



Nevada's Highest Court Determines that Insurers Who Fail to Defend their Insureds may be Liable for Consequential Damages Well Beyond Policy Limits - No Bad Faith Required!

In a lawsuit arising out of a traffic accident, the Nevada Supreme Court ruled that a commercial liability insurer that breached its duty to defend an insured could be liable for damages in excess of the policy limits, even if the insurer acted in good faith. In *Century Surety Co. v. Andrew*,¹ a pedestrian was hit by a truck owned and driven by Michael Vasquez. Vasquez used the truck for both personal use and for his auto detailing business, Blue Streak Auto Detailing, LLC (“Blue Streak”). Vasquez was covered under a personal auto liability insurance policy, as well as a commercial liability policy issued by Century Surety Company (“Century”). The commercial liability policy had a policy limit of \$1 million. The pedestrian sued Vasquez in state court, seeking damages for his personal injuries suffered in the accident.

Century denied coverage because Vasquez was not using the truck for business purposes at the time of the accident. Century refused to settle the claim within the policy limits, and the pedestrian plaintiff subsequently sued both Vasquez and Blue Streak (this time in federal court), asserting that Vasquez was driving in the course of his employment at the time of the accident. Century refused to defend Blue Streak, and the pedestrian plaintiff obtained an \$18 million default judgment against both Vasquez and Blue Streak.

The plaintiff settled with Vasquez and Blue Streak, assumed their rights under the Century policy, and sued Century for failing to defend Blue Streak in the underlying lawsuit. The federal district court concluded that although Century did not act in bad faith, it did breach its duty to defend Blue Streak. The issue of how much of the \$18 million judgment Century could be liable for was presented to the Nevada Supreme Court.

The Nevada Supreme Court determined that Century’s liability was not capped at the \$1 million policy limit. The Court explained that the excess damages are consequential to the insurer’s breach of its duty to defend its insured, because they may not have been incurred if the insurer fulfilled its obligations under the policy.

Courts throughout the country agree that when an insurer fails to defend its insured in a lawsuit, then, at a minimum, the insurer will be responsible for paying the defense costs incurred by the insured. They disagree, however, on whether the insured is entitled to damages beyond the reimbursement of the defense fees it incurred.² The Nevada Supreme Court, adopting the minority view, concluded that an insurer may be liable for all damages that result from its failure to defend the insured, such as interest incurred on a judgment, even if these damages exceed the policy limits. The reasoning behind the Court’s decision was that “insureds pay a premium for what is partly litigation insurance designed to protect . . . the insured from the expense of defending suits brought against him.”³ The Court made an important distinction about the policy limits and damages available to an insured when its insurer fails to defend its insured: the policy limits represent “only the amount the insurer may have to pay in the performance of the [insurance] contract to a third person for personal injuries caused by the insured; they do not restrict the damages recoverable by the insured for a breach of contract by the insurer.”⁴

¹ No. 73756, 134 Nev. Adv. Op. 100, 432 P.3d 180 (Dec. 13, 2018).

² The majority view is that “[w]here there is no opportunity to compromise the claim and the only wrongful act of the insurer is the refusal to defend, the liability of the insurer is ordinarily limited to the amount of the policy plus attorneys’ fees and costs.” *Comunale v. Traders & Gen. Ins. Co.*, 50 Cal.2d 654 (1958). This view is followed by Arizona, California, Connecticut, Kansas, Minnesota, and Washington, to name a few. To contrast, the minority view is that insurers’ liability is not capped at the policy limits. Rather, insurers may be liable for consequential damages stemming from a breach of its obligations under the policy. States that follow the minority view include Colorado, Florida, Georgia, Illinois, New York, and Wisconsin.

³ *Century v. Andrew* at 185.

⁴ *Id.*

The Court concluded that had Century defended Blue Streak in the underlying action, not only could the \$18 million default judgment have been avoided, but the judgment might have been substantially less had Century raised defenses on behalf of Vasquez and Blue Streak. The Court cautioned that an insurer refuses to defend an insured at its own peril, because even though there may ultimately be a basis for denying coverage, an insurer runs the risk of significant exposure if it fails to defend an insured when it should have done so.

The Court explained that, even in the absence of bad faith, the insurer may be liable for a judgment that exceeds the policy limits if the judgment is consequential to the insurer's breach. However, the extent of an insurer's liability depends on the unique facts of each case, and the insured must show that the damages exceeding the policy limits were actually caused by the insurer's failure to defend it in a given case. In addition, the insured has an obligation to take reasonable precautions to protect itself and to mitigate its damages in the event that an insurer refuses to defend the insured.

The *Andrew* decision is significant because it adopts the policyholder-friendly minority view that an insured is entitled to consequential damages flowing from its insurer's failure to defend its insured. The decision serves as a warning to insurers of the potential risks in refusing to defend insureds, even in cases where a claim may not ultimately be covered by the policy, and may help policyholders recover amounts beyond the policy limits without having to show bad faith on the part of the insurer.

For more information contact [Kerianne Kane](mailto:Kerianne.Kane@sdvllaw.com) at 203.287.2136 or kek@sdvllaw.com.