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# PREVIEW; *Draggin' Y Cattle Company, Inc. v. Junkermier, Clark, Campanella, Stevens, P.C.*: Abandonment as Breach

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The Montana Supreme Court oral argument is scheduled for Wednesday, November 14, 2018, at 9:30 a.m. in the Courtroom of the Montana Supreme Court, Joseph P. Mazurek Justice Building, Helena, Montana. Gary M. Zadick is expected to argue on behalf of the Appellant, New York Marine and General Insurance Company (NYM). Timothy B. Strauch and David R. Paoli are expected to argue on behalf of the Appellees, Draggin' Y Cattle Company, Inc., Roger and Carrier Peters, and Junkermier, Clark, Campanella, Stevens, P.C. (JCCS).

## I. INTRODUCTION

This case presents the Court with the question of whether a settlement agreement is unenforceable because it is unreasonable pursuant to Montana law. Within this broad question, the Court must determine whether the district court correctly found NYM had "abandoned" JCCS as well as whether the district court applied the proper reasonableness standard.

## II. FACTUAL AND PROCEDURAL BACKGROUND

In 2004 Larry Addink, a certified public accountant employed by JCCS, advised the Peters on a structure sale of a conservation easement.[1] Following the sale, Addink learned that he had structured the exchange incorrectly, which exposed the Peters to unanticipated tax liability, and he promptly notified JCCS and its insurer, NYM.[2] JCCS held a $2 million professional liability insurance policy from NYM that required NYM to defend JCCS, ensure defense cooperation between JCCS and NYM, and relieved NYM of indemnifying without prior written approval.[3]

In 2011, the Peters filed the underlying claim now in dispute.[4] NYM filed a reservation of rights stating, in pertinent part,

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[1] Appellees' Answer Brief at 11, *Draggin' Y Cattle Company, Inc. v. Junkermier, Clark, Campanella, Stevens, P.C.*, https://perma.cc/7Z52-2SWV (Mont. June 7, 2017) (No. DA 17-0731).

[2] Appellant's Opening Brief at 2, *Draggin' Y Cattle Company, Inc. v. Junkermier, Clark, Campanella, Stevens, P.C.*, https://perma.cc/QBY3-CVEX (Mont. Apr. 17, 2017) (No. DA 17-0731).

[3] *Id.* at 2.

[4] Appellees' Answer Brief, *supra* note 1, at 17.

that "nothing herein or heretofore should be construed as an admission of coverage for liability."[5] NYM determined that the Peters could recover approximately $250,000 in interest on tax liability from the structured sale.[6] However, NYM did not file a declaratory judgment to clarify the scope of coverage owed to its insured.[7]

In 2014, the Peters offered JCCS a settlement agreement for the $2 million policy limit.[8] NYM declined this offer and countered with $100,000, stating that JCCS would be in breach of contract if it settled directly with the Peters without any involvement from NYM.[9] JCCS wished to settle within policy limits to be protected from any excess verdict, but NYM refused to accept any offer NYM deemed to be "unreasonable."[10]

On November 12, 2014,[11] all of the parties participated in an unsuccessful mediation.[12] Hours later, the Peters and JCCS negotiated a settlement agreement, conditioned upon a court reasonableness hearing, of $10 million directly executed against NYM.[13] The following day, the Peters and JCCS executed the settlement agreement consisting of a $10 million judgment, a covenant not to execute the judgment against JCCS, and the conditions that all rights and claims against NYM be assigned to the Peters, and that Addink would be dismissed from the lawsuit.[14]

On December 11, 2017, in state district court, Judge Eddy held that the $10 million settlement agreement was reasonable and entered judgment against the insureds.[15] In relation to the legal framework, Judge Eddy ordered, "[o]f course, in this case [NYM] was defending under a reservation of rights, which makes it distinguishable from the facts of *Tidyman's*, and [the reasonableness of the stipulated judgment] will be analyzed accordingly by the Court consistent with the framework of [*Freyer*] and related cases."[16]

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[5] *Id*. at 18.

[6] Appellant's Opening Brief, *supra* note 2, at 3.

[7] Appellees' Answer Brief, *supra* note 1, at 19.

[8] *Id*.

[9] *Id*. at 21.

[10] *Id*. at 20.

[11] Two days prior to scheduled hearing of NYM's five summary judgment motions. Appellant's Opening Brief, *supra* note 2, at 3.

[12] *Id*. at 24.

[13] Appellees' Answer Brief, *supra* note 1, at 25.

[14] *Id*. at 26.

[15] Appellant's Opening Brief, *supra* note 2, at 7.

[16] *Id* (citing Dkt. 366). This quotation is not included in Appellees' Answer Brief, *supra* note 1, at 28.

On appeal, NYM raises the following issues: 1) did the district court correctly determine NYM abandoned JCCS; and 2) did the district court correctly conclude the same reasonableness standards apply regardless of the mechanism of abandonment?[17]

## III. SUMMARY OF THE ARGUMENTS

### *A. Appellant's Argument*

Appellant argues that the district court used the incorrect reasonableness standard under *Tidyman's Management Services, Inc. v. Davis*,[18] and *Tidyman's Management Services Inc. v. National Union Fire Ins. Co. of Pittsburgh, PA*,[19] in holding that NYM breached its duty to defend by abandonment despite finding that "this is not a breach of the duty to defend case."[20] Appellant contends that the district court erred by equating abandonment with a breach of the duty to defend when an insurer does not waive its rights and limits under the policy[21] and fails to file an improper declaratory action.[22] Appellant argues that it did not abandon, but rather continuously defended, JCCS throughout the litigation by filing a reservation of rights, providing defense counsel, and tendering reasonable defense costs.[23] Appellant contends ultimately that, since NYM provided a defense, *State Farm Mut. Auto Ins. Co. v. Freyer*,[24] should have been the controlling legal framework in evaluating the reasonableness of the settlement.[25]

### *B. Appellees' Argument*

Appellee argues that the district court used the correct reasonableness standard under *Tidyman*, holding that NYM's "abandonment of its insured is just as certain as if it ha[d] breached the duty to defend."[26] Accordingly, there was "no reason to deviate from the analysis developed to consider the reasonableness of settlement agreements" if NYM had actually breached its duty to defend.[27] Appellee contends that NYM abandoned JCCS by offering

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[17] Appellees' Answer Brief, *supra* note 1, at 8.

[18] 330 P.3d 1139 (Mont. 2014) (*Tidyman I).*

[19] 378 P.3d 1182 (Mont. 2016) (*Tidyman II*) (hereinafter both *Tidyman I* and *Tidyman II* are referred to collectively as "*Tidyman*" within the text).

[20] Appellant's Opening Brief, *supra* note 2, at 9–10.

[21] *Id.* at 10.

[22] *Id*. at 12.

[23] *Id*. at 10–11.

[24] 312 P.3d 403 (Mont. 2013).

[25] Appellant's Opening Brief, *supra* note 2, at 9–10.

[26] Appellees' Answer Brief, *supra* note 1, at 39.

[27] *Id*.

unreasonable insurance protection because they: (1) refused to admit coverage; (2) failed to timely file a declaratory action; and (3) unreasonably refused JCCS' requests to either settle within or waive policy limits,[28] which falls outside of established Montana rules and policy.[29] Appellee contends that as a result, JCCS had no other option but to settle or face liability for any excess judgment.[30] As such, Appellees argue that the *Tidyman* framework was correctly applied in Judge Eddy's ultimate finding that the stipulated settlement was reasonable and thus enforceable.[31]

## IV. ANALYSIS

*Tidyman* was the correct legal framework for deciding the reasonableness of the settlement agreement because JCCS reasonably settled after being abandoned by NYM. The following analysis indentifies the legal frameworks of *Tidyman* and *Freyer*, addressing that, while the present factual dispute falls between both decisions, it ultimately lands far closer to *Tidyman*. Accordingly, the *Tidyman* framework for reasonableness should be applied.

Settlement agreements are required to be reasonable.[32] Although a reasonableness hearing for a settlement agreement is not procedurally required under Montana law, when an insurer has breached its duty to defend a hearing is allowed upon the insurer's request.[33] The Court is not required to evaluate a settlement agreement as collusive when the insurer breaches its duty to defend.[34] A reasonableness hearing is required when an insurer overcomes the presumption that the settlement agreement was reasonable.[35] In *Tidyman I*, the Court found the insurers' actions were an unjustifiable breach of its duty to defend.[36] In assessing the reasonableness of a settlement agreement after the insurer has breached its duty to defend, *Tidyman* considers the objective merits underlying the case and any value a reasonable *uninsured* insured person would gain in exchanging a confessing judgment for a covenant not to execute.[37]

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[28] *Id*. at 30.
[29] *Id*. at 32.
[30] *Id*. at 38–39.
[31] *Id*. at 45.
[32] MONT. CODE ANN. § 27–1–302 (2017).
[33] *Tidyman's I*, 330 P.3d 1139, 1152–1153.
[34] *Id*. at 1156 (Citing *Nielsen v. TIG Ins. Co.*, 2006 U.S. Dist. LEXIS 49002 at 32–33 (2006)).
[35] *Id*. at 1154.
[36] *Id*. at 1152.
[37] *Tidyman's II*, 378 P.3d 1182, 1186.

Next, when an insurer abandons its insured, the insured is justified in taking steps to limit their personal liability.[38] When there is an issue surrounding coverage, insurance companies are not required, but are "repeatedly admonished" to defend the insured and file a declaratory action to establish coverage.[39] Once a declaratory action is filed, a pretrial settlement agreement cannot represent consequential damages contemplated by the insurance parties at the time of contract, unless the insurer breaches its duty to defend.[40] In *Freyer*, the Court held that the insurer properly defended the insured but breached its duty to indemnify, which was determined by general contract principles, resulting in a finding that a settlement agreement is unreasonable for any excess over the policy limit.[41]

This case falls between both *Tidyman*, where a settlement agreement could be found to be unreasonable if the insurer, who breached its duty to defend, overcame the presumption in favor of the insured that the settlement agreement is reasonable, and *Freyer*, where *excess* settlement agreement was found unreasonable for an insurer that defended the insured, filed a declaratory action, but breached its duty to indemnify.

Here, NYM cannot overcome the presumption in favor of JCCS's reasonable settlement with the Peters. Even though NYM's duty to defend is not at issue, the district court equated its conduct (i.e., abandonment) as a constructive breach of the duty to defend, making *Tidyman* as the correct legal framework.[42] While it is not an actual breach of the duty to defend, *Tidyman,* as a controlling framework, is far more relevant as opposed to *Freyer*, where general contract principles were used to determine whether the insurer had breached its duty to indemnify the insured. As NYM pointed out, "this is not a breach of the duty to defend case,"[43] so basic contract principles of *Freyer* are not required in this decision. It is true that NYM provided defense by providing defense counsel, paying reasonable defense costs, and filing a reservation of rights.[44]

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[38] *State Farm Mut. Auto Ins. Co. v. Freyer*, 312 P.3d 403, 413 (Mont. 2013) (Citing *Old Republic Ins. Co. v. Ross*, 180 P.3d 427, 433 (Colo. 2008)).

[39] *Id.* at 415.

[40] *Id.* at 414–15 (Citing *Mont. Petroleum Tank Release Comp. Bd. V. Crumleys*, 174 P.3d 948, 960 (Mont. 2008).

[41] *Id.* at 415–16.

[42] This is logically consistent even if Judge Eddy directly ordered *Freyer* to be the controlling legal framework, as Appellant contends was the case. *See* Appellant's Opening Brief, *supra* note 2, at 7.

[43] *Id.* at 9.

[44] Greg Munro, *The Insurer's Reservation of Rights Letter and the Duty to Defend*. Tr Trends 23, 25 (2001). The reservation of rights is a formal mechanism for an insurer to defend the insured, while asserting that a claim may

However, there are many relevant, material facts that the Court would need to overlook for the *Freyer* framework to be proper. First, like *Tidyman*, where the insurer did not provide a defense, NYM ambiguously denied admitting "coverage for liability" in its reservation of rights.[45] Instead of "adequately and fairly inform[ing] the insured of the nature of the coverage dispute and the insurer's position,"[46] NYM cast a wide net across any liabilities above $250,000, which could leave JCCS responsible for a potential verdict upwards of $10 million. Second, unlike *Freyer*, where the insurer provided defense and filed a declaratory action, NYM could have "circumvent[ed] the clear requirement,"[47] and instead ignored Montana precedent and a "maxim of insurance law"[48] by filing a declaratory action to discern the scope of coverage in addition to defending under a reservation of rights. Finally, NYM's unclear defense strategy implicitly encouraged JCCS to protect themselves by settling directly with the Peters and assigning all judgment against NYM.

Since NYM's actions were equivalent to a breach, Montana law does not procedurally require a court to determine the settlement agreement was reasonable. Instead, the settlement is presumed in favor of JCCS to be reasonable, and no an analysis of collusion is required. Looking at the material facts here, it is reasonable to conclude that the objective merits surrounding JCCS's potential excess liability under NYM's bare bones defense made it far more valuable for JCCS to confess judgment in exchange for a covenant not to execute.

## V. CONCLUSION

Based on the above analysis, the Court will likely find that *Tidyman* was the correct legal framework for deciding this case. JCCS reasonably settled with the Peters because NYM abandoned JCCS in its defense. The district court's ruling should be affirmed.

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fall outside of coverage because it is not covered by the original policy or subject to exclusions.

[45] Appellees' Response Brief, *supra* note 1, at 44.

[46] Munro, *supra* note 42 (citing Clinton E. Miller, *How Insurance Companies Settle Cases*, § 363 (2000)).

[47] *Tidyman's I*, 330 P.3d 1139, 1151.

[48] Munro, *When the Undefended Montana Insured Settles and Assigns Rights in Return for a Covenant Not to Execute*, Tr. Trends 21, 22–23 (2012) (citing *Nielsen v. TIG Ins. Co.*, 442 F. Supp. 2d 972, 976 (2006)).