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That Agreement Isn't Worth the Paper It's Printed On: Settlements, Consent Judgments, and Penn-America Insurance Co. v. Osborne

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A settlement is in place. The parties to the litigation have executed an agreement that embodies their negotiations. Some walk away with a release. Others walk away with a check. Still others had their heart set on an assignment of claims against a third-party. Once the consideration changes hands, the parties submit a stipulation of dismissal, or the court enters a consent judgment. Does that mean the dispute is over? For most cases, it does. Occasionally, however, the dispute lives on or is inherited by a third-party against whom claims were assigned. This article explores the circumstances in which settlement agreements are subject to attack in West Virginia, either by the parties or by third-parties against whom they are sought to be enforced.

As a general matter, settlement agreements signal the end of a dispute. They are "highly regarded and scrupulously enforced, so long as they are legally sound."1 Indeed, because "[t]he law favors and encourages the resolution of controversies by contracts of compromise and settlement . . . it is the policy of the law to uphold and enforce such contracts if they are fairly made and are not in contravention of some

law or public policy."2 In West Virginia, parties to a settlement may only re-open it if they overcome the heavy burden of establishing that the settlement was the result of an accident, mistake, or fraud.3 Given these high hurdles, it is the rare case that a litigant will be successful in directly challenging its own settlement agreement.4

But an agreement that resolves a matter among discrete parties does not necessarily fix the obligations of a non-consenting or non-party insurer. "Most attempts to resolve litigation without the consent of the defendant's liability carrier involve three components: (1) an assignment of the defendant's rights against his or her liability insurer to the plaintiff; (2) the plaintiff's covenant not to execute against the defendant's assets; and (3) a judgment establishing the defendant's liability and the plaintiff's damages."5 Due to the potential that such agreements will arise from fraud or collusion, many courts "cast a suspicious eye" on them.6

Accordingly, a consent or confessed judgment against an insured party may be subject to attack when it is entered into without the participation of a relevant liability carrier. For instance, in West Virginia, "a consent or confessed judgment against an insured party is not binding on that party's insurer in subsequent litigation against the insurer where the insurer was not a party to the proceeding in which the consent or confessed judgment was entered, unless the insurer expressly agreed to be bound by the judgment."7 This is because,

[w]hen dealing with consent judgments, courts must ensure that circumstantial guarantees of trustworthiness exist concerning the genuineness of the underlying judgment. The real concern is that the settlement may not actually represent an arm's length determination of the worth of the plaintiff's claim.8

The judiciary's circumspect approach to consent judgments is especially heightened when the underlying agreement is coupled with a covenant not to execute. A covenant not to execute is an agreement by "which a party who has won a judgment agrees not to enforce it."9 Such covenants are suspect because they come with perverse incentives. "When the insured actually pays for the settlement of the claim or when the case is fully litigated, the amount of the settlement or judgment can be assumed to be realistic."10 But when an insured walks away from the agreement with no practical consequences, it has little reason to challenge the amount of the claim, and the accuracy of the judgment becomes questionable.

One potential circumstance is illustrated by Penn-America Insurance Co. v. Osborne, 11 which was decided by the Supreme Court of Appeals of West Virginia in 2017. There, the plaintiff was injured in a timbering accident while conducting work for his employer, H&H Logging Company, on land owned by Heartwood Forestland Fund, IV, Limited Partnership, and leased by Allegheny Wood Products, Inc., for the purpose of harvesting timber.12 The plaintiff sued his employer for deliberate intent and both Heartwood and Allegheny for negligent failure to inspect and/or maintain the land.13 When it came time for the defendants to arrange the defense among their insurers, communications fell apart. H&H requested a defense from its commercial general liability insurer, Penn-America Insurance Company, but Penn-America declined to defend the case against H&H because deliberate intent claims were excluded under the relevant policy.14

For their part, Allegheny and Heartwood requested a defense from Allegheny's

insurer, which accepted coverage. Some time later, Allegheny and Heartwood realized that H&H was contractually obligated to provide them a defense and wrote H&H to demand that it or Penn-America provide a defense. None of the parties ever notified Penn-America that Allegheny and Heartwood had requested a defense against the plaintiff's allegations. Nonetheless, Allegheny and Heartwood moved for leave to file a third-party complaint for a declaration that Penn-America had wrongfully failed to provide them a defense. The court never ruled on the motion, and the third-party complaint was never filed.15

Thereafter, without providing notice to Penn-America, the parties entered into a settlement agreement, stipulating that Penn-America had damaged Allegheny and Heartwood by breaching its contractual obligation to provide them a defense against the plaintiff's allegations.16 The key aspects of the agreement are as follows:

Allegheny and Heartwood consented to a $1,000,000.00 judgment for [the plaintiff's] leg injury, and they agreed to assign to [the plaintiff] any claims they may have had against Penn-America for failing to provide them a defense in the lawsuit. In return, [the plaintiff] covenanted not to execute on the $1,000,000.00 judgment against Allegheny and Heartwood. Instead, he would collect judgment from Penn-America by asserting his assigned claims.17

The plaintiff dismissed his lawsuit against Allegheny and Heartwood and filed a new lawsuit against Penn-America, seeking to recover $1,000,000 as relief for its alleged failure to provide a defense in the plaintiff's case against Allegheny and Heartwood.18

Ultimately, the Supreme Court of Appeals of West Virginia decided that "the consent judgment [was] not binding on Penn-America, and the assignment of claims to [the plaintiff was] void."19 As to the enforceability of the consent judgment itself, the court adhered to its prior reasoning that a consent judgment coupled with a covenant not to execute is especially suspect and deserving of scrutiny. It further reasoned that "[n]one of the parties to the pre-trial settlement agreement had any motive to contest liability or an excessive amount of damages."20 Moreover, the parties valued the claim at $1,000,000 by reference to Penn-America's coverage, not the plaintiff's actual injuries. Because "Penn-America was not a party to the lawsuit in which the consent judgment was entered," the judgment could not be binding on PennAmerica.21

The assignment of bad faith claims by Allegheny and Heartwood fared no better. The Court found that the assignment was based on falsehoods, and that the parties' agreement bore the hallmark characteristics of fraud and collusion.22 As the Supreme Court of Appeals summarized:

[T]he facts underlying Mr. Osborne's assigned claims were misrepresented. Moreover, a $1,000,000.00 valuation of a lawsuit for an injured leg, without any cited evidence regarding permanency of the injury, permanent disability, severity, medical expenses, etc., hardly reflects a "serious negotiation on damages." Lastly, concealment also characterizes the pre-trial settlement agreement because the parties never notified Penn-America of their pre-trial settlement negotiations. Once Penn-America learned after-the-fact of the pre-trial assignment and covenant not to execute, it was prohibited from conducting discovery on the extent of Mr. Osborne's

injuries and damages. Thus, through secretive means, Allegheny and Heartwood awarded Mr. Osborne a $1,000,000.00 windfall for his injured leg with Penn-America's money.23

In essence, the consent judgment entered by the putative insureds was ineffective to subject the insurer to liability or exposure in a subsequent case brought by the plaintiff.

The reasoning of the Supreme Court of Appeals of West Virginia in Penn-America is the majority approach as to whether a consent or confessed judgment can be binding on a third party.23 For those engaged in settling cases on behalf of their insureds, Penn-America counsels against using the settlement agreement as an instrument to foist liability onto a non-party, especially one that has not been given notice of the negotiations. Moreover, insurers against whom consent judgments are sought to be enforced should bear in mind that the enforcers face a steep uphill battle. The Supreme Court of Appeals of West Virginia, along with the majority of courts, looks askance on enforcing such judgments against non-parties.

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1 DeVane v. Kennedy, 205 W. Va. 519, 534, 519 S.E.2d 622, 637 (1999)

2 Syl. Pt. 6, DeVane, 205 W. Va. 519, 519 S.E.2d 622 (quoting Syl. Pt. 1, Sanders v. Roselawn Mem'l Gardens, 152 W. Va. 91, 159 S.E.2d 784 (1968))

3Syl. Pt. 2, Burdette v. Burdette Realty Improvement, Inc., 214 W. Va. 448, 590 S.E.2d 641 (2003) (quoting Syl. Pt. 7, DeVane, 205 W. Va. 519, 519 S.E.2d 622).

4 See, e.g., Burdette, 214 W. Va. 448, 590 S.E.2d 641 (fi nding that a settlement agreement was unenforceable because a party to the agreement had repudiated his signature before the agreement left his attorney's offi ce, thus resulting in no meeting of the minds)

5 John K. DiMugno, Consent Judgments and Covenants Not To Execute: Good Deals or Too Good to Be True? Part II: Practical Concerns About Collusion and Fraud, 25 No. 1 INS. LITIG. REP. 5 (2003).

6 Id

7 Syl. Pt. 7, Horkulic v. Galloway, 222 W. Va. 450, 665 S.E.2d 284 (2008).

8 Id. at 460, 665 S.E.2d at 294 (quoting Ross v. Old Republic Ins. Co., 134 P.3d 505 (Colo. App. 2006)).

9 Covenant, BLACK'S LAW DICTIONARY (10th ed. 2014).

10 Horkulic, 222 W. Va. at 460-61, 665 S.E.2d at 294-95 (quoting Ross, 134 P.3d 505).

11 238 W. Va. 571, 797 S.E.2d 548 (2017).

12 Id. at 573, 797 S.E.2d at 550.

13 Id

14 Id

15 Id. at 574, 797 S.E.2d at 551.

16 Id

17 Id

18 Id

19 Id. at 575, 797 S.E.2d at 552.

20 Id. at 576, 797 S.E.2d at 553

21 Id. at 578-79, 797 S.E.2d at 555-56; cf. Strahin v. Sullivan, 220 W. Va. 329, 647 S.E.2d 765 (2007) (reasoning that the assignment of a bad faith claim may not be made when the insured enters a covenant not to execute as the insured was never actually exposed to an excess verdict that would support a bad faith claim against his insurer).

22 Penn-America, 238 W. Va. at 579-80, 797 S.E.2d at 556-57

23 LITIGATION & PREVENTION OF INSURER BAD FAITH § 3:50 (3d ed. 2018) (referring to Penn-America as representative of the majority rule "that the consent or confessed judgment is simply not binding where the party from which indemnity is sought was not a party to the previous proceeding").