). Rationale: excess carrier has no duty to defend under an indemnity only policy.

XII. What Happens After the Consent Agreement is Entered and the Bad Faith Case is Filed? What Defenses Does a Carrier Have?

1. Consent Judgment may generally be challenged for unreasonableness or bad faith.

2. Purpose: while an Insured may take certain steps to protect itself by entering the Judgment if its insurer wrongfully denies coverage and a defense, the insured does not have carte blanche over the insurer's checkbook.

a. In some jurisdictions, such as Texas and Montana, the court is statutorily (no statutory requirement under Texas law) required to hold a "reasonableness hearing" for a Consent Judgment. Better practice in all jurisdictions (e.g. California)

1. *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 696 (Tex. 1996)

2. *Tidyman's Mgmt. Servs. Inc. v. Davis*, 2014 MT 205, 376 Mont. 80, 330 P.3d 1139 (Mont. 2014).
    a.

3. Consent Judgment must be reasonable and not entered into in bad faith/not collusive.

4. What Defenses Does a Carrier Have?

a. Reasonableness
b. Bad faith,
c. Fraud, or
d. Collusion - absence of an arms-length transaction

1. *Associated Wholesale Grocers, Inc. v. Americold Corp.*, 261 Kan. 806, 934 P.2d 65 (Kan. 1997)

2. *Detroit Edison Co. v. Michigan Mut. Ins. Co.*, 102 Mich. App. 136, 301 N.W.2d 832 (Mich. App. 1981)

3. *Transportation Ins. Co. v. Heiman*, 1999 WL 239917, at *7-8 (Tex. App.—Dallas Apr. 26, 1999, no pet.)

e. No bad faith - Without bad faith, a consent judgment can only be enforced up to the policy limit.

1. **Florida**: consent judgment can only be enforced up to the policy limit, unless there is an additional showing of bad faith. *Perera v. USF&G*, 35 So. 3d 893 (Fla. 2010); *Mobley v. Capitol Specialty Ins.*, 2013 U.S. Dist. LEXIS 101329 (S.D. Fla. 2013).
2. **Minnesota**: *Miller v. Shugart*, 316 N.W.2d 729 (Minn. 1982)
3. **Texas**: *Wilcox v. American Home Assur. Co.*, 900 F. Supp. 850 (S.D. Tex. 1995); *Rhodes v. Chicago Ins. Co.*, 719 F.2d 116 (5th Cir. 1983).

XIII. How Can an Insurer Ultimately Prove That the Consent Agreement was Unreasonable or Collusive/Made in Bad Faith

1. Both *objective* and *subjective* factors are considered

2. Prudent Person standard - prudent person in the position of the insured would have settled for on the merits of the claimant's claim.

3. Has insured made an effort to "minimize his/her liability".

   a. *Fireman's Fund Ins. Co. v. Sec. Ins. Co. of Hartford,* 72 *N.J.* 63, 71, 367 *A.*2d 864 (N.J. 1976)

   b. *Taylor v. Safeco Ins. Co.*, 361 So. 2d 743 (Fla. 1st DCA 1978)

   c. *Yorkshire Ins. Co., Ltd. v. Seger*, 407 S.W.3d 435, 441 (Tex. App.—Amarillo 2013, pet. denied).

4. Can comparative negligence of injured party be considered?

   a. Alton M. Johnson Co. v. M.A.I.Co., 463 N.W.2d 277 (Minn. 1990)

   b. Mid–Continent Cas. Co. v. Am. Pride Bldg. Co., LLC, 534 F. App'x 926, 927-28 (11th Cir. 2013)

5. If cannot retry underlying case, why can jury consider comparative negligence?

   a. Factors courts consider when determining whether a Consent Judgment is reasonable, which envelopes bad faith, fraud, and collusion:

      1. The releasing person's damages;
      2. The merits of the releasing person's liability theory;
      3. The merits of the released person's defense theory;
      4. The released person's relative fault;
      5. The risks and expenses of continued litigation;
      6. The released person's ability to pay;
      7. Any evidence of bad faith, collusion, or fraud;
      8. The extent of the releasing person's investigation and preparation of the case; and,
      9. The interests of the parties not being released.

      Besel v. Viking Ins. Co. of Wisconsin, 49 P.3d 887, 891 (Wash. 2002).

   b. Reasonableness of settlement agreement determined by *degree of probability of the insured's success* and the size of the possible recovery. Including:

      1. The extent of the defendant's liability,
      2. The reasonableness of the damages in comparison with compensatory awards in other cases, (expert testimony)

[P]roof of reasonableness is ordinarily established through use of expert witnesses to testify about such matters as the extent of the defendant's liability, the reasonableness of the damages amount in comparison with compensatory awards in other cases, and the expense which would have been required for the settling defendants to defend the lawsuit.

Chomat v. Northern Insurance Co. of New York, 919 So. 2d 535, 538 (Fla. 3d DCA 2006)

3. The expense which has been required for the settling defendants to settle the suit.

   Bond Safeguard Ins. Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa., No. 6:13-CV-561-ORL, 2014 WL 5325728 (M.D. Fla. Oct. 20, 2014).

   Willcox v. American Home Assurance Co., 900 F. Supp. 850, 855-56 (S.D. Tex. 1995)

6. CANNOT assert defenses which could have been asserted in the underlying tort action.

   a. *Fireman's Fund Ins. Co. v. Imbesi*, 361 N.J. Super. 539, 826 A.2d 735 (N.J. App. Div. 2003).

   b. *Wright v. Hartford Underwriters Ins. Co.*, 823 So. 2d 241 (Fla. 4th DCA 2002).

7. However, facts from underlying case can be presented to the jury as evidence that the Consent Agreement was for an unreasonable amount or was tainted by bad faith, fraud, collusion, or an absence of any effort to minimize liability.

   a. *Bond Safeguard Ins. Co. v. Nat'l Union Fire Ins. Co. of Pittsburgh, Pa.*, No. 6:13-CV-561-ORL, 2014 WL 5325728 (M.D. Fla. Oct. 20, 2014).

      What Coblentz does not do is authorize the insured to indiscriminately load the carrier's wagon with bricks of damage that no reasonable person would expect as consequences of the underlying claim.

   b. *Coastal Refining & Marketing, Inc. v. U.S. Fidelity and Guaranty Co.*, 218 S.W.3d 279, 295-96 (Tex. App.—Houston [14th Dist.] 2007, pet. denied); *Enserch Corp. v. Shand Morahan & Co., Inc.*, 952 F.2d 1485 (5th Cir. 1992).

8. What happens if the consent judgment is deemed unreasonable in amount?

Arizona: If the claimant cannot show that the entire amount of the consent judgment is reasonable, he can recover only the portion proven to be reasonable. If the claimant is unable to prove the reasonableness of any portion of the judgment, the consent judgment is unenforceable. *United Servs. Auto Ass'n v. Morris*, 154 Ariz. 113, 741 P.2d 246 (Ariz. 1987)

Florida: If the consent judgment is determined to be unreasonable in amount, it is unenforceable. The court/jury cannot pick a reasonable number. *Florida Mid-Continent v. American Pride*, 534 Fed. Appx. 926 (11th Cir. 2013)

Minnesota: If the consent judgment is deemed unreasonable, it is unenforceable and the parties are returned to the status quo (i.e., the liability trial is reinstated). *Alton M. Johnson Co. v. M.A.I. Co.*, 463 N.W.2d 277 (Minn. 1990); *Corn Plus Cooperative v. Continental Casualty*, 516 F. 3d 674 (8th Cir. 2009).

Texas: If the court concludes the consent judgment is excessive, the court may enter a remittitur to reduce the damages to an appropriate amount. *United States Aviation Underwriters, Inc. v. Olympia Wings, Inc.*, 896 F.2d 949, 955 (5th Cir. 1990).