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ALERT

Violation of Consent to Settle Clause Precludes Coverage for Consent Judgment

March 23, 2012

Applying Louisiana law, the United States Court of Appeals for the Fifth Circuit has held that a consent judgment entered into between an insured and a claimant is not enforceable by the claimant against an insurer because the parties violated the policy's "no action" clause by failing to comply with the "consent to settle" clause. *New England Ins. Co. v. Barnett*, 2012 WL 715261 (5th Cir. Mar. 6, 2012). In addition, the court held that a bad faith action cannot lie in the absence of an excess judgment.

A claimant brought an action against his former business partner, whose insurer agreed to provide a defense of the claim subject to a reservation of rights. The claimant later amended the suit to add claims for legal malpractice and additional defendants, including the insurer. The parties, including the insurer, initially engaged in settlement negotiations, which proved unsuccessful. The claimant and the insured business partner later settled the matter without the insurer's involvement and agreed to the entry of a consent judgment, whereby the insured assigned his rights against the insurer to the claimant upon the claimant's agreement not to execute the full amount of the judgment against the insured. The insurer subsequently filed suit seeking a declaratory judgment that it was not liable to the claimant for the consent judgment, and the claimant filed a counterclaim against the insurer under Louisiana's direct action statute alleging bad faith and seeking damages in excess of the consent judgment.

The court held first that the consent judgment was not enforceable against the insurer pursuant to the policy's "no action" clause, which stated that "no action shall lie against the Company unless . . . the Insured shall have fully complied with all the terms of this policy." The

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policy contained a "consent to settle" clause, which prohibited the insured from entering into a settlement without the insurer's consent, except at the insured's own cost. Here, because the insurer had not consented to the settlement between the insured and the claimant, the court held that the "no action" clause precluded enforcement of the consent judgment. In so holding, the court rejected the claimant's argument that the "consent to settle" clause violates Louisiana public policy, finding instead that Louisiana courts enforce such provisions unless an insurer wrongfully denies coverage or refuses to participate in settlement negotiations. Here, the insurer agreed to provide a defense of the claim and had made a settlement offer, which the court deemed not unreasonable. Accordingly, the court concluded that the provision was consistent with public policy, and thus the insured's violation of the provision barred enforcement of the consent judgment pursuant to the policy's "no action" clause.

Finally, the court addressed the claimant's bad faith claim. Under Louisiana law, an insurer cannot be liable for bad faith failure to settle in the absence of an adjudicated excess judgment. Here, no such judgment existed. The claimant argued that an excess judgment was still possible because the insured's liability was not tried. The court rejected this argument, finding that the settlement between the claimant and the insured meant that the claims against the insured would never be tried. Thus, because there was no possibility of an excess judgment, the insurer could not be held liable for bad faith.