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COZEN O'CONNOR

Are Consent Judgments in Colorado Dead? Colorado Strictly Enforces "No Voluntary Payments" Clause

On Monday, April 25, 2016, the Colorado Supreme Court issued its decision in *Travelers Prop. Cas. Co. v. Stresscon Co.*, No. 13SC815 (Colo. Apr. 25, 2016), holding that an insurer does not need to show prejudice to enforce a "no-voluntary-payments" provision. In *Stresscon*, the insured settled a claim involving a serious construction accident and resulting delays without consulting its insurer, Travelers. The Travelers policy contained a no-voluntary-payments provision stating: "No insured will, except at that insured's own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than for first aid, without our consent." The District Court denied Travelers' motion for summary judgment and motion for directed verdict, finding by analogy that the "notice-prejudice" rule previously adopted by the Colorado Supreme Court regarding an insured's failure to give timely notice also applied to the no-voluntary-payments provision. The jury returned a verdict for Stresscon against Travelers for bad faith breach of contract, statutory penalties, and attorney fees. The Court of Appeals affirmed.

The Colorado Supreme Court overturned the Court of Appeals decision, finding that the no-voluntary-payments provision is "a fundamental term defining the limits or extent of coverage." The court held that "the no-voluntary-payments provision makes clear that coverage under the policy does not extend to indemnification for such payments or expenses in the first place, and instead, the no-voluntary-payments clause merely specifies that as uncovered expenses they will not be borne by the insurer." The court rejected the Court of Appeals' reliance on *Friedland v. Travelers Indem. Co.,* 105 P.3d 639 (Colo. 2005), where the court adopted a rebuttable presumption of prejudice in favor of the insurer where the late notice occurs after the insured's settlement of the liability case. The court stated that *Friedland* did not implicitly extend the notice-prejudice rule to no-voluntary-payments or consent-to-settle provisions even though *Friedland* also involved a settlement without notice to the insurer. The court distinguished *Friedland* by noting that it had "expressly declined to address" the voluntary payment issue.

In light of the court's holding and its recent holding in *Craft v. Philadelphia Indem. Ins. Co.,* 343 P.3d 951 (Colo. 2015) (rejecting the notice-prejudice rule in the context of claims-made coverage), *Friedland's* notice-prejudice rule may well be limited to a narrow category of pre-settlement, late notice cases involving occurrence-based policies.

The court also sought to reconcile its decision in *Nunn v. Mid-Century Ins. Co.*, 244 P.3d 116 (Colo. 2010). In *Nunn*, the court held that an insured faced with a judgment in excess of policy limits could assign bad faith rights in exchange for a pretrial stipulated judgment with a covenant not to execute. In doing so, the court rejected the argument that a covenant not to execute meant that the insured had no actual damages to assign. Stresscon argued that by recognizing pretrial settlements with covenants not to execute, the *Nunn* ruling necessarily implied that no-voluntary-payment provisions could not be enforced. The court disagreed. As it did in distinguishing *Friedland*, the court limited *Nunn* to its facts, which involved a situation where the insurer initially refused to accept a demand within limits, but subsequently consented to the entry of a stipulated judgment in excess of limits (while only agreeing to contribute it limits and otherwise reserving its rights to contest the reasonableness of the settlement). Distinguishing *Nunn*, the court noted that Stresscon "was never even remotely exposed to a judgment beyond policy limits," drawing a clear line between insureds exposed to excess verdicts and those who are not.

The court left open, however, whether, and to what extent, *Nunn* might be impacted by a no-voluntary-payments defense when an insured is exposed to an excess judgment. "In order to resolve the case before us today, we need not finely construe this or any other particular no-voluntary-payments provision or opine on the circumstances under which an insurer might be

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precluded from relying on such a provision to assert exclusions from coverage or deny coverage altogether."

The court also recognized, for the first time, that in assessing settlement obligations, an insurer is not required to account for "moral hazards," such as the insured's damaged business relationships. In this regard, the court stated, "Insuring against the risk of a specified class of injuries does not include insuring against the risk of damaged business relationships or the loss of future business contracts … and damage or loss of this nature does not demonstrate bad faith[.]"

Looking for a silver lining, policyholder counsel are likely to argue that the Colorado Supreme Court, *in dicta*, implicitly recognized that Colorado's bad faith statutes, C.R.S. §§ 10-3-1115 and 10-3-1116, apply to liability policies as well as first-party policies. However, if *Stresscon* stands for anything, it stands for the proposition that the court's opinions address only the particular issues before it. The appellate issues surrounding Colorado's bad faith statute were abandoned by Travelers at the Court of Appeals, and consequently, were not before the court. *See, Stresscon Corp. v. Travelers Prop. Cas. Co.*, 2013 WL 4874352 at *16 (Colo. App. Sep. 12, 2013). Thus, the application of Colorado's bad faith statute to liability policies likely remains an open issue.

To discuss any questions you may have regarding the issues discussed in this Alert, or how they may apply to your particular circumstances, please contact Christopher S. Clemenson at (720) 479-3894 (cclemenson@cozen.com) or John Daly at (720) 479-3867 (jdaly@cozen.com).