Consent Judgments With Covenant Not To Sue/Enforce

By James T. Mellon and David A. Kowalski

This article provides an overview as to how the courts of each of the 50 states treat consent judgments and covenants not to enforce in the context of a breach of the duty to defend.

An insurer's decision as to whether to accept or reject a tender of defense can have far-reaching consequences. As may be expected, an insurer cannot deny defense and still claim to be able to control the litigation. Indeed, many courts "have held that when an insurer refuses to defend its insured, it does so at its own peril and loses the right to control the defense." *Wells Dairy, Inc. v. Travelers Indem. Co. of Ill.*, 266 F.Supp.2d 964, 967 (N.D. Iowa 2003) (citing cases). However, merely losing control of the defense is not the only peril. Faced with the prospect of defending out-of-pocket, an insured may agree to a consent judgment with a covenant not to sue or enforce—in other words, the consent judgment is collectible only against available insurance, and not against the insured individually. As part of such a consent judgment, there may be an admission of liability, or stipulation to "facts" which would serve to limit or defeat an insurer's coverage defenses.

These consent judgments are often defined by several common features: 1) The insured suffers little or no out-of-pocket liability; 2) The judgment fixes liability, damages, or both; 3) The claimant agrees that the judgment is collectible as to insurance only, and not against the insured personally; and 4) The insured assigns its rights against the insurer to the claimant. STEPHEN R. SCHMIDT, THE BAD FAITH SETUP, 29 Tort & Ins. L. J. 705, 722 (1994). From past experience, another common feature is an unusually high judgment amount, not-so-coincidentally often the limits of the insurance policy. The claimant then brings suit against the insurer, seeking to collect on the consent judgment out of insurance proceeds.

There are several options for a court faced with a suit on a consent judgment. First, the court could hold that the consent judgment is completely enforceable against the insurance company. This effectively reduces the consent judgment suit to the question of whether the insurance company breached its duty to defend the underlying lawsuit that resulted in the consent judgment. Second, the court could hold that the consent judgment is not enforceable against the insurance company. This expands the consent judgment lawsuit to a complete re-litigation of the underlying question of the insured's liability, causation, damages, and resolution of the question of the breach of the duty to defend. Third, the court could take a middle ground—for example, rather than allowing re-litigation of the entire question of underlying liability, the court may only permit the insurance company to challenge whether the consent judgment amount is reasonable or made in good faith, in light of the allegations by the claimant.

In this article, we discuss the various defenses afforded to insurers in the fifty states, and courts' treatment of the most common arguments as to why consent judgments or settlements should or should not be enforceable.

The vast majority of courts hold that the consent judgment is, at least somewhat, enforceable against the insurer if the insurer breaches its duty to defend. *Old Republic Ins Co v Ross*, 180 P.3d 427, 432-33 (Colo. 2008). Other states have modified the rule, for example, allowing enforcement of the judgment where there is any material breach by the insurer, a refusal to accept a reasonable settlement offer, action

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in bad faith, or a defense under reservation of rights with a refusal to settle within policy limits. *Id*. at 433.

Of particular note, all states have recognized one absolute defense for the insurer: a finding that the duty to defend was not breached. Absent breach of the duty to defend, then there is no possibility for coverage of the underlying litigation. If the underlying litigation is not within the terms of coverage, then the consent judgment which ended that litigation cannot be enforced against the insurer. As aptly observed by Michigan's Supreme Court, "it is impossible to hold an insurance company liable for a risk it did not assume." *Hunt v. Drielick,* 852 N.W.2d 562, 566 (Mich. 2014) (internal quote/cite omitted). That is to say, if the insurer did not cover the risk alleged in the lawsuit, then consent judgment or not, there is nothing to enforce against the insurer as the entire matter lies outside the scope of coverage. An insurer may also be permitted to raise defenses such as fraud and collusion.

As may be imagined, each state is free to chart its own course on how to address enforceability of consent judgments against insurers. In 2017, a comprehensive review of each state's position on the issue of the enforceability of a consent judgment against an insurer was prepared. Catalina J. Sugayan and Carol J. Gerner, Litigating the Consent Judgment Case – A 50 State Overview, *Insurance Bad Faith and Extra-Contractual Liability* (June 2017). This article both updates and supplements that review, which serves as a useful resource for practitioners.

States Holding Consent Judgment/ Covenant Not to Execute is Generally Enforceable

Ohio: An insurer breaching the duty to defend cannot defeat a settlement by pointing to provisions on anti-assignment, voluntary payment, cooperation, or no-action clauses. *Patterson v. Cincinnati Ins. Cos.*, 91 N.E.3d 191, 200 (Ohio Ct. App. 2017). When the insurer abandons the insured, it forfeits the right to control the litigation or its resolution and cannot complain absent a showing of fraud. *Sanderson v. Ohio Edison Co.*, 635 N.E.2d 19, 23-24 (Ohio 1994). Such an insurer cannot later complain the settlement is unreasonable or too costly. *Buckeye Ranch, Inc. v. Nortfield Ins. Co.*, 839 N.E.2d 94, 111 (Ohio Comm. Pleas 2005).

States Holding Consent Judgment/ Covenant Not to Execute is Unenforceable

North Carolina: An insurer refusing to defend without justification is estopped from denying coverage and is obligated to pay a settlement amount made in good faith. *Pulte Home Corp. v. Am. S. Ins. Co.*, 747 S.E.2d 614, 617 (N.C. Ct. App. 2007). However, the policy language can render that estoppel rather meaningless, because "when an insurance policy contains language such as 'legally obligated to pay,' an insurer has no obligation to an injured party where the insured is protected by a covenant not to execute." *Terrell v. Lawyers Mut. Liab. Co. of NC*, 507 S.E.2d 923, 927 (N.C. Ct. App. 1998). Virtually all insurance policies contain "legally obligated to pay" language, such that in most cases, a consent judgment with covenant not to execute could not be enforced on the insurer.

West Virginia: The law prohibits an insurer from being bound by a consent judgment entered in a lawsuit to which it is not a party. *Penn-America Ins. Co. v. Osborne*, 797 S.E.2d 548, 553 (W. Va. 2017). This is true unless the insurer agreed to be bound. *Horkulic v. Galloway*, 665 S.E.2d 284, 289 (W. Va. 2008). Where an insurer

negligently refuses to accept a settlement offer, and the insured is subsequently harmed, a claim may exist. *Strahin v. Sullivan*, 647 S.E.2d 765, 771 (W. Va. 2007). However, where the insured's assets are protected, such as by a covenant not to execute, an essential element, damage to the insured, cannot exist. *Id.*

States Holding Consent Judgment/ Covenant Not to Execute is Enforceable, with Caveats

Alabama: An insured with a right to defend, with notice of settlement negotiations, who declines to participate, will be bound to pay any good-faith settlement if coverage exists. *Twin City Fire Ins Co., Inc. v. Ohio Cas. Ins. Co., Inc.*, 480 F.3d 1254, 1258 (11th Cir. 2007) (quoting *Liberty Mut. Ins. Co. v. Wheelwright Trucking Co.,* 851 So.2d 466, 475 (Ala.2002)). Absent notice to the insurer of either the original suit or the settlement, the claimant must prove the insured's liability and that the settlement was reasonable. *Stone Bldg. Co. v. Star Elec. Contractors, Inc.*, 796 So.2d 1076, 1090 (Ala. 2000). The insurer may raise fraud and collusion in defense. *Ex Parte Employers Mut. Cas. Co., Inc.,* 845 So.2d 773, 777 (Ala. 2002). A prior line of Alabama federal court cases which concluded that a covenant not to execute meant the insured was not legally obligated to pay the judgment was determined to be based on an Oregon Supreme Court case which had been subsequently overruled. *Granite State Ins. Co. v. New Way Out, Corp.*, 19-cv-0848, 2021 WL 191637, at *3-4 (S.D. Ala. Jan. 19, 2021).

Alaska: Where an insurer breaches the duty to defend, it may not rely on a cooperation clause to defeat a consent judgment, even if the insured assigns its rights in exchange for a covenant not to execute on the insured's other assets. *Great Divide Ins. Co. v. Carpenter*, 79 P.2d 599, 608 (Alaska 2003). "[I]t is thought that an insured that has been placed at economic risk by its insurer's breach should be allowed to protect itself by shifting the risk to the breaching insurer without first subjecting itself to potential financial ruin." *Id.* at 608-09. The insurer will be liable for the full amount of the consent judgment, to policy limits, if the amount is reasonable. *Heynen v. Allstate Ins. Co.*, 11-cv-00010, 2013 WL 11310636, at *5 (D. Alaska October 30, 2013).

Arizona: Provided the consent judgment is not the product of fraud or collusion, an insurer will be bound by a consent judgment "with respect to all matters which were litigated or could have been litigated in that action." *Colorado Cas. Ins. Co. v. Safety Control Co., Inc.,* 288 P.3d 764, 769-70 (Ariz. Ct. App. 2012). Two separate types of agreements are recognized. A "*Damron* Agreement" arises when defense has been denied, while a *Morris* Agreement arises when the insurer defends, but reserves its right to dispute coverage. *Quihuis v. State Farm Mut. Auto. Ins. Co.*, 334 P.3d 719, 722 (Ariz. 2014). The insurer may defend by asserting the underlying allegations fall outside the scope of coverage. *Id.* If the insurer acts in bad faith in refusing to defend, it may face both contract and tort damages. *Id.* at 730.

Arkansas: An insurer will be bound by a consent judgment, but where the amount is "highly questionable and smack[s] of a subterfuge," the insurer may not be bound by the amount. *Hartford Ins. Co. of Midwest v. Mullinax*, 984 SW.2d 812, 815 (Ark. 1999). The insured has the burden of making the prima facie showing that the consent judgment is covered by the policy. *Kerr v. Gotham Ins. Co.*, No 18-cv-00423, 2019 WL 5268625, at *4 (E.D. Ark. October 17, 2019).

California: "[I]f the insurer wrongfully refuses to defend, leaving the insured to his own resources to provide a defense, then the insurer forfeits the right to control settlement and defense. In that event, the insured is free to settle the lawsuit on his own, and the insurer is bound by a stipulated judgment." *Safeco Ins. Co. v. Superior Ct.*, 84 Cal.Rptr.2d 43, 45 (Cal. Ct. App. 1999). If the insurer acts in bad faith and also refuses to accept a reasonable settlement offer within policy limits, it will be liable for any judgment/settlement, even if in excess of limits. *Anderson v. Nationwide Mut. Ins. Co.,* 339 F.Supp.3d 933, 945 (E.D. Cal. 2018). With a failure to defend, an insured "may 'make the best good faith settlement.'" *Westport Ins. Corp. v. Cal. Cas. Mgmt. Co.,* 249 F.Supp3d 1164, 1180 (N.D. Cal. 2017) (quoting *United Servs. Auto. Ass'n v. Alaska Ins. Co.*, 94 Cal.App.4th 638, 644 (2001)). Because of the potential for fraud and collusion, the insurer should only be bound under circumstances which protect against these concerns. *Pruyn v. Agric. Ins. Co.*, 42 Cal. Rptr.2d 295, 305 (Cal. Ct. App. 1995)

Colorado: A "*Bashor* Agreement" occurs when the insured assigns its claim against the insurer to the claimant and receives a covenant not to execute, but it does not include pretrial stipulated judgments, due to concerns over the lack of arm's length valuation. *Old Republic Ins Co v Ross,* 180 P.3d 427, 431-32 (Colo. 2008). There may be circumstances, such as bad faith, where an insurer will be held bound. *Id.* at 434. In such a case, a stipulated judgment, even in excess of policy limits, is sufficient to establish bad faith damages. *Nunn v. Mid-Century Ins. Co.,* 244 P.3d 116, 122-23 (Colo. 2010). An assignment of a bad faith cause of action is known as a "*Nunn* Agreement." It includes circumstances where an insurer refuses to settle within policy limits. *Auto-Owners Ins. Co. v. Bolt Factory Lofts Owners Ass'n, Inc.*, 487 P.3d 276, 282 (Colo. 2021). The burden is not on the insurer to prove the amount is unreasonable in a *Nunn* agreement. Bolt Factory, 487 P.3d at 284 (disagreeing with the burden placed in *DC-10 Entertainment, LLC v. Manor Ins. Agency, Inc.,* 308 P.3d 1223, 1227 (Colo. Ct. App. 2013)).

Connecticut: Breach of the duty to defend generally renders the insurer liable for settlement and costs, but the insured must show "the settlement is reasonable in proportion to the insurer's liability under its duty to defend." *Capstone Bldg. Corp. v. Am. Motorists Ins. Co.*, 67 A.3d 961, 992 (Conn. 2013). The courts recognize the danger of fraud and collusion, and both matters are properly pled as special defenses under state law. *Black v. Goodwin,* No. 51-91-01, 1992 WL 353635, at *2-3 (Conn. Super. Ct. Jan. 13, 1992).

Delaware: Consent judgments with covenants not enforced are a "protective mechanism available to insureds." *Philadelphia Indem. Ins. Co. v. Bogel,* 269 A.3d 992, 1013 (Del Sup. Ct. 2021). Enforcement turns on whether it is fair to do so, by looking to whether fraud, collusion, or bad faith have tainted the judgment. *Id.* at 1014. The claimant has the initial burden of proving the settlement is reasonable, with the goal to determine

what a reasonably prudent person in the place of the insured would have done. *Id.* at 1016.

D.C.: A claimant's release of the insured from any obligation to personally satisfy a judgment in exchange for the insured's assignment of a cause of action against the insured for failure to settle does not preclude the claimant from recovering against the insurer. *Gray v. Grain Dealers Mut. Ins. Co.*, 871 F.2d 1128, 1133 (D.C. Cir. 1989). Consent to settlement is not required where an insurer places its interest ahead of the insured by failing to give a definitive coverage decision, continues to disclaim liability, and refuses to approve an "excellent" settlement. *Central Armature Works, Inc. v. Am. Motorists Ins. Co.*, 520 F.Supp. 283, 289 (D.D.C. 1980). If the insurer claims the settlement was the product of fraud or collusion, that action does not sound in tort; rather the insurer's only remedy is to seek to have the judgment vacated. *Interstate Fire & Cas. Co., Inc. v. 1218 Wisc., Inc.*, 136 F.3d 830, 836 (D.C. Cir. 1998).

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Florida: A "*Coblentz* Agreement" (*Coblentz v. Am. Surety Co. of NY*, 416 F.2d 1059 (5th Cir. 1969)) is a consent judgment with a covenant not to execute, and an assignment of any rights against the insurer from the insured to the claimant. *In re Estate of Arroyo v. Infinity Indem. Ins. Co.*, 211 So.3d 240, 243 (Fla. Dist. Ct. App. 2017). "[W]hen an insurer refuses to defend its insured from a lawsuit, and the insured later settles the suit by entering into a Coblentz agreement, the insurer is precluded from relitigating the issue of its insured's liability in subsequent proceedings." *Id.* at 246. "In order to enforce a consent judgment entered pursuant to a *Coblentz* agreement, the assignee must bring an action against the insurer and prove: (1) insurance coverage, (2) the insurance company wrongfully refused to defend its insured, and (3) the settlement was reasonable and made in good faith." *Id.* at 247. A "*Cunningham* Agreement" involves "the situation where there is not a previous excess judgment but an insurer and a third-party claimant enter into an agreement and stipulate to try the bad-faith issues first. The parties further stipulate that if no bad faith is found, the third-party claimant will settle for the policy limits." *Perera v. U.S. Fid. & Guar. Co.*, 35 So.2d 893, 899 (Fla. 2010).

Georgia: Where an insurer refuses to defend, it waives policy provisions on consent to settle and is bound by any settlement made in good faith, plus expenses and attorney fees. *Ga. So. & F. Ry. Co. v. U.S. Cas. Co.*, 102 SE2d 500, 502 (Ga. Ct. App. 1958); *Barrs v. Auto-Owners Ins. Co.*, 564 F.Supp.3d 1362, 1371 (M.D. Ga. 2021)). The settlement must be within policy limits. *Piedmont Office Realty Trust, Inc. v. XL Specialty Ins. Co.*, 771 S.E.2d 864, 867 (Ga. 2015).

Hawaii: An insurer refusing to defend forfeits the right to control the defense and to have the insured cooperate; if the duty to defend is breached, the insurer will be liable for all reasonable defense fees and costs. *Sentinel Ins. Co., Ltd. v. First Ins. Co. of Hawai'I, Ltd.*, 875 P.2d 894, 913 (Haw. 1994). The insured can negotiate a good-faith settlement, which is presumptive evidence of the insurer's liability. *Am. Auto. Ins. Co. v. Hawaii Nut & Bolt, Inc.*, No. 15-cv-00245, 2017 WL 5895162, at *6 (D. Hawaii June 27, 2017) (quoting *Sentinel*, 875 P.2d at 913).

Idaho: For breach of the duty to defend, the insurer must indemnify for a settlement, "so long as a potential liability for the insured existed which resulted in a reasonable settlement in view of the size of possible recovery and the probability of the claimant's success against the insured." *Esterovich v. City of Kellogg*, 80 P.3d 1040, 1042-43 (Idaho 2003).

Illinois: Breach of the duty to defend allows the insured to enter into a reasonable settlement. *Guillen v. Potomac Ins Co. of IL*, 785 N.E.2d 1, 11-12 (Ill 2003). The insured must prove the settlement is reasonable before the insurer will be bound. *Id.* at 14. "[T]he litmus test must be whether, considering the totality of the circumstances, the insured's decision conformed to the standard of a prudent uninsured. … Similarly, with respect to the amount of damages agreed to, the test is what a reasonably prudent person in the position of the [insured] would have settled for on the merits of plaintiff's claim. … Courts should take a commonsense consideration of the totality of facts bearing on the liability and damage aspects of plaintiff's claim, as well as the risks of going to trial." *Country Mut. Ins. Co. v. Olsak*, --- N.E.3d --- (Ill 2022) (internal quote/cite omitted). Bad faith, fraud or collusion can render settlement unreasonable, and the court should look to "(1) the amount of the overall settlement in light of the value of the case, (2) a comparison with awards or verdicts in similar cases involving similar injuries, (3) facts known to the settling insured at the time of the settlement, (4) the presence of a covenant not to execute as part of the settlement, and (5) the failure of the settling insured to consider viable available defenses." *Id.*

Indiana: An insurer will be bound by a consent judgment if "(1) the coverage is eventually shown, and so long as the consent judgment (2) is not the product of bad faith or collusion and (3) falls somewhere within a broad range of reasonable resolutions of the underlying dispute.'" Carpenter v. Lovell's Lounge & Grill, LLC, 59 NE3d 330, 338 (Ind. Ct. App. 2016) (quoting Midwestern Indem. Co. v. Laikin, 119 F.Supp.2d 831, 842 (S.D. Ind. 2000)). If the insurer does not file a declaratory until after the judgment enters, the insurer has the burden of proof on bad faith/collusion by clear and convincing evidence. Id. at 340. In refusing to defend, an insurer will be bound by matters necessarily determined in the underlying lawsuit. *State Farm Fire & Cas. Co. v. T.B.*, 762 N.E.2d 1227, 1231 (Ind. 2002). An insurer seeking not to be bound should either defend under reservation of rights or file a declaratory judgment action. *Id.* Wrongful denial of defense precludes litigating contractual coverage defenses. *Berry Plastics Corp. v. IL Nat'l Ins. Co.*, 244 F.Supp.3d 839, 846 (S.D. Ind. 2017).

Iowa: Defense under reservation of rights does not allow an insured to settle

without consent. *Kelly v. Iowa Mut. Ins. Co.,* 620 N.W.2d 637, 642 (Iowa 2000). However, if the insurer is faced with a fair/reasonable settlement demand and a reasonable insurer would pay, the insurer must either abandon coverage defenses and pay, or lose its right to control the settlement. *Id.* at 644-45. If coverage exists, the insurer will be liable if the settlement is fair and reasonable. *Id.* If there is, in fact, no coverage, the insurer is not liable for subsequent settlement. *Westview, Inc. v. Iowa Mut. Ins. Co.*, 728 N.W.2d 224 (Iowa Ct. App. 2006).

Kansas: "Courts in Kansas do not automatically enforce consent judgments against insurers," but rather look to the reasonableness to see if the valuation is the result of arm's length determination. *Gruber v. Estate of Marshall*, 482 P.3d 612, 627 (Kan. Ct. App. 2021). If the settlement is reasonable and in good faith, then it may be enforced against the insurer who has acted in bad faith or is negligent in refusing to settle. *Id.* The claimant has the initial burden to establish reasonableness and good faith, with the insurer bearing the ultimate burden of persuasion. *Id.* "[T]he insurer of a liability or an indemnity policy would be liable for the full amount of its insured's resulting loss, even if that amount exceeds the limit of the policy, for negligence or bad faith in defending or settling an action against the insured." *Bollinger v. Nuss,* 449 P.2d 502, 507 (Kan. 1969).

Louisiana: The insurer is bound if the settlement is in good faith, made on a reasonable basis, and coverage exists for the underlying allegations. *Arceneaux v. Amstar Corp.*, 969 So.2d 755, 771 (La. Ct. App. 2007) (quoting 14 Couch on Insurance 3d § 203.41 and 205.52). At least where the insurer provided a defense, this reasoning does not apply. *New England Ins. Co. v. Barnett*, 465 Fed.Appx. 302, 308 n3 (5th Cir. 2012). A breach of the duty to defend does not waive policy defenses, but if the duty to defend has been breached, an insured is free to settle without the insurer's approval. *Arceneaux v. Amstar Corp.*, 66 So.3d 438, 450, 452 (La. 2011).

Maine: If an insurer breaches the duty to defend, the insured may act to protect its interests, including by settlement, without risking coverage otherwise available. *Cambridge Mut. Fire Ins. Co. v. Perry*, 692 A.2d 1388, 1391 (Me 1997). The settlement amount must be reasonable, and in good faith. *Id.* at 1391. If the underlying allegations are outside the policy, the insurer is not liable on a settlement by the insured. *Harlor v. Amica Mut. Ins. Co.*, 150 A.3d 793, 802 (Me. 2016) Where a settlement is partly covered, and partly not, apportionment of the judgment between the two claims must be made. *Id.*

Maryland: Where the duty to defend is breached, the insured does not lose his right to coverage due to a settlement, but the insurer can challenge the reasonableness of a resulting settlement. *White Pine Ins. Co. v. Taylor*, 165 A.3d 624, 642 (Md. Ct. Spec. App. 2017) (quoting *U.S. Fidelity & Guarantee Co. v. Nat'l Paving & Contracting Co.*, 228 Md. 40, 48, 178 A.2d 872 (1962)).

Massachusetts: Where an insurer defends under reservation of rights, it loses the right to control the defense as to settlement. *Commerce Ins. Co. v. Szafarowicz*, 131 N.E.3d 782, 795 (Mass. 2019). Where a defense is provided, the insurer is not bound by the settlement and can re-litigate liability. *Id.* at 796. Where the duty to defend is breached, even if in good faith, the insurer assumes the risk of a reasonable settlement and defense costs for the underlying claim. *Jefferson Ins. Co. of NY v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, 677 N.E.2d 225, 232 (Mass. App. Ct. 1997).

Michigan: Insurers breaching the duty to defend are liable for all foreseeable damages. *Schiebout v. Citizens Ins. Co. of Am.*, 366 N.W.2d 45, 49 (Mich. Ct. App. 1985). The insurer will be bound by any reasonable settlement entered into in good faith. *Clay v. Am. Continental Ins. Co.,* 531 N.W.2d 829, 832 (Mich. Ct. App. 1995); *Century Indem. Co. v. Aero-Motive Co.,* 336 F.Supp.2d 739, 745 (W.D. Mich. 2004). Unless determined to have no duty to defend, an insurer is only relieved from a consent judgment if it is unreasonable or the product of bad faith. *Bristol West Ins. Co. v. Whitt*, 406 F.Supp.2d 771, 783 (W.D. Mich 2005).

Minnesota: "A *Miller-Shugart* settlement agreement is a settlement between a plaintiff and an insured defendant in which the defendant, having been denied coverage for the claim, agrees that the plaintiff may enter judgment against it for a sum collectible only from the insurance policy." *King's Cove Marina, LLC v. Lamber Comm. Constr., LLC,* 958 N.W.2d 310, 313 n.1 (Minn. 2021). "A *Miller-Shugart* settlement agreement is enforceable against the insurer if the insurer receives notice of the settlement, and the settlement is reasonable and not the product of fraud or collusion." *Id.* at 321. The insurer may raise fraud or collusion as a defense, or that the amount is not what a reasonable prudent person would have settled for. *Am. Family Mut. Ins. Co. v. Donaldson*, 820 F.3d 374, 380 (8th Cir. 2016).

Mississippi: An insurer refusing to defend will be bound by a reasonable settlement, even if entered into without the insurer's consent. *Mavar Shrimp & Oyster Co. v. U.S. Fid. & Guar. Co.*, 187 So.2d 871, 875 (Miss 1966); *Miss. Ins. Guar. Ass'n v. Byars,* 614 SO.2d 959, 964 (Miss. 1993). An insurer breaching its duty to defend does not waive policy limits, however. *Liberty Mut. Fire Ins. Co. v. Canal Ins. Co.*, 177 F.3d 326, 338-39 (5th Cir. 1999).

Missouri: If an insurer denies defense, the insured may settle without consent, as the insurer "cannot have its cake and eat it too." *Sprint Lumber, Inc. v. Union Ins. Co.,* 627 S.W.3d 96, 116 (Mo. 2021). By statute, after an insurer is afforded opportunity to defend, and refuses to do so without reservation, "Section 537.065.1 allows any person with an unliquidated claim for damages to enter into a contract with a tortfeasor to limit the tort-feasor's liability for a judgment to specified assets, including insurance contracts." *Barnett v. Columbia Maint. Co.*, 632 S.W.3d 396, 401 (Mo. Ct. App. 2021). An insurer refusing to defend will be liable to the policy limits, plus litigation fees, expenses, and damages, even if the company acts in good faith, with reasonable belief that there is not coverage. *Communications Unlimited, Contracting Servs., Inc. v. Broadband Infrastructure Connection, LLC,* 558 F.Supp.3d 773, 789 (E.D. Mo. 2021).

Montana: An insurer who breaches the duty to defend cannot complain that the insured took action to limit its liability, and the insurer is liable for resulting defense costs, judgments, and settlements. *Abbey/Land, LLC v. Glacier Constr. Partners, LLC*,

433 P.3d 1230, 1240 (Mont. 2019). The judgment is "presumptively enforceable as the measure of damages," if it is reasonable and not the product of collusion. *Id.*

Nebraska: When an insurer denies defense, the insured may use all reasonable means to avoid personal liability, including a judgment with a covenant not to execute. *Metcalf v. Hartford Acc. & Indem. Co.,* 126 N.W.2d 471, 475-76 (Neb. 1964). An insurer which refused defense is in no position to attack the judgment in the absence of fraud, collusion, or bad faith." *Id.* at 476; *Carlson v. Zellaha*, 482 N.W.2d 281, 283 (Neb. 1992).

Nevada: An insurer which refuses to defend is at least liable for the insured's defense costs in the underlying action. *Century Surety Co. v. Andrew,* 432 P.3d 180, 184 (Nev. 2018).

New Hampshire: An insurer which breaches its duty to defend will be bound by a judgment entered against the insured. *White Mountain Cable Const. Co. v. Transamerica Ins. Co.,* 631 A.2d 907, 912 (N.H. 1993). "An insurer refusing to defend its insured undertakes the risk that the insured will settle and that it may be held liable for damages, and will not be heard to complain about the strict form of the structure of the relief afforded in the underlying case." *A.B.C. Builders, Inc. v. Am. Mut. Ins. Co.*, 661 A.2d 1187, 1191 (N.H. 1995). A covenant not to execute is not the same as a release, so as to relieve the insurer of liability. *Stateline Steel Erectors, Inc. v. Shields,* 837 A.2d 285, 290-91 (N.H. 2003).

New Jersey: The insurer forfeits the right to control the defense when it violates the duty to defend. *Passaic Valley Sewerage Com'rs v. St. Paul Fire & Marine Ins. Co.*, 21 A.3d 1151, 1161-62 (N.J. 2011). The insurer is liable for a consent judgment so long as the amount is reasonable and made in good faith. *Griggs v. Bertram*, 443 A.2d 163, 172 (N.J. 1982). The covenant not to execute will not relieve the insurer from liability. *Id.* at 174-75. The insured has the initial burden of proof as to the reasonable amount and good faith, but the ultimate burden of persuasion is the insurer's. *Phibro Animal Health Corp. v. Nat'l Union Fire Ins. Co. of Pittsburgh, PA*, No. A-5589-13T3, 2016 WL 3884255, at *19 (N.J. Super. Ct. App. Div. July 14, 2016).

New Mexico: An insurer acts at its peril when it refuses to participate in settlement negotiations and will be bound by the settlement, even if it believes, in good faith, there was no coverage. *Rummel v. Lexington Ins. Co.*, 945 P.2d 970, 984 (N.M. 1997). The settlement must be reasonable. *Am. Gen. Fire & Cas. Co. v. Progressive Cas. Co.*, 799 P.2d 1113, 1117-18 (N.M. 1990). A covenant not to execute will not excuse the insurer of its obligation to pay. *Dydek v. Dydek,* 288 P.3d 872, 885-87 (N.M. Ct. App. 2012).

New York: Failure to defend relieves the insured from any obligation to obtain the insurer's consent before settling, but the settlement must be reasonable. *J.P. Morgan Sec. Inc. v. Vigilant Ins. Co.,* 39 N.Y.S.3d 864, 867 (N.Y. Sup. Ct. 2016); *Cardinal v. State,* 107 N.E.2d 569, 573 (N.Y. 1952). The insured may seek reimbursement of a reasonable settlement from the insurer. *City of N.Y. v. Zurich-Am. Ins. Group,* 811 N.Y.S.2d 773, 774 (N.Y. App. Div. 2006). An insurer may challenge reasonableness, including whether the insured would have been found liable had the matter proceeded to trial. *Horn Const. Co., Inc. v. MT Sec. Serv. Corp.*, 468 N.Y.S.2d 415, 416 (N.Y. App. Div. 1983). However, a federal court, applying New York law, has found that the insured need not establish actual liability, only potential liability, with a view to the size of the possible recovery and the degree of probability of the claimant's success against the insured. *Luria Bros. & Co., Inc. v. Alliance Assur. Co., Ltd.*, 780 F.2d 1082, 1091 (2d Cir. 1986); *Harleysville Worcester Ins. Co. v. Wesco Ins. Co., Inc.*, 314 F.Supp.3d 534, 550 (S.D. N.Y. 2018). A covenant not to execute will not remove the settlement from language requiring the insured by "legally obligated to pay as damages." *Westchester Fire Ins. Co. v. Utica First Ins. Co.*, 839 N.Y.S.2d 91, 94 (Ny. App. Div. 2007); *IL Union Ins. Co. v. U.S. Bus Charter & Limo, Inc.*, 291 F.Supp. 3d 286, 292 (E.D. N.Y. 2018).

North Dakota: The North Dakota Supreme Court looked to Minnesota and its *Miller-Shugart* agreements: "an insured defendant may stipulate for settlement of a plaintiff's claims and stipulate judgment may be collected only from the proceeds of any insurance policy, with no personal liability to the defendant. The stipulated judgment is not conclusive on the insurer. The plaintiff judgment creditor must show the settlement was reasonable and prudent." *Medd v. Fonder,* 543 N.W.2d 483, 485 (N.D. 1996). "We stated a *Miller–Shugart* agreement reduced to judgment is enforceable against an insurer if: "(1) the insurer receives notice of the agreement; (2) the agreement is not the result of fraud or collusion; and (3) the agreement is reasonable." *D.E.M. v. Allickson,* 555 N.W.2d 596, 602 (N.D 1996). An insurer can still argue that the underlying allegations do not fall within the terms of coverage. *Forsman v. Blues, Brews, and Bar-B-Ques, Inc.*, 903 N.W.2d 524, 529-30 (N.D. 2017).

Oklahoma: Where an insurer has a duty to defend but refuses to participate in the defense or to take part in a settlement, the insurer cannot thereafter litigate the issue of the parties' negligence. *MIC Prop. & Cas. Ins. Corp. v. Int'l Ins. Co.*, 990 F.2d 573, 577 (10th Cir. 1993) (applying Oklahoma law). The recovery is measured by coverage under the policy and the reasonableness of the settlement. *Id.* The insured is released from policy provisions against settlement and can affect a reasonable and prudent settlement. *Traders & Gen. Ins. Co. v. Rudco Oil & Gas Co.,* 129 F.2d 621, 626 (10th Cir. 1942) (applying Oklahoma law). "An insurer who disputes the insured's demand to defend has three options. It can (1) seek declaratory relief that would define the insurer's rights and obligations; (2) defend the insured under a reservation of rights, or (3) refuse to take any action at the peril of being later found in breach of its duty to defend." *First Bank of Turley v. Fid. & Deposit Ins. Co. of MD*, 928 P.2d 298, 304-05 (Okla 1996). An insurer breaching the duty to defend becomes liable for all reasonable expenses incurred by an insured in defending the third-party action. *Id.* at 305.

Oregon: A covenant not to execute in exchange for an assignment of rights does not, by itself, effect a complete release and extinguish and insured's liability, and consequently, the insurer's as well. *Brownstone Homes Condo. Ass'n v. Brownstone Forest Heights, LLC*, 363 P.3d 467, 480 (Or. 2015). Notably, this decision overruled prior case law holding to the contrary. *E.g., Leach v. Scottsdale Indem. Co.*, 323 P.3d 337, 347 (Or. Ct. App. 2014).

By statute, an insured may assign a cause of action against an insurer and a release given in exchange for the covenant will not extinguish the cause of action against the insurer. Or. Rev. Stat. §31.825. An insured may reasonably settle the claim and the insurer will be liable for the settlement. *N.W. Pump & Equip. Co. v. AM. States Ins. Co.*, 917 P.2d 1025, 1029 (Or. Ct. App. 1996).

Pennsylvania: Where the duty to defend is breached, the insured need not demonstrate bad faith, only that the settlement is fair, reasonable, and non-collusive, and the insurer can be liable up to the policy limits. *Babcock & Wilcox Co. v. Am. Nuclear Ins.*, 131 A.3d 445, 462-63 (Pa. 2015). "[W]hen an insurer wrongfully declines to defend an insured, the insured may enter a reasonable settlement agreement and subsequently seek indemnification from the insurer to the extent that there is actual coverage for the claim." *Keystone Spray Equip., Inc. v. Regis Ins. Co.*, 767 A.2d 572, 576 (Pa. Super. Ct. 2001). The insurer cannot rely on policy obligations imposed on the insured respecting litigation; it breaches the duty to defend. *Brakeman v. Potomac Ins. Co.*, 371 A.2d 193, 200-01 (Pa. 1977). The insured can assign damages for a bad faith claim to an injured plaintiff. *Allsate Prop. & Cas. Ins. Co. v. Wolfe*, 105 A.3d 1181, 1188 (Pa. 2014).

Rhode Island: Breach of the duty to defend may subject the insurer to liability for defense costs, attorney fees, and the award/damages assessed against the insured. *Conanicut Marine Servs., Inc. v. Ins. Co. of N. Am.*, 511 A.2d 967, 971 (R.I. 1986). In limited circumstances, an insured can assign its claims of bad faith against an insurer to a third party, e.g., where "an insurer had refused to settle the case within the limits of the policy and, subsequently, the plaintiff was awarded a judgment in excess of that policy amount, with the insured thereafter assigning to the plaintiff its bad faith claim against the insurer." *Imperial Cas. & Indem. Co. v. Bellini*, 947 A.2d 886, 892-93 (R.I. 2008). However, general assignment is not permitted. *Id.*

South Carolina: Outside the context of insurance, the South Carolina Supreme Court has disallowed a consent judgment and assignment, finding a danger of inflated damages. *Skipper v. ACE Prop. & Cas. Ins. Co.*, 775 S.E.2d 37, 38 (S.C. 2015). However, in the context of a claim against an insurance agent, the claim is assignable. *Fowler v. Hunter,* 697 S.E.2d 531, 534-35 (S.C. 2010). A covenant not to execute is distinct from a release, however, and will not operate to relieve an insurer "of its obligations where the written agreement shows the parties did not intend to do so." *Cobb v. Benjamin*, 482 S.E.2d 589, 592 (S.C. Ct. App. 1997).

South Dakota: When the duty to defend is breached, the insured may settle rather than proceed to trial, but the amount must be "reasonable in view of the size of possible recovery and degree of probability of claimant's success against the insured," and the insurer will have waived policy provisions, such as cooperation clauses. *Wolff v. Royal Ins. Co. of Am.,* 472 N.W.2d 233, 235 (S.D. 1991). An insured can receive a covenant not to execute in exchange for assigning its claim against the insurer, and such agreements are not intrinsically collusive or ineffective for lack of damages. *Kobbeman v. Oleson*, 574 N.W.2d 633, 636-37 (S.D. 1998). The Court has approved *Miller-Shugart* agreements as adopted by Minnesota. *W. Agric. Ins. Co. v. Arba-Azzein,* 940 N.W.2d 865, 867 n.2 (S.D. 2020). An insured may make any good-faith settlement, and the insurer cannot rely on a "no action" or "no voluntary payment" provision to avoid the settlement. *Sacred Heart Health Servs. V. MMIC Ins., Inc.*, 575 F.Supp.3d 1137, 1155 (D. S.D. 2021).

Tennessee: A covenant not to execute does not extinguish the underlying liability to pay damages. *Tip's Package Store, Inc. v. Comm'l Ins. Mgrs., Inc.*, 86 S.W.3d 543, 555 (Tenn. Ct. App. 2001); *Littleton v. TIS Ins Servs., Inc.*, No. E2014–00938–COA–R3–CV, 2015 WL 443740, at*3-4 (Tenn. Ct. App. Feb. 3, 2015) (applying the rule in the insurance context). The insurer forfeits its right to control the defense, and the insured can negotiate a reasonable settlement. *Standard Const. Co., Inc. v. MD Cas. Co.*,359 F.3d 846, 854 (6th Cir. 2004) (applying Tennessee law). An insurer may still litigate whether coverage existed in the first place. *Clark v. Sputniks, LLC,* 368 S.W.3d 431, 438 (Tenn. 2012).

Texas: "[A]n insurer who has wrongfully refused to defend its insured is barred from collaterally attacking a judgment or settlement between the insured and the plaintiff." *Great Am. Lloyd's Ins. Co. v. Vines-Herrin Custom Homes, LLC*, 596 S.W.3d 370, 375 (Tex. App. 2020). Prior case law held the insurer was barred from challenging reasonableness. *Evanston Ins. Co. v. ATOFINA Petrochemicals, Inc.*, 256 S.W.3d 660, 671 (Tex. 2008). However, the Texas Supreme Court has backtracked and held that "an insurer's wrongful failure to defend is no longer dispositive," and "shifted focus toward whether the underlying judgment accurately reflects the plaintiff's damages and thus the insured's covered loss." *Great Am. Ins. Co. v. Hamel*, 525 S.W.3d 655, 665 (Tex. 2017). With the non-adversarial judgments not binding, the parties are "back to square one" on the question of the liability under the insurance policies. *Eagle Supply & Mfg., L.P. v. Landmark Am. Ins. Co.*, 630 S.W.3d 342, 354 (Tex. App. 2021).

In other words, though the decision to deny defense may initially save the insurer expenses, it could end up being a penny-wise, but pound-foolish, endeavor.

Utah: An insurer who refuses to defend will free the insured to enter into a settlement, and the insurer will be bound by any reasonable compromise or settlement. *Gibbs M. Smith, Inc. v. U.S. Fid. & Guar. Co.*, 949 P.2d 337, 344 (Utah 1997). A covenant not to execute does not cure the bad faith conduct of the insurer. *Campbell v. State Farm. Mut. Auto. Ins. Co.,* 840 P.2d 130 (Utah Ct. App. 1992). This case resulted in a punitive damages award in the amount of $145 million, which was taken all the way to the U.S. Supreme Court. The high court determined that a punitive damages award of $145 million on $1 million

in compensatory damages violated due process. *State Farm Mut. Auto. Ins. Co. v. Campbell,* 538 U.S. 408, 429 (2003). Utah recognizes the insurer's liability from an unexecuted judgment entered against the insured. *Christianson v. Holiday Rent-A-Car,* 845 P.2d 1316, 1322 (Utah Ct. App. 1992) (citing *Ammerman v. Farmers Ins. Exch*, 450 P.2d 460 (Utah 1969)).

Virginia: An insurer which denies coverage waives the consent requirements under the policy. *Nationwide Mut. Fire. Ins. Co. v. Erie Ins. Exch.,* 829 S.E.2d 731, 734-35 (Va. 2019). Absent fraud or collusion, the insurer cannot collaterally attack a consent judgment entered into between an insured and an injured party. *Liberty Mut. Ins. Co. v. Eades,* 448 S.E.2d 631, 633 (Va. 1994). A covenant not to execute does not relieve the insurer of its obligation to indemnify. *Beckner v. Twin City Fire Ins. Co.,* No. CL01-642, 2002 WL 31432445, at *6 (Va. Cir. Ct. 2002).

Washington: If an insurer in bad faith refuses to settle, the insured may settle the claim, and the insurer will be liable so long as the settlement is reasonable and in good faith. *Steel v. Olympic Early Learning Ctr.,* No. 50981-4-II, 2019 WL 2291306, at *4 (Wash. Ct. App. May 29, 2019); *Gosney v Fireman's Fund Ins. Co.*, 419 P.3d 447, 463-64 (Wash. Ct. App. 2018). Reasonableness hearings as required by Wash. Rev. Code §4.22.060 apply to covenant judgments. *Bird v. Best Plumbing Group, LLC,* 287 P.2d 551, 557 (Wash. 2012). There is a nine-factor test for reasonableness. *Wood v. Milionis Constr., Inc.,* 429 P.3d 813, 822 (Wash. 2021). Where the insurer acts in bad faith, the amount of the judgment can exceed policy limits. *Bird v. Best Plumbing Group, LLC,* 287 P.3d 551, 555 (Wash. 2012). The typical agreement includes a covenant not to execute. *Id.*

Wisconsin: An insurer which refuses to defend does so at its own peril, loses the right to control the defense or settlement, and will have to pay for the defense if it is reasonable and coverage is found. *Patrick v. Head of the Lakes Co-op Elec. Ass'n,* 295 N.W.2d 205, 209 (Wis. Ct. App. 1980). A stipulated order of judgment and an assignment of indemnification claims was executed. *Deminsky v. Arlington Plastics Machinery,* 657 N.W.2d 411, 414 (Wis. 2003). The Court found that the indemnity agreement was valid and could be enforced. *Id*. at 428.

Wyoming: An insured may enter into a reasonable settlement agreement where the insurer acts in bad faith in refusing to settle within policy limits or breaches the duty to defend. *Crawford v. Infinity Ins. Co.,* 139 F.Supp.2d 1226, 1231 (D. Wyo. 2001), *aff'd*, 64 Fed. Appx. 146 (10th Cir. 2003). However, where the insured and injured party enter into a consent judgment, *res judicata* will not apply to bar the litigation of issues by the insurer. *Eklund v. Farmers Ins. Exch.*, 86 P.3d 259, 265 (Wyo. 2004). "[T]he inclusion of a covenant not to execute in the settlement agreement between an insured and a claimant … 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." *Gainsco Ins. Co. v. Amoco Prod. Co.*, 53 P.3d 1051, 1061 (Wyo. 2002). However, the settlement still must be reasonable, and that is a question of fact. *Id*. at 1071-72.

States which have not Addressed the Issue

Kentucky: Kentucky has allowed a consent judgment and assignment as it pertains to an insurance agent but has not opined as to an insurer. *Associated Ins Serv, Inc v Garcia*, 307 S.W.3d 58, 64 (Ky. 2010).

Vermont: While not directly considering the issue, the Vermont Supreme Court has allowed an insured's assignees to litigate coverage questions. *Serecky v. Nat'l Grange Mut. Ins.*, 857 A.2d 775, 777 (Vt. 2004).

Conclusion

Though it may seem like denying defense would be a cost-saving measure, it can end up costing the insurer dearly in the end. The insurer risks a consent judgment, which—as noted above—in many jurisdictions precludes the insurer from challenging underlying liability. Indeed, an insurer can end up facing a judgment far in excess of what a jury likely would have awarded, without the benefit of discovery in the underlying case, without being able to challenge the amount other than for overall "reasonableness," and stripped of all defenses other than the lack of coverage afforded to the underlying allegations in the first place. A subsequent lawsuit or garnishment action against the insurer is likely. Thus, while underlying litigation expenses may be saved, there are likely to be direct litigation expenses to the insurer in the coverage dispute. On all-but-certain cases of non-coverage, the prudent course is to advise the insurer to defend subject to a reservation of rights. However, one must be cognizant of the law of the particular jurisdictions. As discussed, a few states find that even defending under a reservation of rights may free the insured of its duty to obtain consent prior to settlement.

In other words, though the decision to deny defense may initially save the insurer expenses, it could end up being a penny-wise, but pound-foolish, endeavor. For this reason, many insurers, perhaps begrudgingly, will proceed to defend subject to a reservation of rights and engage separate counsel to litigate the coverage dispute in a declaratory judgment action. In fact, some courts, such as those in Michigan, have explicitly noted that "defending under a reservation of rights is the preferred option." *Central Mich. Bd. of Trustees v. Employers Reinsurance Corp*, 117 F.Supp.2d 627, 632-33 (E.D. Mich. 2000).

Insurers have a variety of options when confronted with a decision to deny defense in a lawsuit in which their insureds are named as defendants. While some allow the assigned claims adjuster to make the decision, others are more prudent and will consult with an in-house or outside attorney. The attorney will presumably have considered the law applicable in the jurisdiction and how a trial judge may view the insurer's obligation. An attorney familiar with the judiciary of the particular jurisdiction may be able to offer insight into how the specific judge assigned to the underlying case may view the insurer's obligation; this insight may be invaluable, as most states have rules that cases arising out of the same subject matter be assigned to the same jurist. In short, the assistance of counsel can be crucial in making the initial decision as to whether to defend the insured—a decision that can have far-reaching and potentially expensive consequences.