The case of the missing insured: A tricky variation on the consent to settle

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There can be no dispute that a "consent to settle" clause in a professional liability insurance policy may impede settlement. As one court acknowledged, these clauses will inevitably have the effect of sapping party resources and unduly consuming judicial time and resources.[1]

Yet, for many professional liability matters, that impediment to settlement is as essential as commercial general liability claims-auto claims and the like. A professional's acknowledgement of liability can significantly damage a sterling reputation cultivated over the course of an entire career.[2] Further, reputational damage can adversely impact the professional's ability to apply for new or continuing state licensure, buy affordable insurance and seek future employment.

This reality is especially acute for medical professionals, as certain state and federal databases, such as the National Practitioner Data Bank, track trials and settlements involving allegations of medical malpractice. Hence, the professional's reputation, as well as any liability for alleged injuries, is at the center of any lawsuit resulting from alleged malpractice.

Insurer-insured disputes focusing on consent to settle clauses typically involve savvy and informed professionals who are keenly aware of the impact that an acknowledgement of liability would have on their reputations. Sometimes, however, insurers become embroiled in quagmires involving an absent insured who cannot consent to a settlement.

> There are a number of pitfalls awaiting defense counsel when the insured is missing and there is no other party to the insurance contract capable of acting on the insured's behalf.

Accordingly, an insurer and its retained defense counsel are stuck trying to extricate the insurer (and the insured) from a likely unfavorable situation. The insurer explores questions about whether the settlement is enforceable, whether defense counsel has complied with the rules of professional conduct, and whether the insurer is acting in good faith in settling the case.

Usually, the latter means terms that are favorable to the insured, not requiring the insured to contribute to the settlement. Looking more closely at these scenarios can provide guidance on how to best resolve and prevent these circumstances with efficiency and finality.

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WHAT DO CONSENT-TO-SETTLE CLAUSES LOOK LIKE?

Consent-to-settle clauses, also referred to as "pride" clauses, can take various forms. One common form is the classic consent provision, where an insured may veto a settlement without any ramification.[3] A classic consent provision states, "We will not settle any claim without your written consent, which shall not be unreasonably withheld."

Another common form is the "full hammer" provision. If the insured refuses to consent to a settlement endorsed by the insurer, the insurer's liability for the cost of defense and indemnity is capped at the amount of the endorsed settlement. The insured is then responsible for any attorney fees and judgment in excess of the endorsed settlement amount.[4]

A typical hammer provision states as follows:

> The company shall … not settle any claim without the written consent of the named insured, which consent shall not be unreasonably withheld. If, however, the named insured refuses to consent to a settlement recommended by the company and elects to contest the claim or continue legal proceedings in connection with such claim, the company's liability for the claim shall not exceed the amount for which the claim could have been settled, including claims expenses up to the date of such refusal, or the applicable limits of liability, whichever is less.[5]

Notably, there exists a modified-hammer provision, which operates similar to the classic hammer provision, yet the insured is liable only for a percentage of any judgment

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in excess of the endorsed settlement — usually between 50 percent and 70 percent.

YOUR OPTIONS WHEN CONFRONTED WITH AN ABSENT INSURED

There are myriad court opinions and great scholarship devoted to scenarios involving an insurer that wants to settle a lawsuit or claim and an insured who wants to clear the company name and take the case to trial. What to do, though, when the policy contains a consent-to-settle provision and the named insured does not affirmatively refuse to endorse or veto settlement, or is not deliberately withholding consent, is unclear and not well explored. Such a scenario, where the insured is missing or totally nonresponsive, does occur.

The challenges facing the insurer under this scenario are real and vexing, as the insurer generally has the burden of obtaining the insured's consent prior to settlement. As problematic as the challenges faced by the insurer are, defense counsel has its own set of serious problems.

It is not atypical for an insured to engage in a healthy debate with defense counsel and the insurer about the strategy of a would-be settlement. Some insured parties may find it difficult to accept what may feel like a concession by entering into a settlement and may spar with counsel on this point. In either case, however, the insured is, at the very least, actively engaged in the process.

A potentially more troublesome problem for the insurer and defense counsel arises in the case of an absent or missing insured.[6] There are a number of pitfalls awaiting defense counsel when the insured is missing and there is no other party to the insurance contract capable of acting on the insured's behalf.[7]

In 2012, the FBI's National Crime Information Center entered over 650,000 missing-person records, albeit many of which were cleared or canceled.[8] So, it is not too farfetched to consider the reality that the insured may unexpectedly "enter radio silence."

One option for the attorney of a missing client is to turn to the local bar association or ethics board for guidance. The American Bar Association, along with several state and local bar associations, has considered this issue and published opinions concerning an attorney's ethical challenges in the face of a missing client.[9] Several rules of professional conduct are instructive here.

Fundamentally, defense attorneys and insurers may not enter into a binding settlement on behalf of the insured without consent. Pursuant to Model Rule of Professional Conduct 1.2(a), "a lawyer shall abide by a client's decision whether to settle a matter." Without exception, a lawyer may not circumvent the delegation of authority to the client in Rule 1.2(a).[10] While an attorney has implicit authority to act on behalf of the client with respect to certain procedural matters, the decision to settle is exclusively the client's.

> In the case of a missing insured, defense counsel must use all the resources at their disposal to find a client who may not want to be found.

Next, the attorney may need to perform some detective work. In light of Model Rule 1.4, an attorney is obligated to keep the client reasonably informed about the status of the matter and to promptly inform the client of any development requiring the client's informed consent.

Accordingly, attorneys are tasked with taking "reasonable steps" to locate and inform their clients of the status of settlement discussions or other critical developments. Of course, as is the case with many ethical dilemmas, the definition of "reasonable" may vary.

In an era of GPS monitoring, social media and other technological advances, there are various tools available to counsel to search for a missing client. At a minimum, attorneys can be expected to call, email and write to the client at the last known residence and place of employment. According to a 1996 North Carolina ethics opinion, an attorney's efforts to reach the client were deemed "more than reasonable" when she attempted to locate the client via the client's health care providers, medical insurance carrier and county property listings.

Internet search engines, social networking sites, public record searches and private investigators may also provide valuable insight. Moreover, these steps, when well documented, may provide risk management support for an attorney in the event that the insured resurfaces and questions the attorney's conduct.

The attorney who has taken reasonable steps to locate a missing client may not be stuck defending the case in perpetuity. In certain circumstances, a client's failure to respond to counsel within a reasonable time may be considered a constructive discharge. Of course, the client has obligations to counsel, and the failure to meet those responsibilities may prevent the attorney from providing effective representation.

In this scenario, Model Rule 1.16 may allow the attorney to withdraw from the representation under these circumstances. To that end, in some jurisdictions, a client's disappearance constitutes appropriate grounds for the lawyer's withdrawal.[11]

PRACTICE TIPS AND CONCLUSION

Consent to settle provisions in an insurance policy were designed to create an impediment to settlement in order to protect the policyholder's reputation. Where insured parties are missing by their own volition (*e.g.*, to escape civil or criminal liability), the policyholder's reputation may be beyond repair.

The requirement for the policyholder to consent to a settlement remains, though. That requirement presents difficult challenges for insurers and defense counsel alike, potentially thwarting any attempt to settle the insured's civil liability on a favorable basis.

We offer the following practice tips to protect defense counsel from potential breaches of their ethical duties to their clients:

- Use a detailed client intake questionnaire and regularly update the client's contact information.
- Document any difficulty in communicating with the client and inform the client of the importance of maintaining consistent communication.
- Take all reasonable steps to locate a client if the client does not timely respond to an inquiry — do not allow significant time to pass without communicating with your client.

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- Document in great detail the steps taken by counsel to locate a missing client.

Defense counsel are better equipped today to find missing persons than ever before. That fact, however, raises expectations, increasing the pressure on defense counsel to deliver the policyholder defendant. Creativity and ingenuity are some of the hallmarks of successful defense counsel. In the case of the missing insured, defense counsel must use all of the resources at their disposal to find a client who may not want to be found.

Additionally, we offer practice tips to protect the insurer from exorbitant verdicts and potential subsequent bad faith exposure:

- Document all instances of non-cooperation by the insured with requests from the insurer or retained defense counsel.
- Immediately begin sending reservation of rights letters citing the policy's cooperation clause and the impact of future non-cooperation.
- As soon as the insurer has suffered significant prejudice, file a declaratory judgment action seeking a declaration that the insured committed a material breach of a condition precedent of the policy (to the extent that your jurisdiction recognizes these principles).

Insurers with a missing insured are likewise placed in an unenviable position with respect to settlement. Insurers may still have hope, however, in the form of a cooperation defense. To preserve that hope, it is imperative that the insurer document the bases for defense from the outset and contemporaneously.[12] Taking the necessary steps to gain proof for a cooperation defense can mean all the difference between an insurer being stuck in an intractable quagmire and walking away relatively unharmed. WJ

NOTES

[1] *See Webb v. Witt*, 876 A.2d 858 (N.J. Super. Ct. App. Div. 2005); *see also Hurvitz v. St. Paul Fire & Marine Ins. Co.*, 109 Cal. App. 4th 918 (Cal. Ct. App. 2003) ("The decision to settle rather than continue litigation invariably involves a conflict between the desire to vindicate oneself and the desire to minimize the costs of litigation and avoid the risk of loss.").

[2] *See Clauson v. New England Ins. Co.*, 83 F. Supp. 2d 278, 281 (D.R.I. 2000), *aff'd*, 254 F.3d 331 (1st Cir. 2001).

[3] It is generally recognized that an insured party's consent to settlement is revocable. *See Lieberman v. Employers Ins. of Wausau*, 419 A.2d 417 (N.J. Super. Ct. App. Div. 1980).

[4] Consent-to-settle clauses even apply to settlements within the policy limits. *See Shuster v. S. Broward Hosp. Dist. Physicians' Prof'l Liab. Ins. Trust*, 591 So. 2d 174 (Fla. 2d Dist. Ct. App. 1992) (absent a consent-to-settle clause, an insurer has a right to settle, within the policy limits, any claim it deems appropriate, even arguably frivolous ones). *See Sec. Ins. Co. of Hartford v. Schipporeit Inc.*, 69 F.3d 1377, 1383 (7th Cir. 1995) (acknowledging the enforceability of a classic hammer provision); *Scottsdale Ins. Co. v. Ala. Mun. Ins. Corp.*, No. 2:11-CV-668-MEF, 2013 WL 5231928 (M.D. Ala. Sept. 16, 2013) (The insurer's invocation of the hammer clause was not in "bad faith" as the insurer "was not acting out of a greater concern for its own financial interest than [the insured's] when it refused to continue the defense of [the insured] after [the insured] refused to accept what [the insurer] reasonably believed to be a settlement that was in [the insurer's] best interest.").

[5] *See Freedman v. United Nat'l Ins. Co.*, No. CV-09-5959 AHM CTX, 2011 WL 781919, at *6 (C.D. Cal. Mar. 1, 2011) (citing *Clauson* with approval and holding that the insurer may invoke the hammer clause only if the insured unreasonably refuses to consent to the settlement, relying upon the preceding sentence, which included the language, the insurer "shall … not settle any claim without the written consent of the named insured, which consent shall not be unreasonably withheld").

[6] An attorney's obligations to the client survive the attorney-client relationship, and therefore, an attorney must treat a missing client the same as all former clients.

[7] If defense counsel represents an additional insured, and the named insured is missing, there is yet another layer of complexity to the scenario, as there is a split of opinion regarding whether the consent must be obtained from the named insured, or whether an additional insured may provide the consent to settle. *Compare Jayakar v. N. Detroit Gen. Hosp.*, 451 N.W.2d 518 (Mich. Ct. App. 1989) (finding that the insurer need not seek consent of the additional insured), with *Mosely v. Wilson*, No. CIV. A. 91-0712, 1991 WL 134285, at *2 (E.D. Pa. July 16, 1991) (the insurer must obtain consent from the additional insured if the additional insured and not the named insured is the party defendant).

[8] FBI, National Crime Information Center Missing Person & Unidentified Person Statistics for 2012, *available at* http://www.fbi.gov/about-us/cjis/ncic/ncic-missing-person-and-unidentified-person-statistics-for-2012.

[9] A similar problem facing the plaintiff's bar is the inability to locate a pre-suit client in the face of a pressing statute-of-limitations deadline.

[10] Suzanne Lever, *Where's Waldo*, Ethics Opinion Articles, 16 N.C. State Bar J. (December 2011).

[11] *See* Wash. State Advisory Opinions 1796, 1873 & 2225.

[12] *See State Farm Fire & Cas. Co. v. King Sports Inc.*, 827 F. Supp. 2d 1364 (N.D. Ga. 2011) (To establish a material breach of the cooperation clause, the insurer must demonstrate that it made a reasonable effort to obtain the insured's cooperation); *Cincinnati Ins. Co. v. Irvin*, 19 F. Supp. 2d 906 (S.D. Ind. 1998) (collection of cases) (following the view that the insured's absence from trial, by itself, is insufficient evidence of prejudice for purposes of establishing a breach of the cooperation clause); *see also Hunter Roberts Constr. Group v. Arch Ins. Co.*, 904 N.Y.S.2d 52 (N.Y. App. Div., 1st Dep't 2010) (To prevail on a noncooperation defense, the insurer has a "heavy burden" to prove that it acted diligently and that its efforts "were reasonably calculated to obtain the insure[d]'s co-operation," but the insured still engaged in "willful and avowed obstruction").

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