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ALERT

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Whose Case Is It, Anyway?

It's your name on the complaint, it's your reputation on the line, it's your insurance policy (and your premium payments). So why should the insurance company get to decide whether or not you can settle?

By Diana Shafter Gliedman

Every year, hotels are subject to a host of lawsuits, both valid and meritless, from guests who claim to have suffered on-premises injury. The defense of such cases can be extremely expensive, and most hotels accordingly purchase commercial general liability insurance to ensure that if they are sued by a third party, their insurance company will pay for the defense.

What many hotel operators fail to recognize, however, is that most liability policies do not simply maintain that the insurance company will *pay* for the defense. They also provide the insurance company with the right, under certain circumstances, to *control* aspects of the defense of the underlying action, including whether and when to settle. As such, whether you want to settle a complex case and simply be done with it, or you're determined to reject settlement and fight a baseless claim to the bitter end, it is crucial to know your rights and the rights of your insurance company. Otherwise, you may end up with less than the insurance coverage to which you are entitled.

Consent to Settle May Not Be "Unreasonably Withheld"

Most standard CGL provisions state that a policyholder may not enter into a settlement without an insurance company's consent, stipulating that "[n]o Claims Expenses shall be incurred or settlements made, contractual obligations assumed or liability admitted with respect to any Claim without the Insurer's written consent, *which* shall not be unreasonably withheld." Other policies do away with the reasonableness requirement altogether, simply stating that "[n]o 'insured' will, except at that insured's own cost, voluntarily make a payment…or incur any expense, other than for first aid, without our written consent." Some insurance policies even purport to limit a policyholder's ability to bring legal action against the insurance company seeking reimbursement for a settlement unless the settlement has been approved. For example, some CGL policies contain a variation of the following condition: "Legal Action Against Us: 'You will have no right of action against us under this policy unless all of its terms have been fully complied with; and the amount that you seek to recover has been determined by settlement with our consent or by final judgment against an insured.'"

At first reading, these provisions seem to suggest that if an insurance company refuses to settle an underlying case, the policyholder is entirely without recourse. This is not the case. Based upon the language of these provisions, it is clear that the policyholder must seek the insurance company's consent before entering into a settlement with a plaintiff. Courts, however, generally do not

ANDERSON KILL
1251 Avenue of the Americas
New York, NY 10020
(212) 278-1000 Fax: (212) 278-1733

ANDERSON KILL
864 East Santa Clara Street
Ventura, CA 93001
(805) 288-1300 Fax: (805) 288-1301

ANDERSON KILL
1600 Market Street, Suite 2500
Philadelphia, PA 19103
(267) 216-2700 Fax: (215) 568-4573

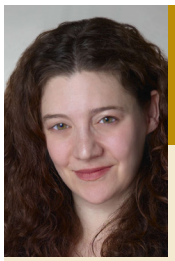
ANDERSON KILL
1055 Washington Boulevard, Suite 510
Stamford, CT 06901
(203) 388-7950 Fax: (203) 388-0750

ANDERSON KILL
1717 Pennsylvania Avenue, Suite 200
Washington, DC 20006
(202) 416-6500 Fax: (202) 416-6555

ANDERSON KILL
One Gateway Center, Suite 1510
Newark, NJ 07102
(973) 642-5858 Fax: (973) 621-6361

ANDERSON KILL
JP Morgan International Plaza III
14241 Dallas Parkway, Suite 650
Dallas, TX 75254
(972) 728-8753 Fax: (805) 288-1301

www.andersonkill.com



who's who

Diana Shafter Gliedman is a shareholder in the New York office of Anderson Kill. Ms. Gliedman represents policyholders in actions ranging from small insurance coverage disputes to multi-party, multi-issue insurance coverage litigations.
dgliedman@andersonkill.com
(212) 278-1036

permit an insurance company arbitrarily to withhold consent to a reasonable settlement. *See Bogan v. Progressive Casualty Insurance Co.*, 521 N.E.2d 447 (Ohio 1988) ("[A]n insurer may not avoid coverage by unreasonably refusing to consent to a settlement . . .").

In *Traders & General Insurance Co. v. Rudco Oil & Gas Co.*, Traders agreed to defend Rudco in any lawsuits filed against it. After an incident involving Rudco and various injured parties, Rudco settled with the parties and sought consent and indemnification from Traders. Traders refused and Rudco sought relief from the court. Finding for Rudco, the court stated (emphasis added):

> [The insurance company's] obligation to defend and to pay is primary and paramount; consequently, its right to control the litigation is first and paramount . . . **But, the rights of the insurer in these circumstances are not absolute, they are subject to moderation by the rule of right and justice. Exclusive authority to act does not necessarily mean the right to act arbitrarily.**
>
> [W]here the insured is clearly liable and the insurer refuses to make a settlement, thus protecting the insured from a possible judgment for damages in excess of the amount of the insurance, the refusal must be made in good faith and upon reasonable grounds for the belief that the amount required to effect a settlement is excessive.

129 F.2d 621, 626-27 (10th Cir. 1942). Many courts have found this to be the rule of law even if the policy does not expressly state that consent will not be withheld unreasonably, because every policy contains an inherent, if unstated, duty of good faith and fair dealing (emphasis added):

> Under liability or indemnity policies in which the insurer assumes the duty of defending or settling suits against the insured, **this obligation is one requiring due care and a strict performance in utmost good faith**. In such case, the insurer owes the duty to exercise reasonable care in conducting the defense, and is liable for damages resulting to the insured by reason of its negligence in performing such duty. . . . It is generally agreed that under policy provisions giving the insurer the right to defend and settle claims against the insured, the insurer may be held liable to the insured for any damage to the insured ensuing where the insurer acts with bad faith toward the insured and improperly refuses or fails to compromise the claim involved. Moreover, there is authority to the effect that this liability of the insurer to the insured also obtains if the insurer **negligently fails to settle a claim against the insured**.

Home Indem. Co. v. Snowden, 223 Ark. 64, 70 (Ark. 1954). See also *In re State Farm Mut. Ins. Co. v. Del Pizzo*, 586 N.Y.S.2d 310, 311, 185 A.D.2d 352 (2d Dep't 1992) (insurer ignored insured's request for release from rights and causes of action flowing from an earlier auto accident and as a result was deemed to acquiesce as a matter of law to the release as well as waive its right to object to insured's settlement with third-party); *Fisher v. USAA Casualty Insur. Co.*, 973 F. 2d 1103, 1107 (3d Cir.

1992) ("Nor may an insurer, once presented with a demand for consent, unduly delay its decision regarding coverage.")

Not All Refusals Are "Unreasonable"

While many courts hold that policyholders should not be bound by capricious or unreasonable refusals to settle, this does not negate the language of the "consent to settle" provision or the obligations it imposes. Indeed, in the case entitled *Vincent Soybean & Grain Co. v. Lloyd's Underwriters of London*, 246 F.3d 1129 (8th Cir. 2001), the court made it clear that an insurance company's refusal to authorize a settlement does not, in and of itself, constitute bad faith, even if the policyholder keeps the insurance company fully informed and involved in settlement discussions:

> Lloyd's was not guilty of bad faith as defined in *Snowden*. It did not unreasonably delay or refuse to take action after notice of the claim — Parr promptly investigated the claim by requesting documents and exchanging letters with Vincent, by speaking with Vincent's owner and insurance agent, and by seeking independent advice regarding the reasonableness of Eubanks's damage claim. Nor did Lloyd's refuse to defend. It accepted defense of the claim and never withdrew from the case. Some three months after notifying Lloyd's of the claim, Vincent wrote Parr, asserting that if Lloyd's did not take "all reasonable efforts" to settle the Eubanks claim within thirty days, Vincent "will no longer consider itself bound by [the cooperation clause.]" Vincent argues that Lloyd's acted in bad faith when it failed to comply with this demand. We disagree. Lloyd's never refused to settle. It simply refused to relinquish control of the settlement process. That was not bad faith; it was part of Lloyd's right to control defense of a claim it had agreed to defend.

Vincent Soybean & Grain Co., 246 F.3d at 1132. See also *Vigilant Ins. Co. v. Bear Stearns Cos., Inc.*, 10 N.Y. 3d 170 (N.Y. 2008).

Policyholders Must Keep Their Insurance Companies Involved and Informed

These cases make it clear that whether or not an insurance company has acted unreasonably by refusing to settle an action is highly fact specific. In order to protect their liability coverage, policyholders contemplating settlement must keep their insurance companies apprised of settlement negotiations, the circumstances of the underlying case, and justification for the settlement amount, preferably from defense counsel. Policyholders should also attempt to provide their insurance companies with sufficient time to review the settlement, raise questions, review relevant documents and speak with defense counsel. If the insurance company still refuses to authorize a settlement that defense counsel believes is advisable and advantageous under the circumstances, the policyholder may then seek to argue that consent was unreasonably withheld, and coverage for the settlement is not voided.

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But Anderson Kill's experience in the hospitality and lodging industry goes beyond insurance coverage. Our Hospitality Industry Group attorneys routinely assist clients with needs relating to real estate and construction, bankruptcy, executive compensation, litigation, finance and a wide range of corporate issues. Our specific experience providing legal services to companies in the hospitality industry ranges from the routine — such as negotiating construction contracts — to the extraordinary — such as litigating a multimillion dollar insurance coverage case arising out of severe hurricane damage to an international resort and acting as insurance counsel to the world's largest chain of casual dining restaurants.

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David P. Bender Jr.
(805) 288-1300 or dbender@andersonkill.com

Diana Shafter Gliedman
(212) 278-1036 or dgliedman@andersonkill.com