UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

* * * No. 73756

DANA ANDREW, as legal guardian on behalf of Ryan T. Pretner, and RYAN T. PRETNER,

Plaintiffs,

v.

CENTURY SURETY COMPANY,

Defendant.

Case No. 2:12-cv-00978-APG-PAL

ORDER CERTIFIYING QUESTION TO THE SUPREME COURT OF NEVADA

Pursuant to Rule 5 of the Nevada Rules of Appellate Procedure, this Court seeks guidance from and respectfully certifies to the Supreme Court of Nevada the following question of law that may be determinative of matters before this Court and as to which there is no clearly controlling precedent in the decisions of the Supreme Court or Court of Appeals of Nevada:

> Whether, under Nevada law, the liability of an insurer that has breached its duty to defend, but has not acted in bad faith, is capped at the policy limit plus any costs incurred by the insured in mounting a defense, or is the insurer liable for all losses consequential to the insurer's breach?

I. BACKGROUND

Plaintiff Ryan Pretner suffered catastrophic brain injuries after he was struck from behind by the side-view mirror of a truck while he was riding his bicycle on the shoulder of a road. The truck was driven by Michael Vasquez. Vasquez worked for Blue Streak, a mobile auto detailing business. Vasquez was personally insured by non-party Progressive Insurance. Blue Streak was insured by Century. Prior to any lawsuit being filed, Century declined to defend Blue Streak on the ground that Vasquez was not working in the course and scope of his employment for Blue Streak at the time of the accident. Century based its decision on Vasquez's statements to the police and to Century's employee that he was not working at the time of the accident.

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Pretner sued Vasquez and Blue Streak in state court. The complaint alleged that Vasquez was driving in the course and scope of employment for Blue Streak at the time of the accident. Pretner's attorney forwarded the lawsuit to Century, but Century again declined to defend Blue Streak. Vasquez and Blue Streak then defaulted in the state court action. Pretner's attorney forwarded the entry of default to Century. Century responded that the claim was not covered. Pretner, Vasquez, and Blue Streak then entered into a settlement agreement. Vasquez and Blue Streak agreed to allow Pretner to pursue a default judgment against them, and Blue Streak assigned to Pretner all of its claims against Century. In exchange, Pretner agreed to not execute against Vasquez and Blue Streak. Additionally, Progressive agreed to tender the $100,000 limits of its policy covering Vasquez.

Pretner moved for a default judgment in the state court action. After a hearing, the state court entered a default judgment against Vasquez and Blue Streak. The default judgment set forth factual findings that were deemed admitted by the default. Those findings include that Vasquez negligently injured Pretner, that Vasquez was working in the course and scope of his employment with Blue Streak at the time, and that consequently Blue Streak was also liable. The default judgment entered against both Vasquez and Blue Streak was for over $18 million. Pretner, as assignee of Blue Streak, then filed this lawsuit against Century for breach of contract, breach of the implied covenant of good faith and fair dealing, and unfair claims practices.

I previously ruled that Century breached its contractual duty to defend Blue Streak as a matter of law because the underlying complaint alleged facts that potentially fell within the policy's coverage, thereby triggering the duty to defend. ECF No. 168. As to the parties' dispute about whether Century was bound by the default judgment against its insured, I reviewed a line of decisions issued by the Supreme Court of Nevada that hold an insurer is bound by a judgment if it has notice of a lawsuit that implicates coverage but does not intervene. I predicted the Supreme Court of Nevada would not extend this line of cases beyond the uninsured motorist context. I therefore concluded Century was not bound by the default judgment. Finally, I set forth the measure of damages for breaching the duty to defend as the reasonable costs of defense in the

underlying action plus the damages reasonably foreseeable at the time of the contract, capped at the policy limit of $1 million. I concluded the recoverable damages were capped at the policy limit because Century did not act in bad faith.

The parties agreed that the issue of damages could be resolved without a jury trial. Accordingly, they filed motions for summary judgment on the damages arising from Century's breach of its duty to defend.

An insured is entitled to recover its costs of defense when an insurer breaches its duty to defend, but it is undisputed that Blue Streak did not incur any defense costs because it defaulted in the underlying personal injury lawsuit. The only other evidence of damages is the default judgment entered against Blue Streak after Century refused to defend it. The parties thus disputed whether this judgment constituted recoverable damages caused by Century's breach of the duty to defend. They also disputed what preclusive effect the underlying default judgment should have.

In ruling on the cross motions for summary judgment, I reconsidered my prior ruling that recovery was capped at the policy limit. ECF No. 210. I predicted that the Supreme Court of Nevada would allow Blue Streak to recover consequential damages for Century's breach of the duty to defend, and that a default judgment is a reasonably foreseeable result of a breach of the duty to defend. I also predicted that the Supreme Court of Nevada would rule that in the context of a breach of the duty to defend, bad faith is not required to impose liability on the insurer in excess of the policy limits.

Century moved for reconsideration of my ruling. ECF No. 218. Shortly thereafter, the United States Court of Appeals for the Ninth Circuit certified to the Supreme Court of Nevada the following question of law:

> Whether, under Nevada law, the liability of an insurer that has breached its duty to defend, but has not acted in bad faith, is capped at the policy limit plus any costs incurred by the insured in mounting a defense, or is the insurer liable for all losses consequential to the insurer's breach?

Nalder v. United Automobile Ins. Co., Ninth Cir. Case No. 13-17441. Given the similarities between the question certified in *Nalder* and the issues present in this case, I stayed this case in anticipation of the Supreme Court of Nevada deciding the question certified in *Nalder*. ECF No. 227.

Recent developments in the *Nalder* case have made it unclear whether the Supreme Court of Nevada will answer the question certified to it by the Ninth Circuit. The parties in this case have agreed that I shoulder certify the same question. ECF No. 251. I agree and therefore certify the same question of law to the Supreme Court of Nevada that was certified in *Nalder*.

II. PARTIES' NAMES AND DESIGNATION OF APPELLANT AND APPELLEE

Plaintiffs: Dana Andrew, as legal guardian on behalf of Ryan T. Pretner, and Ryan T. Pretner.

Defendant: Century Surety Company.

Because my last ruling was in favor of the plaintiffs, defendant Century Surety Company shall be the appellant.

III. NAMES AND ADDRESSES OF COUNSEL FOR THE PARTIES

Counsel for the plaintiffs:

Dennis Prince, Tracy Eglet, and Robert Eglet
Eglet Prince
400 S. 7th Street, Suite 400
Las Vegas, NV 89101

Eric Tran
Lipson Neilson Cole Seltzer & Garin
9900 Covington Cross Dr., Suite 120
Las Vegas, NV 89144

Counsel for the defendant:

James R. Gass and Michael Brennan
Gass Weber Mullins LLC
309 North Water Street, 7th Floor
Milwaukee, WI 53202

Maria Louise Cousineau
Cozen O'Connor
601 South Figueroa Street, Suite 3700
Los Angeles, CA 90017

Martin J. Kravitz
8985 S. Eastern Ave, Suite 200
Las Vegas, NV, 89123

IV. ANY OTHER MATTERS THE CERTIFYING COURT DEEMS RELEVANT TO A DETERMINATION OF THE QUESTIONS CERTIFIED

The Court defers to the Supreme Court of Nevada to decide whether it requires any other information to answer the certified question. The Court does not intend its framing of the question to limit the Supreme Court of Nevada's consideration of the issue.

V. CONCLUSION

Having complied with the provisions of Nevada Rule of Appellate Procedure 5(c), the Court hereby directs the clerk of court to forward this Order under official seal, along with ECF Nos. 168 and 210, to the Supreme Court of the State of Nevada, 201 South Carson Street, Suite 201, Carson City, Nevada 89701-4702.

DATED this 14th day of August, 2017.

ANDREW P. GORDON
UNITED STATES DISTRICT JUDGE

I hereby attest and certify on 8/14/2017 that the foregoing document is a full, true and correct copy of the original on file in my legal custody.

CLERK, U.S. DISTRICT COURT
DISTRICT OF NEVADA
By _____ Deputy Clerk

UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

* * *

DANA ANDREW, as legal guardian on behalf of Ryan T. Pretner, and RYAN T. PRETNER,

Plaintiffs,

v.

CENTURY SURETY COMPANY,

Defendant.

Case No. 2:12-cv-00978-APG-PAL

ORDER DENYING MOTIONS FOR SUMMARY JUDGMENT AND TO STRIKE

(DKT. #192, #194, #197)

This is an insurance dispute arising out of a car accident and subsequent personal injury lawsuit. I have already ruled that defendant Century Surety Company breached its duty to defend its insured, Blue Streak Auto Detailing, as a matter of law. The parties now dispute what damages, if any, were caused by the breach. It is undisputed that Blue Streak incurred no costs of defense because it defaulted in the underlying tort action. The only questions are whether the default judgment against Blue Streak constitutes damages for which Century is liable and, if so, to what extent.

I reconsider and modify my prior ruling that Century's liability in this case is capped at the policy limit of $1 million. Instead, I hold that the default judgment was a reasonably foreseeable consequential damage caused by Century's breach of its duty to defend its insured. I also reconsider my prior ruling that Century is not bound by the default judgment. I now hold that Century is bound by the default judgment, absent unreasonableness, fraud, or collusion. Century has shown the $5 million attorney fee award in the default judgment was unreasonable, so Century is not bound by that portion of the judgment. However, genuine issues of fact remain regarding whether the settlement agreement and subsequent default judgment were obtained through fraud or collusion. That issue, and the amount of recoverable damages, must be tried to a jury.

I. BACKGROUND

Plaintiff Ryan Pretner suffered catastrophic brain injuries after he was struck from behind by the side-view mirror of a truck while he was riding his bicycle on the shoulder of a road.[1] The truck was driven by Michael Vasquez. Vasquez worked for Blue Streak, a mobile auto detailing business. Vasquez was personally insured by non-party Progressive Insurance. Blue Streak was insured by Century. Prior to any lawsuit being filed, Century declined to defend Blue Streak on the ground that Vasquez was not working in the course and scope of his employment for Blue Streak at the time of the accident. Century based its decision on Vasquez's statements to the police and to Century's employee that he was not working at the time of the accident.

Pretner sued Vasquez and Blue Streak in state court. The complaint alleged that Vasquez was driving in the course and scope of employment for Blue Streak at the time of the accident. Pretner's attorney forwarded the lawsuit to Century, but Century again declined to defend Blue Streak. Vasquez and Blue Streak then defaulted in the state court action. Pretner's attorney forwarded the entry of default to Century. Century responded that the claim was not covered.

Pretner, Vasquez, and Blue Streak then entered into a settlement agreement. Vasquez and Blue Streak agreed to allow Pretner to pursue a default judgment against them, and Blue Streak assigned to Pretner all of its claims against Century. In exchange, Pretner agreed to a covenant not to execute against Vasquez and Blue Streak. Additionally, Progressive agreed to tender the $100,000 limits of its policy covering Vasquez.

Pretner moved for a default judgment in the state court action. After a hearing, the state court entered a default judgment against Vasquez and Blue Streak. The default judgment set forth factual findings that were deemed admitted by the default. Those findings include that Vasquez negligently injured Pretner, that Vasquez was working in the course and scope of his employment with Blue Streak at the time, and that consequently Blue Streak was also liable. The default judgment entered against both Vasquez and Blue Streak was for over $18 million.

[1] I previously set forth the facts of this case in more detail at Dkt. #123.

Pretner, as assignee of Blue Streak, then filed this lawsuit against Century for breach of contract, breach of the implied covenant of good faith and fair dealing, and unfair claims practices. I previously ruled that Century breached its contractual duty to defend Blue Streak as a matter of law because the underlying complaint alleged facts that potentially fell within the policy's coverage, thereby triggering the duty to defend. (Dkt. #168 at 8-9.) As to the parties' dispute about whether Century was bound by the default judgment against its insured, I reviewed a line of decisions issued by the Supreme Court of Nevada that hold an insurer is bound by a judgment if it has notice of a lawsuit that implicates coverage but does not intervene. I predicted the Supreme Court of Nevada would not extend this line of cases beyond the uninsured motorist context. (*Id.* at 9-13.) I therefore concluded Century was not bound by the default judgment. (*Id.*) Finally, I set forth the measure of damages for breaching the duty to defend as the reasonable costs of defense in the underlying action plus "the damages reasonably foreseeable at the time of the contract, capped at $1 million." (*Id.* at 15-16.) I concluded the recoverable damages were capped at the policy limit of $1 million because no genuine issue of fact remained that Century did not act in bad faith. (*Id.* at 17.)

The parties agreed that the issue of damages could be resolved without a jury trial. Accordingly, they filed motions for summary judgment on the issue of damages arising from Century's breach of its duty to defend.

An insured is entitled to recover its costs of defense when an insurer breaches its duty to defend, but it is undisputed that Blue Streak did not incur any defense costs because it defaulted in the underlying personal injury lawsuit. The only other evidence of damages is the default judgment entered against Blue Streak after Century refused to defend it. The parties dispute whether this judgment constitutes recoverable damages caused by Century's breach of the duty to defend. They also dispute what preclusive effect the underlying default judgment should have.

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II. ANALYSIS

A. Consequential Damages and the Policy Limits

Pretner bears the burden of showing the default judgment constitutes damages to Blue Streak caused by Century's breach. *See Clark Cnty. Sch. Dist. v. Richardson Constr., Inc.*, 168 P.3d 87, 96 (Nev. 2007). As stated in my prior order, the Supreme Court of Nevada has not specifically set forth the measure of damages for an insurer's contractual breach of the duty to defend. (Dkt. #168 at 14.) However, in the related context of an indemnitor's breach of the duty to defend, the Court stated that the breach "may give rise to damages in the form of reimbursement of the defense costs the indemnitee was thereby forced to incur in defending against claims encompassed by the indemnity provision." *Reyburn Lawn & Landscape Designers, Inc. v. Plaster Dev. Co., Inc.*, 255 P.3d 268, 278 (Nev. 2011) (quotation omitted).

Nevada law provides that in a breach of contract case, a plaintiff may seek compensatory damages, which "are awarded to make the aggrieved party whole and . . . should place the plaintiff in the position he would have been in had the contract not been breached." *Hornwood v. Smith's Food King No. 1*, 807 P.2d 208, 211 (Nev. 1991). This includes expectancy damages, which are determined by the method set forth in the Restatement (Second) of Contracts § 347 (1981). *Road & Highway Builders v. N. Nev. Rebar*, 284 P.3d 377, 382 (Nev. 2012). Under § 347:

> [s]ubject to the limitations stated in §§ 350-53, the injured party has a right to damages based on his expectation interest as measured by
>
> (a) the loss in value to him of the other party's performance caused by its failure or deficiency, plus
>
> (b) any other loss, including incidental or consequential loss, caused by the breach, less
>
> (c) any cost or other loss that he has avoided by not having to perform.

Under the contract, Blue Streak expected Century to provide a defense and, if Blue Streak is found liable on a covered claim, the payment of $1 million. Thus, under § 347(a), Blue Streak's expectancy damages are the costs of defense plus the policy limit of $1 million (applied to any award entered against Blue Streak in the underlying lawsuit).

Under § 347(b), Blue Streak also is entitled to consequential damages for Century's breach of the duty to defend. Consequential losses are those damages that "aris[e] naturally, or were reasonably contemplated by both parties at the time they made the contract." *Hornwood v. Smith's Food King No. 1*, 772 P.2d 1284, 1286 (Nev. 1989) (quotation omitted); *see also* Restatement (Second) of Contracts § 351(1) (1981) ("Damages are not recoverable for loss that the party in breach did not have reason to foresee as a probable result of the breach when the contract was made."). A loss "may be foreseeable as a probable result of a breach because it follows from the breach (a) in the ordinary course of events, or (b) as a result of special circumstances, beyond the ordinary course of events, that the party in breach had reason to know." Restatement (Second) of Contracts § 351(2).

The insurer's duty to defend "is of vital importance to the insured." *Amato v. Mercury Cas. Co.*, 53 Cal. App. 4th 825, 832 (Cal. Ct. App. 1997); *see also Dewitt Constr. Inc. v. Charter Oak Fire Ins. Co.*, 307 F.3d 1127, 1137 (9th Cir. 2002) ("The duty to defend is one of the main benefits of the insurance contract.") (quotation omitted). "The insured's desire to secure the right to call on the insurer's superior resources for the defense of third party claims is, in all likelihood, typically as significant a motive for the purchase of insurance as is the wish to obtain indemnity for possible liability." *Amato*, 53 Cal. App. 4th at 832 (quotation omitted). When the insurer breaches the duty to defend, a default judgment is a reasonably foreseeable result because, in the ordinary course, when an insurer refuses to defend its insured, a probable result is that the insured will default. *See Hamlin Inc. v. Hartford Acc. & Indem. Co.*, 86 F.3d 93, 94 (7th Cir. 1996) ("An insurance company that refuses a tender of defense by its insured takes the risk not only that it may eventually be forced to pay the insured's legal expenses but also that it may end up having to pay for a loss that it did not insure against. If the lack of a defender causes the insured to throw in the towel in the suit against it, the insurer may find itself obligated to pay the entire resulting judgment or settlement even if it can prove lack of coverage."); *Delatorre v. Safeway Ins. Co.*, 989 N.E.2d 268, 276 (Ill. Ct. App. 2013) (stating a default judgment against the insured was "the natural consequence of his insurer's breach of contract"); *Maxwell v. Hartford Union High Sch.*

Dist., 814 N.W.2d 484, 496 (Wis. 2012) (stating that one form of damages that "naturally flow[s] from an insurer's breach of its duty to defend" is "the amount of the judgment or settlement against the insured plus interest," because this is a "measure of damages actually caused by an insurer's breach of the contractual duty to defend") (quotation omitted); *Amato*, 53 Cal. App. 4th at 834 ("When the insurer refuses to defend and the insured does not employ counsel and presents no defense, it can be said the ensuing default judgment is proximately caused by the insurer's breach of the duty to defend.") (emphasis omitted).

Courts disagree, however, on whether, in the absence of bad faith, an insured can recover in excess of the policy limits when the insurer breaches the duty to defend. Some courts state that in the absence of bad faith, an insurer who breaches the duty to defend is liable on the underlying settlement or judgment only to the extent of the policy limits. *See, e.g.*, *State Farm Mut. Auto. Ins. Co. v. Paynter*, 593 P.2d 948, 954-55 (Ariz. Ct. App. 1979) (holding that the insurer's liability for refusing to defend "should be confined to the limits of the policy"); *Waite v. Aetna Cas. & Sur. Co.*, 467 P.2d 847, 851 (Wash. 1970) (stating an insurer who wrongfully refuses to defend "will be required to pay the judgment or settlement to the extent of its policy limits" and reimburse the defense costs); *Schurgast v. Schumann*, 242 A.2d 695, 705 (Conn. 1968) (stating that an insurer that breached its contractual duty to defend was "under a duty to pay the judgment obtained against [the insured] up to the limit of liability fixed by its policy"); *Comunale v. Traders & Gen. Ins. Co.*, 50 Cal. 2d 654, 659 (Cal. 1958) ("Where 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."). Courts adhering to this rule do not always explain why the damages for a breach of the duty to defend are capped by the policy limit on the separate duty to indemnify.

One explanation of the reasoning behind this rule is that "the measure of damages for the breach of a contract for the payment of money is the amount agreed to be paid with interest," and a breach of the duty to defend "cannot be held to enlarge the limitation as to the amount fixed as reimbursement for injuries to persons." *Mannheimer Bros. v. Kansas Cas. & Sur. Co.*, 184 N.W.

189, 191 (Minn. 1921). This explanation does not address consequential damages resulting from the breach of the duty to defend. The duty to defend is not based on the contractual promise to pay a certain amount of money to an injured person. Instead, it is a promise to provide a defense, the breach of which may result in consequential damages to the insured beyond the policy limits. *Mannheimer*'s reasoning makes sense in terms of the duty to indemnify because absent bad faith, the parties would expect the insurer to pay only the policy limits on indemnification. But it does not explain why a breach of the duty to defend should be subject to the policy's indemnification limit, which is a separate duty with separate remedies for its breach. *See Stockdale v. Jamison*, 330 N.W.2d 389, 393 (Mich. 1982), *holding limited by Frankenmuth Mut. Ins. Co. v. Keeley*, 447 N.W.2d 691 (Mich. 1989), ("Some cases state that an insurance contract is for the payment of a specific sum of money, ignoring the separate duty to defend.").

Courts that have limited damages to the policy limits have suggested that there may be circumstances where the breach of the duty to defend may require the insurer to pay in excess of the policy limits. *See Rogan v. Auto-Owners Ins. Co.*, 832 P.2d 212, 218 n.4 (Ariz. Ct. App. 1991) ("Obviously, there may be other circumstances in which a causal connection between . . . the refusal to defend and the excess judgment occurs," and offering the example where "the insured suffers a default or final judgment without the benefit of an attorney."); *Mannheimer Bros.*, 184 N.W. at 191 (declining to address whether damages would be capped by the policy limits if, for example, the insurer had a duty to defend but failed to appeal and the appeal would have been successful). Other courts have affirmatively held that the breach of the duty to defend may require the insurer to pay in excess of the policy limits where that breach proximately causes the excess judgment against the insured, such as where the insured defaulted, because the judgment constitutes consequential damages. *See Khan v. Landmark Am. Ins. Co.*, 757 S.E.2d 151, 156 (Ga. Ct. App. 2014) (stating that "the possible damages at issue are not merely those within the indemnity coverage of the policy, but are those further damages that may flow from breach of the contract to defend" as consequential damages); *Delatorre*, 989 N.E.2d at 276 (holding insurer's failure to defend caused default and insurer therefore was liable for judgment

in excess of policy limits as consequential damages); *Maxwell*, 814 N.W.2d at 496-97 ("When an insurer breaches a duty to defend its insured, the insurer is on the hook for all damages that result from that breach of its duty . . . includ[ing] damages beyond the policy limits."); *Reis v. Aetna Cas. & Sur. Co. of Ill.*, 387 N.E.2d 700, 710 (Ill. Ct. App. 1978) (stating that "damages for a breach of the duty to defend are not inexorably imprisoned within the policy limits, but are measured by the consequences proximately caused by the breach"); *Thomas v. W. World Ins. Co.*, 343 So.2d 1298, 1302 (Fla. Ct. App. 1977) (stating "the insurer may be liable for an excess judgment where (1) due to the actions of the insurer, the insured suffers a default or final judgment without benefit of an attorney, and (2) the insured can prove the final judgment would have been lower had the suit been properly defended").

Thus, in the context of a breach of the duty to defend, bad faith is not required to impose liability on the insurer in excess of the policy limits. This does not negate the distinction between a breach of the contractual duty to defend and a bad faith breach of the contract. There are still consequences for an insurer acting in bad faith, including that it may require the insurer to pay even unforeseeable consequential damages as well as punitive damages. *See Bainbridge, Inc. v. Travelers Cas. Co. of Conn.*, 159 P.3d 748, 756 (Colo. Ct. App. 2006) ("If the circumstances are sufficiently egregious to constitute a tort, then the consequential damages include all damages that were proximately caused by the breach, regardless of foreseeability."); *White v. Unigard Mut. Ins. Co.*, 730 P.2d 1014, 1017-18 (Idaho 1986) (same); *United Fire Ins. Co. v. McClelland*, 780 P.2d 193, 198 (Nev. 1989) (punitive damages). Moreover, there is no justification for making a special rule about consequential damages for insurers. Nevada's usual rule is that any party that breaches a contract is liable for consequential damages. Insurers should be held to the same standard. *Stockdale*, 330 N.W.2d at 392 ("If the insurer had an obligation to defend and failed to fulfill that obligation, then, like any other party who fails to perform its contractual obligations, it becomes liable for all foreseeable damages flowing from the breach."); *Thomas*, 343 So.2d at 1304 ("It seems only fair that an insurer whose contracts are by their very nature 'adhesive' should be held to at least the same standard of damages applicable to other contracting parties.").

In Nevada, the amount expected to be paid under a contract is not the only measure of damages for a breach. Nevada also allows recovery of consequential losses. Thus, if the default judgment was a reasonably foreseeable consequence of Century's breach, then Century is liable for the entire amount of the default judgment as consequential damages resulting from the breach of its duty to defend, regardless of the policy limits.

Century argues that if it is liable for the entire default judgment amount, then the insured is receiving policy benefits he did not contract for and the insurer is paying for a risk it did not contractually agree to cover. But Century is confusing its indemnification obligations with its duty to defend. Century agreed to defend its insured, and under Nevada law it is liable for consequential damages arising from a breach of that duty, even if its separate duty to indemnify would limit recovery to $1 million for a breach of that contractual provision.

Century next argues that if it is liable for the entire default judgment without capping it at the policy limit, the insured is placed in a better position than it would have been in had Century performed its contractual obligations. According to Century, if it had performed, the most Blue Streak could have hoped for is $1 million plus costs of defense. This again confuses the duty to indemnify with the duty to defend. If Century had performed, by Century's own arguments Blue Streak would have had a complete defense to any liability (that is, Blue Streak would not be liable because Vasquez was not driving in the course and scope of his employment). Blue Streak therefore would have been entitled to a judgment in its favor against Pretner. Instead, Blue Streak defaulted and now has an $18 million judgment against it. *See Delatorre*, 989 N.E.2d at 276 (stating the "general rule . . . for breach of contract [is to] place the injured party in the same position it would have been in had the contract been fully performed. Here, no default, no default judgment.") (internal citation omitted).

As to foreseeability, Century argues that it was not reasonably foreseeable at the time of contracting that it would have to pay for a non-covered claim. But holding Century liable for the default judgment would not be based on Century indemnifying Blue Streak for a non-covered claim. It is based on Century having to pay for all consequential damages arising out of a breach

of its duty to defend its insured. Century has not argued it was unforeseeable that its insured, a mobile auto detailing business, could cause a car accident resulting in catastrophic injuries. It also was foreseeable that a plaintiff's attorney would allege that the business's vehicle was being used in the course and scope of employment at the time of the accident. It therefore was foreseeable at the time of contracting that if Century refused to provide a defense in the face of such allegations, a substantial default judgment against its insured could result.

As for proximate cause, Century has consistently asserted that Vasquez was not in the course and scope of employment at the time of the accident. Thus, by Century's own position, had it defended Blue Streak, Blue Streak would have obtained a judgment in its favor instead of an $18 million judgment against it. Consequently, Century's breach of its duty to defend proximately caused the default judgment. *See Thomas*, 343 So.2d at 1302; *Rogan*, 832 P.2d at 218 n.4 (stating "there may be . . . circumstances in which a causal connection between . . . the refusal to defend and the excess judgment occurs," such as where "the insured suffers a default or final judgment without the benefit of an attorney").[2]

In sum, Nevada law allows for recovery of all reasonably foreseeable consequential damages for a breach of contract, regardless of the good or bad faith of the breaching party. There is no special rule for insurers that caps their liability at the policy limits for a breach of the duty to defend. I therefore reconsider my prior ruling that because Century did not act in bad faith, its liability is capped at the $1 million policy limits. A district court "possesses the inherent procedural power to reconsider, rescind, or modify an interlocutory order for cause seen by it to be sufficient," so long as it has jurisdiction. *City of L.A., Harbor Div. v. Santa Monica Baykeeper*, 254 F.3d 882, 885 (9th Cir. 2001) (quotation and emphasis omitted); *see also Smith v. Clark Cnty. Sch. Dist.*, 727 F.3d 950, 955 (9th Cir. 2013) ("It is common for both trial and appellate courts to reconsider and change positions when they conclude that they made a mistake."). The

[2] For an example of when the breach of the duty to defend would not proximately cause an excess judgment, *see Rogan*, 832 P.2d at 217 (stating there is no causal connection between the breach of the duty to defend and an excess judgment where the insured defends itself because "[g]iven competent counsel to represent the insured, the judgment would be the same as if the defense had been conducted by the insurer's counsel").

default judgment represents consequential damages to Blue Streak that may be recoverable as a result of Century's breach of the duty to defend.

B. Reconsideration of the Binding Effect of the Underlying Judgment

Century contends that it should not be bound by the default judgment, including the amount of the judgment. In a prior order, I agreed with Century's position. I noted that the "Nevada Supreme Court has held that where an insurer has notice of an adversarial proceeding that implicates uninsured motorist coverage under its policy but refuses to intervene, the insurer will be bound by the judgment thereafter obtained." (Dkt. #168 at 9-10 (citing *Allstate Ins. Co. v. Pietrosh*, 454 P.2d 106, 111 (Nev. 1969)).) I noted that the *Pietrosh* court subverted the normal privity requirement for claim and issue preclusion, but that the "public policy favoring intervention and 'avoiding multiple litigation . . . carries greater weight' than the policy requiring privity for application of preclusion in the insurance context." (*Id.* at 10 (quoting *Pietrosh*, 454 P.2d at 111).)

I considered two other cases in the uninsured motorist context, *State Farm Mutual Automobile Insurance Company v. Christensen*, 494 P.2d 552 (Nev. 1972) and *Estate of Lomastro v. American Family Insurance Group*, 195 P.3d 339 (Nev. 2008). (*Id.* at 10-11.) *Christensen* held that an insurer who elects not to intervene in its insured's lawsuit against an uninsured motorist is bound by a default judgment entered against the uninsured motorist. 494 P.2d at 553. The Supreme Court of Nevada reached a similar result in *Lomastro*. There, the insurer did not intervene in its insured's lawsuit against the uninsured motorist until after the uninsured motorist had defaulted. 195 P.3d at 1063. The trial court allowed intervention, but it held that the entry of default barred the insurer from contesting the uninsured motorist's liability. *Id.* The Supreme Court of Nevada affirmed, holding that the entry of default was sufficient to bind the insurer. *Id.* at 1067-69.

After reviewing these cases, I concluded they were "best limited to the context of uninsured motorist claims" because the Supreme Court of Nevada had not extended the principles to the general liability context. (Dkt. #168 at 12-13.) Additionally, the cases eliminated the

privity requirement in this particular context where it would be virtually impossible for the insured to show his insurer was in privity with the uninsured motorist. (*Id.*) I noted that the Supreme Court of Nevada later held, in a case not involving insurance, that a default judgment based on a defendant's failure to answer does not have preclusive effect because the issues have not been actually litigated under these circumstances. (*Id.* at 13 (citing *In re Sandoval*, 232 P.3d 422, 425 (Nev. 2010)).) As a result of this analysis, I held the *Pietrosh*, *Christensen*, and *Lomastro* line of cases is best limited to the uninsured motorist context and Century therefore is not bound by the default judgment against Blue Streak. (*Id.*)

After reevaluating relevant authority, including *Pietrosh*'s reasoning and other jurisdictions' decisions, I now reconsider my earlier decision. Many jurisdictions hold that when an insurer has notice of the lawsuit against its insured and breaches its duty to defend, it is bound by the resulting judgment, default judgment, or settlement, in the absence of fraud or collusion, with respect to all material findings of fact necessary to the judgment or settlement.[3] This is a

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[3] *See Pershing Park Villas Homeowners Ass'n v. United Pac. Ins. Co.*, 219 F.3d 895, 901 (9th Cir. 2000) (applying California law and stating it is the "general rule . . . that an insurer that wrongfully refuses to defend is liable on the judgment against the insured," and it is "no defense that the ultimate judgment against the insured is not rendered on a theory within the coverage of the policy."); *Hamlin Inc.*, 86 F.3d at 94; *St. Paul Fire & Marine Ins. Co. v. Vigilant Ins. Co.*, 919 F.2d 235, 240-41 (4th Cir. 1990) (applying North Carolina law that an insurer who breaches the duty to defend "is estopped from denying coverage and is obligated to pay the amount of any reasonable settlement made in good faith by the insured") (quotation omitted); *Colorado Cas. Ins. Co. v. Safety Control Co.*, 288 P.3d 764, 770 (Ariz. Ct. App. 2012) ("As long as the stipulated judgment is not fraudulent or collusive, an insurer that has failed to defend is bound by the judgment with respect to all matters which were litigated or could have been litigated in that action.") (quotation omitted); *Chandler v. Doherty*, 702 N.E. 2d 634, 639 (Ill. Ct. App. 1998) (stating that when an insurer breaches its duty to defend, "the insurer is estopped from asserting any policy exclusions or defenses in a later garnishment action by the insured or a judgment creditor"); *Willcox v. Am. Home Assur. Co.*, 900 F. Supp. 850, 855 (S.D. Tex. 1995) ("As a consequence of the breach, the insurer is liable for any damages assessed against the insured, up to the policy limits, subject only to the condition that any settlement be reasonable."); *Pruyn v. Agric. Ins. Co.*, 36 Cal. App. 4th 500, 514 (Cal. Ct. App. 1995) ("It is the general rule that a liability insurer who has had an opportunity to defend the underlying action brought against its insured is bound by the judgment against its insured as to all issues which were litigated in the action.") (quotation omitted); *Paynter*, 593 P.2d at 950 (collecting cases applying the "general rule" that "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"); *Kelly v. Cherokee Ins. Co.*, 574 S.W.2d 735, 737 (Tenn. 1978) ("We have no quarrel with the general rule that in the absence of fraud or collusion an insurer, who has the duty to defend, has timely notice and defends or elects not to defend, is bound by the judgment in such a case as to issues which were or might have been litigated therein."); *Hogan v. Midland Nat'l Ins. Co.*, 476 P.2d 825, 832 (Cal. 1970) ("An insurer that has been notified of an action and refuses

consequence of the insurer's breach of the duty to defend. *Pruyn v. Agric. Ins. Co.*, 36 Cal. App. 4th 500, 515 n.15 (Cal. Ct. App. 1995) ("One of the consequences of an insurer's failure to defend is that it may be bound, in a subsequent suit to enforce the policy . . . by the express or implied resolution in the underlying action of the factual matters upon which coverage turns."). It is designed to encourage the insurer to participate to avoid multiple lawsuits over the same issues and to prevent inconsistent judgments. *See Hamilton v. Maryland Cas. Co.*, 41 P.3d 128, 135 (Cal. 2002) ("In effect, when the insured tenders the suit, the carrier is receiving its chance to be heard. Having rejected the opportunity and waived the chance to contest liability, it cannot reach back for due process to void a deal the insured has entered to eliminate personal liability.") (quotation omitted); *Exec. Risk Indem., Inc. v. Jones*, 171 Cal. App. 4th 319, 333-35 (Cal. Ct. App. 2009) ("It is not unfair that an insurance company is not entitled to relitigate issues in a second lawsuit that it had the right to litigate in the initial lawsuit. Rather, that potential result will encourage the insurance company to participate in the initial action.").

These policy concerns are similar to those identified by the Supreme Court of Nevada in *Pietrosh*. There, the Court noted that insurance policies are not "ordinary" contracts because they are "complex instrument[s], unilaterally prepared and seldom understood by the insured." 454 P.2d at 110. Consequently, the insured and insurer "are not similarly situated. The company and its representatives are expert in the field; the insured is not." *Id.* The Supreme Court of Nevada therefore "place[s] the burden of affirmative action upon the insurance company." *Id.* Additionally, the Court concluded that "the avoidance of multiple litigation" carried "greater weight" than concerns about privity and forcing the insurer to intervene. *Id.* at 111.

These policy considerations, along with the related concern of preventing inconsistent judgments, are not unique to the uninsured/underinsured motorist context. Rather, they are magnified when an insurer breaches its duty to defend its insured because the insurer not only had

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to defend on the ground that the alleged claim is not within the policy coverage is bound by a judgment in the action, in the absence of fraud or collusion, as to all material findings of fact essential to the judgment of liability of the insured. The insurer is not bound, however, as to issues not necessarily adjudicated in the prior action and can still present any defenses not inconsistent with the judgment against the insured.") (quotation omitted).

the opportunity to participate, it had a contractual obligation to do so. Further, binding an insurer to the underlying judgment when it breaches its duty to defend incentivizes it to resolve all doubts about the duty to defend in the insured's favor by raising the risk level for an insurer who opts not to defend. *See United Nat'l Ins. Co. v. Frontier Ins. Co., Inc.*, 99 P.3d 1153, 1158 (Nev. 2004) (en banc) ("If there is any doubt about whether the duty to defend arises, this doubt must be resolved in favor of the insured."); Restatement (Second) of Judgments § 58 cmt. a ("The duty to provide a defense is enforced by rules creating strong disincentives against default in performance of the duty.").

> This is consistent with the Restatement (Second) of Judgments § 58:
>
> (1) When an indemnitor has an obligation to indemnify an indemnitee (such as an insured) against liability to third persons and also to provide the indemnitee with a defense of actions involving claims that might be within the scope of the indemnity obligation, and an action is brought against the indemnitee involving such a claim and the indemnitor is given reasonable notice of the action and an opportunity to assume its defense, a judgment for the injured person has the following effects on the indemnitor in a subsequent action by the indemnitee for indemnification:
>
> > (a) The indemnitor is estopped from disputing the existence and extent of the indemnitee's liability to the injured person; and
> >
> > (b) The indemnitor is precluded from relitigating those issues determined in the action against the indemnitee as to which there was no conflict of interest between the indemnitor and the indemnitee.

See also id. cmt. a, illus. 1; Restatement (First) of Judgments § 107 cmts. c, f (1942) (stating that if an indemnitor owes a duty to defend and "fails to give this assistance at the time when it is of greatest importance, it is fair that he should abide by the result of the trial" even in the case of a default judgment, so long as there is no fraud or collusion). The Supreme Court of Nevada looks to the Restatement of Judgments for guidance. *See, e.g., Alcantara ex rel. Alcantara v. Wal-Mart Stores, Inc.*, 321 P.3d 912, 915-18 (Nev. 2014); *Personhood Nevada v. Bristol*, 245 P.3d 572, 576 (Nev. 2010). Thus, I predict[4] that the Supreme Court of Nevada would extend the *Pietrosh* line

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[4] When a federal court interprets state law, it is bound by the decisions of the state's highest court. *Assurance Co. of Am. v. Wall & Assocs. LLC of Olympia*, 379 F.3d 557, 560 (9th Cir. 2004). Where the state's highest court has not decided the issue, a federal court must predict how the state's highest court would decide. *Orkin v. Taylor*, 487 F.3d 734, 741 (9th Cir. 2007). I may use "decisions from other

of cases beyond the uninsured/underinsured motorist context to bind an insurer who breaches its duty to defend in the general liability context and would preclude the insurer from re-litigating material findings of fact essential to the judgment against the insured.

This includes precluding the insurer from re-litigating a coverage defense that contradicts the facts necessary to the underlying judgment. Some courts allow an insurer who breaches its duty to defend to contest whether the underlying judgment or settlement actually falls within the policy's coverage.[5] These courts reason that the duty to defend and the duty to indemnify are separate contractual obligations, so allowing an insured to recover the amount of the judgment or settlement for a non-covered claim confuses the two duties and their appropriate remedies. *See Flannery v. Allstate Ins. Co.*, 49 F. Supp. 2d 1223, 1227-28 (D. Colo. 1999); *Sentinel Ins. Co., Ltd. v. First Ins. Co. of Hawai'i, Ltd.*, 875 P.2d 894, 912 (Haw. 1994) (stating that binding an insurer to a finding of coverage based on a breach of the duty to defend "subverts any meaningful distinction between the duty to defend and the separate duty to indemnify and, in many cases, serves no more than to punish the insurer for the breach of a contractual duty"). These courts also reason that precluding the insurer from challenging coverage creates a bargain the parties did not agree to by extending coverage to non-covered claims. *See Colonial Oil Indus. Inc. v. Underwriters Subscribing to Policy Nos. TO31504670 & TO31504671*, 491 S.E.2d 337, 339 (Ga.

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jurisdictions, statutes, treatises, and restatements as guidance." *Assurance Co.*, 379 F.3d at 560 (quotation omitted).

[5] *See, e.g.*, *Dewitt Constr. Inc.*, 307 F.3d at 1137 (applying Washington law); *Enserch Corp. v. Shand Morahan & Co., Inc.*, 952 F.2d 1485, 1493 (5th Cir. 1992) (stating that although the breaching insurer is bound by a finding of the insured's liability, coverage is a different question, and coverage cannot be created through estoppel); *Underwriters at Lloyds v. Denali Seafoods, Inc.*, 927 F.2d 459, 464 (9th Cir. 1991) (stating "an insurer's failure to defend a claim ultimately found not to be covered by the policy should not be subject to reimbursement within the policy limits"); *Flannery v. Allstate Ins. Co.*, 49 F. Supp. 2d 1223, 1227-28 (D. Colo. 1999) (noting disagreement and collecting cases on both sides, and ultimately adopting the rule that an insurer is not precluded from contesting coverage); *Colo. Cas. Ins. Co.*, 288 P.3d at 771 (stating an insurer "is liable for the stipulated judgment only if the judgment constituted a liability falling within its policy"); *Colonial Oil Indus. Inc. v. Underwriters Subscribing to Policy Nos. TO31504670 & TO31504671*, 491 S.E.2d 337, 339 (Ga. 1997); *Missouri Terrazzo Co. v. Iowa Nat'l Mut. Ins. Co.*, 740 F.2d 647, 652 (Mo. Ct. App. 1984) (stating that "an insurance company is liable to the limits of its policy plus attorney fees, expenses and other damages where it refuses to defend an[] insured who is in fact covered") (quotation omitted).

1997) (stating that the duty to indemnify is independent of the duty to defend, and breach of the duty to defend "should not enlarge indemnity coverage beyond the parties' contract"); *Sentinel Ins. Co., Ltd.*, 875 P.2d at 912 (citing cases); *Servidone Constr. Corp. v. Sec. Ins. Co. of Hartford*, 64 N.Y.2d 419, 424 (1985) ("By holding the insurer liable to indemnify on the mere 'possibility' of coverage perceived from the face of the complaint . . . the court has enlarged the bargained-for coverage as a penalty for breach of the duty to defend, and this it cannot do.").

But other courts allow the breaching insurer to contest coverage only so long as it does not contradict any findings in the underlying judgment against its insured. These courts reason that the insurer had not only the opportunity but the obligation to participate in the litigation, and the insurer therefore cannot re-litigate any issue decided in the judgment, default judgment, or settlement against its insured. Additionally, requiring the insurer to participate or be bound prevents multiple lawsuits on the same questions and avoids potential inconsistent results. *See* n.2 *supra*.

Because the Supreme Court of Nevada has already expressed its policy preferences in favor of putting the burden on the insurer to intervene and avoiding multiple lawsuits, and because that Court tends to follow the Restatement, I predict it would hold that an insurer cannot re-litigate any issue of coverage that would contradict the facts necessary to the insured's liability in the underlying action. However, the insurer is bound only to those matters necessary to resolve the insured's liability. Thus, if an insurer has other coverage defenses that do not deny the factual findings in the underlying judgment or settlement, the insurer still may raise those defenses. *See, e.g.*, *Hogan v. Midland Nat'l Ins. Co.*, 476 P.2d 825, 832 (Cal. 1970) (stating the insurer is not bound "as to issues not necessarily adjudicated in the prior action and can still present any defenses not inconsistent with the judgment against the insured") (quotation omitted); *Pruyn*, 36 Cal. App. 4th at 515 n.15 (stating that "where the issues upon which coverage depends are not raised or necessarily adjudicated in the underlying action, then the insurer is free to litigate those issues in the subsequent action and present any defenses not inconsistent with the judgment.

against its insured"); Restatement (Second) of Judgments § 58(1)(b); Restatement (First) Judgments § 107 cmt. g (1942).

Here, Century knew the underlying complaint alleged Vasquez was working in the course and scope of his employment for Blue Streak, and it knew an entry of default had been entered against Blue Streak. Under Nevada law, facts in the complaint are deemed admitted by an entry of default. *Lomastro*, 195 P.3d at 345. Thus, Century assumed the risk that these facts would be found against its insured if a default judgment was entered. If Century wanted to litigate the issue of whether Vasquez was in the course and scope of his employment, it should have "provided a defense, reserved its rights, and filed a motion for summary judgment in the early stages of the [u]nderlying [l]awsuit to resolve that issue up front." (Dkt. #168 at 9 n.3.) Or it could have provided a defense and filed a separate lawsuit for a declaration that it owed no duty to defend. But what it cannot do is abandon its insured, allow a default judgment to be taken, and then re-litigate any fact necessarily decided in the default judgment. Permitting it to do so would contravene the Supreme Court of Nevada's policy choice to give greater weight to avoiding multiple lawsuits than to concerns about privity or forcing an insurer to intervene. Additionally, precluding Century from re-litigating these issues prevents inconsistent judgments and encourages insurers to comply with their duty to defend.

At the September 17, 2015 hearing, Century argued that it should not be bound by the underlying judgment because an insurer who denies coverage has a conflict of interest with its insured. Some courts acknowledge an exception from the usual rule that an insurer is bound by the underlying judgment where the insurer and insured have a conflict of interest. *See Farm Bureau Mut. Auto. Ins. Co. v. Hammer*, 177 F.2d 793, 801 (4th Cir. 1949); *State Farm Fire & Cas. Co. v. Garrity*, 785 F.2d 1225, 1226 (4th Cir. 1986); *Fireman's Fund Ins. Co. v. Rairigh*, 475 A.2d 509, 514-15 (Md. Ct. App. 1984); *Kelly v. Cherokee Ins. Co.*, 574 S.W.2d 735, 737 (Tenn. 1978).

I need not decide whether the Supreme Court of Nevada would recognize an exception for a conflict of interest and what an insurer must do to validly invoke this exception[6] because there is no conflict of interest in this case. After the September 17, 2015 hearing in this case, the Supreme Court of Nevada issued a decision which addresses whether an insurer must provide independent counsel for its insured when there is a conflict of interest between the insurer and its insured. *State Farm Mut. Auto. Ins. Co. v. Hansen*, --- P.3d ----, Adv. Op. No. 74 (Sept. 24, 2015) (en banc). There, the Court held that if a conflict exists, "Nevada law requires the insurer to satisfy its contractual duty to provide representation by permitting the insured to select independent counsel and by paying the reasonable costs of such counsel." *Id.*, Adv. Op. at 9. The Court also held that "a reservation of rights does not create a per se conflict." *Id.* at 11. Rather, the question is whether there is "an actual conflict of interest." *Id.* Nevada Rule of Professional Conduct 1.7(a) is the standard to determine whether there is an actual conflict. *Id.* Under that Rule, there is a conflict of interest for a lawyer to represent two clients if: "(1) [t]he representation of one client will be directly adverse to another client; or (2) [t]here is a significant risk that the representation of one or more clients will be materially limited by the lawyer's responsibilities to another client, a former client or a third person or by a personal interest of the lawyer."

There is no such conflict here because Century's reason for denying coverage would have given Blue Streak a complete defense to the claims against it. If Century was correct that Vasquez was not working in the course and scope of employment with Blue Streak, then the very reason Century denied it owed Blue Streak a defense would have entitled Blue Streak to a judgment in Blue Streak's favor against Pretner. Century's and its insured's interests were therefore aligned in showing that Vasquez was not driving in the course and scope of employment

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[6] *See Wear v. Farmers Ins. Co. of Wash.*, 745 P.2d 526, 528 (Wash. Ct. App. 1987) (stating an insurer is not bound by the underlying judgment if a conflict exists and the insurer defended under a reservation of rights); *State Farm Mut. Auto. Ins. Co. v. Glasgow*, 478 N.E.2d 918, 923 (Ind. Ct. App. 1985) (stating a conflict of interest "preclude[s] the application of collateral estoppel . . . only where: (1) the insurance company actually participates in some part of the insured's defense in the underlying tort action, either directly or by reimbursing the insured's personal attorney, . . . and (2) the insurance company gives its insured clear and prompt notice of the existence and nature of the conflict of interest, and its implications for the insured"); Restatement (Second) of Judgments § 58(2) cmt. a.

at the time of the accident. *See also Spring Vegetable Co. v. Hartford Cas. Ins. Co.*, 801 F. Supp. 385, 393 (D. Or. 1992); Restatement (Second) of Judgments § 58(2) (stating a conflict of interest "exists when the injured person's claim against the indemnitee is such that it could be sustained on different grounds, one of which is within the indemnitor's obligation to indemnify and another of which is not").

Because Blue Streak could be liable only if Vasquez was working in the course and scope of his employment at the time of the accident, that fact necessarily was decided by the default judgment against Blue Streak. The default judgment recited this specific finding. The default judgment also determined the judgment amount, which in this case reflects the measure of damages suffered by Blue Streak as a result of the breach of the duty to defend. Century therefore cannot relitigate those issues. It is bound by the default judgment unless, as discussed below, the settlement agreement and subsequent default judgment were unreasonable, fraudulent, or collusive.[7]

C. Unreasonable, Fraudulent, or Collusive Settlement

When an insurer refuses to defend its insured, the insured "may, without forfeiture of his right to indemnity, settle with the [injured party] upon the best terms possible, taking a covenant not to execute." *Samson v. Transamerica Ins. Co.*, 30 Cal. 3d 220, 240 (Cal. 1981) (quotation omitted); *see also Willcox v. Am. Home Assur. Co.*, 900 F. Supp. 850, 855 (S.D. Tex. 1995) ("It is well settled under Texas law that once an insurer has breached its duty to defend, as in the instant case, the insured is free to proceed as he sees fit; he may engage his own counsel and either settle or litigate, at his option."). In this context, "the covenant not to execute is not a release which would permit the insurer to escape its obligations." *Paynter*, 593 P.2d at 953; *see also Willcox*, 900 F. Supp. at 856 (stating that "in Texas, a covenant not to execute against the insured, given by the plaintiff in an underlying suit, does not release the insurance carrier from

[7] At the September 17, 2015 hearing, Pretner argued that Century has never contended the settlement agreement and resulting default judgment were unreasonable or the product of fraud or collusion. But Century has raised these issues from the beginning of the case. (Dkt. #7 at 19; Dkt. #22 at 20-25.) Century did not continue to argue the point in subsequent filings because I previously ruled that Century was not bound by the default judgment.

liability"). A "covenant not to execute is merely a contract and not a release." *Globe Indem. Co. v. Blomfield*, 562 P.2d 1372, 1375 (Ariz. Ct. App. 1977). "[T]herefore, . . . the insured's tort liability remains but . . . he has an action for breach of contract if the plaintiff attempts to collect the judgment in violation of the covenant." *Id.* Allowing the breaching insurer to argue that the insured suffered no damages because of the covenant not to execute would "wholly undermine the purpose of such agreements." *Paynter*, 593 P.2d at 953. It also would deprive the insured who has been abandoned by its insurer of a means to protect itself. *Globe Indem. Co.*, 562 P.2d at 1376. Consequently, an insurer is bound by its insured's settlement (and any resulting judgment) so long as the settlement and judgment are reasonable and not collusive or fraudulent. *Pruyn*, 36 Cal. App. 4th at 515 ("Courts have for some time accepted the principle that an insured who is abandoned by its liability insurer is free to make the best settlement possible with the third party claimant, including a stipulated judgment with a covenant not to execute. Provided that such settlement is not unreasonable and is free from fraud or collusion, the insurer will be bound thereby."); *see also* n.2 *supra*.

Here, Century is bound by the default judgment's damage amount as a measure of Blue Streak's consequential damages, unless it can show that the default judgment amount was unreasonable or that it was procured through fraud or collusion. As discussed below, the default judgment amount is unreasonable because it awards $5 million in attorney's fees without a legal basis. Additionally, genuine issues of fact remain as to whether the default judgment was procured through fraud or collusion.

1. Unreasonable Judgment Amount

The state court entered a judgment in the amount of $12,888,492.66 in damages plus $6,295.99 in costs. (Dkt. #14-27 at 6.) The state court added another $5,155,396.80 in attorney's fees. (*Id.*)

Century argued at summary judgment that the default judgment was unreasonable in amount because it included the attorney's fee award even though Pretner did not seek attorney's fees in the application for default judgment and even though there was no legal basis to award the

fees. (Dkt. #22 at 24.) Pretner responded that a district court has discretion to award attorney's fees following a default judgment. (Dkt. #49 at 26 (citing *Foster v. Dingwall*, 227 P.3d 1042, 1052 (Nev. 2010) (en banc).)

In Nevada, a district court generally may not award attorney's fees "unless authorized to do so by a statute, rule or contract." *Davis v. Beling*, 278 P.3d 501, 515 (Nev. 2012). Nevada statutorily allows recovery of attorney's fees where (1) "the prevailing party has not recovered more than $20,000" or (2) the court finds that a claim or defense "was brought or maintained without reasonable ground or to harass the prevailing party." Nev. Rev. Stat. §§ 18.010(2)(a)-(b).

Here, Pretner recovered more than $20,000, so the attorney fee award could not have been based on § 18.010(2)(a). Because Vasquez and Blue Streak defaulted, they did not maintain any defense. As a result, there was not (and could not have been) a finding that they acted without reasonable grounds or to harass under § 18.101(2)(b). Consequently, there was no legal basis to award attorney's fees.

Additionally, the award of over $5 million in attorney's fees for prosecuting a default judgment was unsupported. Pretner did not request attorney's fees in the application for default judgment and presented no documentary evidence to support the award. (Dkt. #14-26 at 12-13.)

Pretner's reliance on *Foster* is misplaced. There, the district court awarded attorney's fees for discovery violations and for frivolous claims and defenses, as allowed under § 18.010(2)(b). 227 P.3d at 1052. That court therefore had a basis to award attorney's fees under a discovery rule and by statute. In contrast, Pretner has not identified any statute, rule, or contract to support the fee award.

The attorney's fee award was unreasonable because it had no legal or factual basis. However, Century has never challenged the settlement (as opposed to the judgment) as being unreasonable. Nor has Century argued that the remaining $12 million judgment was unreasonable. Accordingly, the maximum amount of the default judgment that Century may be liable for is $12,494,788.65 ($12,488,492.66 in damages and $6,295.99 in costs).

2. Fraudulent or Collusive Settlement and Resulting Judgment

It is not fraudulent or collusive for the insured to assign its rights against its insurer and to receive a covenant not to execute in return. *Samson*, 30 Cal. 3d at 240-41. By executing such an agreement, the insured "attempt[s] only to shield himself from the danger to which [his insurer] exposed him." *Id.* at 241 (quotation omitted); *see also Damron v. Sledge*, 460 P.2d 997, 1001 (Ariz. 1969) ("It cannot be held that as a matter of law collusion exists simply because a defendant chooses not to defend when he can escape all liability by such an agreement, and must take large financial risks by defending."). And where there is "significant independent adjudicatory action by the court," the "risk of a fraudulent or collusive settlement between an insured and the claimant" is mitigated. *Pruyn*, 36 Cal. App. 4th at 517.

But an insurer is not bound by "those trial proceedings which are clearly a patent sham collusively designed to create a judgment for which liability insurance coverage would then exist." *Id.* at 517 n.16. A "stipulated or consent judgment which is coupled with a covenant not to execute against the insured brings with it a high potential for fraud or collusion" because "the insured's best interests are served by agreeing to damages in any amount as long as the agreement requires the insured will not be personally responsible for those damages." *Id.* at 518 (quotation omitted). Consequently, "a stipulated judgment should only bind an insurer under circumstances which protect against the potential for fraud and collusion." *Id.*

The Supreme Court of Nevada has not addressed what constitutes fraud or collusion in this context. But other courts have indicated that fraud and collusion occur "when the purpose is to injure the interests of an absent or nonparticipating party, such as an insurer or nonsettling defendant." *Cent. Mut. Ins. Co. v. Tracy's Treasures, Inc.*, 19 N.E. 3d 1100, 1120 (Ill. Ct. App. 2014); *see also Andrade v. Jennings*, 54 Cal. App. 4th 307, 327 (Cal. Ct. App. 1997). Some examples of fraud or collusion are self-evident, such as where the insured agrees to testify falsely to create coverage or the parties collusively agree to an unsupportable amount of damages. *Damron*, 460 P.2d at 1001.

But generally what may constitute fraud or collusion is a fact-intensive inquiry determined on a case-by-case basis. *Andrade*, 54 Cal. App. 4th at 327. Factors to consider include, but are not limited to, whether the settlement was unreasonable; whether it involved any misrepresentation or concealment of material facts; whether there was a lack of arms-length negotiation; whether there were "attempts to affect the insurance coverage" or to "artificially increase damages flowing from the insurer's breach of the duty to defend"; and whether there is "profit to the insured." *Cent. Mut. Ins. Co.*, 19 N.E. 3d at 1120 (quotation omitted). Additionally, the fact finder may consider the settlement amount compared to the value of the case or awards in similar cases, the facts known to the settling insured, whether there is a covenant not to execute, and the failure of the settling insured to consider viable available defenses. *Id.* at 1121; *Andrade*, 54 Cal. App. 4th at 331. Other relevant factors may include whether the non-participating insurer knew about the prove-up hearing and whether the presiding judge was informed that there was a covenant not to execute. *Andrade*, 54 Cal. App. 4th at 325-26, 332-33.

Whether a settlement agreement was fraudulent or collusive is an issue of fact. *Cent. Mut. Ins. Co.*, 19 N.E. 3d at 1121. The insurer who breached its duty to defend bears the burden of showing by a preponderance of the evidence that the agreement was fraudulent or collusive. *See Nunn v. Mid-Century Ins. Co.*, 244 P.3d 116, 123 (Colo. 2010) (characterizing the issue of collusion as an affirmative defense for the insurer to raise and prove); *Pruyn*, 36 Cal. App. 4th at 530 ("It is sound and rational to conclude that the burden of showing that the settlement does not reflect the fact and amount of the insured's liability should fall upon the insurer whose breach has occasioned the settlement.") (quotation and emphasis omitted); *see also Clark Cnty. Sch. Dist.*, 168 P.3d at 94 (stating an affirmative defense raises "new facts and arguments that, if true, will defeat the plaintiff's . . . claim, even if all allegations in the complaint are true") (quotation omitted).

Genuine issues of material fact remain regarding whether the settlement agreement was the product of fraud or collusion. Viewing the facts in the light most favorable to Century, a reasonable jury could find the settlement agreement was fraudulent or collusive. The underlying

complaint alleged that Vasquez was in the course and scope of his employment despite Vasquez's steadfast position from the day of the accident that he was on a personal errand and was not working at the time of the accident. Vasquez told Century and Progressive that he was not working at the time of the accident. (Dkt. #192-3 at 3-5.)[8] After Pretner sued Vasquez, Progressive (Vasquez's personal insurer) did not defend Vasquez despite Vasquez's insistence that he had defenses based on Pretner's potential negligence. (*Id.* at 3.) Instead, Progressive provided him an attorney only to advise him about signing the settlement agreement. (*Id.* at 5; Dkt. #192-17.) When confronted with the agreement, Vasquez did not want to sign it because he maintained his position that he was not at work at the time of the accident and therefore Century should not be liable. (Dkt. #192-3 at 5; Dkt. #192-21.) He nevertheless agreed to take a default on both his own and Blue Streak's behalf in exchange for a covenant not to execute. A reasonable jury could find that agreement set the stage for Pretner's counsel to obtain a default judgment that manufactured coverage even though there was no evidence supporting coverage under the Century policy.

Although there was a default judgment hearing before an independent judge in state court, there is no evidence the judge was advised that both Century and Vasquez disputed whether Vasquez was driving in the course and scope of employment at the time of the accident and that this fact was important because it would trigger liability for a non-participating insurer. No evidence was presented to the judge showing Vasquez in fact was driving in the course and scope of his employment at the time of the accident. (Dkt. #192-22.) There also is no evidence the

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[8] Pretner moves to strike Vasquez's declaration, arguing that Century cannot rely on after-acquired evidence to support its decision not to defend Blue Streak. Pretner also argues Vasquez cannot submit an affidavit contradicting the facts recited in the default judgment against him. I deny the motion to strike. The question of whether Century breached its duty to defend has been resolved against Century, and Century does not offer the Vasquez declaration on that issue. As to whether Vasquez can offer testimony contradicting the default judgment's findings, nothing in the settlement agreement precludes him from providing an affidavit in litigation between other parties. Indeed, if the settlement agreement required Vasquez to testify falsely about whether he was acting in the course and scope of his employment, that would weigh heavily in favor of finding fraud and collusion. The default judgment is not Vasquez's sworn testimony on the subject, and he therefore is not contradicting his own prior sworn testimony. Vasquez's testimony is competent and probative on the remaining questions in this lawsuit. Accordingly, I deny the motion to strike.

judge was told about the settlement agreement with the covenant not to execute. Although Century had notice of the lawsuit and the entry of default, there is no evidence Century knew Vasquez and Blue Streak had settled in exchange for a covenant not to execute. Nor is there evidence Century was notified of the application for default judgment or the date and time of the default judgment hearing. (Dkt. #73-2 at 230, 235 (certificates of service showing application for default judgment and date and time of hearing served only on Progressive attorney).) Viewing the totality of these circumstances in the light most favorable to Century, a reasonable jury could find the settlement agreement and resulting default judgment were the product of fraud or collusion designed to manufacture coverage where none existed under the Century policy.

On the other hand, viewing the facts in the light most favorable to Pretner, a reasonable jury could find that the settlement and resulting default judgment were not fraudulent or collusive. The complaint alleged the facts potentially triggering coverage under the Century policy before the parties entered into the settlement agreement. Although Vasquez denied he was acting in the course and scope of employment, he is a layperson who may not understand all of the factors that would inform the inquiry. Pretner advised Century of the lawsuit and of the default, and thus Century had the opportunity and the duty to litigate the issue. Instead, Century abandoned its insured.

A reasonable jury could find that Vasquez then did the only thing he could to avoid substantial liability for both Blue Streak and himself personally based on the catastrophic injuries Pretner suffered. *Samson*, 636 P.2d at 240-41 ("When the insurer exposes its policyholder to the sharp thrust of personal liability by breaching its obligations, the insured need not indulge in financial masochism.") (quotation omitted). Indeed, a reasonable jury may find it ironic that Century would expect Vasquez to forego a settlement and expose Blue Streak and himself to substantial liability in order to protect Century's interests when Century had breached its duty to defend Blue Streak as it was contractually required to do.

Moreover, Vasquez did not agree to testify falsely that he was driving in course and scope of employment, and the parties did not agree to any damages amount, much less an inflated

amount. Instead, Vasquez and Blue Streak agreed to default, as they had already done anyway. They also agreed that a state court judge would decide whether a default judgment was warranted and, if so, in what amount. A reasonable jury could conclude Century knew the complaint alleged facts potentially triggering coverage and knew its insured had defaulted and thereby admitted those facts. Century therefore should have monitored the litigation and attended the default judgment hearing if it wanted to contest Blue Streak's liability and the amount of that liability. Accordingly, a reasonable jury could conclude that "[a]ny resulting damage to [Century] was caused not by [Vasquez's] supposed misconduct but by [Century's] own intransigence." *Id.*

Material issues of fact remain regarding whether the settlement agreement and the default judgment were the product of fraud or collusion. That issue therefore must be presented to a jury.[9]

III. CONCLUSION

IT IS THEREFORE ORDERED that defendant Century Surety Company's motion for summary judgment **(Dkt. #192) is DENIED**.

IT IS FURTHER ORDERED that plaintiffs' motion for summary judgment **(Dkt. #194) is DENIED**.

IT IS FURTHER ORDERED that plaintiffs' motion to strike **(Dkt. #197) is DENIED**.

IT IS FURTHER ORDERED that the parties shall file a proposed joint pretrial order as required under the Local Rules.

DATED this 28th day of September, 2015.

ANDREW P. GORDON
UNITED STATES DISTRICT JUDGE

[9] Century stated at the September 17, 2015 hearing that discovery should be re-opened on the issue of fraud and collusion. However, Century raised this defense from the outset and discovery proceeded for over a year before I ruled Century was not bound by the default judgment. Century therefore had ample opportunity to investigate its fraud or collusion defense.

UNITED STATES DISTRICT COURT

DISTRICT OF NEVADA

* * *

DANA ANDREW, as Legal Guardian of RYAN T. PRETNER, and RYAN PRETNER, individually,

Plaintiffs,

v.

CENTURY SURETY COMPANY, a foreign corporation; and DOES 1-10, inclusive,

Defendants.

Case No. 2:12-cv-00978-APG-PAL

Order Granting and Denying In Part Plaintiffs' and Defendant's Motions for Reconsideration

Pending before the Court are the parties' respective motions for reconsideration (ECF## 127, 132) of this Court's Order denying their cross-motions for summary judgment (ECF #123). For the reasons discussed below, the Court grants reconsideration and enters the following Order.

I. Background and Procedural History

The background and procedural posture of this case are set forth in detail in this Court's October 10, 2013 Order, and are incorporated herein by reference. The following is relevant to the parties' cross-motions for reconsideration.

On January 12, 2009, plaintiff Ryan Pretner was riding his bicycle on the eastbound shoulder of St. Rose Parkway in Las Vegas, Nevada.[1] Michael Vasquez was driving his truck when the truck's side-view mirror struck Pretner's head, resulting in a catastrophic brain injury.

At the time of the accident, Vasquez was covered under two insurance policies, one issued by defendant Century Surety Company ("Century") and the other issued by Progressive

[1] There remains a factual dispute among the parties as to whether Mr. Pretner was lawfully riding his bicycle on the shoulder of St. Rose Parkway, or whether he was riding on the white solid line of the highway itself. *Compare* Plaintiffs' Motion, (EFC#14-1 at 6), *with* Declaration of Michael Vasquez ("Vasquez Declaration"), (ECF#25 at 2). That issue is irrelevant to the pending motions.

Insurance (not a party to this litigation). The Century policy insured Vasquez's business, Blue Streak Auto Detailing ("Garage Policy"). (ECF#14-2 at 2). Following the accident, Vasquez told the police that "he had just gotten off work," and that he "was on his way to his Uncle's home coming from his house." (ECF#14-1 at 9 & 18). Shortly after the accident, Vasquez reported the claim to Progressive Insurance. On January 13, 2009, Vasquez confirmed in a recorded statement that he was off work and "just going to run errands." (ECF#23-1 at 7). On June 12, 2009, Vasquez signed an affidavit in which he stated that he "was driving from home...and going to [his] aunt and uncle's house...for the purpose of a visit." (Vasquez Declaration at ¶10; ECF#25-1 at 3). Vasquez did not notify Century about the accident until March 26, 2009 because he believed that the accident did not occur while he was driving on Blue Streak business. (Vasquez Declaration at ¶11). When Century's adjuster called Vasquez to discuss the accident, Vasquez apparently confirmed to the adjuster that Vasquez was not on Blue Streak business at the time of the accident. (ECG#24-1 at 19).

On May 26, 2009, Plaintiffs demanded that Century settle for its policy limits in exchange for a complete release. (ECF#14-9). On June 5, 2009, Century denied coverage because Vasquez was not driving his truck in the course of his business at the time of the accident. (ECF#14-10 at 3). Thus, Century rejected Plaintiffs' demand. (ECF#14-11).

On January 7, 2011, Plaintiffs filed in state court the underlying lawsuit entitled *Lee Pretner and Dana Andrew as Legal Guardians of Ryan T. Pretner v. Michael Vasquez and Blue Streak Auto Detailing, LLC*, Clark County Case No. A-11-632845-C ("Underlying Lawsuit"). (ECF#14-12). In their Complaint, Plaintiffs alleged that: (1) Vasquez was an agent and/or employee of Blue Streak; (2) at the time of the accident he was driving his truck in the course and scope of his employment with Blue Streak; and (3) Vasquez was negligent in operating the truck, causing injury to Pretner. (*Id.* at 3-5). Plaintiffs' counsel forwarded a copy of the Complaint to Century. (ECF#14-13). Subsequently, Century informed Blue Streak and Vasquez that after a "complete review" of the Complaint, Century was again denying coverage based on the police

reports and Vasquez's consistent statements that he was not operating the truck in connection with the business. (ECF#14-20).

Blue Streak and Vasquez failed to answer the Underlying Lawsuit, so defaults were entered against them. (ECF#23-1 at 51). Plaintiffs sent Century copies of the defaults. (ECF#14-22). Century responded that its policy did not cover the loss. (ECF#14-23).

On October 20, 2011, Vasquez and Blue Streak entered into a settlement agreement ("Settlement Agreement") under which Progressive Insurance paid Plaintiffs the $100,000 policy limit under its policy. Plaintiffs agreed not to execute upon any judgment entered against Vasquez and Blue Streak, and Vasquez and Blue Streak assigned to Plaintiffs their rights against Century under the Garage Policy. (ECF#14-25).

Plaintiffs sought entry of default judgment in the Underlying Lawsuit, requesting $12,496,084.52 in damages. (ECF#14-26). The Application claimed that "[a]t the time of the accident, Vasquez was in the course and scope of his employment with Blue Streak...." (*Id.* at 3). No opposition was filed to the Application, and no one appeared at the hearing to challenge it. (ECF#26-2). Following the hearing, the court entered default judgment ("Default Judgment") against Vasquez and Blue Streak, finding that:

> 1. On January 12, 2009, Ryan T. Pretner was riding his bicycle traveling eastbound on the paved shoulder of St. Rose Parkway. While riding his bicycle, defendant Vasquez negligently collided with Pretner violently throwing him from his bicycle to the ground resulting in serious, catastrophic and life altering injuries.
>
> 2. At the time of the accident, Vasquez was an employee and/or agent of defendant Blue Streak Auto Detailing, LLC. At the time of the accident, Vasquez was in the course and scope of his employment and/or agency of Blue Streak acting in furtherance of its business interests. Accordingly, defendant Blue Streak is legally liable for the injuries and damages sustained by Pretner caused by defendant Vasquez's negligence.
>
> 3. As a result of the negligence of the defendants, Pretner sustained catastrophic and life altering injuries. Among the injuries Pretner sustained was a severe traumatic brain injury. . . . .

(ECF#14-27 at 5). According to the Court Minutes, Plaintiffs' counsel "requested and the COURT ORDERED 40% contingency attorney fees in the amount of $5,155,396.80 and costs in the amount of $6,295.99." (ECF#26-2). The total amount of the Default Judgment is $18,050,185.45 plus accruing interest. (*Id.* at 6).

On April 23, 2012, Plaintiffs, as assignees of Blue Streak and Vasquez, filed the instant lawsuit against Century in Nevada state court ("Bad Faith Action"). (ECF#1 at 8). Century removed it to this Court. (ECF#1).

Meanwhile, Century filed a Motion for Leave to Intervene in the Underlying Lawsuit, seeking to set aside the Default Judgment. (ECF#26-3). Century argued that the Default Judgment was based on misrepresentations of fact, including that the accident took place while Vasquez was driving in the course and scope of his employment with Blue Streak. (ECF 26-4 at 4). On December 10, 2012, the state court heard and denied Century's Motion to Intervene. The court stated that:

> I think [Century] stuck their head in the sand and said, ['Hey, we] determined we're not going to have coverage here because of what we believe the facts to be. So we're going to stand back and we're not going to defend. We're not going to intervene. We're not going to seek any reservation of rights or any declaratory relief. We're just going to let the baby fall forward and hopefully we won't have any involvement. Then oops. It's going into default. I know the lawsuit says course and scope of employment. Clear as day on page 3 of the facts alleged in the complaint. But that's okay. Now they're in default.[']
>
> Just like I'm certain that Mr. Prince could guess that the insurance company was going to try and take a position of, [']you know what[?'] ['T]his wasn't course and scope.['] I would fall out of my chair if the insurance company said [']even though the lawsuit was filed alleging course and scope, even though it went into default, I never guessed they were actually assess [sic] that position when they came in for judgment and put it in the order.[']

(ECF #60 at 33). The state court denied Century's Motion to Intervene because (1) it was untimely filed; (2) Century knew of the pendency of the action and had an opportunity to participate, but chose not to; and (3) the entry of Default Judgment was valid. (*Id.* at 47-48). Century did not appeal the denial of its Motion to Intervene.

In this Bad Faith Action, the parties filed cross-motions for Summary Judgment, which the Court denied in its October 10, 2013 Order. (ECF#123.) The Court concluded that issue preclusion did not bind Century to the findings in the Underlying Lawsuit, that *Rooker-Feldman* was inapplicable to this case, that the assignment in the Underlying Lawsuit was immaterial, and that issues of material fact relating to Century's investigation supported denying its motion for summary judgment with respect to the breach of contract and bad faith claims. (*Id.*)

Subsequently, Plaintiffs filed a Motion for Reconsideration or in the Alternative for Certification of a Question of Law to the Nevada Supreme Court. (ECF#127.) Plaintiffs move the Court to decide whether Century breached its duty to defend, and if so, to determine the extent of damages flowing from that breach, or certify the question to the Nevada Supreme Court. (*Id.* at 6.) Plaintiffs also ask the Court to specifically determine whether Century is bound to the default judgment in the Underlying Lawsuit. (*Id.*)

Century likewise filed a Motion for Clarification, or in the Alternative, Motion for Reconsideration. (ECF#132.) Century moves the Court to rule specifically on the breach of the duty to defend claim, the bad faith claim, and to determine the measure of damages, if any. (*Id.* at 2.)

ANALYSIS

1. Reconsideration is appropriate under Fed. R. Civ. P. 54(b).

Rule 54(b) provides that:

> [A]ny order or other decision, however designated, that adjudicates fewer than all the claims or the rights and liabilities of fewer than all the parties does not end the action as to any of the claims or parties and may be revised at any time before the entry of judgment adjudicating all the claims and all the parties' rights and liabilities.

Fed. R. Civ. P. 54(b). Put more simply, "absent an express entry of final judgment, all orders of a district court are 'subject to reopening at the discretion of the district judge.'" *W. Birkenfeld Trust v. Bailey*, 837 F.Supp. 1083, 1085 (E.D. Wash. 1983) (quoting *Moses H. Cone Mem'l Hosp. v. Mercury Const. Corp.*, 460 U.S. 1, 12 (1983)). After reviewing the parties' respective motions, the Court concludes that reconsideration of its prior Order is warranted.

2. Plaintiffs' Motion for Reconsideration (ECF #127).

Plaintiffs' Motion raises the following issues: (i) whether Century owed a duty to defend the defendants in the Underlying Lawsuit, (ii) the measure of damages against an insurer that breaches the duty to defend, and (iii) whether Century is bound by the Default Judgment.

(a) Century owed a duty to defend the defendants in the Underlying Lawsuit.

Century asserts that "the existence of a duty to defend under a particular insurance policy is a question of law because it involves the interpretation of a written contract." (ECF#127 at 9.) That question of law begins with determining whether Nevada is a "four corners" jurisdiction—that is, does the duty to defend arise solely from the allegations contained within the four corners of the Complaint, or may the insurer investigate the facts underlying the Complaint in order to determine whether coverage (and thus the duty to defend) exists. (ECF#127 at 2.)

The Nevada Supreme Court has never explicitly held that Nevada follows the "four corners" rule, but it has used language that implies that it embraces the rule. In *United Nat'l Ins. Co. v. Frontier Ins. Co., Inc.*, 120 Nev. 678, 687, 99 P.3d 1153, 1158 (2004), the court stated that "[a] potential for coverage only exists when there is arguable or possible coverage. Determining whether an insurer owes a duty to defend is achieved by comparing the allegations of the complaint with the terms of the policy." *Id.* (citing *Hecla Min. Co. v. New Hampshire Ins. Co.*, 811 P.2d 1083, 1089 (Colo. 1991) ("the obligation to defend arises from allegations in the complaint, which if sustained, would impose a liability covered by the policy")). Plaintiffs assert that this is the four corners rule. (ECF#127 at 10.) Century counters that *United National* did not adopt the four corners rule, but rather held that "an insurer must investigate the 'facts behind a complaint' before denying a defense, signifying that an insurer is not limited solely to considering the allegations in a complaint in determining its duty to defend." (ECF #134 at 4 (quoting *United National*, 99 P.3d at 1158).) The Nevada Supreme Court's opinion is not clear:

> The duty to defend is broader than the duty to indemnify. There is no duty to defend "[w]here there is no potential for coverage." *Bidart v. Am. Title Ins. Co.*, 103 Nev. 175, 177, 734 P.2d 732, 733 (1987). In other words, "[a]n insurer ... **bears a duty to defend its insured whenever it ascertains facts which give rise to the potential of liability under the policy.**" *Gray v. Zurich Insurance*

> *Company*, 65 Cal.2d 263, 54 Cal.Rptr. 104, 419 P.2d 168, 177 (1966). Once the duty to defend arises, "this duty continues throughout the course of the litigation." *Home Sav. Ass'n v. Aetna Cas. & Surety*, 109 Nev. 558, 565, 854 P.2d 851, 855 (1993). If there is any doubt about whether the duty to defend arises, this doubt must be resolved in favor of the insured. *Aetna Cas. & Sur. Co., Inc. v. Centennial Ins. Co.*, 838 F.2d 346, 350 (9th Cir. 1988) (interpreting California law). The purpose behind construing the duty to defend so broadly is to prevent an insurer from evading its obligation to provide a defense for an insured **without at least investigating the facts behind a complaint.** *Hecla Min. Co. v. New Hampshire Ins. Co.*, 811 P.2d 1083, 1090 (Colo.1991).
>
> However, "the duty to defend is not absolute." *Aetna Cas. & Sur. Co.*, 838 F.2d at 350. A potential for coverage only exists when there is arguable or possible coverage. *Morton by Morton v. Safeco Ins. Co.*, 905 F.2d 1208, 1212 (9th Cir. 1990) (interpreting California law). **Determining whether an insurer owes a duty to defend is achieved by comparing the allegations of the complaint with the terms of the policy.** *Hecla*, 811 P.2d at 1089–90.

120 Nev. at 686-87, 99 P.3d at 1158 (emphasis added). The second paragraph (particularly the last sentence) seems to adopt the four corners rule by stating that the insurer must compare the allegations in the (four corners of the) complaint with the terms of the policy. However, the first paragraph says the insurer may "investigat[e] the facts behind a complaint" to ascertain whether "facts [exist] which give rise to the potential of liability under the policy." *Id.*

The most plausible reading is that the "facts" an insurer must rely on are those alleged in the complaint, rather than facts derived from an insurance company's investigation. *United National* relied on *Hecla*, a case from Colorado, which explicitly applies the four corners rule. *See Cyprus Amax Minerals Co. v. Lexington Ins. Co.*, 74 P.3d 294, 299 (Colo. 2003) (citing *Hecla* and affirming that "we have long held that to determine whether a duty to defend exists, courts must look no further than the four corners of the underlying complaint (the 'four corners' or 'complaint' rule)"). Moreover, both *United National* and *Hecla* discuss the strong public policy that the duty to defend is to be construed broadly to enforce "the insured's legitimate expectation of a defense." *See Hecla*, 811 P.2d at 1090. Finally, the Nevada Supreme Court decided *United National* consistently with the four corners doctrine, never looking past the allegations contained in the complaint in determining whether a duty to defend existed. The logical conclusion is that Nevada has adopted the four corners doctrine even though the Nevada Supreme Court has yet to explicitly state that.

Several cases from this District have concluded that Nevada has adopted the four corners rule. *See OneBeacon Ins. Co. v. Probuilders Specialty Ins. Co.*, 2009 WL 2407705 *8 (D. Nev. Aug. 3, 2009) ("Nevada has adopted the [four corners rule] pursuant to which an insurer that seeks to avoid its duty to defend its insured may only do so by comparison of the complaint in the underlying litigation to the terms of the policy."); *Beazley Ins. Co. v. Am. Econ. Ins. Co.*, 2013 WL 2245901 *4 (D. Nev. May 21, 2013) (quoting *OneBeacon Ins.*, 2009 WL 2407705 at *8); *Liberty Ins. Underwriters Inc. v. Scudier*, 2013 WL 3427902 *4 (D. Nev. July 8, 2013) (same); *Discover Prop. & Cas. Ins. Co. v. Scudier*, 2013 WL 2153079 *4 (D. Nev. May 16, 2013) (same);

On the other hand, at least two decisions from this District have looked beyond the four corners of the complaint when applying *United National*. (ECF#134 at 4 (citing *United Nat. Ins. Co. v. Assurance Co. of Am.*, 2012 WL 1931521 *3 n.2 (D. Nev. May 29, 2012) ("The Court assumes for the purpose of this order, without determining whether the Nevada Supreme Court would so hold, that an insurer may go beyond the four corners of a complaint to matters of public record in making its coverage/duty to defend determination."); *Gary G. Day Constr. Co., Inc. v. Clarendon Am. Ins. Co.*, 459 F. Supp. 2d 1039, 1050 (D. Nev. 2006) (citing *United National*, 99 P.3d at 1158 ("The duty arises when the allegations of the complaint and the facts known to the insurer indicate a potential for coverage."[2])).

Century contends that an exception to the four corners rule exists where the allegations in the complaint are not bona fide, but rather are framed only to trigger a duty to defend under an insurance policy. (ECF#22 at15 (citing *Cotter Corp. v. A.M. Empire Surplus Lines Ins. Co.*, 90 P.3d 814, 829 n.9 (Colo. 2004).) Century points out that on the basis of this exception, the Tenth Circuit approved an insurer's reliance on extrinsic evidence in rejecting a defense. *Pompa v. Am. Family Mut. Ins. Co.*, 520 F.3d 1139, 1146 (10th Cir. 2008). However, in *Pompa* the court held that reliance on extrinsic evidence was appropriate where the insurer first provided a defense and then later sought to recover defense costs from the insured. *Id.* Here, Century failed to first

[2] However, in *Day Construction* the court never applied its statement of the rule because both parties failed to "submit[] argument or evidence demonstrating a duty to defend." 459 F. Supp. 2d at 1050.

provide a defense, and unlike the insurance carrier in *Pompa*, Century is not relying on extrinsic evidence to seek recovery of the costs of defending its insured. Thus, Century's proffered exception to the four corners rule is inapplicable here.

The Court concludes that the Nevada Supreme Court would adopt the four corners rule. Thus, an insurance company's duty to defend is determined "by comparing the allegations of the complaint with the terms of the policy." *United National*, 99 P.3d at 1158.

Here, the complaint in the Underlying Lawsuit alleged, among other things, that Vasquez was driving in the course and scope of his employment with Blue Streak when he negligently hit Pretner, causing him catastrophic injuries. (*See generally* ECF#14-12.) Century's Garage Policy included coverage for such an event. At the time of the accident, Vasquez's truck was covered under the policy. Comparing the allegations contained in the complaint with the Garage Policy, it appears there was at least a potential for coverage under the policy. Accordingly, Century breached its duty to defend.[3]

(b) Century is not bound by the Default Judgment by operation of law.

Plaintiffs urge this Court to apply a line of Nevada cases arising in the uninsured motorist context to hold that Century is bound by the findings in the Default Judgment in the Underlying Lawsuit. (ECF#127 at 17.) Century counters that the holding and rationale in those cases are limited to the uninsured motorist context. (ECF#157 at 2.) For the reasons discussed below, the Court agrees with Century.

The Nevada Supreme Court has held that where an insurer has notice of an adversarial proceeding that implicates uninsured motorist coverage under its policy but refuses to intervene, the insurer will be bound by the judgment thereafter obtained. *Allstate Ins. Co. v. Pietrosh*, 85

[3] If Century's investigation led it to believe that Vasquez was not driving within the course and scope of his employment with Blue Streak, it could have provided a defense, reserved its rights, and filed a motion for summary judgment in the early stages of the Underlying Lawsuit to resolve that issue up front.

Nev. 310, 316, 454 P.2d 106, 111 (1969). This is true notwithstanding the fact that it subverts the element of privity normally required for the application of the principles of claim and issue preclusion. *Id.*

The insurance policy at issue in *Pietrosh* included a provision stating that any judgment obtained by its insured against an uninsured motorist would not be binding upon the insurance company. 454 P.2d at 110. The insurance company received notice of litigation by its insured against an uninsured motorist, but did not intervene, seek arbitration, or consent to the suit. *Id.* The court emphasized that insurance policies are not ordinary contracts but rather are "complex instrument[s], unilaterally prepared and seldom understood by the insured. The parties are not similarly situated. The company and its representatives are expert in the field; the insured is not." *Id.* (citation omitted.) Because of this, the court would "not hesitate to place the burden of affirmative action upon the insurance company...." *Id.* The court concluded that it was unreasonable for the insurer to do nothing, and held that where an insurer has notice of litigation that may give rise to coverage under its policy and fails to intervene, it will be bound by the judgment thereafter obtained against the uninsured motorist. *Id.* at 110-11.

The court noted that its holding "subvert[ed] the requirement of privity normally present with the application of [principles of claim and issue preclusion]. Privity is absent here." *Id.* at 111. The court reasoned that the public policy favoring intervention and "avoiding multiple litigation carries . . . greater weight" than the policy requiring privity for application of preclusion in the insurance context. *Id.* The Nevada Supreme Court has not applied *Pietrosh* in any context other than uninsured motorist litigation.

In *Christensen*, the Nevada Supreme Court applied the holding and rationale of *Pietrosh* to bind a non-intervening insurer to a finding of liability in a default judgment entered against an uninsured motorist. 88 Nev. 160, 494 P.2d 552. Christensen was injured in a collision with an

uninsured motorist. She sued the uninsured motorist, notified her insurer, and the insurer elected not to intervene. After obtaining default judgment against the uninsured motorist, Christensen sued her insurance carrier. The court held that the insurance carrier was bound by the default judgment. The court noted that the effect of *Pietrosh* was "to impliedly pronounce the insurer as an indirect party," and then extended that notion to the context of a default judgment. *Id.* at 553. Like *Pietrosh*, the Nevada Supreme Court has never applied *Christensen* outside of the uninsured motorist context.

In *Lomastro*, Lomastro died while driving Leach's car. 195 P.3d at 342. Leach was uninsured. Lomastro's insurance carrier denied Lomastro's parents' uninsured motorist claim. Lomastro's parents sued Leach claiming negligent entrustment, and notified their insurance carrier of the action. Leach did not answer the complaint. Before seeking entry of default, the Lomastros notified their insurance carrier that they intended to do so. After entering default against Leach, the Lomastros once again notified their insurance carrier of this development. Finally, after receiving notice of a hearing for entry of default judgment, the Lomastros' insurance carrier moved to intervene.

The trial court allowed intervention, but held that the entry of default precluded the insurance carrier from contesting Leach's liability. The Lomastros then amended their complaint to assert causes of action against the insurance carrier, including breach of the implied covenant of good faith and fair dealing. The insurance carrier moved for summary judgment on the basis that uninsured motorist coverage does not apply to single-vehicle accidents. The trial court granted the motion for summary judgment, and cross-appeals followed.

Citing both *Pietrosh* and *Christensen*, the Nevada Supreme Court reversed the lower court's grant of summary judgment and held that uninsured motorist coverage does apply to single-vehicle accidents. 195 P.3d at 351. However, the court affirmed the lower court's conclusion that entry of default against Leach was sufficient to bind the insurer. *Id.* at 344-45.

The court noted that "entry of default acts as an admission by the defending party of all material claims made in the complaint." *Id.* Entry of default, therefore, generally resolves the issues of liability and causation and leaves open only the extent of damages."[4] *Id.* at 345. The court relied on the holdings in *Pietrosh* and *Christensen* that the lack of privity normally required for application of preclusion would be ignored in the context of uninsured motorist claims. *Id.* Similarly to *Pietrosh* and *Christensen*, *Lomastro* has never been applied in the general liability insurance context.

The *Pietrosh*, *Christensen*, and *Lomastro* line of cases is best limited to the context of uninsured motorist claims. The Nevada Supreme Court has never applied them in the general liability context, as Plaintiffs ask this Court to do. The fact that they have not been expanded to that context is not surprising, given the court's explicit exemption of only the privity element of preclusion. Privity between parties "designat[es] a person so identified in interest with a party to former litigation that he represents precisely the same right in respect to the subject matter involved." *United States v. Schimmels (In re Schimmels)*, 127 F.3d 875, 881 (9th Cir. 1997); *Stratosphere Litig. L.L.C. v. Grand Casinos, Inc.*, 298 F.3d 1137, 1143 (9th Cir. 2002) (quoting same).[5] Rather than require an insured to bear the burden of proving privity between the insurer and the uninsured motorist (which likely would be impossible), the Nevada Supreme Court opted for subverting the requirement all together. *Pietrosh*, 454 P.2d at 111. As Century persuasively argues, "the reason insurance companies were bound by the judgments in the *Pietrosh* line of

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[4] Under Nevada issue preclusion law, this would be insufficient to meet the "actually litigated" element, yet the court bound the insurance company to the liability established by the entry of default. As discussed below, however, the Nevada Supreme Court did not confront the "actually litigated" requirement in the context of a default judgment until two years after it decided *Lomastro*.

[5] The Ninth Circuit recognizes several relationships "sufficiently close" to justify a finding of privity for purposes of preclusion:

> First, a non-party who has succeeded to a party's interest in property is bound by any prior judgment against the party. Second, a non-party who controlled the original suit will be bound by the resulting judgment. Third, federal courts will bind a non-party whose interests were represented adequately by a party in the original suit. In addition, "privity" has been found where there is a "substantial identity" between the party and nonparty.

Schimmels, 127 F.3d at 881.

cases, was not that the companies did not defend their respective insureds, but that they did not intervene to assert their defenses to the claims of their insureds against the at-fault parties." (ECF#157 at 3.) Because contractual privity does not exist between the insurer and the uninsured tortfeasor, the Nevada Supreme Court eliminated that requirement in this context. 454 P.2d at 111. However, the Nevada Supreme Court has not completely abandoned that requirement for all other applications of preclusion; that fact supports the conclusion that the *Pietrosh* line of cases should be limited to the uninsured motorist context.[6]

This is further confirmed by the Nevada Supreme Court's decision in *In re Sandoval*, 232 P.3d 422 (Nev. 2010). In that case, the court held that "[w]hen a default judgment is entered based on failure to answer, issue preclusion is not available because the issues raised in the initial action were never actually litigated." 232 P.3d at 423. This decision came two years after *Lomastro*. The Nevada Supreme Court could have used *Sandoval* to extend the *Pietrosh* line of cases beyond the uninsured motorist context but chose not to. Nothing in *Sandoval's* holding or rationale suggests it was limited to the facts of that case. The Nevada Supreme Court has never applied the *Pietrosh* trilogy in the general liability context, and this Court will not expand it so. Accordingly, the *Pietrosh* trilogy has no bearing on this Action as the analysis under those cases is properly limited to the uninsured motorist context.

(c) The proper measure of damages for breach of the duty to defend

Plaintiffs assert that because Century breached its duty to defend, (1) the defendants in the Underlying Lawsuit had the right to enter into the Settlement Agreement with Plaintiffs, and (2) Century is liable for all the consequential damages proximately caused by that breach, including amounts in excess of the policy limits. (ECF#127 at 11-16.) In its earlier Order denying the

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[6] Even were the Court to apply the *Pietrosh* line of cases in the general liability context, Plaintiffs would still be required to prove the remaining elements of issue preclusion: identity of issues, final judgment on the merits, and whether the issue was actually litigated. *Five Star Capital Corp. v. Ruby*, 124 Nev. 1048, 1055, 194 P.3d 709, 713 (2008). The Nevada Supreme Court never announced a default judgment rule that completely displaces the preclusion inquiry, and this Court is disinclined to do so now. Under the *Pietrosh* trilogy, only the element of privity need not be proved.

cross-motions for summary judgment, the Court found that Vasquez' assignment of rights to Plaintiffs was valid (ECF#123 at 14-16), and Century has not asked for reconsideration of that finding. Thus, the Court need only consider the proper measure of damages when an insurer breaches the duty to defend.

Plaintiffs urge that when an insurer breaches the duty to defend, the appropriate finding is liability against the insurer for the full amount of the resulting judgment, even if it exceeds the policy limits. (ECF#127 at 13.) Plaintiffs rely on several cases from other jurisdictions, none of which stands for the proposition that *by itself* the breach of the duty to defend creates liability for the full amount of damages of a resulting judgment. Instead, those cases analyze damages in the context of the insurer's bad faith.[7] Plaintiffs also cite to *Allstate Ins. Co. v. Miller*, 125 Nev. 300, 313-14, 212 P.3d 318, 327-28 (2009), in which the Nevada Supreme Court analyzed several factors underlying bad faith but never held that mere breach of the duty to defend was a sufficient basis for awarding the full amount of the resulting judgment that exceeds the policy limits. The court recognized that *"[i]f an insurer violates its duty of good faith and fair dealing* by failing to adequately inform the insured of a reasonable settlement opportunity, the insurer's actions can be a proximate cause of the insured's damages arising from a foreseeable settlement or excess judgment." *Id.* (emphasis added.)

It does not appear that the Nevada Supreme Court has articulated the measure of damages for an insurer's mere breach of the duty to defend absent bad faith. However, in *Reyburn Lawn & Landscape Designers, Inc. v. Plaster Dev. Co., Inc.*, 255 P.3d 268, 277 (Nev. 2011), the court

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[7] *See e.g., Besel v. Viking Ins. Co. of Wisconsin*, 146 Wash. 2d 730, 735, 49 P.3d 887, 890 (2002) ("[I]f an insurer acts *in bad faith* by refusing to effect a settlement for a small sum, an insured can recover from the insurer the amount of a judgment rendered against the insured, even if the judgment exceeds contractual policy limits.") (emphasis added); *Amato v. Mercury Cas. Co.*, 53 Cal. App. 4th 825, 831, 61 Cal. Rptr. 2d 909 (1997) ("Breach of an insurer's duty to defend violates a contractual obligation and, *where unreasonable*, also violates the covenant of good faith and fair dealing, for which tort remedies are appropriate.") (emphasis added); *Rupp v. Transcon. Ins. Co.*, 627 F. Supp. 2d 1304, 1320 (D. Utah 2008) ("[T]he heart of the insurer's fiduciary duty, when handling third-party claims against its insured, is to guard the best interests of the insured as zealously as it would its own. If the insurer's decision to reject offers of settlement and go to trial is *unreasonable*, it is at that time that the breach of duty occurs, which is the crux of the insured's cause of action for bad faith.") (emphasis added) (citations omitted).

considered the measure of damages where an indemnitor breached a duty to defend. The court stated that such a clause "is construed under the same rules that govern other contracts." *Id.* Citing California law, the court held that "[t]he breach of that duty, 'may give rise to damages in the form of reimbursement of the defense costs the indemnitee was thereby forced to incur' in defending 'against claims encompassed by the indemnity provision.'" *Id.* (quoting *Crawford v. Weather Shield Mfg. Inc.*, 44 Cal. 4th 541, 557, 187 P.3d 424, 433 (2008).).

Similarly, courts in Colorado have held that the measure of damages for breach of the duty to defend begins with the proposition that the breach is fundamentally a breach of a contractual duty. *Bainbridge, Inc. v. Travelers Cas. Co. of Connecticut*, 159 P.3d 748, 756 (Colo. Ct. App. 2006). When an insurer breaches the duty to defend, damages are characterized as general damages and consequential damages. *Id.* General damages include attorney fees and the reasonable costs of defense. *Id.* (citing *Giampapa v. Am. Fam. Mut. Ins. Co.*, 64 P.3d 230, 237 n.3 (Colo. 2003)). Consequential damages include those damages that arise naturally from the breach and were reasonably foreseeable at the time of contract. *Id.* (citing *Vanderbeek v. Vernon Corp.*, 50 P.3d 866, 870–72 (Colo.2002)).

No Nevada case supports the Plaintiffs' argument that an insurer who breaches its duty to defend is automatically liable for the full amount of the resulting judgment even if it exceeds the limits of the insurance policy. California[8]—another jurisdiction the Nevada Supreme Court relied on in articulating the duty to defend in *United National*, 120 Nev. at 687, 99 P.3d at 1158—recognizes that "[w]here there is no opportunity to compromise[9] 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

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[8] Both Century and Plaintiffs rely extensively on California law when it supports their respective positions. *See e.g.*, Plaintiffs' Motion for Reconsideration, (ECF#127 at 9, 12, 13); Century's Motion for Summary Judgment, (ECF#73 at 18 (urging the Court to consult California insurance law because *United National* relied more heavily on California law than any other state)).

[9] The Court acknowledges that Plaintiffs had sent Century an offer of settlement. However, as discussed below, under *United National*, Century permissibly relied on facts extrinsic to the complaint in determining it had no duty to indemnify. Indeed, the complaint had not yet been filed. Because there was no apparent evidence suggesting that Century's Garage Policy would provide coverage, Century reasonably believed it had no duty to defend. Thus, it is reasonable to conclude that no real opportunity to compromise existed under that settlement offer.

amount of the policy plus attorneys' fees and costs." *Comunale v. Traders & Gen. Ins. Co.*, 50 Cal. 2d 654, 659, 328 P.2d 198 (1958).[10] Similarly, Nevada has not recognized extra-contractual damages for breach of the duty to defend in the absence of a finding of bad faith. Given that and the holding in *Comunale*, the Court concludes that the Nevada Supreme Court would not allow for extra-contractual damages if the insurer did not act in bad faith.[11]

Here, the claims alleged in the underlying complaint gave rise to the possibility of coverage under Century's policy. Century breached its duty to defend under the policy, and thus is liable for damages. As discussed below, there is insufficient evidence in the record to support a finding of bad faith by Century. To the contrary, its investigation revealed that the accident likely was not a covered event. Absent bad faith, the breach of the duty to defend results in typical contractual damages. Because the defendants in the Underlying Lawsuit did not hire counsel and did not file any responsive pleadings, they apparently incurred no costs or attorney fees. Accordingly, Century's liability for breaching its duty to defend is restricted to the damages reasonably foreseeable at the time of the contract, as capped by the $1 million policy limit.

3. Century's Motion for Clarification or Reconsideration (ECF#132).

Century's Motion seeks reconsideration of the following language from this Court's prior Order:

> Although this evidence is thin, at this point it is barely sufficient to establish **a potential factual dispute** whether Century conducted its investigation in good faith. **Discovery ultimately may not produce sufficient evidence** to sustain Plaintiffs' burden of proof on this point. But at this stage of the case, summary judgment in favor of Century must be denied to the extent Century

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[10] Notably, Plaintiffs rely in part on *Comunale* in asserting that they are owed the full amount of the judgment. (ECF#127 at 13.)

[11] In a diversity action, this Court applies the substantive law of the forum state; in this case, Nevada law controls. *Mirch v. Frank*, 295 F. Supp. 2d 1180, 1183 (D. Nev. 2003) (citing *St. Paul Fire & Marine Ins. Co. v. Weiner*, 606 F.2d 864, 867 (9th Cir.1979)). In interpreting state law, federal courts are bound by the pronouncements of the state's highest court. *Id.* (citing *Dyack v. Commonwealth of N. Mariana Islands*, 317 F.3d 1030, 1034 (9th Cir.2003)). In the absence of a controlling state decision, a federal court applying state law must apply the law as it believes the state supreme court would apply it. *Id.* (citing *Gravquick A/S v. Trimble Navigation Intn'l. Ltd.*, 323 F.3d 1219, 1222 (9th Cir.2003)).

> relies only on Vasquez's statements to "conclusively establish" he was driving in a capacity outside the scope of Century's insurance coverage.

(ECF#132 at 3 (quoting ECF#123 at 12) (emphasis added).) Century points out that discovery was closed at the time the Court entered its Order. Thus, there could be no additional discovery to "produce sufficient evidence to sustain Plaintiff's burden of proof" that Century acted in bad faith. Century next asserts that it met its burden of presenting evidence that negated an essential element in Plaintiffs' claim (bad faith), and thus the burden shifted to Plaintiffs to establish a genuine—rather than a potential—issue of material fact.

The bad faith inquiry sounds in tort for the breach of the covenant of good faith and fair dealing. *U.S. Fid. & Guar. Co. v. Peterson*, 91 Nev. 617, 620, 540 P.2d 1070 1071 (1975). Because the touchstone in determining bad faith is reasonableness, bad faith is usually a question of fact for the jury. *Allstate Ins. Co. v. Miller*, 125 Nev. 300, 310, 212 P.3d 318, 325 (2009). However, when there is no factual basis for concluding that the insurer acted in bad faith, a court may determine the issue of bad faith as a matter of law. *Am. Excess Ins. Co. v. MGM Grand Hotels, Inc.*, 102 Nev. 601, 605, 729 P.2d 1352, 1355 (1986).

Here, Century reasonably relied on the fact that Vasquez repeatedly and "unequivocally confirmed to Century and to the police that he was not driving for the business at the time of the accident." (ECF#22 at 2-3.) Although the Court has found above that Century breached its duty to defend (based on the four corners of the complaint), Vasquez's statements—and the lack of contrary evidence—establish that Century did not act in bad faith in denying coverage. Plaintiffs have failed to provide evidence to show a genuine dispute of material fact as to the reasonableness of Century's decision. Thus, the Court grants Century's cross-motion for summary judgment on the claims of bad faith and violations of the Unfair Claims Practices Act. Accordingly, Plaintiffs are not entitled to recover any damages in excess of the $1 million policy limit.[12]

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[12] This holding is consistent with Nevada's rule on the duty to indemnify. The duty to indemnify arises when an insured "becomes legally obligated to pay damages in the underlying action that gives rise to a claim under the policy." *United Nat'l Ins. Co. v. Frontier Ins. Co., Inc.*, 120 Nev. 678, 686, 99 P.3d 1153, 1157 (2004). In *United National*, the court discussed the duty to indemnify in a different part of the

III. CONCLUSION

For the foregoing reasons, Plaintiffs' Motion for Reconsideration (ECF#127) is **GRANTED IN PART AND DENIED IN PART**, and Century's Counter-Motion for Reconsideration (ECF#132) is **GRANTED IN PART AND DENIED IN PART.**

Century breached its duty to defend the defendants in the Underlying Lawsuit. However, Century is not bound by the default judgment entered against the defendants in the Underlying Lawsuit. Plaintiffs may recover the damages incurred as a result of Century's breach of its duty to defend that were reasonably foreseeable at the time of the contract, but those damages are capped by the $1 million limit in the Garage Policy. A trial will be needed to determine the amount of those damages.

Summary judgment is entered in favor of Century on Plaintiffs' claims of bad faith and violation of the Unfair Claims Practices Act.

DATED this 29th day of April, 2014.

ANDREW P. GORDON
UNITED STATES DISTRICT JUDGE

I hereby attest and certify on 8/14/2017 that the foregoing document is a full, true and correct copy of the original on file in my legal custody.

CLERK, U.S. DISTRICT COURT
DISTRICT OF NEVADA

By _____ Deputy Clerk

UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEVADA

opinion from the duty to defend, and it rejected an analysis based on the four corners rule. *Id.* at 1157-58. "The right to indemnification for litigation expenses should not depend on the pleading choices of a third party, who through an excess of caution or optimism may allege far more than he can prove at trial." *Id.* at 1158 (citation and quotations omitted). Instead, the court considered evidence extrinsic to the complaint and concluded that the defendants had no duty to indemnify. *Id.*