MITCHELL | HAMLINE
School of Law

Journal of Law and Practice

Volume 4 Article 2

2010

# Failure to Allocate? Nobody Pays: Using Miller Shugart Settlements in Cases of Questionable Insurance Coverage

Jerome Abrams

# Failure to Allocate? Nobody Pays: Using Miller Shugart Settlements in Cases of Questionable Insurance Coverage

**Keywords**
Insurance law, Liability insurance

# FAILURE TO ALLOCATE? NOBODY PAYS: USING MILLER SHUGART SETTLEMENTS IN CASES OF QUESTIONABLE INSURANCE COVERAGE

**Judge Jerome Abrams***

## I. Introduction

The central concept behind insurance in general, and liability insurance in particular, is risk transfer.[1] The simple nature of paying some amount of money in advance of a future event, which could result in a greater loss, provides some measure of economic security.[2] However, there can be many uncertainties involved in risk transfer through insurance.[3]

Multiple causes of loss, timing issues, scope of coverage, and even issues as basic as the meaning of terms in the insurer's undertaking in accepting a transferred risk may at some point be in doubt.[4] Insurance issuers typically rely on a general statement of what they are willing to accept in language that is often very different than the losses and causes of losses insured. Multiple forces often collide when a potentially transferred risk and a resulting loss lacks clarity in its origins.[5]

For a policyholder facing economic vulnerability and possible financial ruin from a risk they thought they had transferred to their insurer, news that the insurer questions whether the risk is actually covered by the purchased insurance can be devastating. Insureds are routinely thrust into financial uncertainty as a consequence of their insurer's views of what is or is not covered.[6] This financial uncertainty creates tremendous tension between a policyholder and their insurer, and frequently results in an adversarial, rather than a harmonious, relationship between insured and insurer. Insureds and their counsel rely on

---

* Judge Jerome Abrams is a 1981 graduate of William Mitchell. He spent the first 27 years of his legal career sorting out complicated issues, such as insurance coverage for his clients before he became a Judge in early 2008. His experience includes numerous trials and appeals in multiple jurisdictions, including the 8th Circuit Corn Plus decision which is discussed in this article. He has been a member of the American Board of Trial Advocates since 1996, teaches a course at several law schools concerning the management of complex litigation from curriculum he developed, and continues to write, lecture, and work on various topics of interest to civil practitioners and their clients.

[1] *See generally*, Carter v. State Farm Mut. Auto. Ins. Co., 808 A.2d 466 (D.C. 2002); *see also* Richardson v. GAB Business Services, Inc., 161 Cal. App. 3d 519 (5th Dist. 1984).

[2] *See generally*, 808 A.2d 466 (D.C. 2002); 161 Cal. App. 3d 519 (5th Dist. 1984).

[3] St. Paul Fire & Marine Ins. Co. v. Lefton Iron & Metal Co., Inc., 694 N.E.2d 1049 (5th Dist. 1998) (recognizing that the presence of a risk is the essence of an insurance contract).

[4] *See, e.g.*, Miller v. Shugart, 316 N.W.2d 729 (Minn. 1982).

[5] *See id.*

[6] *See, e.g.*, Wayne v. Staples, Inc., 37 Cal. Rptr. 3d 544 (2d Dist. 2006). Wayne demonstrates the inherent uncertainty in insurance contracts: The mere fact a contract involves shifting and distributing risk of loss does not necessarily mean the agreement constitutes an insurance contract for purposes of statutory regulation. See id.

insurance policies as some type of asset that can be employed to offset pending financial disaster.[7]

This article explores an avenue of available responses by an insured to their insurer's questioning or denial of coverage under a liability insurance policy. The following discussion closely examines *Miller-Shugart* settlements,[8] from the initial adoption of the concept, through the decision by the 8th Circuit Court of Appeals in *Corn Plus Cooperative v. Continental Casualty*.[9] In particular, the article explores what happens when a claim is settled by the policyholder which may be both covered and uncovered under the applicable policy. Perhaps even more succinctly stated, this article examines whose duty it is to allocate between covered and uncovered losses when a policyholder settles based on a *Miller-Shugart* settlement.

Much has taken place in refining the circumstances, timing, and consequences of what an insured can do under a *Miller-Shugart* settlement in the quarter century since the case was initially decided. Courts have now seemingly come full circle, from permitting a policyholder to stipulate to a judgment against himself to be covered by insurance when they think they have no coverage, to denying collection of a covered judgment - even after litigation establishing the policy covers certain of the claims being asserted.

Danny DeVito said it best when playing the part of Deck Shifflet in the film "The Rainmaker:"[10] "There's nothing better than sticking it to an insurance company."[11] Policyholders and their lawyers need to know in the *Miller-Shugart* context when "sticking it to [your] insurer" will be successful and when it will be a dismal failure.

## II. NUTS AND BOLTS

Liability insurance exists to provide financial protection for policyholders, principally in situations where financial liability exist to third parties. Common examples are automobile liability insurance policies and commercial general liability policies wherein the policyholder is granted protection from the financial consequences of an "accident." The words used to provide the grant of coverage, that is what risk(s) are being accepted by the insurer in exchange for the premium paid is crucial.[12]

Liability insurance typically follows an ancient format: a grant of coverage[13] at the beginning of the policy; which is followed by conditions the policyholder or claim must meet or the parties must follow;

[7] *See, e.g.*, Erik F. Gerding, Code, Crash, and Open Source: the Outsourcing of Financial Regulation to Risk Models and the Global Financial Crisis, 84 Wash L. Rev. 127 (2009) (mentioning the use of insurance as financial protection).

[8] *See supra* note 4.

[9] 516 F.3d 674 (8th Cir. 2008).

[10] The Rainmaker (Paramount Studios DVD 1997). This film is based on the novel of the same title: John Grisham, The Rainmaker (Doubleday ed., 1995).

[11] *Id.*

[12] *See generally*, Gen. Cas. Co. of Wis. v. Mid-Continent Agencies, Inc., 485 N.W.2d 147 (Minn. Ct. App. 1992).

[13] This is sometimes called the "insuring clause."

thereafter come exceptions to and exclusions from coverage.[14] Invariably, there are also definitions which address some, but not all, of the significant terms used in the policy.[15] Further details of what additional terms of coverage, or any other aspect of the policy, may be modified by endorsements.[16]

To the casual observer, the layout of an insurance policy, its syntax, and even its organization of concepts is at best Byzantine. An apt observation of liability insurance was once described in as: "An insurance policy is like old underwear. You don't discover the gaps in coverage until you've had an accident." Simply, understanding what is covered by an insurance policy is an exercise in fortitude, patience, and frequently frustration.

Insurers have tried for many years to standardize concepts and terms in broadly marketed policies.[17] The risks, which are the subject of liability coverage and how they arise, are as diverse as anything our society can face. It stands the test of reason that the documents which explain the insurer's obligation in response to the unknown events and circumstances are often, at best, diffuse expressions of undertaking. Nevertheless, it is the absence of clear understanding on the part of the insurer in making its own commitment as to what is covered, as well as the policyholder's trepidation that sow the seeds of potential controversy. When in doubt as to whether or not coverage exists, policyholders typically act rationally in taking steps to insulate themselves from the harsh consequences of a potentially uncovered loss.

Commonly, however, the seeds of controversy between a policyholder and its insurer are slow to germinate. Typically, coupled with an insurer's duty to pay the financial consequence of a transferred risk – to indemnify the policyholder from loss – there is also a duty to provide defense counsel.[18] It is axiomatic in the law of insurance that an insurer's duty to defend under a liability policy is interpreted more broadly than its duty to indemnify.[19] Thus, the controversial nature of whether a particular claim is or is not covered by the policy can lay dormant for a long time in situations where an insurer is actually defending.[20]

Moreover, the developments revealed through investigation and litigation of liability claims often provide the necessary context for an insurer's decision-making concerning whether or not a policy does or does not provide coverage for a particular loss.[21] There can be many genuine circumstances under which even the most thorough investigation and the hardest fought ligation in a defense of a liability claim will not neatly resolve whether the policy should respond to indemnify the insured for the financial consequences of that claim. Often there are no means of ascertaining what, if anything, about the liability claim being

[14] *See generally*, Minn. Mut. Fire & Cas. Ins. Co. v. Manderfeld, 482 N.W.2d 521 (Minn. Ct. App. 1992).

[15] *See id.*

[16] *See, e.g.*, Rabid Leasing, Inc. v. Nat'l Am. Ins. Co., 263 F.3d 820 (8th Cir. 2001).

[17] *See, e.g.*, ISO Line-of-Insurance Programs, http://www.iso.com/Products/Policy-Language-and-Rules/ISO-Line-of-Insurance-Programs-loss-costs-rules-policy-forms.html (last visited May 3, 2010).

[18] *See* Allan D. Windt, Representation of Insurance Companies & Insureds, 1 Insurance Claims and Disputes 5th § 4:1 (2010).

[19] *See, e.g.*, Cyprus Amax Minerals Co. v. Lexington Ins. Co., 74 P.3d 294 (Colo. 2003).

[20] *See id.*

[21] *See id.*

made will actually trigger coverage obligations from the insurer.[22] In these situations it is often necessary to test the insurance obligations against the known, established, or to be established, facts in litigation. This is often done through declaratory judgment actions in which a court is asked to declare the rights and obligations of parties pursuant to the insurance policy, a contract which is subject to the purview of state and federal declaratory judgment actions.[23]

There are other variables in the insurer/insured "Do I have coverage?" circumstance. On some occasions the claim being asserted is, on its face, one which the insurer rejects through an outright denial of coverage. Often, with latent injury situations there can be great difficulty in establishing when a covered loss, if any, took place. Timing may mean a great deal to the policyholder, and its liability insurers. Thus, litigation is required to determine if an insured's particular loss is covered based on how and when the loss happened.

Sometimes there is a middle ground where the insurer will defend under a "reservation of rights." Under a reservation of rights, the insurer notifies the policyholder why it thinks there is no coverage under the policy terms, and defines specifically which terms it feels may create the doubt as to whether or not coverage exists.[24] Nevertheless, the insurer will provide counsel to defend the claim.[25] The "reservation" is in the insurer's "right" to deny coverage if in the course of the investigation or defense circumstances arise that allow the insurer to deny all obligations under the policy.[26] The term "reservation of rights" has a particular meaning in the insurance milieu, and above all else is intended to allow an insurer to fulfill its promise to defend on an interim basis under its defense obligation within the policy while avoiding an estoppel that by so doing it owes indemnification for any loss.[27]

## III. CONTRACT PRINCIPLES

The law which predominates the field of insurance is that of contract. The transferred risk terms are articulated in the policy, which is binding between the issuer of the insurance and the policyholder.[28] Not only does this policy set forth duties and rules for the insurer to follow, but it also places duties on the insured.[29]

---

[22] "Trigger" is the shorthand used to describe the method by which the policy is activated. *See* N. States Power Co. v. Fid. & Cas. Co. of N.Y., 523 N.W.2d 657, 663 (Minn. 1994).

[23] *See* Minn. Stat. §§ 555.01-555.16 (2009) ("Declaratory Judgments Act"); see also 28 U.S.C. § 2201(a) (2009) ("Federal Declaratory Judgment Act").

[24] *See generally*, William T. Barker, Insurer Control of Defense: Reservations of Rights and Right to Independent Counsel, 71 Def. Couns. J. 16, 17 (2004).

[25] *See id.*

[26] *See id.*

[27] *See* Am. States Ins. Co. v. Ankrum, et al., 651 N.W.2d 513, 517 (Minn. Ct. App. 2002).

[28] *See* Harrington v. Agr. Ins. Co. of Watertown, N.Y., 229 N.W. 792, 793 (Minn. 1930).

[29] *Id.*

Typically, the duties of the policyholder after paying the premium are limited to cooperation with the insurer and to mitigate damages.[30] Examples of the former and latter are the most easily understood portions of most liability insurance policies, and incorporate concepts of cooperation, communication, preservation, and mitigation. To be clear, most liability insurance policies frown on or prohibit the type of conduct that is featured in this article; that is, confession or stipulation to a judgment in favor of the liability claimant against one's self to be covered by the insurer's policy. And this of course is exactly what was done by the policyholder in the *Miller-Shugart* case.

As was observed in the *Miller-Shugart* case:

"While the defendant insureds have a duty to cooperate with the insurer, they also have a right to protect themselves against plaintiff's claim. * * * If . . . the insureds are offered a settlement when their insurance coverage is in doubt, surely it cannot be said that is not in their best interest to accept the offer. Nor, do we think, can the insurer who is disputing coverage compel the insureds to forgo a settlement that is in their best interests."[31]

There is something of a pathway, albeit a narrow one, in which a policyholder can pass off its own liability to a claimant in exchange for the claimant having a direct challenge at the insurer and its reasons for balking at providing coverage.

The *Miller-Shugart* scenario plays out as follows: 1) some incident takes place which gives rise to a claim against a policyholder; 2) the policyholder provides notice to its insurer they want the insurer to handle the claim, usually invoking both the defense and indemnification duties under the policy; 3) the insurer questions or even denies the claim for reasons it explains; 4) the policyholder fearing personal liability – or at least uninsured exposure - makes a deal to settle the claim solely recoverable from the insurance coverage which arguably covers the claim; 5) the final paperwork allows the claimant to have a judgment against the policyholder collectible from the insurance coverage if it is established.[32] Notice of the pending *Miller-Shugart* style proposed settlement is typically communicated to the insurer.

Once a *Miller-Shugart* settlement is completed, litigation ensues to collect on the judgment. This is done through a garnishment proceeding, which gives the claimant a direct action against the insurer[33]– as the latter is holding property of the judgment debtor.[34]

The judgment, of course, has to be for a particular sum of money. The test of reasonableness of the judgment is applied to the amount agreed to between the policyholder and claimant.[35] However,

[30] *See generally*, Minn. Mining and Mfg. Co. v. Travelers Indem. Co., 457 N.W.2d 175, 179 (Minn. 1990).

[31] Miller v. Shugart, 316 N.W.2d 729, 733-34 (Minn. 1982).

[32] Britton D. Weimer, et al., Miller-Shugart Stipulations, 22 Minn. Prac., Insurance Law & Practice §3.6 (2009 ed.)

[33] *See* Gary Kilpatric, The Curious Case of Raskob v. Sanchez: Direct Actions Against Auto Insurers in New Mexico, ("The modern rule is that in the absence of a contractual or statutory provision allowing a direct action, an injured claimaint or plaintiff has no right to such an action against the insured for the tortfeasor. [According to Raskob v. Sanchez, 970 P.2d 580, (N.M. 1998)] a number of states have, however enacted direct action statutes, but most have limited their application by requiring that liability be found on the part of the insured before an action can be brought against an insurance carrier.)

[34] Miller-Shugart, 316 N.W.2d at 733-34.

[35] *Id.* at 735.

reasonableness in a *Miller-Shugart* setting may not be the result of hard bargaining. So long as there is some basis for the amount and it is not the product of fraud or collusion, if coverage is established, it is the amount the insurer will have to pay.[36]

It all comes down to whether or not insurance coverage exists. If so, and the stipulated judgment is not fraudulent or collusive, the insurer pays a claim which was never determined on its merits.[37] This operates as a consequence within the range of foreseeable outcomes for any insurer who denies or improperly limits coverage to its policyholder.[38] And while there is some debate in the case law as to whether a complete denial of coverage is required for the policyholder to be justified in reaching a *Miller-Shugart* settlement,[39] many cases including the original *Miller-Shugart* litigation did not begin as an outright denial of coverage. The case we most closely examine here, *Corn Plus Coop.*, involves a factual background wherein the insured was defended by its liability insurer under reservation of rights.[40]

The core principles underlying *Miller-Shugart* settlements[41] in these types of cases is to place the insurer at risk as to the consequences of its position concerning coverage. The *Miller-Shugart* court aptly noted: "Nevertheless, it seems to us, if a risk is to be borne, it is better to have the insurer who makes the decision to contest coverage bear the risk. Of course, the insurer escapes the risk if it should be successful on the coverage issue and, in that event, it is the plaintiff who loses."[42]

Historically, up until the time of the *Corn Plus* case, it was the insurer or claimant who paid the price for an incorrect determination of coverage. Since *Corn Plus*, an important element has been added to the insured's list of duties: allocation of settled losses among those which are covered and noncovered under the policy.[43] Failure to do so will render a *Miller-Shugart* agreement unenforceable – even if coverage has previously been established for some elements of the claimed loss against the policyholder.[44]

## IV. POLICYHOLDER'S BURDEN TO ALLOCATE

Keeping in mind the two circumstances under which allocation between covered and uncovered losses, *i.e.* when losses arise over a period of time (latency) or when losses are outside the scope of the policy regardless of when they arose, it remains the policyholder's burden to establish insurance coverage.[45] As was noted in *N. States Power Co. v. Fidelity & Cas. Co. of N. Y.*, "consistent with longstanding principles

---

[36] *Id.* at 734. Subject, of course, to policy limits and ignoring for these purposes the possibility of some type of bad faith or extra contractual liability claim. *See, e.g.* Minn. Stat. § 604.18 (bad faith statute).

[37] *See* Miller-Shugart, 316 N.W.2d at 733.

[38] *See id.*

[39] *See* Zurich Reinsurance (UK) Ltd. v. Canadian Pacific Ltd., 613 N.W.2d 760 (Minn. Ct. App. 2000).

[40] 516 F.3d 674 (8th Cir. 2008).

[41] Miller-Shugart settlements are recognized in many jurisdictions, albeit under different names.

[42] Miller-Shugart, 316 N.W.2d at 734.

[43] Corn Plus, 516 F.3d at 681.

[44] *See id.*

[45] *See id.* at 678.

of insurance law, the insured bears the burden of proving the policy was 'triggered' and therefore coverage is available."[46]

The temporal requirement of when the injury triggers the policy has been the subject of lengthy debate, largely beginning with coverage of asbestos claims.[47] Keene gave rise to the "all sums" approach, which allows the policyholder to select which insurer of many, over time, should pay for a particular loss.[48] *Forty-Eight Insulations* gave insurers a trigger theory that polices "pro rata by time on the risk" are triggered, which is a different form of allocation.[49] Neither theory of trigger provides certainty in all situations.

Minnesota follows an "actual injury" rule or "injury in fact" rule which requires an analysis of when the injury actually happened and triggers the policy in place at that time.[50]

While beyond the scope of this article, the determination of whether to allocate or not in latent injury situations is a formidable undertaking in itself.[51] Allocation of injury over time is likely the policyholder's burden, assuming it is required to determine which portion of a loss is covered in a Miller-Shugart setting. For reasons explained infra, the Corn Plus court made no distinction among the several reasons why allocation may be required.

Equally, and germane to this article are circumstances where multiple types of losses are the result of the insured's conduct. Even without a Miller-Shugart settlement, at some point, covered losses have to be distinguished from uncovered losses before the insurer responds. In this latter allocation setting, it is not focused on the timing of when the loss occurred, but rather the nature of the injury itself.[52]

Under the Corn Plus decision, and unlike the latent injury situations described above, there is no room for doubt who must do the allocating. The policyholder must, or it faces the loss of coverage for aspects of the claim even if insurance coverage has already been established.

## V. BUILDING A CASE

The factual setting for Corn Plus stems from the ever difficult insurance context of a construction project.[53] An entity named Wanzek contracted with Corn Plus in January of 2001 to perform mechanical work for an expansion project of Corn Plus' ethanol-production facility.[54] As often happens in these

[46] 523 N.W.2d 657, 663 (Minn. 1994).

[47] *See, e.g.*, Keene Corp. v. Insurance. Co. of North. America, 667 F.2d 1034 (D.C. Cir. 1981); Insurance Co. of N. Am. v. Forty-Eight Insulations, Inc., 633 F.2d 1212 (6th Cir. 1980).

[48] *See* Keene, 667 F.2d at 1047.

[49] 633 F.2d at 1225.

[50] Wooddale Builders v. Maryland Cas., 667 N.W.2d 405 (Minn. 2003).

[51] *See* Domtar Inc. v. Niagara Fire Ins. Co., 563 N.W.2d 724 (Minn. 1997)

[52] *See id.*

[53] 516 F.3d 674, 676 (8th Cir. 2008).

[54] *See id.*

circumstances, there was a serious back-and-forth dispute concerning quality of workmanship and timeliness of payments, resulting in Corn Plus withholding payments from Wanzek.[55] Wanzek's response was to file a mechanic's lien action for nearly $1.4 million.[56]

Eventually, in 2002, Corn Plus sued Wanzek in federal court.[57] Wanzek responded by filing a mechanic's lien foreclosure action in state court.[58] Ultimately, the parties agreed that it was the state court action that would be the vehicle for resolving the dispute over the quality of the building work performed by Wanzek, and related disputes under the contract.[59] The principal basis of the argument between Corn Plus and Wanzek was the quality of the welding work performed by Corn Plus in the maze of piping involved in the fuel plant expansion.[60] The nature of these allegations of defective work involved directly Wanzek's liability insurance policy's exclusions for "your work" and "impaired property."[61] There is little room for doubt that the trial court, when looking at these exclusions, had no difficulty in finding that Wanzek's liability insurance policy excluded from coverage the cost of repairing and replacing defective welds, including any loss production time during any plant repairs.[62]

Corn Plus' claimed damages were not limited to repairing or replacing the allegedly defective work of Wanzek.[63] The process of producing alcohol involves large-scale fermentation. Corn Plus was claiming that the defects arising from the poor and incomplete weldments performed by Wanzek resulted in the trapping of some of the residual material from fermentation and distilling, thereby creating a haven for bacteria to grow and multiply.[64] Whether or not the defective welds caused this bacterial growth, and its consequent economic impact on Corn Plus, including additional cleaning, shutdowns for cleaning, antibiotics to treat the bacteria, et cetera, were all hotly disputed.[65] Nevertheless, the trial court held, in determining summary judgment brought by Wanzek, that the liability insurance policies available to cover Wanzek did include coverage for "bacterial contamination of the corn mash used in Corn Plus' ethanol facility and those damages causally related to that contamination, which include increased antibiotic treatments, increased operational costs to disinfect the corn mash and clean pipes, and plant shutdowns necessary to change cooling lines and address centrifuge issues."[66] Consequently, the trial

---

[55] *See id.*

[56] *See id.*

[57] Corn Plus Coop. v. Continental Cas. Co., 444 F. Supp.2d 981, 984 (D. Minn. 2006)

[58] *See id.*

[59] *See id.*

[60] *See id.* at 983.

[61] *See* Corn Plus, 516 F.3d at 678-79.

[62] *See* Corn Plus Coop., 444 F.Supp.2d at 984.

[63] See id. at 992 (concluding that the policy provides "coverage for the bacterial contamination of the corn mash used in Corn Plus's ethanol facility and those damages causally related to that contamination").

[64] *See id.* at 983.

[65] *See id.* at 990; *see also* Corn Plus, 516 F.3d at 679.

[66] *See* Corn Plus Coop., 444 F.Supp.2d at 992.

court made it abundantly clear that some elements of Corn Plus' claimed damage were covered by the liability insurance policies available to Wanzek to protect against such claims.[67]

It should be noted that Wanzek's primary insurance company, Continental, did hire defense counsel to represent Wanzek and defend against these claims.[68] The parties were initially unsuccessfully in mediating these claims in June of 2003.[69] By December 2003, the parties discussed and proposed a Miller-Shugart settlement in the amount of $2.5 million.[70] In March of 2004 Wanzek and Corn Plus executed a Miller-Shugart settlement agreement for the same amount.[71] In this settlement agreement, Wanzek stipulated to a judgment that based upon an admission that its negligence resulted in a $2.5 million loss in Corn Plus' fermentation and ethanol facility.[72] Corn Plus paid Wanzek just under $400,000 to resolve their mechanic's lien claims.[73] Importantly, there were at least seven separate categories of damages that had been claimed by Corn Plus resulting out of Wanzek's work including: loss of production during weld repair; cost to repair welds; radiography and quality control for weld repairs; liquidated contract damages; attorneys' fees and costs; estimated losses for subsidy payments that would be missed while repairs were underway; and antibiotics and agents to control infections.[74]

While the alleged total damages were over $7,600,000, no effort was ever made by Wanzek or Corn Plus to determine which of these damages were caused by Wanzek's allegedly defective welds.[75] Nor, did the record ever reflect that there was any proof that the welds contributed to much of the damages claimed.[76] Wanzek was concerned however that even if there would not be any proof associated with the defective welds and the increased production costs in terms of damages, that if the welds were established as defective under the contract, that is not meeting a contract specification, that it could still be held liable and under such circumstances would likely not have any insurance coverage available to it.[77]

The final and recognized unusual feature of the Miller-Shugart settlement was a provision that indicated that were the Court to reject the reasonableness of the $2.5 million settlement stipulated to by the parties that the Court could determine on a summary basis "the largest fair and reasonable settlement amount" if it was not $2.5 million.[78] Additionally, the Miller-Shugart settlement agreement indicated that the settlement would be final even if any portion of the settlement agreement was found invalid, illegal, or

---

[67] *See id.* at 992.

[68] *See* Corn Plus, 516 F.3d at 677.

[69] *See id.*

[70] *See id.* Corn Plus made a $2.5 million cash settlement offer, but Wanzek ultimately rejected it. Wanzek countered with a proposed Miller-Shugart agreement in the same amount.

[71] *See id.*

[72] *See id.*

[73] *See id.*

[74] *See* Corn Plus Coop., 444 F. Supp.2d at 992.

[75] *See* Corn Plus Coop. v. Continental Cas. Co, No. 04 Civ. 4270, 2007 WL 107676, at *3 (D. Minn. Jan. 9, 2007).

[76] *See id.*

[77] *See id.*

[78] *See id.* at 4.

unenforceable.[79]

It was the failure to allocate damages for the portion of the settlement that was purportedly covered, combined with the indefinite nature of the settlement amount that gave the 8th Circuit Court the opportunity to affirm two central principles.[80] One, that allocation between covered and uncovered losses is mandated in stipulated judgment situations entered into by policyholders; and, two, it is unreasonable as a matter of law for a policyholder to stipulate to a judgment recoverable from insurance proceeds amounts which the policyholder itself failed to indicate the source of the claimed damage.[81]

Under Minnesota law, the burdens imposed by the initial Miller-Shugart case that notice be provided, that the settlement not be the product of fraud or collusion, and the settlement is reasonable and prudent are all burdens to be borne by the parties seeking enforcement of the Miller-Shugart agreement.[82] The question of reasonableness is determined based upon factors known to the parties at the time of the settlement.[83]

In its arguments to the 8th Circuit, Corn Plus was contending that existing case law which required allocation in Miller-Shugart situations when multiple defendants were present, did not apply to this situation.[84] The rule in Bob Useldinger & Sons v. Hangsleben, 505 N.W.2d 323, 331 (Minn. 1993), was urged to be distinguishable from the facts before the Court in Corn Plus.[85] The thrust of their argument was the compelling circumstances when multiple defendants are present requiring allocation do not exist when there is a single defendant such as Wanzek in this case.[86] The 8th Circuit rejected this argument with dispatch, "that distinction is unpersuasive and contrary to precedent, under which the failure to allocate the settlement amount by damage items precludes enforcement of a Miller-Shugart agreement consisting of covered and noncovered claims."[87] The Court cited other Minnesota law which had historically required allocation in other situations involving insurance coverage, including Ebenezer Society v. Dryvit Systems, Inc., 453 N.W.2d 545 (Minn. Court App. 1990).[88] And the 8th Circuit further referenced, "the requirement in Bob Useldinger & Sons that an insured allocate damages among multiple defendants applies with equally compelling logic to the allocation of damage items in cases of a single defendant. Absent such allocation, a judicial determination into the reasonableness of the Miller-Shugart settlement is impractical since the parties are naturally in a better position to calculate the damages. Moreover, parties would also be tempted to inflate their covered claims post hoc if they were permitted to designate a settlement amount without damage allocation."[89] The Court of Appeals thus agreed with the trial court

---

[79] *See id.*

[80] Corn Plus, 516 F.3d at 682.

[81] *See id.*

[82] *See* Miller-Shugart, 316 N.W.2d at 735.

[83] *See* Jorgenson v. Knutson, 662 N.W.2d 893, 904-05 (Minn. 2003)

[84] Corn Plus, 516 F.3d at 682.

[85] *See id.*

[86] *See id.*

[87] *See id.*

[88] *See id.*

[89] *See id.*

that absent an allocation between covered and noncovered items, the Miller-Shugart agreement is unreasonable as a matter of law.[90]

Corn Plus' fallback position was pursuant to its settlement terms, leaving room for the court to be the final determiner of what constituted reasonable damages for covered claims. Thus, Corn Plus sought to avoid the consequences of a settlement being found unreasonable.[91] In Alton M. Johnson Co,[92] the court held that when a settlement is found unreasonable, the parties are returned to the underlying litigation. The 8th Circuit rejected this novel settlement approach, insisting that the unusual nature of Miller-Shugart warrants policy consideration different than the usual rule from traditional settlements.[93] The reasoning is that a Miller-Shugart settlement will impose an amount upon a nonparticipant. The liability insurer does not have a voice in determining the amount of the settlement. Consequently, and in partial reliance on Koehnen v. Herald Fire Ins. Co., 529 (8th Cir. 1996), the Court found that the public policy in Alton M. Johnson was sufficient to thwart the proposed contract term which imposed the burden on the court to allocate between covered and uncovered claims.

## VI. CONCLUSION

There was a time when parties to a dispute could easily shift responsibility for paying a partially uncovered claim to their insurer. In those halcyon days, all it took was a willingness on the part of the claimant to accept an amount—usually a large one—for a claim that came close to the available coverage. Thereafter it was a contest between the claimant and insurer to resolve solely reasonableness of the amount, freedom from collusion of the settlement, and whether the policy had to respond to the loss. The simplicity in the former road to recovery now has a pothole in it of immense magnitude—the duty to determine and allocate between covered and uncovered losses. This is not merely a dip in the road; it can swallow up the entire settlement.

Counsel are cautioned that the relative ease of past Miller Shugart settlements should be replaced with circumspection whenever there is the potential for any portion of the loss to be outside the coverage of applicable insurance. As appealing as it may be to accept a large settlement and have only to litigate with an insurer to collect, Corn Plus tells us allocation between covered and uncovered portions of the claim is an essential prerequisite to enforcement of a Miller Shugart settlement agreement.

---

[90] *Id.*

[91] Alton M. Johnson Co. v. M.A.I. Co., 463 N.W.2d 277, 280 (Minn. 1990).

[92] *Id.*

[93] *See* Corn Plus, 516 F.3d at 679.