

SPECIAL SECTION: **HOSPITALITY & GAMING**

# The Right to Settle

*Protecting the right to control your case*

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Every year, hotels are subject to a host of lawsuits, both valid and meritless, from guests who claim to have suffered an on-premises injury. The defense of such cases can be extremely expensive, and most hotels accordingly purchase commercial general liability (CGL) insurance so 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 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 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

*Your insurance policy may dictate whether you settle a complex case or fight a baseless claim to the bitter end.*

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 permit an insurance company to arbitrarily 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

[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) (emphasis added). 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.

Under liability or indemnity policies in which the insurer assumes the duty of defending or settling suits against the insured,



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**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) (emphasis added). See also *In re State Farm Mut. Ins. Co. v. Del Pizzo*, 586 N.Y.S.2d 310, 31, 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 *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 – [Lloyd's assigned counsel] 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 [claimant'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 [Lloyd's assigned counsel], asserting that if Lloyd's did not take "all reasonable efforts" to settle the [claimant's] 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 1131. See also *Vigilant Ins. Co. v. Bear Stearns Cos., Inc.*, 10 N.Y.3d 170 (N.Y. 2008)

In a few states, such as New Jersey, it is the rule that compliance with a consent to settle provision is a condition precedent to recovery under the policy and their breach can cause a forfeiture of coverage. *Griggs v. Bertram*, 88 N.J. 347, 360 (N.J. 1982). As such, under New Jersey law, "an insured cannot take any meaningful steps toward an early settlement of the claim without risking loss of coverage." *Griggs*, 88 N.J. at 360. See also *New Jersey Eye Center, P.A. v. Princeton Ins. Co.*, 394 N.J. Super. 557, 570-571 (App. Div. 2007) (emphasis added) (noting that a consent to settle provision constitutes a condition precedent, and "based upon this analysis, we do not find it necessary to even consider

whether the findings of the judge below, that the procedure adopted was not the product of bad faith or collusion and the damages were reasonable ... *In our judgment, that is simply immaterial because the purported settlement represented such a fundamental breach of the insured's obligation to [its insurance company]?).* However, "[w]hile the right to control settlements reserved to insurers is an important and significant provision of the policy contract, it is a right which an insurer forfeits when it violates its own contractual obligation to the insured" – for example, by unreasonably delaying the investigation or handling of a covered claim or by otherwise breaching the implied duty of good faith and fair dealing inherent in all insurance policies. *Fireman's Fund Ins. Co. v. Security Ins. Co.*, 72 N.J. 63, 71-72, 77 (N.J. 1976).

Thus, in New Jersey, in order to demonstrate that a policyholder is entitled to coverage notwithstanding a settlement entered into without the insurance company's consent, a policyholder must show that the insurance company breached its policy in a material way, the underlying settlement was reasonable and the underlying settlement was entered into in good faith.

#### **Keep Insurance Companies 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.