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Consequences of an Insurer's Breach of the Duty to Defend: Columbia Casualty Co. v. HIAR Holdings, LLC in the Context of the ALI Restatement of the Law of Liability Insurance

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the ALI Restatement of the Law of Liability Insurance (June 2016)
By Jeffrey E. Thomas

An insurer's duty to defend in connection with liability insurance policies is well-established and reasonably well understood. The consequences for the breach of that duty, however, are much less clear. On one hand, one might argue that this duty is a contractual duty giving rise to contractual remedies. The insured provides its own defense and, if the insurer wrongfully failed to provide a defense, the insured is entitled to reimbursement of its defense costs. On the other hand, this remedy seems insufficient; the value on an insurer's participation in the defense of a case goes beyond well merely paying the legal fees. It includes advice, strategy, and a greater likelihood that the insurer will participate in a settlement. In an attempt to account for the intangible benefits of a defense, another approach to the consequence of an insurer's breach of the duty to defend is like a forfeiture; an insurer which wrongfully refuses to defend may give up its policy defenses.

The American Law Institute is wrestling with this issue, along with many others, in the preparation of the first Restatement of the Law of Liability Insurance. The early approach taken by the reporters was a fairly aggressive version of the forfeiture approach: "A liability insurer that breaches the duty to defend a claim loses the right to defend the claim, the right to assert any control over the settlement of the claim and the right to contest coverage for the claim."[1] This was a kind of strict liability approach to breach of the duty to defend. Various objections were raised to this approach, and it was softened by the reporters. A later iteration of the rule is more of a negligence approach: "An insurer that lacks a reasonable basis for its breach of the duty to defend a claim also loses its right to contest

[1] Principles of the Law of Liability Insurance § 58(1) (Preliminary Draft No. 3, Feb. 8, 2012). This project started as a "principles" project, but in 2015 was changed into the more familiar "restatement" project. The general sentiment of those involved with the project seems to be that a "restatement" should more closely track the current state of the law rather than be as aspirational as a "principle" project may be. This may be part of the reason for the way that the Restatement's position on the consequences of the breach of the duty to defend has evolved in the way that it has. The black letter rule, comments and reporters notes for this version of the rule are included as Appendix 1.

coverage for the claim."[2] The most recent version of the rule softens it even further, to something close to bad faith: "An insurer that breaches the duty to defend without a reasonable basis for its conduct must provide coverage for the legal action for which the defense was sought, notwithstanding any grounds for contesting coverage that the insurer could have preserved by providing a defense under a reservation of rights pursuant to § 15."[3]

The work of the American Law Institute on this issue provides an interesting backdrop against which to consider the rule applicable in Missouri. Just a few years ago, the Missouri Supreme Court in *Columbia Casualty Co. v. HIAR Holding LLC*,[4] aligned Missouri law with the more strict-liability approach for an insurer's breach of its duty to defend. The court articulated the consequences of the breach of the duty to defend in this way: "The insurer that wrongly refuses to defend is liable for the underlying judgment as damages flowing from its breach of its duty to defend."[5] Of course, "wrongfully" refusing to defend could mean without a reasonable basis, with bad faith, or in any way that breaches the contractual duty. However, a careful reading of *HIAR* shows that "wrongfully" merely means the breach of the contractual duty to defend. We first begin with an analysis of the *HIAR* opinion and the authority upon which it relied, and will then consider subsequent develops in Missouri which have a bearing on understanding and applying the Missouri Rule.

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[2] Restatement of the Law Liability Insurance § 19(2) (Preliminary Draft No. 2, October 9, 2015).
[3] Restatement of the Law Liability Insurance § 19(2) (Tentative Draft No. 1, April 11, 2016). This draft was approved at the American Law Institute 2016 Annual Meeting. *See* American Law Institute Website, https://www.ali.org/projects/show/liability-insurance/#_status, last visited June 15, 2016. This version of the rule is intended to represent "a middle ground between the rule in some jurisdictions that an insurer that breaches the duty to defend loses the right to contest coverage even if it had a reasonable basis for its conduct and the rule in other jurisdictions that the insurer that breaches the duty to defend retains the ability to contest coverage." *Id*. comment c. In addition, the rule is meant to reflect "one of the leading standards for what constitutes a bad-faith breach" although "without using the term 'bad faith breach,' [it] leaves room for courts to adopt a different standard for bad-faith breach in other contexts for other remedies." *Id*. The black letter rules, comments and reporters notes for section 19 are included as Appendix 2.
[4] 411 S.W.3d 258 (Mo. 2013).
[5] 411 S.W.3d at 265 (citing Schmitz v. Great American Assur. Co., 337 S.W.3d 700, 708-709 (Mo. 2011)).

Columbia Casualty Co. v. HIAR Holding LLC

The claim in *HIAR* concerned unsolicited junk faxes sent out as part of a marketing campaign. A class action suit seeking injunctive relief and statutory damages of $500 per fax contended that the sending of the faxes violated the Telephone Consumer Protection Act (TCPA). HIAR tendered the defense of the claim to Columbia Casualty, its CGL carrier, under the property damage and advertising injury coverages. Columbia refused to provide a defense or to fund a settlement within the policy limits, which were $1,000,000 per occurrence, $2,000,000 aggregate. HIAR defended itself at its own expense, and ultimately settled the case for $5,000,000 with an assignment of its insurance claim to the class. A garnishment action on the policy followed. The trial court ruled that Columbia had breached its contractual duty to defend HIAR, that the claims were covered under the policy, and that Columbia was liable for the full amount of the settlement. The Missouri Supreme Court affirmed.

The court began its analysis by framing the issue as whether an insurer "that wrongfully refuses to defend an insured can be liable to indemnify the insured for an underlying judgment for damages that is adjudged to be reasonable."[6] It answered in the affirmative, relying on *Schmitz v. Great American Assurance Co.*[7] for the proposition that "when an insurer is bound to protect its insured from liability, it is bound by the liability determination in the litigation to which the insured is a party, so long as the insurer had the opportunity to control and manage the litigation."[8] The court emphasized that the key point was the "**opportunity** to control and manage the litigation" rather than the duty to do so.[9]

Failure to defend, however, does not preclude any subsequent challenge by the insurer. The insurer can "relitigate the issue of the reasonableness of the damages the insured has been declared to

[6] 411 S.W.3d at 264.
[7] 337 S.W.3d 700 (Mo. 2011).
[8] 411 S.W.3d at 264 (citing *Schmitz*, 337 S.W.3 at 709).
[9] 411 S.W.3d at 264 (quoting *Schmitz*, 337 S.W.3d at 709-710) (emphasis in original).

owe," but "only if the insured is trying to enforce a settlement amount that has not been the subject of a judgment by a trial judge approving its reasonableness."[10] If the trial court has approved the reasonableness of the settlement (as it had in *HIAR*), "the insurer is not entitled to a second hearing on reasonableness in any garnishment or declaratory judgment action based on the policy."[11] The court then stated: "The insurer that wrongly refuses to defend is liable for the underlying judgment as damages flowing from its breach of its duty to defend."[12] It added this rationale from *Schmitz*: "The 'insurer cannot have its cake and eat it too by both refusing coverage and at the same time continuing to control the terms of settlement in defense of an action it had refused to defend.'"[13]

In applying these rules to the facts of the case, the court first considered whether Columbia Casualty had "wrongfully refused to defend HIAR."[14] It held that Columbia had wrongfully refused to defend because the lawsuit sought damages covered by the policy, not a penalty or fine that would not have been covered. The court noted that the policy provided coverage for "those sums that the insured becomes legally obligated to pay as damages."[15] Although the Missouri Supreme Court had previously decided that the term "damages" in a liability insurance policy did not include "awards imposing fines and penalties,"[16] the court was convinced by the analysis of the Eighth Circuit that the TCPA $500 per fax statutory damages constituted "a liquidated sum for uncertain and hard-to-quantify actual damages."[17] In particular, the court found persuasive the availability of "'treble damages . . . separate from fixed damages'" which "showed that the $500-per-occurrence statutory damages awards, by themselves, are

[10] 411 S.W3d at 265.
[11] 411 S.W.3d at 265 (citing *Schmitz*, 337 S.W.3 at 708-709
[12] 411 S.W.3d at 265 (citing *Schmitz*, 337 S.W.3d at 708-709).
[13] 411 S.W.3d at 265 (quoting *Schmitz*, 337 S.W.3d at 710).
[14] 411 S.W.3d at 265.
[15] 411 S.W.3d at 265 (quoting the policy).
[16] 411 S.W.3d at 266 (citing Farmland Industries, Inc. v. Republic Ins. Co., 941 S.W.2d 505, 510-511 (Mo. 1997)).
[17] 411 S.W.3d at 267 (quoting Universal Underwriters Ins. Co. v. Lou Fusz Automotive Network, Inc., 401 F.3d 876, 881 (8th Cir. 2005).

not a penalty."[18] To the extent that a previously decided Missouri Court of Appeals decision could be understood to hold that the $500 per-fax damages were "penal,"[19] the Missouri Supreme Court held that "it no longer should be followed on this issue."[20]

Once the damages issue was addressed, the court turned to whether the damages were because of property damage or advertising injury as required by the policy. The court held that both applied. As to property damage, Columbia argued that any damage did not arise from an "occurrence" because it was not accidental. The court rejected this argument because the trial court had determined "that HIAR's action is in violating the TCPA reflected negligent conduct, as it found that HIAR did not intend to violate the TCPA and did not intend injury to the class."[21] The Supreme Court concluded that there was "[n]othing in the record" to support Columbia's contention "that HIAR sent the faxes intending to injure the recipients or violate the TCPA."[22] Somewhat surprisingly, the issue of whether receiving junk faxes constituted property damage was not addressed.

The court also rejected the argument that the advertising injury coverage did not apply because the class did not claim a violation of their privacy. Columbia argued that the TCPA was concerned about the "costs and business disturbances" caused by junk faxes, "not at protecting [recipients] from violations of privacy interests."[23] However, the court found that the class "alleged privacy violations pursuant to the TCPA, which has been recognized as providing privacy protections."[24] The court also

[18] 411 S.W.3d at 267 (quoting *Universal Underwriters*, 401 F.3d at 881).
[19] *See* 411 S.W.3d at 267 (citing Olsen v. Siddiqi, 371 S.W.3d 93, 97 (Mo. Ct. App. 2012).
[20] 411 S.W.3d at 268.
[21] 411 S.W.3d at 269.
[22] 411 S.W.3d at 269.
[23] 411 S.W.3d at 270.
[24] 411 S.W.3d at 270.

found that the privacy interests protected by the act extended to protecting the privacy rights of businesses as well as individuals.[25]

The court then turned to Columbia's other defenses. The first was the somewhat novel assertion that the claim was excluded by the contractual liability exclusion. Columbia argued that the settlement amounted to a "gratuitously assumed" liability because the settlement was premises on receipt of 10,000 faxes (bringing damages to $5,000,000), but only 488 class member made claims under the settlement.[26] This novel theory could not be supported by any case law, and the trial court's judgment indicated that there was still time for class members to submit claims under the settlement. In addition, the court found that the damages were "defined by the settlement agreement and not by how many claims were submitted [by class members]."[27] The court also rejected Columbia's defense based on notice and failure to cooperate. The court found that Columbia was timely informed of the claims and of the settlement offer, and that Columbia on both occasions refused to defend or provide coverage. Although Columbia asserted that it was not given notice of an amendment to the petition, the court found that Columbia was not prejudiced by that omission and that the theory of liability was established independent of the amendment.[28]

Having determined that the claim was covered by the insurance policy, it followed that Columbia had a duty to defend.[29] But what were the damages for the breach of that duty? Columbia argued that for it to be liable for the full $5,000,000 settlement, which was well beyond its policy limits of $1,000,000 per occurrence/$2,000,000 aggregate, the class would have to show that it acted in bad faith. Because "no 'bad faith' allegation was presented in this case," Columbia argued that the trial court

[25] 411 S.W.2d at 270.
[26] 411 S.W. at 271.
[27] 411 S.W.3d at 271.
[28] 411 S.W.3d at 271-272.
[29] 411 S.W.3d at 272.

erred in awarding extra-contractual damages.[30] The court did not agree with this analysis. It relied on the analysis earlier in the opinion that "Columbia's wrongful refusal to defend HIAR put it in a position to indemnify HIAR for all damages flowing from its breach of the duty to defend."[31]

In addition, however, the court noted that the class argued there were "sufficient allegations . . . that Columbia was acting in bad faith."[32] The court appears to accept this argument, but is not entirely clear about it. The court explained the argument this way: "Because Columbia wrongfully denied coverage and even a defense under a reservation of rights, and also refused to engage in settlement negotiations, Columbia should not avoid liability for the settlement entered in this case. Columbia cannot benefit from its wrongful refusal to assume control of the proceedings."[33] It then concluded, ambiguously: "As such, the trial court did not err in determining Columbia's liability for the class's settlement."[34]

Implications of *HIAR*

Although the Missouri Supreme Court did not unequivocally support the strict-liability forfeiture approach to breach of the duty to defend, its analysis provides significant support for this approach. The stated rule is: "The insurer that wrongly refuses to defend is liable for the underlying judgment as damages flowing from its breach of its duty to defend."[35] The key term in this rule is "wrongfully," which could be interpreted as requiring negligence or bad faith. However, it can also be interpreted as merely requiring a breach of the duty. That interpretation is supported by the absence of consideration by the court of negligence or bad faith, and by the affirmative rejection of the argument that liability must be

[30] 411 S.W.3d at 273.
[31] 411 S.W.3d at 273.
[32] 411 S.W.3d at 273.
[33] 411 S.W.3d at 274 (citations to Shobe v. Kelly, 279 S.W.3d 203, 209-211 (Mo. Ct. App. 2009) omitted).
[34] 411 S.W.3d at 274.
[35] 411 S.W.3d at 265 (citing Schmitz v. Great American Assur. Co., 337 S.W.3d 700, 708-709 (Mo. 2011)).

predicated on the showing of bad faith. From that rejection, it can be inferred that that all the insured (or its assignees) must show is that the insurer breached its duty to defend.

Moreover, the court implicitly rejected a defense based on the reasonableness of the insurer's refusal to defend. Columbia relied on *Olsen v. Siddiqi*, 371 S.W.3d 93 (Mo. Ct. App. 2012), which held that the TCPA statutory penalty did not constitute "damages" for purposes of liability insurance coverage. This reliance would support an argument that the refusal to defend was reasonable.[36] Although the court did not address such a reasonableness argument, the court was aware of *Olsen* (which it overruled) and the court rejected the requirement of a showing of bad faith, which is the affirmative theory to which the reasonableness argument would respond as a defense.

On the other hand, the strength of the interpretation of *HIAR* as adopting strict-liability is somewhat mitigated by the court's reference to bad faith as an alternative theory for liability. Because Columbia was given the opportunity to settle within its policy limits, but rejected such a settlement, HIAR had at least a prima facie case for bad faith failure to settle.[37] Perhaps the Supreme Court was willing to affirm Columbia's liability beyond its policy limits at least in part because Columbia had the opportunity to avoid the excess exposure by accepting a settlement within limits. It is possible that a subsequent case where the insurer had no opportunity to settle within limits might be distinguished from *HIAR*.

While this alternative theory gives some room for argument, the court did not strongly endorse this alternative theory. Its analysis of the bad faith theory, focused more on the breach of the duty to defend than on the bad faith refusal to settle. The court treated the failure to settle as an aside ("and

[36] Such an argument was not raised by the appeal. *See* Appellant's Substitute Brief, Columbia Cas. Co. v. HIAR Holdings, 2013 Mo. S. Ct. Briefs LEXIS 9 (Mar. 18, 2013).
[37] *See*, *e.g.*, Scottsdale Ins. Co. v. Addison Ins. Co., 448 S.W.3d 818, 828 (Mo. 2014); Zumwalt v. Utilities Ins. Co., 228 S.W.2d 750, 754-755 (Mo. 1950); Truck Ins. Exch. v. Prairie Framing, LLC, 162 S.W.2d 64, 93-94 (Mo. Ct. App. 2005); Landie v. Century Indem. Co., 390 S.W.2d 558, 563 (Mo. Ct. App. 1965).

[Columbia] also refused to engage in settlement discussions") while focusing on the fact that Columbia "wrongly denied coverage and even a defense under a reservation of rights."[38] The court's concluding rationale also focuses on breach of the duty to defend: "Columbia cannot benefit from its wrongful refusal to assume control of the proceedings." Thus, it seems likely that the court would have *sustained* the judgment even without the insurer's failure to settle. Columbia's "wrongful refusal to assume control of the proceedings" was due to its breach of the duty to defend. Having breached that duty (and the contract), the court was not going to permit Columbia to benefit by imposing its policy limits.

Extension of *Schmitz v. Great American Assurance Co.*

The Missouri Supreme Court relied explicitly on *Schmitz* to reach its conclusions about the breach of the duty to defend. The court reasoned: "*Schmitz* **instructs** the decision in this case."[39] While *Schmitz* was similar in that it involved a refusal to defend based on the purported applicability of an exclusion, it was different because it involved a section 537.065 agreement. The court's reliance on *Schmitz* in *HIAR* therefore extends the public policy behind such agreements, authorized by statute, to cases that do not involve such an agreement.

In *Schmitz* a woman was killed in a fall from a portable rock climbing wall at a minor league baseball game. Her parents brought a wrongful death claim against the baseball team and its owner. The owner settled for $700,000, and the parents proceeded against the team, which had primary and an excess liability insurance coverage. The primary insurer denied it owed a duty to defend or indemnify because the policy contained an exclusion for amusement devices. The parents entered into a section 537.065 agreement with the insured and were awarded $4.5 million in damages.[40] After the parents

[38] 411 S.W.3d at 274.
[39] 411 S.W.3d at 264.
[40] 337 S.W.3d at 703-704.

obtained summary judgment in the garnishment action holding that the exclusion was inapplicable, the primary insurer, which had limits of $1 million, settled on behalf of the team for $700,000.

The garnishment action proceeded against the excess insurer for the remaining $2.88 million in damages. The insurer argued that the exclusion applied, that the amount of the judgment was unreasonable, that the excess policy did not apply because the primary policy had not been exhausted, and that it was not bound by the 537.065 agreement because the refusal to defend was justified. The trial court in the garnishment proceeding found the judgment of $4.5 million was unreasonable, so reduced it to $2.2 million. But the court also found that the excess policy did not cover the judgment because the primary policy had not been exhausted.[41]

The Missouri Supreme Court reversed the trial court as to reasonableness of the judgment and as to exhaustion. The court held that collateral review of the amount of the judgment was not proper. Collateral review under *Gulf Insurance Co. v. Noble Broadcast*[42] only applies to ***settlements*** under section 537.065, not to judgments.[43] The court also held that the primary policy had been exhausted. The key to exhaustion was whether the insurer was obligated to pay the full limit, not whether it had actually done so.[44] In addition, the court noted that the policy recognized that an insured might agree to "fund by self-insurance or *means other than insurance.*"[45] Consequently, the policy was exhausted by the underlying insurer's payment of $700,000 combined with the insured's release of the remaining $300,000 of the $1 million policy limit.[46]

[41] 337 S.W.3d at 705.
[42] 936 S.W.2d 810 (Mo. 1997).
[43] 337 S.W.3d at 708-709.
[44] 337 S.W.3d at 706.
[45] 337 S.W.3d at 707.
[46] 337 S.W.3d at 707.

The court also rejected the insurer's additional arguments regarding coverage. The court held that the amusement device exclusion was inapplicable because the definition of "amusement device" was "any device or equipment a person rides for enjoyment," and the climbing wall was not a "ride."[47] The court also held that the insurer was bound by the section 537.065 agreement even though the insurer asserted that its refusal to defend was justified. Because the trial court "correctly found that the rock climbing wall was not an amusement device so that the exclusion did not apply," this "rendered Great American's refusal to defend or to provide coverage unjustified."[48]

The Missouri Supreme Court's handling of this last argument is the source of the language that is cited and quoted in *HIAR*. The court noted that when "one is bound to protect another from liability, he is bound by the result of the litigation to which such other is a party, provided he had the opportunity to control and manage it."[49] The court emphasized that the "standard is whether the insurer had the **opportunity** to control and manage the litigation, not whether the insurer had the **duty** to control and manage the litigation."[50] "Once an insurer unjustifiably refuses to defend or provide coverage, the insured may, without the insurer's consent, enter an agreement with the plaintiff to limit its liability to its insurance policies."[51] The court rejected the ability of an insurer to refuse to defend, but then later to rely on other policy defenses. It reasoned that an insurer "cannot have its cake and eat it too by both refusing coverage and at the same time continuing to control the terms of settlement in defense of an action it had refused to defend."[52]

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[47] 337 S.W.3d at 708.
[48] 337 S.W.3d at 710.
[49] 337 S.W.3d at 709 (quoting Drennen v. Wren, 416 S.W.2d 229, 234-235 (Mo. Ct. App. 1967) (quoting Listerman v. Day & Night Plumbing & Heating Serv., 384 S.W.2d 111, 118-119 (Mo. Ct. App. 1964)).
[50] 337 S.W.3d at 709-710.
[51] 337 S.W.3d at 710.
[52] 337 S.W.3d at 710.

While both cases were addressing the insurer's failure to defend, *HIAR* goes further that *Schmitz* because it applies the analysis without the public policy overlay from section 537.065. In *Schmitz* the insured and the claimant had entered into a 537.065 agreement.[53] This statute authorizes an insured to reach a settlement with the claimant to limit recovery to the insurance policy.[54] The purpose of this statutory authorization is to allow an insured to protect its assets through such a settlement when an insurer refuses to do so. By entering in a 537.065 agreement, the insured takes advantage of this statutory approval for its conduct. Where an insured does not enter into such an agreement, it may can be argued that the usual common law contract rules should apply. Under those rules, breach of the duty to defend would entitle the insured to reimbursement of legal fees, but perhaps not more than that, especially not liability beyond the policy limits.

On the other hand, entering into a 537.065 agreement to allow the claimant to make a claim directly on the insurance policy may not be materially different than an insured who reaches a settlement agreement without reference to or reliance on 537.065. The primary differences between these two approaches is that in the latter the insured may have more personal exposure and that the case may be subject more litigation. These differences probably do not justify treating the two situations differently. If anything, the insurer is getting a greater benefit from the insured bearing some of the risk and litigating the case. Consequently, the danger of an insurer wanting to "have its cake and eat it too" seems just as great, or greater, when the insured is acting without the benefit of section 537.065,

***Schmitz* supports a strict-liability approach**

The court's analysis in *Schmitz* provides additional support for reading *HIAR* as imposing a kind of strict liability for breach of the duty to defend. In *HIAR* the rule as articulated by the Missouri

[53] 337 S.W.3d at 703.
[54] *See* R.S. Mo. § 537.065.

Supreme Court is: "The insurer that wrongly refuses to defend is liable for the underlying judgment as damages flowing from its breach of its duty to defend."[55] A key term here is "wrongful." This could suggest that an insurer must act in bad faith, or at least negligently, before it has to pay for all "damages flowing" from the breach. In *Schmitz*, however, the court does not use the terms "wrongful." Instead, the Missouri Supreme Court framed the issue as whether the refusal to defend was "unjustified."[56] This is an easier standard to meet. A breach of contract is generally considered to be unjustified because of the prior agreement supported by consideration. Wrongfulness may connote something more culpable than a mere breach of contract.

The strict-liability approach is further supported by *Schmitz* because the Missouri Supreme Court specifically rejected a defense of the insurer based on a purported "honest mistake." The court held that the insurer's "claim that its refusals were an honest mistake is of no consequence. 'That the refusal of the insurer to defend on the ground that the claim is outside the policy is an honest mistake, nevertheless constitutes an unjustified refusal and renders the insurer liable to the insured for all resultant damages from that breach of contract.'"[57] The court draws the connection between breach of contract and being unjustified, and imposes liability for consequential damages even with a relatively innocent state of mind. This is the language of strict liability. An insurer that makes "an honest mistake" still has to pay the consequential damages.

Case Law Subsequent to *HIAR*

[55] 411 S.W.3d at 265 (citing Schmitz v. Great American Assur. Co., 337 S.W.3d 700, 708-709 (Mo. 2011)).
[56] *See* 337 S.W.2d at 709-710 (the heading identified the issue as "Unjustifiable Refusal to Defend" and the court found that the trial court's rejection of the exclusion "rendered Great American's refusal to defend or to provide coverage unjustified").
[57] 337 S.W.3d at 710 (quoting Whitehead v. Lakeside Hosp. Ass'n, 844 S.W.2d 475, 481 (Mo. Ct. App. 1992)).

Two cases that have been decided in Missouri subsequent to *HIAR* have some bearing on its interpretation. The first was *Allen v. Continental Western Ins. Co.*,[58] decided by the Missouri Supreme Court in 2014. Although that case held that the insurer did not breach the duty to defend because an exclusion resulted in no potential for insurance coverage under the facts of the case,[59] it is noteworthy that the court's analysis turned entirely on whether there was coverage under the policy without regard for the reasonableness of the insurer's position. The *Allen* court concluded: "the 'expected or intended injury' exclusion plainly barred coverage for Franklin's intentional acts at the outset of Whipple's lawsuit, and Continental Western did not have a duty to defend."[60]

The second case, *McDonald v. Ins. Co. of Pennsylvania*,[61] the Missouri Court of Appeals followed the Supreme Court's analysis in *HIAR*. *McDonald* concerned damages for a trailer of frozen food that was ruined by delay in transportation. The claimants sued the transporter, its cargo insurer, and the insurer of the damaged food, and settled the claims against the two insurers for $62,500. The transporter defaulted, and the court entered a judgment for $116,664.66, the amount of damages determined by the court. The claimant then initiated a garnishment proceeding against the transporter's liability policy. The liability insurer had refused to defend the case because of a purported exclusion[62] and also sought an offset for the prior settlements. The court of appeals, citing to *HIAR*, noted that "The insurer that

[58] 436 S.W.3d 549 (Mo. 2014).
[59] The case concerned the repossession of a minivan. The claimant alleged that the insured, a payday and title lending company, "'deprived her of possession and control' [of the minivan] without her authorization." 436 S.W.3d at 550. The insured tendered the case to its general liability carrier, Continental Western, which refused to provide a defense due to the exclusion for intended or expected harm because the repossession "was intentional." *Id.* The insured argued that its alleged "mistaken beliefs" that the claimant was in default was enough to avoid the exclusion. *Id.* at 553. The court rejected this argument. Even if it were factually true, "there was no potential for coverage under the policy because Whipple sought recovery only for damages Franklin intended, which the policy unambiguously excluded." *Id*.
[60] 436 S.W.3d at 556.
[61] 460 S.W3d 58 (Mo. Ct. App. 2015).
[62] The trial court granted summary judgement to the claimant that the damages were covered by the policy. The exclusion for goods in "care, custody and control" did not apply because the damage occurred when the food was not in the transporter's control. 460 S.W.3d at 63. This part of the trial court's ruling was not raised on appeal.

wrongfully refuses to defend is liable for the underlying judgment as damages flowing from its breach of its duty to defend."[63] Because the liability insurer had refused to defend, it was not entitled to raise the defense of an offset because it had the "opportunity to control and manage the litigation" but failed to do so.[64]

Refusing to allow the insurer to receive an offset for the prior settlements looks like a penalty for the insurer's failure to provide a defense. Although there is some room to contend otherwise, the claimant was able to use the liability insurer's failure to defend to get a double recovery. [65] The insured defaulted and the claimant submitted the full amount of its damages to the court.[66] Neither the liability insurer, nor the insured, were present in the underlying default judgment, so there was no one with an incentive seek an offset. Yet the court of appeals nonetheless enforced the default judgment because of the liability insurer's failure to defend. The court takes the phrase "liable for the underlying judgment as damages flowing from its breach of its duty to defend"[67] quite literally, and does not seem concerned about the reasonableness of the offset or the fact that the judgment was uncontested and resulted in a windfall for the claimant.

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[63] 460 S.W.3d at 66 (quoting Columbia Cas. Co. v. HIAR Holding, LLC, 411 S.W.3d 258, 265 (Mo. 2013)).
[64] 460 S.W.3d at 66.
[65] As an alternative basis for its decision, the court of appeals notes that the allocation of the prior settlements "was a question of fact" that should have been addressed by the trial court in the underlying default judgment. 460 S.W.3d at 66. In addressing that question of fact, the insured would have the burden of proving an overlap between the settlement and the judgment. *Id*. While all of this is certainly true, because the offset argument was not raised by the parties or addressed by the court, there is no reason for the court's assumption that the settlements and the judgment were not duplicative. The evidence strongly suggests that the settlements were duplicative. The original suit that was settled claimed damages of $75,000.00 (settled by insurers for $62,250). 460 S.W.3d at 62. The default damages were as follows: $70,472.75 for lost frozen food, labor costs from delay of $693.75, lost profit of $27,085.73, and lost business of $18,412.43, for a total of $116,664.66. This total was the amount of the default judgment. 460 S.W.3d at 63. It is hard to imagine how these damages could not be duplicative with the settlement against the insurers that insured the frozen food.
[66] The default damages were $70,472.75 for lost frozen food, $693.75 for labor costs, $27,085.73 for lost profits, and $18,412.43 for lost business, for a total of $116,664.66. This total was the amount of the default judgment. 460 S.W.3d at 63.
[67] 411 S.W.3d at 265 (citing Schmitz v. Great American Assur. Co., 337 S.W.3d 700, 708-709 (Mo. 2011)).

Does Breach of the Duty to Defend Waive Policy Defenses without Breach of the Duty to Indemnify?

Although the above analysis demonstrates that under Missouri law the breach of the duty to defend waives an insurer's policy defenses where the insurer also breached its duty to indemnify, the case law has not yet addressed the question of whether breach of the duty to defend alone will waive policy defenses. It is axiomatic that the duty to defend is broader than the duty to indemnify, and that it applies to the mere potential for coverage.[68] Consequently, an insurer may owe a duty to defend, but as the case develops it may turn out that the insurer is not obligated to provide indemnification. If the insurer breaches its duty to defend in this situation, has it waived its policy defenses?

If one takes the statement of the Missouri rule literally, the insurer that breaches its duty to defend is obligated to pay for the subsequent liability without regard for whether the insurer had a duty to indemnify. The rule, once again, states: "The insurer that wrongly refuses to defend is liable for the underlying judgment as damages flowing from its breach of its duty to defend."[69] This rule says nothing about the duty to indemnify, and because the duty to defend is separate and independent of the duty to indemnify, it follows that breach of the duty to defend is sufficient to trigger liability for the underlying judgment. On the other hand, in both *HIAR* and *Schmitz* the court found that the insurer had breached its duty to indemnify as well. In both cases, the duty to defend and the duty to indemnify were treated together, as one and the same. Where the breach of the insurer's conduct breaches both the duty to defend and the duty to indemnify, the insurer's conduct is more "wrongful" and "unjustified." Thus,

[68] *See*, *e.g.*, Allen v. Continental Western Ins. Co., 436 S.W.3d 548, 552 (Mo. 2014); McCormack Baron Mgmt. Servs., Inc. v. American Guar. & Liab. Ins. Co., 989 S.W.2d 168, 170 (Mo. 1999); *see also* SETH D. LAMDEN, 3-17 NEW APPLEMAN ON INSURANCE LAW LIBRARY EDITION § 17.01[1][b].
[69] 411 S.W.3d at 265 (citing Schmitz v. Great American Assur. Co., 337 S.W.3d 700, 708-709 (Mo. 2011)).

perhaps the Missouri courts will not go so far as the rule seems to indicate when faced with the case in which there was a breach of the duty to defend but no breach of the duty to indemnify.