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Breaching Insurer's Liability Not Capped, Nev. Justices Say

By **Jeff Sistrunk**

Law360 (December 14, 2018, 6:12 PM EST) -- The Nevada Supreme Court ruled Thursday that an insurance company that breaches its duty to defend its policyholder can be held liable for "consequential damages" beyond the policy limits even if it didn't act in bad faith, allowing a traffic accident victim to proceed with his claim that Century Surety Co. must cover an \$18 million judgment he obtained against Century's insured.

Answering a certified question from a Nevada federal court, the state justices refused Century's call to adopt the majority view taken by courts around the country — that a breaching insurer's liability is generally capped at its policy limits, plus any defense costs that a policyholder paid out of pocket due to the breach.

Instead, the Nevada high court endorsed the minority view — that damages for an insurer's breach of its defense duty are not "automatically limited" to the amount of the policy, but rather depend on the facts of each case. Under that approach, the damages total may include consequential damages tied to the insurer's breach, such as a judgment against the policyholder that exceeded the policy limits, the justices found.

Here, Century's policyholder, Blue Streak Auto Detailing LLC, was hit with an \$18 million default judgment after the insurer refused to defend it in a lawsuit alleging that company owner Michael Vasquez negligently struck Ryan Pretner with his truck, leaving Pretner with severe brain injuries. With the Nevada high court's ruling, Pretner and his legal guardian, Dana Andrew, can press their bid to put Century on the hook for the entire judgment.

"Unlike the minority view, the majority view places an artificial limit to the insurer's liability within the policy limits for a breach of the duty to defend," Chief Justice Michael L. Douglas wrote for the unanimous court. "That limit is based on the insurer's duty to indemnify but '[a] duty to defend limited to and coextensive with the duty to indemnify would be essentially meaningless; insureds pay a premium for what is partly litigation insurance designed to protect ... the insured from the expense of defending suits brought against him.'"

The long-running coverage dispute dates back to January 2009, when Pretner was hit by Vasquez's truck as he was riding his bike on the shoulder of a road in Henderson, Nevada. According to court documents, the accident left Pretner with permanent brain injuries requiring lifelong care.

At the time, Vasquez's mobile auto detailing business, Blue Streak, held a \$1 million commercial general liability policy with Century, court filings indicate. The insurer refused to cover the

accident after investigating and concluding that the CGL policy didn't apply because Vasquez wasn't driving his truck in the "course or scope of his employment" with Blue Streak at the time of the crash, according to court documents.

Pretner and Andrew proceeded to sue Vasquez and Blue Streak in Nevada state court in January 2011, alleging that Vasquez was driving in the course of his employment when he struck Pretner. Century, however, declined to defend Blue Streak and its owner, leading them to default in the case, according to court filings.

In October 2011, Vasquez and Blue Streak agreed to a settlement under which Pretner and Andrew would not seek to recover any eventual judgment out of their personal assets, according to court documents. In exchange, Blue Streak assigned its rights under the Century policy to the accident victim and his guardian, court papers say.

Following an April 2012 hearing, a Nevada judge entered the \$18 million default judgment against Vasquez and Blue Streak based on the conclusion that "Vasquez negligently injured Pretner, that Vasquez was working in the course and scope of his employment with Blue Streak at the time, and that consequently Blue Streak was also liable." According to court papers, Vasquez and Blue Streak offered no defense to the claims.

Wielding the assignment of Blue Streak's policy rights, Pretner and Andrew then sued Century, asserting that the insurer must pay the full judgment because it breached its duty to defend the auto detailing company.

In a series of decisions issued over several years, U.S. District Judge Andrew Gordon held that, while Century had not acted in bad faith, it had indeed flouted its duty to defend Blue Streak. The judge initially found that Century's liability for its breach was capped at the \$1 million policy limit, but later reconsidered and said the insurer could potentially be held liable for the default judgment. However, the judge said that a jury must weigh whether the October 2011 settlement and subsequent judgment were the result of fraud and collusion.

At the urging of both sides, Judge Gordon agreed in August 2017 to ask the Nevada Supreme Court to decide whether a breaching insurer can be held liable for consequential damages. He stayed the case pending an answer on that question.

In Thursday's decision, the Nevada high court sided with Pretner and Andrew, saying that an insurer that refuses to defend its policyholder "takes the risk not only that it may eventually be forced to pay the insured's legal expenses but also that it may end up having to pay for a loss that it did not insure against."

"Accordingly, the insurer refuses to defend at its own peril," Chief Justice Douglas wrote.

The state high court further held that a claimant doesn't need to show that an insurance company acted in bad faith in order to recover consequential damages tied to the insurer's breach. Citing the Michigan Supreme Court's 1982 decision in *Stockdale v. Jamison*, the Nevada justices said that, because an insurer's duty to defend arises from contractual obligations, a breach of that duty can be determined objectively "without reference to the good or bad faith of the insurer."

"In other words, an insurer's breach of its duty to defend can be determined objectively by comparing the facts alleged in the complaint with the insurance policy," Chief Justice Douglas wrote. "Thus, even in the absence of bad faith, the insurer may be liable for a judgment that exceeds the policy limits if the judgment is consequential to the insurer's breach."

But the state high court added that its decision doesn't mean that "an entire judgment is automatically a consequence of an insurer's breach" of its defense duty. The scope of an insurer's liability for a breach will depend on the "unique facts" of a given case and should be determined by a jury, the justices said.

"Rather, the insured is tasked with showing that the breach caused the excess judgment and 'is obligated to take all reasonable means to protect himself and mitigate his damages,'" Chief Justice Douglas wrote.

The Nevada high court did not decide whether Pretner and Andrew can collect the entire default judgment from Century and returned the case to Judge Gordon's court.

Dennis M. Prince of Eglet Prince, who represents Andrew and Pretner, told Law360 that the decision "is probably one of the most significant opinions regarding insurance law in the past 25 or 30 years, given the breadth of the Nevada Supreme Court's holdings on an insurer's duty to defend and the consequences of a breach of that duty."

"Under this opinion, insurers now stand equal to every litigant in terms of being held liable for consequential damages of their wrongful conduct," Prince said. "There will not be any artificial limit on a claimant's ability to recover where an insurer has breached its duty to defend."

Counsel for Century did not immediately respond to a request for comment Friday.

Century is represented by Martin J. Kravitz of Christian Kravitz Dichter Johnson & Sluga, James Ric Gass and Michael S. Yellin of Gass Weber Mullins LLC and Maria L. Cousineau of Cozen O'Connor.

Andrew is represented by Dennis M. Prince of Eglet Prince.

The case is Century Surety Co. v. Dana Andrew et al., case number 73756, in the Supreme Court of the State of Nevada.

--Editing by John Campbell.

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