The Arizona Association of Defense Counsel

Common Defense

FALL 2014

A Magazine for Arizona Defense Attorneys

19th ANNUAL BARRY FISH MEMORIAL GOLF TOURNAMENT

On May 3rd, 2014 members raised $16,068 for the ALS Association

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Interview with John Bouma, Distinguished Service Award Honoree

Celebrate his achievements at the Fall Kickoff, September 11.

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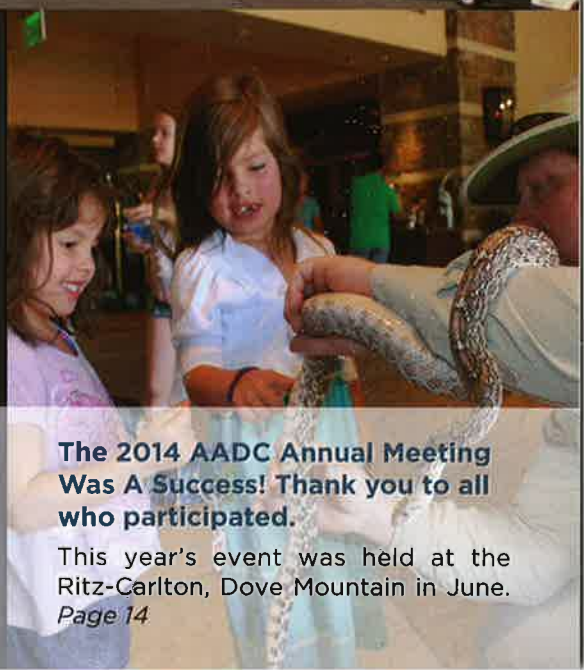

The 2014 AADC Annual Meeting Was A Success! Thank you to all who participated.

This year's event was held at the Ritz-Carlton, Dove Mountain in June.

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Limiting Stipulated Judgments Resulting from a Damron Agreement to Covered Claims When the Judgment Includes both Covered and Uncovered Claims

By Jasmina Richter and Shanks Leonhardt, Sanders & Parks, P.C.

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Arizona Damron/Morris law is unilaterally unfavorable to insurers. Even worse there are many issues left unaddressed by the Arizona Supreme Court and, therefore, much uncertainty when defending against the enforceability of these types of agreements. For instance, can a plaintiff enforce a stipulated judgment resulting from a Damron agreement when the judgment contains both covered and uncovered damages?

Consider the following hypothetical. The insured defendant and the plaintiff enter into a Damron agreement following an insurer's denial of coverage. The plaintiff seeks to enforce a stipulated judgment against an insurance company resulting from a Damron agreement. The stipulated judgment provides for $500,000 as general damages and $1,500,000 as treble damages. The general damages are covered, but treble damages are not covered under the express terms of the policy. Can the plaintiff enforce the stipulated judgment for the full amount of $2,000,000 or is the plaintiff limited to the covered damages of $500,000?[1]

There are no Damron cases in Arizona that address the issue of whether an insurer can modify a judgment resulting from a Damron Agreement to reflect only covered claims when there are both covered and uncovered claims. The cases contemplate situations where coverage is either triggered or it is not triggered and, therefore, the judgment is either completely invalid or fully enforceable against the insurer.

There are a number of cases holding that in a Damron situation the insurer is entitled to raise all of its coverage defenses. There are also cases holding that if an insurer chooses not to defend, it rolls the dice and is no longer able to challenge a resulting judgment except on coverage grounds and for collusion and fraud. *See Parking Concepts, Inc. v. Tenney,* 207 Ariz. 19, n. 3, 83 P.3d 19, 22 n. 3 (2004) ("[I]n cases where the insurer has refused to defend and the parties enter into a Damron agreement, **the insurer has no right to contest the stipulated damages on the basis of reasonableness**, but rather may contest the settlement only for fraud or collusion.") (emphasis added); *see also State Farm Mut. Auto. Ins. Co.*, 122 Ariz. 198, 200, 593 P.2d 948, 950 (1979) ("The general rule...in the absence of fraud or collusion, an insurance company which refuses to defend its insured is bound by a judgment against its insured with respect to all matters which were litigated or could have been litigated in that action.")

In a Morris setting where the insurer is defending the insured subject to a reservation of rights, a judgment is only enforceable against an insurer if it is shown by a preponderance of the evidence to be reasonable. There are no Arizona cases directly addressing a similar reasonableness requirement for a judgment resulting from a Damron agreement. *See* Robert Bruno, *Damron Revisited: Reasonableness the True Judgment*, Arizona Attorney, December 2004 (observing that the reasonableness standard should apply to a stipulated judgment resulting from a Damron agreement and discussing cases supporting this view as well as unfavorable dicta.) Our courts have often pointed out that there are significant differences between an insurer that has provided a defense and is able to intervene for purposes of a reasonableness hearing and "an insurer that provided no defense and was consequently only able to attack a judgment for collusion

1 This hypothetical is purposely simple, but more difficult questions arise when the stipulated judgment does not separate the damages into those that are clearly covered and uncovered.

Limiting Stipulated Judgments *(continued)*

or fraud." *Himes v. Safeway Ins. Co.*, 205 Ariz. 31, 41, 66 P.3d 74, 85 (App. 2003); *citing Damron v. Sledge*, 105 Ariz. 151, 155, 460 P.2d 997, 1001; *Mora v. Phoenix Indem. Ins. Co.*, 196 Ariz. 315, 319-20, ¶¶'s 17-18, 996 P.2d 116, 120-21. A plaintiff may argue that these cases provide that the insurer can litigate coverage, but that if coverage is triggered for any claim, the insurer will not be able to challenge the judgment further except on fraud or collusion grounds.

However, there is a good argument to be made that the insurer is not challenging the "reasonableness" of the stipulated judgment, but rather making sure that the insured is limited only to the insurance coverage that it purchased, which is a principle that has been repeated by Arizona courts. *United Services Auto. Ass. v. Morris*, 154 Ariz. 113, 120 ("An insured's settlement agreement should not be used to obtain coverage that the insured did not purchase."); *Colorado Cas. Ins. Co. v. Safety Control Co., Inc.*, 228 Ariz. 517, 269 P.3d 693, 699-700 ("But an agreement under Damron or Morris does not create coverage 'than an insured did not purchase.' To the contrary, the [insurer] is liable only if the judgment constitutes a liability falling within its policy."); *Arizona Property and Cas. Ins. Guar. Fund v. Martin*, 210 Ariz. 478, 482, 113 P.3d 701, 705 (App. 2005) (an insured cannot obtain coverage it did not purchase and to rule otherwise would upset the careful balance between the interests of the insurer and the insured in Morris type agreements.)

Arizona courts have used this limitation-to-the-coverage-purchased principle to reduce stipulated judgments to policy limits when there is no evidence that an insurer rejected a reasonable settlement offer within policy limits. *State Farm Mut. Auto. Ins. Co. v. Paynter*, 122 Ariz. 198, 593 P.2d 948 (App. 1979) (holding "a refusal to defend in and of itself does not expose the insurance carrier to greater liability than that contractually provided in the policy"); *Rogan v. Auto-Owners Ins. Co.*, 171 Ariz. 559, 832 P.2d 212 (App. 1992) ("[we] hold that when an insurer denies coverage in bad faith, it is not liable for the amount of a judgment entered against its insured that exceeds the policy limits absent a refusal of a reasonable settlement offer, unless the insured can establish other causal connection between the insured's act and the excess judgment").

Using this same reasoning, even if a Court rejects an insurer's attempt to challenge the reasonableness of a stipulated judgment entered pursuant to a Damron agreement, the insurer may still be able to attack the amount of the judgment when there are covered and uncovered amounts. The insurer can argue that the judgment should be reduced by amounts that are beyond the contractually-agreed upon terms. The insurance contract only imposed on the insurer the duty to defend the insured against claims potentially covered by the policy and the duty to indemnify the insured for covered claims. In other words, in our hypothetical, the insurer can argue that it was never obligated to pay for uncovered treble damage amounts ($1,500,000) since the insured is not entitled to insurance it did not purchase.

It is important to note that this is not a settled area of the law and that Arizona courts have never addressed this specific issue. There is a good argument to be made that the judgment should only be limited to covered claims, but there is always risk associated with litigating issues of first impression.