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Court backs insurer in dispute over settlement

Commentary by **Laura Besvinick**

The situation is not uncommon. An insurance policyholder is sued and demands coverage for the lawsuit from its insurer. The insurer, as permitted and provided by Florida law, offers to defend the insured but reserves its right to deny coverage should the insured be found liable.


Besvinick

The insured accepts the defense provided by the insurer, and the lawsuit proceeds. But the insured party becomes nervous and demands settlement. The insurer disagrees with the insured's evaluation of the case and refuses to settle.

The insured argues the insurer has a good faith duty to settle the case as a matter of Florida law, but the insurer argues it is entitled to control the defense and any settlement.

Can the insured settle the lawsuit over the insurer's objections and expect the insurer to be liable?

In *Continental Casualty Company v. City of Jacksonville*, the 11th U.S. Circuit Court of Appeals interpreted state law and answered with a resounding "no." The court affirmed a district court decision holding Jacksonville's unauthorized settlement of a mass tort action over its insurer's objection vitiated any insurance coverage for the deal.

The case arose from a lawsuit filed by thousands of Jacksonville residents alleging physical and emotional injuries caused by their exposure to lead and other contaminants from incinerators and dump sites owned and operated by the city. With the lawsuit pending, the city sent a notice of the lawsuit to its insurer, seeking coverage.

The insurer agreed to defend the city subject to a complete reservation of rights and provided the city with counsel of its choice.

Although the city accepted the insurer's defense, it insisted it was entitled to control the defense and settlement.

The insurer repeatedly objected, but Jacksonville entered into private negotiations with the plaintiffs and ultimately agreed to a two-tiered settlement. The city paid the plaintiffs $25 million and stipulated to a $75 million consent judgment that could only be enforced against the insurer.

Senior U.S. District Judge Harvey Schlesinger in Jacksonville held and the 11th Circuit affirmed the city's conduct breached the cooperation provision of the policy and eliminated insurance coverage for the settlement.

In the process, the appellate court confirmed several important principles of Florida insurance law and practice.

First, an insurer who provides a defense to a lawsuit subject to a reservation of rights meets its contractual obligations under the policy and has the right to control the defense and any settlement.

Second, when an insurer meets its contractual obligation by providing a defense subject to a reservation of rights, the insured is bound by the cooperation provision in the insurance policy and cannot settle the lawsuit without the insurer's consent and expect the insurer to be held liable.

Third, when an insurer is providing a defense subject to a reservation of rights and the two disagree on a settlement, the disagreement does not constitute a breach of the insurer's good faith duty to settle that releases the insured from its duty to cooperate. As long as the insurer is providing the insured with a defense, the insurer retains the right to decide whether and when to settle — and the insured must cooperate.

Finally, if the insured breaches its duty to cooperate and settles without its insurer's consent, the insurer will not be bound by the settlement if it was prejudicial to the insurer and the insurer exercised good faith and due diligence to secure the insured's cooperation, even if unsuccessfully.

Although prejudice is often a question of fact, where the facts are undisputed, prejudice may be determined as a matter of law.

In the Jacksonville case, the court held "the city's duplicity" in conducting private negotiations was substantially prejudicial because it prevented the insurer from providing input at critical stages in negotiations and rendered its efforts to obtain the city's cooperation futile.

The court also held the insurer's multiple written requests for information on the status of settlement talks and repeated admonition that the city was not free to settle without its consent demonstrated the required good faith and due diligence to obtain the city's cooperation.

The case decided in April makes clear that an insured cannot have cake and eat it, too.

When an insured accepts a defense subject to a reservation of rights, it cannot enter into a settlement without its insurer's consent — without risking its insurance coverage for the settlement. ■

Laura Besvinick, a partner in Hogan & Hartson's Miami office, represented the insurer in the trial court and on appeal. Her practice focuses on the defense of legal and accounting professional liability claims and insurance companies in complex coverage and insurance bad-faith actions.