

District Court Grants Summary Judgment to Insurer Under "Consent to Settlement" Provision; Denies Summary Judgment on Alleged Breach of Duty to Defend

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The United States District Court for the Northern District of Illinois has granted summary judgment to an insurer, determining that the definition of "loss," the cooperation clause, and a "benefits due" exclusion all applied to bar coverage for the insured's unauthorized settlement with its former partners in a dispute regarding benefits due under an ERISA plan. *Fed. Ins. Co. v. Arthur Andersen LLP*, 2005 WL 1838440 (Aug. 2, 2005). However, the court denied summary judgment on the parties' cross-motions regarding whether the insurer had breached its duty to defend the insured and, accordingly, also denied summary judgment on whether the insurer was estopped under Illinois law from asserting the preclusive coverage defenses. The court also denied the insurer's motion regarding the insured's claim under Section 155 of the Illinois Insurance Code, determining that a question of fact existed as to whether the insurer's six-month delay in issuing a coverage decision constituted "vexatious and unreasonable conduct" as required by that statute.

The insured obtained an "Executive Protection Policy" that included fiduciary liability coverage from the insurer. The policy specifically defined "Wrongful Act[s]" with respect to "Sponsored Plan[s]" (e.g., employee benefit plans) as "any breach of responsibilities upon fiduciaries imposed by ERISA . . . or law of the United States . . . and any negligent act, error or omission in the Administration of any Sponsored Plan." The policy required the insured to cooperate with the insurer in connection with any claim, and to obtain written consent from the insurer for settlement of any claim in excess of \$250,000. The policy excluded coverage for any loss that "constitutes benefits due or to become due under the terms of a Benefit Program . . . [meaning] any Sponsored Plan."

The underlying claim arose in March 2002, when a group of retired partners of the insured sued to obtain a lump-sum distribution of their retirement benefits in the wake of the insured's "well-publicized difficulties." Among the causes of action cited in the two suits were breach of the partnership agreement and breach of fiduciary requirements for managing the retirement plan. In May 2002, the insured's broker notified the insurer by letter of the two suits, and asked for consent to the insured's choice of counsel. The letter, however, did not request that the insurer join in the defense of those suits. The insurer acknowledged the notice, and reserved

rights under the policy. The insurer also called the broker to ask "several questions" immediately thereafter, and the broker agreed to obtain the requested information.

In June 2002, the insurer emailed the broker, noting that it had yet to receive the documentation previously requested. The insured provided the requested information in August 2002. In September 2002, the insured provided the insurer with an amended complaint, an arbitration demand, and a group of "election letters" from the retired partners demanding payment from the insured under the terms of the partnership agreement. In November 2002, the insurer denied coverage and declined to participate in settlement of the litigation. In January 2003, the insured settled under terms that released the insured and an individual insured from "any Claim against any person or entity for damages based on loss of Basic Retirement Benefits . . ." in return for \$168 million. The insurer subsequently initiated a declaratory judgment action regarding its alleged obligations under the policy.

In 2004, the court granted summary judgment to the insured with respect to whether the initial complaint triggered a duty to defend under the policy. At that time, however, the court did not rule on whether the insurer had breached that duty through its course of conduct. The insured subsequently moved for summary judgment regarding the breach and asserted, *inter alia*, that, if the carrier had breached its duty to defend, it was estopped from asserting any coverage defenses. The insurer cross-moved on the estoppel issue, certain coverage defenses, and the insured's counter-claim under Section 155 of the Illinois Insurance Code.

With respect to the insured's motion, the court first considered the argument that the insurer breached its duty to defend by waiting too long after it had received notice of the initial claim to seek a declaratory judgment regarding its coverage obligations. The court noted that an insurer has an obligation to respond in a timely manner, but that if the insured does not respond in a cooperative fashion, the insurer may be relieved of its duty to defend. The court, citing the delay in filing the declaratory judgment and the insured's failure to respond promptly to information requests, concluded that whether the insured was unresponsive was a disputed issue of material fact and denied summary judgment. With respect to the cross-motions regarding the insured's argument that the insurer should be estopped from asserting defenses to coverage due to its alleged tardy response to the claim, the court concluded that the same material issue of fact that precluded a determination on whether the duty to defend was breached likewise precluded a determination of whether estoppel applied to bar coverage defenses.

Despite its determination regarding the duty to defend and estoppel issues, the court considered the insurer's summary judgment motion on the coverage defenses, noting that coverage questions were issues of law it could resolve regardless of whether estoppel ultimately applied to bar the insurer's defenses to coverage. Accordingly, with respect to the policy's definition of "Loss," the court indicated that the policy's definition required that Loss result from a "Wrongful Act." It thus determined that the election letters provided as claims to the carrier were not covered because they did not allege any Wrongful Act. The court then noted that, while the claims arising from the lawsuits and the arbitration demands did allege Wrongful Acts and thus might give rise to Loss, the insurer's other coverage defenses barred coverage.

In that regard, the court concluded that the policy's cooperation clause and the "benefits due" exclusion both barred the insured's claim. With respect to the cooperation clause, the court cited the failure of the insured to obtain the carrier's written consent in advance of the \$168 million settlement as a breach preventing coverage. In doing so, it explicitly rejected the insured's argument that all the insured was required to do was give the insurer the opportunity to consent, finding that contention at odds with the policy's plain language. Similarly, the court determined that the "benefits due" exclusion unambiguously applied, as the underlying claimants sought retirement benefits governed by ERISA, notwithstanding the insured's efforts "to characteriz[e] its loss otherwise."

Finally, the court denied the insurer's motion on the Section 155 claim, through which the insured sought attorney's fees and other litigation costs due to the insurer's alleged unreasonable delay and "vexatious" manner. According to the court, in order to determine whether an insurer has been "vexatious and unreasonable," the totality of the circumstances must be considered. Citing the material factual dispute identified with respect to the alleged breach of the duty to defend, the court indicated that a reasonable jury could rely upon the six-month delay in responding to the notice to determine that the insurer's conduct was vexatious and unreasonable. Therefore, the court determined a material issue of fact remained in dispute and denied the carrier's motion for summary judgment on this issue.

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