DIVISION ONE
FILED: 11/08/2011
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BY: DLL

IN THE COURT OF APPEALS
STATE OF ARIZONA
DIVISION ONE

LENNAR CORPORATION, a Delaware corporation; LENNAR HOMES OF ARIZONA, INC., an Arizona corporation; and LENNAR COMMUNITIES DEVELOPMENT, INC., a Delaware corporation, Appellants, v. TRANSAMERICA INSURANCE COMPANY (now known as TIG Insurance Company); UNITED STATES FIDELITY & GUARANTY COMPANY; and UNITED STATES FIRE INSURANCE COMPANY, Appellees.	No. 1 CA-CV 10-0686 DEPARTMENT B **MEMORANDUM DECISION** (Not for Publication - Rule 28, Arizona Rules of Civil Appellate Procedure)

Appeal from the Superior Court in Maricopa County

Cause No. CV2000-018645

The Honorable Robert A. Budoff, Judge (Retired)

AFFIRMED

Fennemore Craig, P.C. Phoenix
By Timothy Berg
John J. Balitis, Jr.
Theresa Dwyer-Federhar
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Co-Counsel for Appellants

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By Thomas P. Burke, II
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By Terrence P. Woods
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Attorneys for Appellee United States Fire Insurance Company

S W A N N, Judge

¶1 In this construction defect case, the developer's insurer accepted a tender of defense more than two years after the case began. Though the developer had already retained defense counsel at its own expense in the interim, the insurer offered to provide a defense through substitute counsel. The developer elected to accept representation by substitute counsel, and also chose to continue to be represented by its original counsel. When the developer sought to have the insurer pay for the services of both counsel, the insurer refused. On summary judgment, the superior court held that the insurer was

not obliged to pay for both sets of lawyers. We agree, and therefore affirm.

FACTS AND PROCEDURAL HISTORY[†1]

¶2 Beginning in fall 1998, the insureds, Lennar Corporation, Lennar Homes of Arizona, Inc., and Lennar Communities Development, Inc. (collectively "Lennar") were sued by homeowners in the Pinnacle Hill development on a variety of construction defect-related claims. Lennar tendered the claims to its insurers, including the appellees in the present appeal, TransAmerica Insurance Company, United States Fidelity & Guaranty Company and United States Fire Insurance Company (collectively "the Insurers").

¶3 During the initial phase of the litigation with the homeowners in late 1998, Lennar retained John Balitis with Fennemore Craig ("Fennemore") as defense counsel. In January 2001, Gerling American ("Gerling") -- one of Lennar's other insurers -- accepted the tender of the homeowner claims and agreed to participate in Lennar's defense subject to a reservation of rights. In April 2001, Gerling sought to retain

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[†] The panel has found it appropriate to amend the caption, and the parties are directed to use the above caption on all future documents filed in this appeal.

[1] We view the evidence in the light most favorable to the party against whom summary judgment was entered and resolve all inferences from the evidence in that party's favor. *Prince v. City of Apache Junction*, 185 Ariz. 43, 45, 912 P.2d 47, 49 (App. 1996).

Jill Herman with Lorber, Greenfield & Polito ("Lorber") to represent Lennar in the suit and to terminate payment of any subsequent fees charged by Fennemore in Lennar's defense.

¶4 By letter dated June 12, 2001, Herman informed Lennar that she was "ready, willing and able" to defend it in the lawsuits. Lennar responded by asserting that Gerling was obliged to continue to pay Fennemore's fees and costs, because Balitis served as a necessary "independent counsel" in view of a conflict of interest created by Gerling's reservation of rights. Lennar then proposed that Herman participate as "co-counsel-of-record" such that Balitis and Herman would "each play a significant and active role in Lennar's defense." Lennar further detailed that the workload would be divided between the firms to minimize duplicative efforts, Herman would maintain Lennar's confidences regarding coverage defenses, Herman would report to Lennar and Lennar would control the defense, and both firms' fees and all case costs and fees would be paid by Gerling.

¶5 Gerling refused the bulk of Lennar's proposal, arguing that no conflict of interest existed and agreeing only to allow Herman and Balitis to act as co-counsel-of-record. Gerling acknowledged that it would "fully and completely defend Lennar" and that continued retention of Balitis would be at Lennar's own expense, but it would pay all of Herman's fees. Lennar then

demanded that Balitis act as lead counsel and noted that its consent to allow Herman to participate in the case would not serve as a waiver of any rights related to later reimbursement of Fennemore's fees by Gerling.

¶6 Gerling held to its position that it had the authority to control Lennar's defense, that Herman should share equally in all decision-making and workload, and that all fees associated with Lennar's continuation of Fennemore's services would be Lennar's responsibility. It further asserted that "anything less [than agreement to these terms] is a breach of the cooperation clause." Lennar agreed to the role that Gerling wanted Herman to play, but continued to assert that it was not waiving its rights to seek payment for Fennemore's fees at a later date.

¶7 Gerling instructed Herman to disregard any coverage issues and proceed with Lennar's defense. It agreed to defer the question of Fennemore's fees subject to a series of conditions including: a requirement that all primary carriers be involved in any judicial determination regarding responsibility for those fees; upon a judicial determination that Lennar was entitled to reimbursement of Fennemore's fees, any remaining issues would be submitted to binding arbitration; Gerling retained rights to assert coverage defenses and it would only pay Balitis, if at all, at the rate it paid Herman. Lennar

rejected these conditions and reasserted that it simply wished for Gerling to recognize that "by allowing Ms. Herman to participate in Lennar's defense, Lennar is not waiving any right it otherwise has to recover" Fennemore's fees. Lorber filed a notice of association of counsel on September 17, 2001.

¶8 In 2000, the Insurers brought a declaratory judgment action against Lennar to determine the extent of their coverage obligations. On January 25, 2010, insurers Fidelity & Guaranty Insurance Company ("FGIC") and Fidelity & Guaranty Insurance Underwriters, Inc. ("FGIU") moved for partial summary judgment on the issue of Lennar's ability to recover Fennemore's fees incurred after September 17, 2001. FGIC and FGIU argued that Lennar was not entitled to reimbursement for Fennemore's fees accrued from Herman's retention in 2001 until the last settlement in October 2003, because Lennar was provided a full defense by Gerling through Herman and because no conflict of interest existed that would create a necessity for independent counsel. The appellees in the present appeal joined in the motion on February 26, 2010, but disputed Fennemore's fees from April 2001 rather than September 2001.[2]

¶9 Lennar argued in response that Gerling did not provide a full defense because Fennemore continued to play a "critical

[2] FGIC and FGIU settled their claims with Lennar following the summary judgment ruling and have been dismissed from this appeal.

and necessary role in Lennar's defense" and that it was entitled to maintain Fennemore as independent counsel. Lennar argued that in the face of the two "untenable options" of firing Fennemore and taking Lorber or refusing Lorber and continuing with Fennemore, it chose the "viable" third option of receiving a "partial" defense from Lorber and the remainder of its defense from Fennemore -- all to be paid by its insurers.

¶10 The trial court found that the Insurers were entitled to judgment as a matter of law on the ground that the fees incurred by Lennar's "continuing representation by its chosen law firm of Fennemore Craig were not reasonable and necessary" given the defense provided by Lorber. The court allowed Lennar Fennemore's fees up to September 17, 2001 -- rather than the April 2001 date argued by the Insurers -- because those fees were "reasonable and necessary" for Fennemore to get Herman "up to speed" with the Pinnacle Hill suits.

¶11 Lennar timely appeals. We have jurisdiction pursuant to A.R.S. § 12-2101(B).

STANDARD OF REVIEW

¶12 Summary judgment should be granted "if the facts produced in support of the claim or defense have so little probative value, given the quantum of evidence required, that reasonable people could not agree with the conclusion advanced by the proponent of the claim or defense." *Orme Sch. v. Reeves*,

166 Ariz. 301, 309, 802 P.2d 1000, 1008 (1990). In reviewing a grant of summary judgment, we determine de novo whether any genuine issues of material fact exist and whether the trial court properly applied the law. *Eller Media Co. v. City of Tucson*, 198 Ariz. 127, 130, ¶ 4, 7 P.3d 136, 139 (App. 2000).

DISCUSSION

¶13 There is no longer any dispute that Lennar was entitled to a defense from its insurers in the Pinnacle Hill litigation; however, it is also clear that it was not entitled to co-defense counsel at the Insurers' expense. Because we find that the trial court properly applied the law, we affirm.

I. FENNEMORE ACTED AS CO-COUNSEL, NOT INDEPENDENT COUNSEL, AND THAT ROLE WAS NOT JUSTIFIED BY ANY POTENTIAL CONFLICT OF INTEREST BETWEEN THE INSURED AND ITS INSURERS.

¶14 A law firm retained by an insurer to defend an insured owes its loyalty and agency solely to the insured. *Parsons v. Cont'l Nat'l Am. Grp.*, 113 Ariz. 223, 227-28, 550 P.2d 94, 98-99 (1976). "[W]hen a conflict actually arises, and not simply when it potentially exists, the lawyer's duty is exclusively owed to the insured and not the insurer." *Paradigm Ins. Co. v. Langerman Law Offices, P.A.*, 200 Ariz. 146, 150, ¶ 16, 24 P.3d 593, 597 (2001) (citations omitted).

¶15 By citing *Fulton v. Woodford*, 26 Ariz. App. 17, 545 P.2d 979 (1976), Lennar starts down the correct path to understanding when it might be permissible to have counsel-of-

choice in a conflict of interest situation, but its argument takes an unwarranted step beyond the holding of that case. *Fulton* acknowledged that a conflict of interest "obviously" exists when, as here, an attorney employed by an insurer to defend an insured does so under a reservation of rights, but the court went on to hold that the insured can give informed consent to the continued representation by the attorney that the insurer provides. *Id.* at 20, 545 P.2d at 982. The case does not stand for the proposition that the availability of representation with informed consent implies an entitlement to *multiple* defense firms at the insurer's expense.

¶16 *Joseph v. Markovitz*, 27 Ariz. App. 122, 127, 551 P.2d 571, 576 (1976) is also distinguishable. There, the insurer insured both sides of a case and the insurance contract allowed it to control the defense of each side. On public policy grounds, this court held that despite the insurer's specific waiver of control over the defense, the conflict demanded that the insured be allowed to refuse the insurer's demanded counsel and choose his own attorney to be paid by the insurer. *Id.* at 127-28, 551 P.2d at 576-77. But even in *Markovitz,* the insured did not get to employ *both* his counsel of choice and insurer's chosen counsel at the insurer's expense.

¶17 Here, Gerling did not insure both Lennar and the Pinnacle Hill plaintiffs -- or even the subcontractors allegedly

at fault -- and Gerling had no authority to control the defense of any other party in the litigation. There is no suggestion in the record that Herman was acting in any manner as an agent of Gerling or the insurers collectively. Nor is there any evidence that Herman was "captive counsel" or that Lorber was a "captive firm." Herman was specifically directed by Gerling to disregard any issues or facts related to coverage, and there is no evidence that she faced conflicting loyalties.

¶18 The only ground for the argument that a conflict existed was Gerling's reservation of rights upon agreeing to defend Lennar. But even if the reservation of rights gave rise to a conflict between Gerling and Lennar, such a conflict would not justify the role that Fennemore actually played in Lennar's defense.

¶19 Given the potential for conflict that existed between Gerling and Lennar because of the reservation of rights, Lennar could reasonably have reshaped Fennemore's role to that of an independent guardian of its rights concerning coverage. But Lennar chose instead to have two lead defense attorneys equally participating in the decision-making and workload. Because such an arrangement was not justified by a conflict of interest -- actual or potential -- we find no legal authority upon which Lennar was entitled to reimbursement for Fennemore's continued service as co-counsel after it accepted Lorber's representation.

¶20 We held in *Edler v. Edler,* 9 Ariz. App. 140, 449 P.2d 977 (1969), that "when an insurance company elects not to defend and the assured then retains counsel and defends himself, the assured may then *reject* the belated offer of the insurance company to re-enter and participate in the defense of the law suit." *Id.* at 142-43, 449 P.2d at 979-80 (emphasis added) (citation omitted). In *Manny v. Estate of Anderson*, 117 Ariz. 548, 549-50, 574 P.2d 36, 37-38 (App. 1977), we applied the same principle in a circumstance where the insurer *never* indicated it was willing to defend and a default judgment was entered against the insured. And we acknowledged the right to reject again in *McGough v. Insurance Co. of North America,* 143 Ariz. 26, 33-34, 691 P.2d 738, 745-46 (App. 1984), but held that where an insurer twice refused to defend and then offered to continue on retainer the attorney who had been representing the insureds, the insureds had no right to refuse the insurer's offer.

¶21 These cases teach that an insured has the right to *reject* its insurer's choice of counsel and maintain its own under certain circumstances. But these cases do not stand for the proposition that an insured has the right to *accept* -- partially or fully -- insurer's choice of counsel in the role of co-counsel with the insured's choice of counsel.

¶22 In further support of the contention that it was entitled to continue with Fennemore after Gerling retained

Lorber, Lennar argues that Gerling never fully defended it because Herman's work was only part of the joint defense provided by the Lorber and Fennemore firms. The problem with this argument is that Lennar never allowed Lorber to provide a full defense because it insisted that Balitis and Herman act as co-counsel. There is nothing in the record to suggest that Lorber was not willing and able to handle the entire representation on its own.

¶23 In fact, Lennar conceded at oral argument that Gerling offered to provide and pay for a full defense either by Lorber or by Fennemore at Lorber's rate. Lennar further disclaimed any effort to seek -- in the alternative to all of Fennemore's fees -- an amount equal to Fennemore's hours billed at Lorber's rate. Lennar has taken an "all or nothing" approach to this litigation, and we approach our decision accordingly.

¶24 We note, too, that we see no impediment to the present appellees' adoption of Gerling's position. Lennar was entitled to one full defense in satisfaction of the one indivisible duty all of its insurers had to defend. The duty to defend Lennar was satisfied once Gerling offered a full defense; at that point, any claims that Lennar may have had against its other insurers for defense costs became Gerling's claim.

¶25 Had Lennar asserted that Gerling's late acknowledgement of its duty to defend constituted breach of that

duty and seasonably insisted that Fennemore continue as sole defense counsel, it would have a more powerful argument that Gerling (and therefore the other insurers who failed to acknowledge the duty to defend) had forfeited choice of counsel by the delay. But even if it had successfully retained Fennemore as its sole defense counsel, Lennar still would not have had a claim against other insurers for their dilatory responses to the tender -- the other insurers' intransigence would have resulted in an obligation for higher defense costs (the Fennemore rate compared to the Lorber rate). In that event, Gerling, not Lennar, would have been the proper party to seek contribution. Because we find that no issues of material fact exist and the trial court properly applied the law, we affirm.

CONCLUSION

¶26 For the foregoing reasons, we affirm the grant of summary judgment in favor of the Insurers.

/s/
_____
PETER B. SWANN, Judge

CONCURRING:

/s/
_____
MARGARET H. DOWNIE, Presiding Judge

/s/
_____
DONN KESSLER, Judge