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Consent to Settlement: A Review of the Recent Supreme Judicial Court Decision in *Rawan v. Continental Casualty Company*

IMPLICATIONS FOR DESIGN PROFESSIONALS AND THEIR INSURERS

Case Highlights

- Court upheld validity of “consent to settlement” provisions in liability insurance policies issued to design professionals (DP)
- Even when unquestionably at fault - and liability is “reasonably clear” - insured may refuse to provide consent
- Reputational interest of DPs in settling liability claim is not inconsistent with obligation of insurers to investigate and settle claims under MGL ch. 93A /176D
- Insurers are not excused from acting in good faith – both toward their insureds and claimants
- *Amicus* (“friend of court”) brief filed by Donovan Hatem, LLP on behalf of ACEC/MA and AIA/MA

The Parties

Dispute arose out of negligent design of structural components in new home construction in Westboro, MA

Homeowners: Douglas and Kristen Rawan

Structural Engineer: Kanayo Lala, P.E.

Insurer: Continental Casualty Company (CNA)

The Policy

Professional Liability Policy issued by CNA contained unusual consent-to-settlement provision (no hammer clause):

> ***"We [the insurer] will not settle any claim without the informed consent of the first Named Insured."***

- Policy limits at time claim made and reported:
  - $500,000 per claim / $1,000,000 in aggregate

- Lower policy limits during subsequent policy year:
  - $250,000 / $500,000

Comparison with Hammer Clause

CNA policy

"[Insurer] will not settle any claim without the informed consent of the first Named Insured."

Typical PL policy language with hammer clause

For **Claims** covered under Coverage A.1, Coverage A.2 or under both Coverage A.1 and A.2, the Company will not settle or compromise the **Claim** without the consent of the **Insured**. Under all Coverages of this Policy, if the **Insured** refuses to consent to a settlement or compromise recommended by the Company and elects to contest such **Claim** or continue legal proceedings in connection with such **Claim**, then the Company's liability for the **Claim** shall not exceed the amount for which the **Claim** could have been so settled plus **Claim Expenses** incurred up to the date of such refusal subject to the applicable limit of liability under this Policy.

Issues Presented

"[W]hether consent-to-settle clauses in professional liability policies violate an insurer's obligations under G.L. ch. 93A and 176D because the insurer has entered into a contract with its insured that provides the insured with a right to consent to, or reject, any settlement offer. More precisely, the issue is whether such a contract conflicts with an insurer's statutory obligation to effectuate a prompt settlement under G.L. c. 176D, §3(9)(f), once liability has been clearly established." *Rawan*, 483 Mass. at 663.

Issues Presented

1. Can “consent to settlement” provisions be reconciled with an insurer’s statutory obligations under G.L. ch. 93A and 176D consistent with public policy concerns?
2. Did insurer act reasonably and in good faith in investigating and (not) settling claim where DP refused to consent to settlement?
3. Can an insurer insulate itself from bad faith liability by relying on the refusal to consent, even if liability is “reasonably clear”?

FACTUAL BACKGROUND

Trial Proceedings and Appeal

PHASE I

- Suit filed by Rawans in August 2011 in Worcester Superior Court
- Complaint alleged negligence, breach of contract, implied warranty and violation of G.L. ch. 93A (consumer protection statute)
- Missteps in case handling, eventually led to trial and jury verdict against DP in amount of **$710,000** - including partial double damage award, interest and attorney's fees
- No appeal from jury verdict and damage award

PHASE II

- Rawans proceed on claim of bad faith against insurer, asserting claims for violations of G.L. chapters 93A and 176D.
- Trial court allowed insurer's Motion for Summary Judgment, and denied Rawans' cross-motion.
- Appeal - SJC took case on direct appellate review bypassing Appeals Court.

Report of Claim / Initial Case Handling

- Prior to filing suit, Lala admitted to client that he had made structural miscalculations in reports filed with the town.
- Adjuster opened pre-claim file – but under wrong policy year with lower policy limits ($250k instead of $500k)
- Early settlement efforts – many stops and starts – were ultimately unsuccessful
- CNA suggested early mediation based on policy limits of $250,000
- In August 2012, defense counsel appointed.

Expert Analysis: Liability established at early stage in proceedings

April 2012

- Rawans' expert (Neil Mitchell, P.E.) identifies multiple structural design errors and deficiencies in structural calculations

July 2012

- CNA retains consulting expert (Thomas Hager, P.E.) to conduct peer review of the structural design

Expert Analysis (*cont.*)

August 2012

- Report issued by N. Mitchell, Rawans' expert:

  "This was the worst example of improper engineering that I have seen in my 45 years of professional practice."

- Report is provided to all parties, including Lala's expert

September 2012

- T. Hager, Lala's expert, completes peer review and issues report:

Expert Analysis (*cont.)*

- Hager confirms all conclusions of plaintiffs' expert: "same serious design errors" and additional errors related to overstresses in repaired beams.

  > *"Sorry for the bad news but… I side with Mitchell's conclusions and concerns for the structural adequacy of this house."*

- Defense expert concludes: (1) structural design did not satisfy minimum requirements of MA Building Code; (2) Lala failed to follow sound structural engineering practices; and (3) Lala did not meet the minimum acceptable standard of care.
- No opinion requested or rendered regarding cost of repair.

Defense of Claims in Trial Court

Discovery disputes

1. Defense counsel argued Hager's report was protected as mediation work product under G.L. ch. 233, §23C
    - Ultimately, Superior court rejected this argument and ordered the report be produced.
2. Defense counsel refused to disclose information regarding policy limits.
    - Court orders this information be provided on a motion to compel.
    - Actual policy limits are disclosed in June 2013 (showing 2x amount of coverage previously communicated to plaintiffs).

Actual fact discovery was minimal

Settlement Discussions

October 1, 2012: Rawans send G.L. ch. 93A demand letters to both CNA and Lala – seeking ***$272,890*** for repairs.

October 9, 2012: CNA rejects demand. Asserts Rawans have not provided sufficient documentation of loss. No counter-offer made.

November 29, 2012: ***With Lala's verbal consent***, CNA makes settlement offer of ***$100,000*** (2 weeks after Hager issued report).

Settlement Discussions (*cont.)*

December 2012: Rawans reject settlement offer. Issue new settlement demand seeking policy limits and state intent to seek additional $ from Lala and CNA for bad faith.

May 2013: Rawans increase settlement demand to ***$1,324,390***.

June 2013: ***After*** close of discovery, defense counsel first retains damages expert. The expert never visits site but opines repair cost of $100,000 - $120,000 based on 10-15 minute conversation with cost estimator.)

December 2013: CNA renews prior settlement offer of ***$100,000*** (with Lala's consent). Offer is rejected.

September 2014 (on eve of trial): Defense counsel makes settlement offer of ***$35,000***. CNA claims it had no prior knowledge of offer made by defense counsel. Rawans respond with reduced demand of ***$900,000***.

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Verdict After Trial

- 6-day jury trial results in plaintiffs' verdict in amount of $400,000.
- Judge awards additional $40,000 for G.L. ch. 93A violation (2x actual damages) plus $87,000 in attorneys' fees.
- Total judgment, including prejudgment interest and 93A award, is **$710,000**.
- Defense costs incurred through trial: $359,000; attorney's fees and costs erode policy limits.
- CNA tenders remaining policy limit of $141,000.
- Balance of judgment, **$569,000**, is paid by Lala.
- No appeal taken.

Phase II: Bad Faith Claims

- In Phase II, case proceeds to questions concerning the consent-to-settlement provision of the policy.
- Parties cross-move for summary judgment.
- Court issues summary judgment in favor of insurer, concluding that the insurer's "hands were tied" because DP did not consent to settle and therefore it was "legally precluded from making efforts to settle."
- Court did not consider whether DP had sufficient information to make an "informed consent" decision, or any other aspect of the pretrial settlement discussions

Parties' Positions on Appeal

Plaintiffs' position

- DP's right to control (and reject) settlement of the claim conflicts with G.L. ch. 176D and violates public policy.
- Insurer violated Chapters 93A and 176D by failing to effect a reasonable settlement after liability became reasonably clear.

Insurer's position

- CNA was obligated to honor insured's refusal to provide consent to settlement.
- In any event, CNA's claims-handling practices were reasonable.

No position taken by DP

Amicus (ACEC / AIA-MA) Positions

Positions advanced by Amicus

- Design professionals have a strong interest in contractual protections of settlement consent provisions – they are an essential component of design professional policies.
- Typically, “consent to settlement” provisions include a mechanism for securing the design professional’s consent.
- Despite fact that the policy here required “informed consent,” right to consent can be reconciled with public policy mandates by ensuring that the insured is provided with sufficient information and guidance to make an informed decision.
- The SJC can and should articulate objective standards for guiding the insured’s settlement consent.

Rawan Decision - Recap

- Consent to settle provisions are valid and do not conflict with insurers' statutory obligations to effect a prompt settlement once liability is clearly established
- Consent-to-settle provisions "are both significant safeguards for insureds to defend their professional reputations and important incentives for the purchase of such insurance" which is voluntary for design professionals
- Competing contractual rights and statutory obligations are not mutually exclusive, but can be reconciled in ways that are consistent with good public policy and benefit design professionals

Rawan Decision – Recap (cont.)

- Court articulated several factors for insurers to satisfy statutory obligations under G.L. chapters 93A and 176D, including:
  - "a thorough investigation of the facts,
  - a careful attempt to determine the value of the claim,

  good faith efforts to convince the insured to settle for such an amount,

  and
  - the absence of misleading, improper or extortionate conduct."

What Went Wrong

CNA COULD HAVE BETTER INFORMED ITS INSURED TO OBTAIN THE INSURED'S CONSENT TO SETTLEMENT IN SEVERAL RESPECTS:

I. **Once liability was reasonably clear, insurer should not have delayed in advancing timely settlement**
II. **Likelihood of plaintiff's verdict (above policy limits) not communicated properly**
III. **Claims could have been settled early on without significantly depleting policy limits**

Lessons Learned

1) PL policies for design professionals can – and should – include consent-to-settlement provision
2) Insurers must provide DP's with a realistic assessment of liability and damages, including exemplary damages, fees, interest, etc., based upon reasonably conducted fact, technical and legal evaluations
3) Defense counsel should do all of above and in addition: assess the risk of excess exposure, including the anticipated erosion of policy limits due to defense and expert fees and costs
4) DP's should expect clear, specific, timely and objectively reasonable settlement recommendations from defense counsel and from their insurer. If possible – work together cooperatively from same "playbook"

QUESTIONS & DISCUSSION