THE PASCHOS LAW UPDATE NEWSLETTER
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I. I. GENERAL LITIGATION

It is the Responsibility of the Court to Make a Determination Regarding a Challenge to a Class Action Waiver in an Arbitration Agreement

In *Puleo v. Chase Bank USA,* --- F.3d ---, 2010 WL 1838762 (3d. Cir. (Pa.) May 10, 2010), Francis and Trish Puleo ("the Puleos") brought suit challenging retroactive interest-rate increases on the account balances of their Chase Bank credit cards. Although the Chase Bank Cardmember Agreement governing their credit cards contained an Arbitration Agreement expressly barring class actions, the Puleos brought their suit in a representative capacity, arguing that the class action waiver was unconscionable. After Chase moved to compel arbitration, the Puleos urged the District Court to order the parties to arbitrate their class claims, notwithstanding the Arbitration Agreement's ban on class actions, but argued that the question of whether the class action waiver was unconscionable was a question for the arbitrator, not the court. The District Court rejected their arguments, concluding that the Puleos' challenge to the enforceability of the class action waiver was a question of arbitrability for the court to decide.

On appeal, the Puleos argued that the District Court never should have addressed the unconscionability of the class action waiver and instead should have left that issue to be decided by an arbitrator. Appellee Chase Bank argued that it was proper for the District Court to assess the unconscionability of the class action ban because the Puleos' unconscionability challenge to the class action waiver presented a question of arbitrability for the court to decide.

The Third Circuit acknowledged the well-settled general rule that when a contractual party challenges the validity of an arbitration agreement by contending that one or more of its terms is unconscionable and unenforceable, a question of arbitrability is presented. The Puleos' argued that this general rule should not apply to their case. The Puleo's argued, among other things, that because they are willing to arbitrate (although not under the express terms of their Arbitration Agreement), no question of arbitrability existed.

The court found this argument self-contradictory, providing:

In order to present their class claims to an arbitrator, the Puleos needed to obtain a court order that invalidated the Arbitration Agreement's class action waiver and that compelled class arbitration. This is because unless it addressed the validity of the ban on class arbitration, the District Court could not have ordered the parties to submit their dispute to class arbitration without running afoul of the FAA's directive that arbitration agreements be enforced in

accordance with their terms. . . And without a court order compelling class arbitration, the Puleos could not have presented their class claims to the arbitrator-the rules of the American Arbitration Association ("AAA") make plain that . . . a contract bans class arbitration, the AAA will not hear class claims "unless an order of a court directs the parties to the underlying dispute to submit any aspect of their dispute involving class claims, consolidation, joinder or the enforceability of such provisions, to an arbitrator." * * * * * We decline to indulge the Puleos' desire to have it both ways-i.e., to have the District Court compel the parties to arbitrate class claims without first addressing the validity of the class action waiver.

The court also declined to agree with the Puleos' contention that because the parties' Arbitration Agreement contained a severability clause, the District Court erred in considering the unconscionability of the class action waiver.

The court therefore affirmed the District Court's order compelling the parties to arbitrate their claims on an individual basis and held that the District Court properly exercised its responsibility to decide issues of arbitrability and we thus will affirm.

II. INSURANCE COVERAGE

Primary Insurer May Be Held Liable to an Excess Insurer for Prejudgment Interest Awarded to the Plaintiff in an Underlying Tort Action Based on the Primary Insurer's Alleged Failure to Engage in Good Faith Settlement Negotiations

In *New Jersey Manufacturers Ins. Co. v. National Cas. Co.*, --- A.2d ---, 2010 WL 1706012 (N.J. Super. A.D. April 29, 2010), the underlying matter involved a wrongful death claim filed by Bernard and Gloria Brodsky against an employee of Grinnell Haulers and William Horsman. Horsman, who was not insured, filed for bankruptcy, and the bankruptcy court discharged Horsman from any debt arising from the accident. Grinnell had a primary insurance policy with plaintiff New Jersey Manufacturers Insurance Company (NJM), with a coverage limit of $1 million, and an excess policy with defendant National Casualty Company (NCC), which provided an additional $4 million in coverage.

At that trial, the only issues were the apportionment of fault. The jury found Grinnell sixty percent negligent and Horsman forty percent negligent. On appeal, the court concluded that the trial court erred in the instructions and reversed and remanded for a new trial.

Before the trial on remand, Grinnell's counsel informed NCC's counsel that NJM had authorized payment of its full $1 million policy limit to settle the Brodskys' claims. However, NCC's counsel allegedly asked Grinnell's counsel to withhold this offer from the Brodskys' counsel in order to convince the Brodskys to settle for less than $1 million. Around the same time, the Brodskys lowered their settlement demand to $1.5 million. However, NCC allegedly offered to contribute only $100,000 to meet this demand, insisting that NJM pay the remaining $1.4 million. NJM

refused to pay this amount, taking the position that it was not obligated to pay anything above its $1 million policy limit to settle the case.

At the trial on remand, Grinnell was again found sixty percent negligent and Horsman was again found forty percent negligent. A judgment in the amount of $1,640,000 was entered against Grinnell, plus $580,322.07 of prejudgment interest. NJM paid its $1 million policy limit and NCC paid the remaining $640,000 of the damages award. The carriers agreed to equally divide responsibility for payment of the $580,322.07 in prejudgment interest reserving the right to litigate their obligation for payment of this obligation.

NJM subsequently brought this action seeking a determination that NCC is obligated to pay the full amount of the prejudgment interest awarded to the Brodskys. NCC filed a counterclaim seeking a determination that NJM is responsible for payment of the prejudgment interest. The trial court decided the case on NJM's motion for summary judgment, determining that NJM was only responsible for its $1 million policy limit and that NCC was responsible for the entire judgment above this amount, including $580,322.07 in prejudgment interest. On appeal, the court reversed the summary judgment and concluded that a primary carrier such as NJM may be held liable for the payment of prejudgment interest, even if such payment exceeds its policy's coverage limit, if the carrier did not engage in good faith negotiations to settle the claim within the policy's coverage limit.

The primary issue presented by this appeal is whether NCC's conduct relating to the negotiations for settlement of the Brodskys' claims is relevant to NCC's claim against NJM for the entire amount of prejudgment interest awarded the Brodskys. In determining the relevance of NCC's conduct relating to the negotiations for settlement of the Brodskys' claims, the court cited the case, *Rova Farms Resort, Inc. v. Investors Ins. Co. of America,* 65 N.J. 474 (1974) which is the seminal case dealing with an insurer's obligation to engage in good faith negotiations with a party asserting a claim against its insured. Under *Rova Farms*, if the insurer fails to negotiate in good faith, the insurer may become liable for the full amount of a judgment against its insured even though it exceeds the policy's coverage limit.

The court found that under *Rova Farms*, an insurer that fails to negotiate in good faith is not automatically liable for any judgment in excess of the policy limit. Instead, the insurer, here NJM, may raise as an affirmative defense that there was no realistic possibility of a settlement within the policy limits and that its insured would not have contributed whatever amount above the policy limit would have been required to settle the case. The court held that NJM may conduct appropriate discovery to support such a defense. Finally, the court held that if NJM was found to have negotiated in bad faith, NJM could only be liable for prejudgment interest above its policy limit for the period of time following the it's breach of its duty of good faith in settlement negotiations.

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