

Failure to Obtain Consent Negates Coverage for Settlement

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The United States Court of Appeals for the Fourth Circuit, looking both to Maryland law and Tennessee law, has held that an insured's breach of a policy provision requiring it to obtain the insurer's consent before settling any claim negates coverage without regard to whether the insurer was prejudiced by the breach. *Perini/Tompkins Joint Venture v. ACE Am. Ins. Co.*, 2013 WL 6570947 (4th Cir. Dec. 16, 2013).

The case involved primary and excess commercial general liability policies issued by the same insurer to a construction company hired to build a hotel. During the course of the project, part of the building collapsed, causing significant property damage and delaying completion of the hotel. The owner of the hotel subsequently sued the construction company. Without providing notice of the suit to its insurer and without seeking or obtaining consent from its insurer, the insured settled the claim and agreed to credit the hotel owner approximately \$26 million toward the balance due under the parties' original contract.

More than six months later, the insured sought to recover the settlement amount under its policies. The insurer denied coverage, taking the position that the insured breached the "voluntary payment clause" in the policies, which provided that "[n]o insured will, except at that insured's own cost, voluntarily make a payment, assume an obligation, or incur any expense . . . without [the insurer's] consent." The insurer also relied on the policies' "no-action clause," which provided that an insured may sue to recover on a settlement only if the settlement is one agreed to and signed by the insurer.

In the coverage litigation that followed, the parties did not dispute that the insured failed to seek and to obtain the insurer's consent to the settlement. The construction company did, however, argue that regardless of whether the court followed the law of Maryland or Tennessee, a showing of prejudice was required to support a denial of coverage based on the voluntary payment and no-action clauses. The court disagreed, first pointing out that the prejudice requirement imposed by Section 19-110 of the Maryland Code is limited to instances in which coverage is denied based on late notice or lack of cooperation. The court noted that the state intermediate appellate court has held that the statute should not be read "to be applicable to any defense raised by the insurer" and that it is "inapplicable when an insurer defends on the basis that its insured failed to meet the condition precedent set forth in a no-action clause." The court further read the same state court decision as holding that "an insured's failure to obtain the insurer's prior consent to a settlement does not ever require prejudice," even under the common law of Maryland, because an insurer

would always have “the impossible burden . . . of showing collusion or demonstrating, after the fact, the true worth of a settled claim.” Based on this logic, the court also predicted that the highest court in Tennessee likewise would conclude that an insurer presented with a settlement as a *fait accompli* need not demonstrate prejudice to disclaim coverage.

Additionally, the court concluded that, even if a showing of prejudice was required, the result would be the same here because an insurer is prejudiced as a matter of law when an insured delays notifying the insurer of a claim until after its resolution. In this regard, according to the court, the delay vitiates the insurer's rights under the policies, including the insurer's rights to investigate, defend, control, and settle the suit against its insured.