FIRST DIVISION
Order filed August 3, 2015
Modified Upon Denial of Rehearing November 9, 2015

No. 1-14-0928
2015 IL App (1st) 140928-U

IN THE
APPELLATE COURT OF ILLINOIS
FIRST JUDICIAL DISTRICT

ILLINOIS EMCASCO INSURANCE COMPANY, Plaintiff Appellee/Cross-Appellant, v. NATIONWIDE MUTUAL INSURANCE COMPANY, Defendant Appellant/Cross-Appellee	Appeal from the Circuit Court of Cook County. 01 CH 20759 Honorable Kathleen M. Pantle, Judge Presiding.
NATIONWIDE MUTUAL INSURANCE COMPANY, individually and as assignee of TRIUMPH DEVELOPMENT CORPORATION, Counter Plaintiff-Appellant/Cross-Appellee v. ILLINOIS EMCASCO INSURANCE COMPANY, Counter Defendant-Appellee/Cross-Appellant.	

JUSTICE CONNORS delivered the judgment of the court.
Presiding Justice Delort and Justice Harris concurred in the judgment.

ORDER

¶ 1 *Held*: No conflict of interest existed because there was no substandard conduct of the insureds' attorneys and cases finding a conflict of interest are distinguishable. A primary insurer does not owe a duty to settle to the excess insurer when the primary insurer does not control the underlying defense. The motion for sanctions was properly denied; affirmed in part, reversed in part. Cause remanded.

¶ 2 This coverage litigation between Nationwide Mutual Insurance Company (Nationwide) and Illinois Emcasco Insurance Company (Emcasco) comes to us after an extensive trial in which Nationwide and Emcasco litigated the costs associated with the defense of an underlying case, *Harold James Orange v. Midwestern Steel Sales, Inc. et al.* Nationwide appeals the trial court's judgment order and amended judgment order as well as several orders entered prior to trial. Emcasco cross-appeals the denial of its motion for sanctions.

¶ 3 **I. BACKGROUND**

¶ 4 A. The Underlying *Orange* Case

¶ 5 In the underlying case, Harold James Orange (Orange) sued Triumph Development Corporation (Triumph) and Midwestern Steel Sales, Inc. (Midwestern) for an ankle injury he sustained while working as an employee of Up-Rite Steel (Up-Rite). The injury occurred at a work site where Triumph was the general contractor and Midwestern was the sub-contractor. Midwestern sub-subcontracted with Up-Rite, Orange's employer, to perform the steel erection at the work site.

¶ 6 Triumph had a commercial general liability primary policy with Nationwide that had a $2 million limit. In excess of that primary policy, Triumph also had an umbrella policy with a $10 million limit with Nationwide. Midwestern had direct liability coverage with Emcasco including a commercial general liability primary policy with a $1 million limit. In excess of the primary

policy, Midwestern also had an umbrella policy with a $5 million limit with Emcasco. Midwestern was not an insured under Nationwide's policies. Triumph was an "additional insured" under Emcasco's primary and excess policies. Therefore, Emcasco was solely liable for Midwestern but would share any liability of Triumph with Nationwide.

¶ 7 Triumph initially tendered its defense in the *Orange* case to Nationwide and Nationwide's "house counsel" at the Law Offices of Mark R. Rudloff. Then, on May 13, 1998, Triumph tendered its defense to Emcasco. On June 3, 1998, Emcasco accepted the defense of Triumph under a reservation of rights. Emcasco appointed the law firm of O'Connor, Schiff and Myers to represented Triumph (initial lawyer). Midwestern also tendered its defense to Emcasco and Emcasco appointed Richard Nugent to represent Midwestern.

¶ 8 Emcasco's claim file for Midwestern was initially handled by Bob Blonn and then by Bob Coon from September 1999 until the end of the *Orange* trial. Emcasco's claim file for Triumph was handled by Mike Genender. Both claims handlers, Coon and Genender, were supervised by the branch manager, Rich Schulz, who was also an employee of Emcasco. According to the testimony of Coon, Genender, and Schulz, there were two distinct files for Midwestern and Triumph though they were initially kept adjacent to one another and had the same claim number until September 2000. Genender testified that he was unaware of either claims handler for Midwestern, Blonn or Coon, physically looking at the Triumph file. However, on three different occasions, Genender, Coon, and Schulz discussed potential damages in the *Orange* case, but not liability or confidential information.

¶ 9 The record demonstrates that Emcasco made efforts to obtain information from Nationwide during the *Orange* litigation. Nationwide was generally either not responsive to Emcasco's requests or was not actively managing Triumph's file at the Nationwide office. On

three occasions in late 1998, the Emcasco-appointed attorney for Triumph and the claims handler for the Triumph file, wrote to Nationwide requesting a copy of its insurance policy but never received one. Nationwide employee log notes reveal that the insurer was aware of the request for its policy and in March of 1999, Nationwide notes reveal that it was aware that it had not yet sent its policy to Emcasco. In a note dated May 23, 2000, Schulz decided that Emcasco would stop trying to obtain the Nationwide insurance policy. He wrote: "Mike [Genender] will talk to coverage counsel to discuss the timing on putting the hammer to Nationwide." The note also referenced Emcasco's desire to get control of the defense of *Orange*. Nationwide used this note as the basis for the allegation that Emcasco had a plan to shift liability from Midwestern, its insured, to Triumph, its additional insured.

¶ 10 Nationwide's efforts to monitor Triumph's liability as the *Orange* litigation progressed are as follows. From September 1998 until August 1999, Nationwide maintained an open file on the *Orange* case and Triumph's liability therein. Between August 1999 and December 2000, the Triumph file was closed. Nationwide reopened its Triumph claim file in December 2000. Between December 2000 and October 2001, Nationwide raised its reserve on the Triumph file from $5,000 to $150,000. On five occasions, the claim representative at Nationwide (claim representative) called the attorney representing Triumph at trial. More often than not, the Triumph attorney did not return the calls.

¶ 11 On March 30, 1999, Triumph's counsel at the Law Offices of Mark Rudoff wrote to Triumph's initial lawyer stating: "we believe that a conflict of interest exists between [Emcasco] and Triumph." The letter demanded that Emcasco either "1) waive the aforesaid reservation of rights; or 2) relinquish control of the defense of Triumph to independent counsel of Triumph's choice at [Emcasco's] expense, including attorney fees." In response to this letter, Emcasco

withdrew the reservation of rights on August 10, 1999. The letter concluded: "Since this portion of the Reservation of Rights has been withdrawn, [Emcasco does] not believe there appears to be any conflict with our attorneys to continue to vigorously defend the Additional Insured, Triumph Development."

¶ 12 In February 2000, plaintiff's attorney in the *Orange* case made a $5 million settlement demand against both defendants. It is unclear from the record whether the initial lawyer for Triumph made Nationwide aware of the demand.

¶ 13 In November 2000, Emcasco learned that the initial lawyer it had appointed for Triumph's defense was conflicted and that he had failed to perfect a third-party action for contribution. As a result, Emcasco appointed Kurt Meihofer to take over Triumph's defense in December 2000.

¶ 14 Shortly before the *Orange* trial, the Nationwide claim representative for Triumph's file prepared a 15-point summary about Triumph’s liability in *Orange*. In formulating the summary, the claim representative had access to Meihofer's written assessment of the *Orange* case in which he anticipated the verdict somewhere between $600,000 and $2 million for both defendants. In the same assessment, Meihofer opined that the "worst case" scenario for Triumph's liability to be between $1.5 and $2 million. On October 24, 2001, Meihofer informed the claim representative at Nationwide that the plaintiff's demand in *Orange* was $5 million. The claim representative made a note with that $5 million demand and also noted "demand keeps going up." The claim representative did not concede any awareness of a settlement demand before the *Orange* trial began.

¶ 15 At various times before trial, several assessments of Triumph and Midwestern's respective liability were made. The initial lawyer for Triumph wrote to Emcasco saying

settlement would not be cheap and that there was a potential verdict of $2 million total, 80% of which would be apportioned to Triumph. In December 2000, Meihofer communicated to an employee at Nationwide that Triumph's liability would exceed Emcasco's $1 million primary policy limit. In February of 2001, Meihofer told Triumph employees that Triumph was likely more than 50% liable and that Meihofer would be exploring other coverage in addition to Emcasco's coverage. Before trial, Meihofer told the claim representative at Nationwide that the settlement demand was $5 million. Nugent, the Emcasco-assigned attorney for Midwestern, consistently assessed Midwestern's liability between 0% and 20%. Before trial, Nugent filed a motion for summary judgment on Midwestern's behalf.

¶ 16 The *Orange* case went to trial in early November 2001. Emcasco sent a representative to evaluate Midwestern's exposure; Nationwide did not. Before the jury reached a verdict, the Orange plaintiff indicated he was willing to settle for $1.9 million against Triumph and Midwestern. The Orange plaintiff was unwilling to settle against the defendants independently. By letter, Emcasco informed the claim representative at Nationwide that it would offer its $1 million primary policy limits and suggested that Nationwide provide the remaining $900,000 to satisfy the Orange plaintiff's $1.9 million demand. On November 7, 2001, Meihofer and Genender informed Nationwide's claim representative that Triumph's liability in *Orange* was more than $1.9 million and urged Nationwide to provide the remaining $900,000 to settle the case. The claim representative spoke with her superiors at Nationwide and conveyed a $200,000 offer to Emcasco. The next day, the claim representative was given authority to offer $250,000. The claim representative could not recall the reasoning for the increase. The plaintiff in *Orange* rejected the combined offer of $1.25 million. When further pressed to meet the $1.9 million

demand, Nationwide's claim representative reiterated the $250,000 offer and said that the $1.9 million demand was not a "feasible settlement."

¶ 17 Ultimately, the jury returned a $7.17 million judgment against Triumph and Midwestern. The jury allocated 95% liability to Triumph ($6,814,825) and 5% liability to Midwestern ($358,675). Emcasco paid Midwestern's portion and then Emcasco and Nationwide negotiated and paid off the judgment pursuant to a non-waiver agreement that remains confidential.

¶ 18 B. This Coverage Litigation

¶ 19 In December 2001, Emcasco filed this coverage action against Nationwide alleging, among other things, that Nationwide breached its duty to settle. Nationwide filed a counterclaim alleging that Emcasco breached its duty to defend Triumph because Emcasco was a conflicted insurer. On January 16, 2002, Triumph assigned its rights to all actions and claims, except legal malpractice claims, it might have against Emcasco to Nationwide. The parties alleged the following counts in their complaints:

¶ 20 **1. Emcasco's Amended Complaint**

Count	Allegation	Trial court rulings	Our ruling
Count I	Nationwide is estopped from raising a policy defense based on the allegation that Nationwide failed to provide a defense to Triumph in the *Orange* case.	o The court found that Emcasco alone had a duty to defend Triumph on September 22, 2008.* o The court granted summary judgment in favor of Nationwide on this count on May 20, 2010.*	Affirmed
Count II	Nationwide is a co-primary insurer with Emcasco for the benefit of Triumph and is obligated to pay 50% of	o The court granted summary judgment to Nationwide on this count on May 20, 2010.*	Affirmed

	all defense costs for Triumph.		
Count III	Nationwide should bear 2/3 of any unsatisfied judgment in excess of coverage available under either insurer's primary policy and Emcasco should bear 1/3 of the same amount.	o The court denied Nationwide's request for summary judgment on this count on May 20, 2010.* o Addressed, in the alternative to Count IV, in the final order in favor of Emcasco and pro-rata apportionment.	Affirmed
Amended Count IV	Nationwide as a primary carrier breached its duty to settle to Emcasco as the excess carrier.	o The court denied Nationwide's request for summary judgment on this count on May 20, 2010.* o Addressed in final order and post-judgment orders in favor of Emcasco.	Reversed

¶ 21 **2. Nationwide's Second Amended Counterclaim**

Count	**Allegation**	**Pre-trial rulings**	**Our ruling**
Count I	Triumph's tender to Emcasco was targeted and, as a result, both of Emcasco's policies apply before the Nationwide policy.	o On July 18, 2008, the trial court ruled that Nationwide's primary policy applied before Emcasco's excess policy defeating subparts (a), (g), and (h) of Nationwide's requested relief.* o On September 22, 2008, the court granted subparts (b) and (c) of the relief namely, that Nationwide's primary policy was deactivated upon Emcasco's	All pre-trial rulings are affirmed

		acceptance of Triumph's defense.* o The remaining requested relief was denied in the final order (i, d, e, f).	
Amended Count II	The Emcasco primary policy applies before the Nationwide primary policy.	o On September 22, 2008, the court ruled that the Emcasco primary policy applied before Nationwide's primary policy.*	Affirmed
Amended Count III	Emcasco is estopped from asserting a policy defense to coverage based on Emcasco's conflict of interest in shifting liability from Midwestern to Triumph.	o The trial court granted Emcasco's motion to dismiss Amended Count III on July 14, 2010.*	Affirmed
Count IV	Emcasco is estopped from raising a defense to coverage based on its misrepresentation that it would settle the underlying claims against both Triumph and Midwestern for $1.9 million.	o Addressed in the final order in favor of Emcasco.	Affirmed
Count V	Emcasco is estopped from raising a defense to coverage based on its vexatious and unreasonable conduct toward Triumph.	o Addressed in the final order in favor of Emcasco.	Affirmed
Count VI	Emcasco committed common law bad faith as a result its failure to provide a reasonable and competent defense to Triumph.	o Addressed in the final order in favor of Emcasco.	Affirmed
Count VII	Emcasco committed common law fraud toward Triumph as a result of Emcasco's failure to provide a reasonable and competent defense to Triumph.	o Addressed in the final order in favor of Emcasco.	Affirmed

Count VIII	Emcasco violated the Illinois Consumer Fraud and Deceptive Business Practices Act by concealing that its strategy was to increase Triumph's exposure while reducing Emcasco's exposure.	o Addressed in the final order in favor of Emcasco.	Affirmed
Amended Count IX	Emcasco failed to disclose the potential liability to Triumph or to Nationwide and promissory estoppel bars it from asserting any defenses to coverage.	o Stricken on July 14, 2010.* o Emcasco's motion to dismiss the amended count was denied on November 24, 2010.* o Amended count was addressed in the final order in favor of Emcasco.	Affirmed
Amended Count X	Emcasco is estopped from asserting a defense to coverage based on its breach of the duty to defend to Triumph by controlling the defense in *Orange* in favor of Midwestern.	o Stricken on July 14, 2010.* o Emcasco's motion to dismiss the amended count was denied on November 24, 2010.* o Amended count was addressed in the final order in favor of Emcasco.	Affirmed
Amended Count XI	The Emcasco excess policy was targeted and the Nationwide excess policy was deselected.	o Addressed in the final order in favor of Emcasco.	Affirmed

¶ 22 We address five issues on appeal: (1) whether Emcasco had a conflict of interest in providing Triumph's defense; (2) whether Nationwide's primary coverage owed a duty to settle to Emcasco's excess coverage; (3) whether Nationwide was liable for prejudgment interest based on its breach of the duty to settle to Emcasco as an excess carrier; (4) whether Nationwide made a valid selective tender to Emcasco's excess policy; and, (5) whether the trial court erred in denying Emcasco's motion for sanctions under Supreme Court Rule 137.

¶ 23 We affirm the trial court on issues (1), (4), and (5). We reverse the trial court on issues (2) and (3). Accordingly, we deny Nationwide's request for relief in its opening brief except the following requested relief: (g) a declaration that Nationwide did not breach a duty to settle; (h) a finding that no prejudgment interest applies to any amount the trial court found owing by Nationwide attributable to the duty to settle; and (part of (i)) we remand for a determination of litigation costs in light of this ruling.

¶ 24 **3. Trial Court's Final Order**

¶ 25 After a lengthy bench trial in this coverage litigation, the trial court issued a very thorough ruling on March 18, 2013 (final order) addressing two themes of Nationwide's case: whether Emcasco had a plan to shift liability from its insured to its additional insured and whether Emcasco hid information from Nationwide. The trial court's final order also addressed eight counts of Nationwide's counterclaims that had not been dismissed prior to trial as well as two remaining counts of Emcasco's amended complaint. Both "themes" as well as each of the counts were resolved in favor of Emcasco.

¶ 26 Addressing Emcasco's alleged plan to shift liability from Midwestern to Triumph, the trial court found that the Emcasco-appointed attorneys properly fulfilled their fiduciary duties to both Midwestern and Triumph, that Nationwide presented no evidence of a conflict between Emcasco and its insureds, and that the testimony of the attorneys and claim representatives did not give any factual basis for the existence of the shifting plan. Accordingly, the trial court concluded that Emcasco did not breach its duty to defend Triumph and was not required to offer Triumph representation by independent counsel. The court also rejected the second theme of Nationwide's case, namely, the allegation that Emcasco hid information from Nationwide. The

court found that Nationwide could have known of the potential liability to Triumph if it had assessed the underlying case when it had opportunities to do so.

¶ 27 As to Emcasco's Amended Count IV, the trial court found that Nationwide had a duty to settle the *Orange* case, and that it breached that duty by failing to offer $900,000 toward the $1.9 million settlement demand. The court also granted Emcasco's request for prejudgment interest. Because of this ruling, the trial court found it unnecessary to address Emcasco's alternative argument in Count III which requested that Nationwide and Emcasco share liability for any judgment against Triumph over the two insurer's primary policies on a pro-rata basis.[1]

¶ 28 The trial court's order also summarized the lengthy testimony at trial. We include a summary of the trial court's findings as to witness credibility relevant to the conflict of interest issue below.

¶ 29 Once Triumph tendered its defense to Emcasco, Emcasco set up a "Chinese Wall" to avoid conflicts with its defense of its named insured, Midwestern, under the same insurance policy. One claims handler was assigned to the Midwestern file and another claims handler was assigned to the Triumph file. Two separate files were maintained for each insured although the two files had the same claim number until August 2000. The Midwestern claims handler kept electronic notes and never accessed the notes of Triumph's claims handler, which were kept on

[1] With respect to the remaining counts of Nationwide's Amended Counterclaim, the court ruled in favor of Emcasco on each: Count (IV) Nationwide failed to prove reliance for any intentional misrepresentation cause of action; Count (V) Emcasco's conduct was not unreasonable to justify any remedy under the Illinois Code of Civil Procedure section 155 (215 ILCS 5/155 (West 2012)) nor was there a showing that Triumph was damaged; Count (VI) Illinois does not recognize a cause of action for "bad faith failure to defend" or for a "defective defense"; Count (VII) Nationwide produced no evidence that Emcasco perpetuated any kind of fraud on Triumph; Count (VIII) the allegations alleged against Emcasco simply did not amount to statutory fraud against Triumph; Count (IX) there were no communications between Emcasco and Triumph such that Emcasco could have promised anything outside the insurance policy; Count (X) there is no evidence that there was a plan to shift liability, thus Emcasco was not a conflicted insurer and did not breach its duty to defend; Count (XI) Nationwide's letters purporting to effectuate a targeted tender to Emcasco's excess policy were insufficient. As to Count I, the court denied Nationwide's request for attorney fees (215 ILCS 5/155 (West 2012)) and its request that the court find Emcasco's excess policy was obligated to indemnify Triumph. The court also rejected Nationwide's vertical targeted tender argument.

paper and electronically. At no point did the claims handlers look at the physical file for the other insured. The two claims handlers and their supervisor discussed the case—technical violations of the Chinese Wall—but those discussions did not involve confidential information.

¶ 30 Schulz, the branch manager for Emcasco and supervisor of both claims handlers, made a note in which he referenced "putting the hammer to Nationwide" and getting control of the *Orange* defense. The trial court found Schulz's explanation of this note credible: the note was a message to the claims handler of the Triumph file that he relay to Nationwide the consequences of not settling the *Orange* case.

¶ 31 As to Meihofer, the attorney for Triumph, the trial court found that Emcasco did not direct him in the defense of Triumph as he was an independent contractor. The trial court also found Meihofer's testimony credible in that, in December 2000, Meihofer assessed that Triumph's defense was not promising and its liability was high because Triumph was the general contractor for the worksite on which Orange was injured. The trial court also believed Meihofer's explanation of the jury form which instructed jurors to allocate liability between the insureds and the Orange plaintiff: namely, given the evidence at trial, Midwestern was likely less than 25% liable.

¶ 32 As to Nugent, the attorney for Midwestern, the trial court found that Emcasco did not direct him in the defense of Midwestern as he was an independent contractor and he testified credibly that he did not observe anything to suggest that Meihofer shifted liability to Triumph.

¶ 33 **4. Orders Issued Prior to the Final Order**

¶ 34 In addition to the final order, Nationwide and Emcasco include several other orders in their notices of appeal designated by an asterisk in paragraphs 20 and 21.[2]

[2] Emcasco also appeals an order entered August 10, 2012 denying its motion to strike a witness' trial testimony in its notice of appeal.

¶ 35 Furthermore, Nationwide appeals an order on Emcasco's three post-trial motions for a) prejudgment interest; b) litigation costs; and c) a motion for entry of money judgment attributable to Nationwide's breach of the duty to settle.[3] The court granted Emcasco's motion for prejudgment interest and the motion for entry of a money judgment order. It granted in part and denied in part the motion for award of litigation costs. In its cross-appeal, Emcasco appeals the portions of this order denying certain litigation costs.

¶ 36 Parties also appeal the trial court's order of March 13, 2014 denying Emcasco's motion for sanctions against Nationwide and its lawyer in this case.

¶ 37 **II. ANALYSIS**

¶ 38 **A. First Issue – Whether Emcasco Had A Conflict of Interest**

¶ 39 As to the first issue, the parties dispute whether Emcasco was a conflicted insurer in its defense of its additional insured, Triumph. We affirm the trial court's finding that there was no conflict of interest.

¶ 40 Nationwide argues that Emcasco had a continuing conflict of interest that triggered its obligation to offer Triumph representation by independent counsel in the underlying *Orange* case. Specifically, Nationwide argues that (1) the two insureds, Triumph and Midwestern, had diametrically opposed interests and (2) that Emcasco had a financial interest in providing a less vigorous defense to Triumph because Emcasco was 100% liable for Midwestern's liability but would share any liability of Triumph with Nationwide. Nationwide contends that Emcasco, through its appointed attorneys, shifted liability from Midwestern to Triumph. Nationwide complains that Emcasco failed to disclose this conflict or offer independent counsel, thereby breaching its duty to defend Triumph.

[3] The trial court entered an Amended Judgment Order on August 13, 2013 *nunc pro tunc* to August 2, 2013.

¶ 41 Emcasco, on the other hand, contends that the only conflict in this case was a financial one between the two insurers, and that such a conflict did not require Emcasco to offer Triumph independent counsel. Emcasco also argues that the appointment of separate claim representatives and separate defense counsel for the Midwestern and Triumph files resolved any potential conflict of interest. Furthermore, Emcasco disputes that a plan to shift liability from Midwestern to Triumph existed.

¶ 42 This issue involves both questions of fact and questions of law. *Joel R. by Salazar v. Board of Education of Mannheim School District 83, Cook County, Ill.*, 292 Ill. App. 3d 607, 612 (1997). "The review of a mixed question of law and fact necessitates three steps be taken by the appellate court. The first step in this process is the establishment of basic, primary or historical facts: facts in the sense of a recital of external events and the credibility of their narrators. The second step is the selection of the applicable legal rule. The third step *** is the application of the law to fact or, in other words, the determination of whether the rule as applied to the established facts has been violated. *Id.* (citing *United States v. McConney*, 728 F.2d 1195, 1200 (9th Cir.1984) (*en banc*)). The questions of fact are reviewed under the manifest weight of the evidence standard (*Id.* at 613), whereas questions of law are reviewed *de novo* (*Id.*).

¶ 43 Factually, no conflict existed because the trial court's assessment of the credibility of the witnesses was not against the manifest weight of the evidence. The trial court found that neither Meihofer nor Nugent displayed substandard conduct and that the insureds' files were handled—with few exceptions—independently of one another. See *supra* (¶¶ 29-32). The trial court found that both lawyers credibly denied that they were part of a plan to shift liability from Midwestern onto Triumph. See *supra* (¶¶29-32). The trial court also found that the lawyers credibly denied that Emcasco directed the defense of Triumph or Midwestern. See *supra* (¶¶29-32). Upon

review of the extensive record, we find these factual findings were not against the manifest weight of the evidence as there is support in the record for each. Moreover, the appellate court will not substitute its judgment for that of the trial judge as to the credibility of witnesses. *Brown v. Zimmerman*, 18 Ill. 2d 94, 102 (1959).

¶ 44 We now turn to the second step in a mixed question of law and fact analysis, the applicable legal rule on conflict of interest. Nationwide's conflict of interest analysis asks us to presume that, since there was an opportunity for Triumph's defense counsel to be beholden to Emcasco's interests at the expense of Triumph's interests, defense counsel did so. We disagree with Nationwide's premise. It has not been the practice of Illinois courts to presume unethical, substandard behavior of attorneys. Moreover, this premise has been rejected by factual findings of the trial court. See *supra*, 29-32.[4] We proceed to analyze the conflict of interest issue from the premise that the attorneys' conduct met their legal and ethical obligations as the trial court found.

¶ 45 We briefly review the legal and ethical duties at play in any case that involves an insurer, one or more insureds, and attorneys assigned or retained by the insurer. First, when an insurer retains or assigns an attorney to represent an insured in a claim, the attorney is deemed to represent both the insured as well as the insurer. *Waste Management Inc. v. International Surplus Lines Insurance Co.*, 144 Ill. 2d 178, 194 (1991) (citing *Rogers v. Robson, Masters, Ryan, Brumend and Belom*, 74 Ill. App. 3d 467, 472 (1979)). The attorney-client relationship between the insured and the attorney hired by his insurer imposes upon the attorney the same professional obligations that would exist had the attorney been personally retained by the insured. *Rogers*, 74

[4] Nationwide disputes that the testimony of those involved or aware of Triumph's defense is relevant to the conflict of interest issue. Instead, Nationwide contends conflict obligations are triggered at the outset of the underlying litigation with the underlying complaint. But, the extensive 52-volume record however, does not contain a copy of the underlying *Orange* complaint. Therefore, we must construe the record against the Nationwide on this point. *Foutch v. O'Bryant*, 99 Ill. 2d 389, 392 (1984) (any doubts which may arise from the incompleteness of the record will be resolved against the appellant).

Ill. App. 3d at 472. See also *Allstate Insurance Co. v. Keller*, 17 Ill. App. 2d 44, 52 (1958). Second, the retained attorney is bound by the Illinois Rules of Professional Conduct including Rule 1.7(a)(2) which states that a concurrent conflict of interest exists if "there 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." Ill. R. Prof. Conduct 1.7(a)(2). Third, the insurer has a fiduciary duty and a duty of good faith to its insureds. In sum, an insurer must not put its own interests ahead of the protection it has promised to its insured. *Briseno v. Chicago Union Station Co.*, 197 Ill. App. 3d 902, 906 (1990).

¶ 46 As a matter of law, the situation at hand is not a conflict of interest. Nationwide has not supplied, nor has our own research uncovered, a case that stands for the proposition that a defending insurer is necessarily conflicted if the insurer shares the costs of judgment against the additional insured but not the named insured. Instead, Nationwide relies on cases that have one or more of the following characteristics: (1) underlying allegations that are not covered by the insured's policy; (2) an insured who becomes responsible for a judgment in the underlying case if certain facts are proven true; (3) opposing defense strategies for each insured. The instant case has none of the three characteristics and therefore is distinguishable from all of the cases relied on by Nationwide.

¶ 47 Turning to the first characteristic, parties do not dispute that all underlying allegations in the *Orange* case are covered by the Emcasco and Nationwide insurance policies. Therefore, this case is unlike *Maryland Casualty Co. v. Peppers*, 64 Ill. 2d 187, 197-98 (1976) on which Nationwide relies. In *Peppers*, the court found a conflict of interest for an attorney representing both an insurer and an insured when the insurer would have been relieved of the obligation to

pay any judgment if the insured's actions were found to be intentional, rather than negligent. *Id.* at 197. If the insured's actions were intentional, liability would shift from the insurer to the insured. *Id.* Because of this conflict, the court said, serious ethical questions "prohibit an attorney from representing both the interests of [the insurer] and of [the insured]." *Id.* See also *Nandorf*, 134 Ill. App. 3d at 138 (finding an insurer must relinquish control of its insured's defense and reimburse the insured for independent counsel where the allegations in the underlying suit involved covered compensatory damages and noncovered punitive damages). In the instant case, no facts could be proven in the *Orange* case that would take the "case outside the scope of policy coverage." *American Family Mutual Insurance Co. v. W.H. McNaughton Builders, Inc.*, 363 Ill. App. 3d 505, 511 (2006). No matter what facts were proven in the *Orange* trial, Triumph would have been covered by either Emcasco or Nationwide up to the applicable policy limits.

¶ 48 Nationwide also relies on cases in which underlying allegations against an insured, if proven, expose the insured to liability. See *Nandorf, Inc. v. CNA Insurance Cos.*, 134 Ill. App. 3d 134, 135 (1985); *Mobil Oil Corp. v. Maryland Casualty Co.*, 288 Ill. App. 3d 743, 756 (1997); *Illinois Municipal League Risk Management Ass'n v. Seibert*, 223 Ill. App. 3d 864, 876 (1992). For example, in *Mobil Oil* the insured would be liable for any punitive damage judgment whereas the insurer would be liable for any compensatory judgment. *Mobil Oil*, 288 Ill. App. 3d at 756. In our case, it would be another insurance company, Nationwide, who would be liable for a judgment in excess of Emcasco's primary policy not the insured, Triumph.

¶ 49 As to the third characteristic, Nationwide relies on cases finding a conflict of interest when the representation of two insureds calls for two opposing defense strategies. In *Murphy v. Urso*, 88 Ill. 2d 444 (1981) the insureds—a driver and school who employed the driver—had adverse interests and the supreme court excused the insurer from its duty to defend both the

driver and school. *Murphy*, 88 Ill. 2d at 454. The court explained that the insurer could not avoid a conflict of interest because it was in the driver's interest to show employment with the school, while it was in the school's interest to disassociate from the driver. *Id.* at 453. The insurer's interests aligned with the school defendant and conflicted with the driver's because the insurer would not have to indemnify the driver if, at the time of underlying accident, he was operating the school's vehicle without approval or outside the scope of his employment. *Id.* at 454. In *Murphy*, the best defense strategy for one defendant was diametrically opposed to the best defense strategy for the other defendant.

¶ 50 Like the first and second characteristics, we can also distinguish our case on the basis of the third characteristic. That is, the two insureds, Midwestern and Triumph, did not have opposing defense strategies. The best defense strategy for Midwestern in the *Orange* case was also the best defense strategy for Triumph: namely, to minimize the recovery of the Orange plaintiff. However, Nationwide's argument on this point asks us to go one step further and find a conflict of interest when a case presents "opposing financial incentives of the insurers" rather than "opposing defense strategies" as *Murphy* described. Nationwide asks us to find a conflict when the defense strategy for one *insurer* may conflict with the defense strategy of the other *insurer*. We decline to find a conflict based on financial incentives between two insurers who both owed duties to defend and indemnify their insured, Triumph.

¶ 51 Moreover, Nationwide's in-house counsel acknowledged a potential conflict two years before trial in a letter stating: "we believe that a conflict of interest exists between [Emcasco] and Triumph." Rudoff's letter demanded that Emcasco either "1) waive the aforesaid reservation of rights; or 2) relinquish control of the defense of Triumph to independent counsel of Triumph's choice at Emcasco's expense, including attorney fees." That letter was not specific as to the

particular conflict but demanded that Emcasco *either* waive its reservation of rights or allow Triumph to choose independent counsel at Emcasco's expense. Emcasco chose to waive its reservation of rights.

¶ 52 A conflict of interest can only be resolved with full disclosure and acceptance or by allowing the insured to select his or her own attorney and reimburse the costs of that defense. *Peppers,* 64 Ill. 2d at 198-99. A disclosure letter to the insured must be sufficient to inform the insured of his rights to a fair defense. *Allstate Insurance Co. v. Carioto,* 194 Ill. App. 3d 767, 777 (1990). We do not hold that the letter from Nationwide's in-house counsel resolved the potential conflict of interest, but we observe that the trial court could have interpreted the letter as Triumph's acquiescence to Emcasco's continued defense as long as Emcasco waived its reservation of rights. C.f., *Seibert,* 223 Ill. App. 3d at 870 (the trial court found that a letter from an insurer to an insured about a potential conflict of interest as simply communicating the possibility of conflict rather than a concession that the conflict existed). It would be fair to suggest that, by this letter, Triumph acquiesced to a defense controlled by Emcasco given the option in the letter for Emcasco to proceed without a reservation in place. At the very least, it seems disingenuous for Nationwide to now allege that Emcasco gave "no notice of an actual or potential conflict, and never offered to provide independent counsel selected by the insurer."

¶ 53 **B. Second Issue – Whether Nationwide Had A Duty To Settle To Emcasco's Excess Policy**

¶ 54 As to the second issue, Nationwide argues that it had no duty to settle for the Orange plaintiff's $1.9 million demand for two reasons: (1) Nationwide did not control the defense of *Orange* and (2) there was no probability of recovery in excess of the combined $3 million limits

of the Emcasco and Nationwide primary policies.[5] Furthermore, Nationwide argues that the trial court erred in finding that it had a duty to settle to Emcasco as an excess carrier because (1) Emcasco could not assert a breach of duty as subrogee of Triumph, as subrogation rights were never asserted in this litigation, and (2) the appellate court in *U.S. Fire Insurance Co. v. Zurich Insurance Co.*, 329 Ill. App. 3d 987, 1003 (2002) found that Illinois does not impose a duty to settle by the primary carrier to the excess carrier.

¶ 55 Emcasco contends that a primary insurer's duty to settle within policy limits is triggered in multi-carrier situations if a carrier has control of settlement negotiations whether or not that carrier also had control of the defense of the underlying litigation. It further contends that "control" over the settlement rested solely with Nationwide once Emcasco offered its primary policy limits to the Orange plaintiff. Emcasco argues that our decision in *Schal Bovis*, 314 Ill. App. 3d 562, 572-73 (1999) was simply "better reasoned" than *U.S. Fire*, and therefore we should follow *Schal Bovis* in recognizing a primary insurer's duty to settle to an excess insurer.

¶ 56 The trial court ruled in favor of Emcasco finding a duty to settle between a primary and excess carrier. In so ruling, the trial court relied on *Schal Bovis* for the proposition that a primary carrier has a duty to an excess carrier to act reasonably and in good faith in attempting to settle claims within a primary insurer's policy limits and that all three parties—an insured, primary insurer, and excess insurer— must act reasonably and in good faith in considering the others' interests in settlement which, in this case, was a $1.9 million. The trial court found that "Nationwide was in control of settlement negotiations because Emcasco offered its entire [primary] policy limits and Nationwide's legal obligation was to pay next under principles of horizontal exhaustion." The trial court concluded that Nationwide could have contributed

[5] Triumph was an additional insured on Emcasco's $1 million primary policy and a named insured on Nationwide's $2 million primary policy.

$900,000 to meet the $1.9 million demand but "inexplicably" failed to do so. The trial court awarded Emcasco damages of $1,596,175 based on that breach.

¶ 57 Before turning to the main issue, we reject Nationwide's argument that Emcasco's umbrella policy would apply to indemnify Triumph after Emcasco's primary policy limits were exhausted and before Nationwide's primary policy applied. Horizontal exhaustion, rather than vertical, has always been the law in Illinois. *United States Gypsum Co. v. Admiral Insurance Co.*, 268 Ill. App. 3d 598, 653 (1994); *Kajima Construction Services, Inc. v. St. Paul Fire and Marine Insurance Co.*, 368 Ill. App. 3d 665, 673–74 (2006). Nothing in the Emcasco insurance policy, including its "drop down" provision, persuades us to adopt a different rule in this case. We also note that Emcasco was not obligated by a duty to settle by offering $900,000 from its excess policy because the "duty to settle does not obligate the insurer to perform the impossible by offering more than called for by the policy." *Central Illinois Public Service Co. v. Agricultural Insurance Co.*, 378 Ill. App. 3d 728, 738 (2008).

¶ 58 It is well-established that an insurer has a duty to act in good faith to its insured in responding to settlement offers. *Haddick v. Valor*, 198 Ill. 2d 409, 414 (2001). To determine whether a party has breached this duty to settle, courts look for two factors: 1) a carrier's control over defense and settlement negotiations and 2) a reasonable probability of a finding of liability against the insured in excess of policy limits. *Haddick v. Valor*, 198 Ill. 2d at 416. In *Cramer v. Insurance Exchange Agency*, 174 Ill. 2d 513 (1996), the Illinois Supreme Court acknowledged that the insurer owed its insured a duty to settle and that this duty arose out of the *contractual* covenant of good faith and fair dealing between the [insurer and insured]. (Emphasis added.) *Cramer*, 174 Ill. 2d at 524. See also *Chandler v. American Fire & Casualty Insurance Co.*, 377 Ill. App. 3d 253, 255 (2007) ("Any bad-faith failure to settle would be a tort arising from [a]

contractual obligation"). This duty is a narrow exception to Illinois courts' otherwise steadfast refusal to recognize an independent tort arising from the breach of a contractual covenant. *Voyles v. Sandia Mortgage Corp.*, 196 Ill. 2d 288 (2001) (refusing to find an independent cause of action for a breach of the duty of good faith and fair dealing).

¶ 59 The precise question before us is whether Nationwide, an insurer providing primary coverage, had a duty to settle to Emcasco, another insurer, who was providing excess coverage to a common insured, Triumph.

¶ 60 In Illinois, "[t]he determination of whether a duty exists—whether the defendant and the plaintiff stood in such a relationship to one another that the law imposed upon the defendant an obligation of reasonable conduct for the benefit of the plaintiff—is an issue of law to be determined by the court." (Citations omitted.) *Kirk v. v. Michael Reese Hospital and Medical Center*, 117 Ill. 2d 507, 525 (1987). See also *Thompson v. County of Cook*, 154 Ill. 2d 374, 382 (2003). We review a question of law *de novo*. *Hendricks v. Riverway Harbor Service St. Louis Inc.*, 314 Ill. App. 3d 800, 808 (2000).

¶ 61 Two appellate cases reached different conclusions on whether a duty to settle runs from a primary to an excess carrier, *Schal Bovis* and *U.S. Fire*. In *Schal Bovis*, the appellate court gave two bases for finding that a duty to settle ran from a primary carrier to an excess insurer: first, because "an excess insurer is subrogated to the rights of its insured's primary carrier when forced to pay a claim" and second, absent subrogation, there is a three-way duty of care to act reasonably and in good faith in settling meritorious claims within the policy limits between the policyholder, the primary insurer, and the excess insurer. *Id.* at 571-72. The court relied on *Transit Casualty Co. v. Spink Co.*, 156 Cal. Rptr. 360 (1979) for the following proposition:

> This [three-way relationship between the policyholder, the primary insurer and the excess insurer] creates reciprocal duties of care in the conduct of settlement negotiations; when a claim threatens to exceed the primary coverage, the reasonable foreseeability that the claim may reach the excess policy creates a three-way duty of care to act reasonably and in good faith in settling meritorious claims within the policy limits. The insured, primary carrier and excess carriers must therefore act reasonably and in good faith towards one another in considering the others' interests in negotiating a settlement.

Id. at 572.

¶ 62 In finding a duty to settle, the *Schal Bovis* court weighed the 1) likelihood of injury to the excess carrier, 2) magnitude of the burden of guarding against that injury, and 3) consequences of placing the burden of negotiating in good faith upon a primary insurer. *Id.* at 572-73. The court noted that the existence of a legal duty to settle between a primary and excess carrier would be in the public interest and would promote judicial economy by incentivizing primary insurers to settle cases when expected liability approached the limits of that primary policy. *Id.*.

¶ 63 In the majority opinion of *U.S. Fire*, which was authored by one of the concurring judges of the *Schal Bovis* opinion, the court limited *Schal Bovis*' finding of a direct duty to settle between a primary and excess carrier without explicitly overruling that proposition. The court stated that *Schal Bovis* only "'predicted' that Illinois would recognize" that a primary insurer owes a direct duty to an excess insurer in dicta. 329 Ill. App. 3d at 1002. The court concluded, relying on *Twin City Fire Insurance Co. v. Country Mutual Insurance Co.*, 23 F.3d 1175, 1180 (7th Cir. 1994) and *Walbrook Insurance co. v. UNARCO Industries, Inc.*, No. 90 A 519, 1992 WL 159266 (N.D. Ill. 1992), that "Illinois does not impose a duty by the primary insurer to the excess carrier, despite the 'predictions' of the various courts and authority outside Illinois'

jurisdiction." *Id.* at 1003. The court also noted that the Seventh Circuit held that a "primary insurer does not have a tort duty to excess insurer because it has a contractual remedy against the primary insurer." *Id.* The court in *U.S. Fire* affirmed the trial court's dismissal of an excess insurer's allegation that a primary insurer owed direct duties to it. 329 Ill. App. 3d at 1002.

¶ 64 Since *Schal Bovis*, Illinois courts have not found that a primary insurer has a duty to settle to an excess insurer. See *U.S. Fire Insurance Co. v. Zurich Insurance Co.*, 329 Ill. App. 3d at 1003. Two federal cases, while not binding on this court, found that the Illinois Supreme Court would impose a direct duty to settle (*Ranger Insurance Co.v. The Home Indemnity Co.*, 714 F.Supp. 956 (N.D. Ill. 1989); *American Centennial Co v. American Home Assurance Co*., 729 F.Supp. 1228, 123-31-32 (N.D. Ill. 1990)) then, just a few years later, two other federal cases reached the opposite conclusion (*Walbrook Insurance co. v. UNARCO Industries, Inc.*, No. 90 A 519, 1992 WL 159266 (N.D. Ill. 1992); *Twin City Fire Insurance Co. v. Country Mutual Insurance Co.*, 23 F.3d 1175, 1180 (7th Cir. 1994)). The latter two cases found that the absence of a contractual relationship between the primary and excess carriers and/or the availability of the contractual remedy of subrogation to the excess carrier, suggested that Illinois would not recognize a primary carrier's direct tort duty to an excess carrier.

¶ 65 Two cases—one federal and one state case—reached opposite conclusions for a duty to settle between two excess carriers. In *Liberty Mutual Insurance Co. v. American Home Assurance Co.*, 348 F. Supp. 2d 940 (N.D. Ill. 2004), the court found no direct duty running from an underlying excess insurer to a secondary excess insurer because the underlying excess insurer did not exert control over the defense of the underlying litigation. The court commented: "courts are often reluctant to impose an independent duty upon a primary insurer's liability to excess insurers when no contractual relationship exists." *Id.* at 954. The same court also distinguished

Schal Bovis because, unlike the primary carrier in *Schal Bovis*, the underlying excess carrier in *Liberty Mutual* did not exert control over the litigation in any significant way. *Id.* at 958. Finally, the court noted that its conclusion was supported by the Illinois Supreme Court's requirement of "control" before imposing a duty to settle. *Id.* at 958 (citing *Haddick*, 198 Ill. 2d 409, 416 (2001)). However, just four years later, the appellate court in *Central Illinois Public Service* relied on *Schal Bovis* to find the possibility of a duty to settle between two excess carriers. 378 Ill. App. 3d at 736. Distinguishing *Liberty Mutual*, the court in *Central Illinois* found that there was a question of fact as to whether a lower-tiered excess insurer might have controlled the litigation process, precluding a finding of summary judgment in the lower-tiered excess insurer's favor. *Id.* at 735-36.

¶ 66 To complicate matters, the case on which *Schal Bovis* relied to find a tort duty, *Transit Casualty v. Spink Corp*., 156 Cal. Rptr. 360 (1979), was overruled in *Commercial Union Assurance Companies v. Safeway Stores, Inc.*, 164 Cal. Rptr. 709 (1980). While the majority view in other jurisdictions seems to be that no such direct duty exists, some states do recognize the direct duty, as was noted in the *U.S. Fire* dissent. *U.S. Fire*, 329 Ill. App. 3d at 1006 (citing *Peter v. Travelers Insurance Co.*, 375 F. Supp. 1347 (C.D. Cal.1974); *Phoenix Insurance Co. v. Florida Farm Bureau of Mutual*, 558 So. 2d 1048 (Fla. Dist. Ct. App. 1990); *Ranger Insurance Co. v. Travelers Indemnity Co.*, 389 So. 2d 272 (Fla. Dist. Ct. App. 1980); *Great Southwest Fire Co. v. CNA Insurance Co.*, 547 So. 2d 1339 (La. Ct. App.1989); *Hartford Casualty Insurance Co. v. New Hampshire Insurance Co.*, 628 N.E.2d 14 (Mass. 1994); *Commercial Union Insurance Co. v. Medical Protective Co.*, 393 N.W.2d 479 (Mich. 1986) and *American Centennial Insurance Co. v. Canal Insurance Co.*, 843 S.W.2d 480 (Tex. 1992)). Therefore, "'in the absence of clear Illinois case law overturning the holding in *Schal Bovis* [, *Inc.*], this [c]ourt

proceeds upon the theory that the direct, common law duty between primary insurers and excess insurers is still a possible legal theory in Illinois.'" 378 Ill. App. 3d at 734 (citing *Liberty Mutual Insurance Co. v. American Home Assurance Co.*, 348 F.Supp.2d 940, 956-57 (N.D. Ill 2004) which noted that *U.S. Fire* and *Twin City Fire Insurance Co.* had expressed doubt about the finding of a direct duty between primary and excess insurers as the court in *Schal Bovis* stated.) However, we are unconvinced that a tort duty to settle can exist between a primary and excess insurer in this case when those parties are not in a contractual relationship and when the primary insurer exerted almost no control over the underlying defense and settlement negotiations.

¶ 67 In the context of the contractual relationship between an insured and insurer, *Haddick* requires that the insurer exert "exclusive control" over the defense and settlement negotiations of the underlying case before imposing a duty to settle on the insurer. *Haddick*, 198 Ill. 2d at 414. That authority to exert control arises out of the language of the insurance contract which generally "gives the insurer the right to 'make such investigation, negotiation, and settlement of any claim or suit as it deems expedient.'" *Id.* Emcasco argues that *Haddick*'s control requirement relies on the insurance policy provision that gives an insurer the *right to settle* a case and does not rely on the provision that gives an insurer the *right to defend* a case. Emcasco concludes that the insurer's settlement authority is determinative of a duty to settle. We do not agree. Control of the defense of the litigation, not only over settlement negotiations, is a critical factor in courts' analysis of a duty to settle. See, e.g. *Central Illinois Public Service Co.*, 378 Ill. App. 3d at 735; *Liberty Mutual*, 348 F. Supp. 2d 940, 958 (N.D. Ill. 2004) ("Control over the defense of the litigation is an important factor in deciding whether to impose a duty.").

¶ 68 Assuming *Haddick* requirements—control and reasonable probability of settlement in excess of the policy limit—apply even outside a contractual relationship as between two insurers,

it seems unlikely that Nationwide controlled the defense and settlement negotiations for purposes of finding a duty to settle if its approval of settlement was required *but no other element of control over the defense of Orange was apparent*. Nationwide was not involved in the *Orange* discovery: it did not even respond to Emcasco's requests for its insurance policy. Nationwide did not, for example, suggest a litigation strategy, proffer witnesses to testify on its insured's behalf, nor did it send a representative to trial. In fact, the record does not reveal that Nationwide exerted any influence over the *Orange* defense at all. The only element of control Nationwide exerted was to decide not to offer $900,000 to satisfy the Orange plaintiff's settlement demand.

¶ 69 While we find the control element lacking and therefore, do not impose a duty to settle on Nationwide, our decision does not imply that Nationwide is free to take advantage of its own inaction in the underlying litigation and settlement in order to avoid having "control" over the litigation and thereby, avoid a duty to settle. Our decision, while stopping short of imposing a duty to settle on Nationwide, by no means condones Nationwide's conduct of ignoring requests for its policy and not actively managing its insured's liability in *Orange*. Therefore, we find that the trial court's ruling in favor of Emcasco and against Nationwide on Amended Count IV of Emcasco's complaint is reversed.

¶ 70 **C. Third Issue - Whether Nationwide Is Liable For Prejudgment Interest Attributable to Its Breach of the Duty to Settle Owed to Emcasco's Excess Policy**

¶ 71 As to the third issue, Nationwide contends that it is not liable for prejudgment interest on damages attributable to Nationwide's supposed breach of the duty to settle because any breach was a tort action for which prejudgment interest cannot be awarded. Emcasco avers that the trial court correctly awarded prejudgment interest. Emcasco was awarded prejudgment interest (at a 5% simple interest rate between March 14, 2003 and August 2, 2013) on (1) the damages of

$1,596,175 which was the amount Emcasco paid out of its excess policy to satisfy the judgment against Triumph in *Orange* and (2) 10% premium on the non-waiver agreement between the two parties in the amount of $159,617.50.[6] The total prejudgment interest awarded to Emcasco was $828,917.15.

¶ 72 Having found no duty to settle in this case, no amount is owing to Emcasco based on a breach of that duty. Therefore, we also reverse the trial court's decision to award Emcasco prejudgment interest based on Nationwide's breach of the duty to settle in the amount of $828,917.15.

¶ 73 **D. Fourth Issue - Whether Nationwide Made a Valid Selective Tender to Emcasco's Umbrella Policy**

¶ 74 Regarding the validity of its tender to Emcasco's umbrella policy, Nationwide argues that four letters from Triumph to Emcasco effectuated the tender so that Emcasco's excess policy should have provided coverage before Nationwide's excess policy. Emcasco disputes that the letters were valid tender offers to the excess policy.

¶ 75 Our supreme court has clearly established an insured's right to select exclusive coverage from among multiple concurrent insurance policies, not consecutive policies. *John Burns Construction Co. v. Indiana Insurance Co.*, 189 Ill. 2d 570, 574 (2000). The selective tender rule, as recognized by Illinois courts, gives an insured covered by multiple concurrent policies the right to choose which insurer will defend and indemnify it with respect to a specific claim. *Id.* The insured may choose to forego an insurer's assistance for various reasons, including the insured's fear that premiums will increase or that the policy will be canceled in the future. *Cincinnati Cos. v. West American Insurance Co.*, 183 Ill. 2d 317, 326 (1998). Based on

[6] Nationwide and Emcasco entered into a "Non-Waiver Agreement as to Funding Settlement of the Underlying Case" in February 2003. Paragraph F of that Agreement allows the prevailing party to recover from the non-prevailing party a premium of 10%.

the fact that an insured has a right to choose from among its concurrent insurers, this court has also found "no reason why this rule cannot or should not be applied to concurrent excess insurance coverage." *North River Insurance Co. v. Grinnell Mutual Reinsurance Co.*, 369 Ill. App. 3d 563, 575 (2006).

¶ 76 The trial court found that Nationwide did not make a successful tender to Emcasco's excess policy. It found a 1998 letter from Triumph's corporate counsel was sent prior to the exhaustion of Emcasco's primary policy and thus could not have targeted Emcasco's excess policy. Two letters sent in 2002 were not at all clear in targeting Emcasco's excess policy and, by that time, Triumph had assigned its rights against Emcasco to Nationwide.[7] Therefore, by the time the letters were sent later that year, Triumph had no interest to tender. The 2010 letter was not a successful tender to Emcasco's excess policy because the right to selectively tender belonged to Triumph alone, and the 2010 letter was from Mr. Steven Novosad, the attorney for Nationwide in this coverage action.

¶ 77 The trial court's factual findings, concluding that no targeting of Emcasco's excess policy was effectuated, were not against the manifest weight of the evidence. *Staes & Scallan, P.C. v. Orlich*, 2012 IL App (1st) 112974, ¶ 35; *Nakomis Quarry Company v. Dietl*, 333 Ill. App. 3d 480, 483-84 (2002). Additionally, we agree with the trial court's conclusion that the balance to be paid by the excess policies, neither of which was targeted, is a pro-rata allocation.

¶ 78 We agree with the trial court that the timing of the first three letters (May 13, 1998; August 6, 2002; September 16, 2002) did not effectuate a tender to Emcasco's excess policy. In November of 2001, Emcasco indicated it would exhaust its $1 million primary policy limit for the judgment against Midwestern and Triumph in the underlying case. Any purported tender to Emcasco's excess policy prior to that date, including the 1998 letter, was ineffective. *North*

[7] See *supra*, ¶ 19.

River, 369 Ill. App. 3d at 574. The 2002 letters were also ineffective because, on January 16, 2002, Triumph assigned its rights to Nationwide and had no remaining interests to tender to Emcasco's excess policy. Finally, while a post-settlement deactivation to one insurer and a targeted tender to another insurer, is a viable method for targeting (*Richard Marker Associates v. Pekin Insurance Co.*, 318 Ill. App. 3d 1137, 1140-1144 (2001)), the 2010 letter was not an effective post-settlement tender in this case. The 2010 letter came four years after Nationwide filed this coverage action, eight years after Triumph assigned its rights to Nationwide, and was written by the attorney in this case when the right to tender is the insured's alone. See *John Burns*, 189 Ill. 2d at 574.

¶ 79 Moreover, contrary to Nationwide's position that the 1998 correspondence "should have been clear" that Triumph intended to deselect Nationwide's excess policy in favor of Emcasco's excess policy, nothing in the substance or attachments to the letters was sufficient to put Emcasco on notice that its excess policy was responsible for any loss immediately after its primary policy was exhausted. The language of the 2010 letter stated: "I request that you [Emcasco] accept [Triumph's] defense and indemnify [it] for any loss it may incur in the defense of this case." While no "magic words" are necessary to effectuate a targeted tender (*State Auto Property and Casualty Insurance Company v. Springfield Fire and Casualty Company*, 394 Ill. App. 3d 414, 420 (2009)), this language is bereft of any reference to Emcasco's excess policy. The certificate of insurance attached to Triumph's initial tender letter dated May 13, 1998, noting that Triumph was an additional insured under Emcasco's primary and excess policies, does not make any more explicit what is completely absent in the letter itself: Triumph's intention to target Emcasco's excess policy. Also, Illinois precedent disfavors expanding the targeted tender doctrine beyond its originally intended scope." *AMCO Insurance Co. v. Cincinnati Insurance*

Co., 2014 IL App (1st) 122856, ¶ 15 (2014) (noting that the doctrine has been criticized in recent years). Without a proper tender to Emcasco's excess policy and under the principles of horizontal exhaustion, Nationwide's primary policy must pay after Emcasco's primary limits are exhausted.

¶ 80 Accordingly, the payments are as follows. The total judgment from the *Orange* case of $7,173, 500 million is reduced by two payments from Emcasco's primary policy: $358,675 (for Midwestern's 5% liability) and $641,325 (for Triumph's 95% liability). Then, Nationwide's primary policy must pay its $2 million limits. This leaves a balance of $4,173,500 to be paid from excess layers of coverage.

¶ 81 Because both excess policies contain "other insurance" clauses, the remaining amount ($4,173,500) is to be divided between Nationwide and Emcasco in the same proportion as the respective policy limits of the subject umbrella policies ($10 million for Nationwide; $5 million for Emcasco) bear to the total limits of the umbrella policies ($15 million). *American Service Insurance Co. v. Jones*, 401 Ill. App. 3d 514, 527 (2010); *Ohio Casualty Insurance Co. v. Oak Builders, Inc.*, 373 Ill. App. 3d 997, 1004 (2007); *State Farm Fire and Casualty Co v. Utica National Insurance Group*, 375 Ill. App. 3d 230, 234 (2007) (Carriers are to share in the loss on a pro-rata basis where the "other insurance" clauses in both umbrella policies were excess clauses). Accordingly, of the $4,173,500 balance to be paid from excess layers of coverage, Emcasco's excess policy should pay $1,043,375 (5/15 or 1/3) and Nationwide's excess policy should pay $3,130,125 (10/15 or 2/3).

¶ 82 In its order dated August 2, 2013 and its amended judgment order *nunc pro tunc*, the trial court also awarded other litigation costs in the amount of $4,630.95 to Emcasco pursuant to section 5-108 of the Illinois Code of Civil Procedure (735 ILCS 5/5-108 (West 2012)) and Supreme Court Rule 208 (eff. Oct. 1, 1975). Because we reverse the trial court's ruling on

Nationwide's duty to settle and therefore also reverse its ruling on prejudgment interest, we remand the issue of costs to the trial court for a determination pursuant to section 5-108 (735 ILCS 5/5-108 (West 2012)) and Supreme Court Rule 208 in light of this ruling.

¶ 83 **E. Fifth Issue - Whether the Trial Court Erred in Denying Emcasco's Motion for Sanctions Under Supreme Court Rule 137**

¶ 84 For its cross-appeal, Emcasco contends that the trial court erred in denying its motion for sanctions against Nationwide because seven counts of Nationwide's counterclaim lacked legal and factual support in violation of Rule 137. Specifically, Emcasco complains that because discovery was well underway before Nationwide filed its November 2006 amended counterclaim, Nationwide and its attorney knew that there was no legal or factual basis for its allegations in it counterclaim and subsequent amendments. We review the trial court's decision to deny Emcasco's motion for sanctions against Nationwide and its attorney for abuse of discretion. *Olsen v. Staniak*, 260 Ill. App. 3d 856, 863-64 (1994).

¶ 85 Supreme Court Rule 137 states, in pertinent part, that

> [t]he signature of an attorney or party constitutes a certificate by him that he has read the pleading, motion or other document; that to the best of his knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good-faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation."

Ill. S. Ct. R. 137 (eff. Feb. 1, 1994). Courts must use an "objective standard in evaluating what was reasonable under the circumstances as they existed at the time of filing. *** It is not

sufficient that the plaintiff 'honestly believed' that the allegations raised were grounded in fact or law." (Citations omitted.) *Sterdjevich v. RMK Management Corp.*, 343 Ill. App. 3d 1, 19 (2003).

¶ 86 The purpose of the Supreme Court rule requiring client and counsel to make a reasonable inquiry to support legal claims of defenses is not to penalize litigants simply for lack of success in litigation, but rather, to prevent abuse of the judicial process by penalizing the litigant who brings vexatious or harassing actions that are based on false statements or are without legal foundation. *Regan v. Ivanelli*, 246 Ill. App. 3d 798, 817-18 (1993). Attorneys have an ongoing obligation to dismiss suits or withdraw pleadings as soon as it becomes apparent that they lack merit. *Walsh v. Capital Engineering & Manufacturing Co.*, 312 Ill. App. 3d 910, 915-16 (2000). When reviewing a decision on a motion for sanctions, the primary consideration is whether the trial court's decision was informed, based on valid reasoning, and follows logically from the facts. *Sanchez v. City of Chicago*, 352 Ill. App. 3d 1015, 1020 (2004). Finally, because of Rule 137's penal nature, it must be strictly construed. *Medical Alliances, LLC v. Health Care Service Corp.*, 371 Ill. App. 3d 755, 757 (2007) (citing *Dowd & Dowd, Ltd. v. Gleason*, 181 Ill. 2d 460, 487 (1998)). We find the court's decision to deny sanctions to be informed, based on valid reasoning and following logically from the facts.

¶ 87 Emcasco complains that the trial court erred in generally evaluating the allegedly offending counts of the counterclaim instead of undertaking a count-by-count review. While Emcasco argues that we must independently analyze each of the counts of Nationwide's counterclaim, it also concedes that there is no case law endorsing *or* rejecting this approach. We too are unaware of any case law mandating a count-by-count analysis. Given that we review only for abuse of discretion, we will not undertake the count-by-count analysis without clear case law supporting that approach.

¶ 88 The trial court's analysis of the motion for sanctions focused on the two themes of Nationwide's case because, if the trial court accepted the existence of a shifting plan, then it would "legally follow that Emcasco breached its duties to Triumph." If however, the trial court did not accept the existence of a shifting plan, Emcasco would not have breached its duties and Nationwide could be liable for sanctions pursuant to Rule 137.

¶ 89 As discussed above, as the trial court concluded, we too do not accept that Emcasco was a conflicted insurer based on the existence of a plan to shift liability. But, there are facts, as the trial court noted, that support such a theory. Nationwide offered a possible motive for shifting liability between Midwestern and Triumph based on the fact that Emcasco's potential exposure for a judgment against Triumph was less than its potential exposure for a judgment against Midwestern. The shifting plan was supported by the fact that three meetings between the claims handlers for Triumph and Midwestern occurred, even though Genender, Coon, and Schulz, testified that they discussed damages, not confidential information, in those meetings. Moreover, the fact that the initial attorney for Triumph failed to reveal a conflict in defending Triumph could call into question Emcasco's interest.

¶ 90 Three other trial court findings in denying sanctions relied on the fact that Nationwide interpreted the record differently than Emcasco and could support Nationwide's arguments. First, Schulz's note about "putting the hammer" to Nationwide could be interpreted to support Nationwide's theory that Emcasco was a conflicted insurer. Second, Emcasco's answer was not an admission of the shifting plan but could be construed.[8] Third, whether Nationwide had targeted Emcasco's excess policy in the letters was susceptible to multiple interpretations. While

[8] In its answer to Nationwide's counterclaim Emcasco stated the following, which Nationwide referenced in this coverage action as evidence of Emcasco's shifting plan: "Emcasco admits that the Nationwide policy issued to Triumph would not provide coverage to Midwestern for the underlying case. Emcasco admits that with respect to the handling of the defense of Midwestern in the underlying case, it was in Midwestern's interest, and therefore in Emcasco's interest as to that particular claim file, for liability to rest with some party other than Midwestern."

Nationwide's interpretations of the record were ultimately rejected, one could argue in good faith that those interpretations provided the factual basis for Nationwide's conflict and targeting arguments.

¶ 91 As to Nationwide's allegation that Emcasco hid information, the court noted that this allegation relied in part on the existence of the hammer plan. The court also noted that Meihofer admitted he did not return all of the claim representative's phone calls, which could be construed as intentional by Nationwide. But, just as the court conceded there were verifiable facts that could have supported the liability shifting plan, those verifiable facts supported, albeit unsuccessfully, a claim that Emcasco hid information. Given the trial court's thorough explanation of its objective analysis and reasoning, we hold that a reasonable person could have taken the view adopted by the trial court. *Sterdjevich*, 343 Ill. App. 3d at 19.

¶ 92 Moreover, in a case like this in which the discovery and motion stage of litigation lasted over ten years, the record is over fifty volumes and the trial lasted almost one month with many witnesses, it would be futile for this court to now try to recreate the precise chronology of the discovery process and match facts, or the lack thereof, from that discovery process to facts alleged in Nationwide's multiple pleadings in order to determine whether Nationwide had sufficient factual support for each one of their counts at the time of their filing. It is sufficient that we find the trial court's justification for denying Emcasco's motion for sanctions to be informed, based on valid reasoning, and following logically from the facts. This is especially true given that we have ruled in favor of Nationwide on issues (2) and (3) whereas Emcasco had prevailed on all claims that were decided at trial.

¶ 93 Affirmed in part; reversed in part; remanded for a determination of costs.