STATE OF NORTH CAROLINA
COUNTY OF WAKE

IN THE GENERAL COURT OF JUSTICE
SUPERIOR COURT DIVISION
19 CVS 02793

MURPHY-BROWN, LLC and SMITHFIELD FOODS, INC.,

Plaintiffs,

v.

ACE AMERICAN INSURANCE COMPANY; et al.,

Defendants.

ORDER ON PRE-TRIAL ISSUES

1. **THIS MATTER** is before the Court on the parties' Joint Statement of Legal Issues to be Decided Prior to Trial ("Pre-Trial Issues List," ECF No. 771). In preparation for trial, the parties have jointly asked the Court to resolve certain disputed legal issues, which are fully discussed below.

FACTUAL AND PROCEDURAL BACKGROUND

2. This lawsuit was originally filed on 5 March 2019. (Compl., ECF No. 4.)

3. The broader factual and procedural background of this case—which is quite extensive—is discussed in great detail in a series of prior opinions from this Court. *See Murphy-Brown, LLC v. Ace Am. Ins. Co.*, 2023 NCBC LEXIS 93 (N.C. Super. Ct. Aug. 7, 2023); *Murphy-Brown, LLC v. Ace Am. Ins. Co.*, 2023 NCBC LEXIS 94 (N.C. Super. Ct. Aug. 7, 2023); *Murphy-Brown, LLC v. Ace Am. Ins. Co.*, 2023 NCBC LEXIS 96 (N.C. Super. Ct. Aug. 7, 2023).

4. As the Court's prior opinions in this case discuss in detail, Plaintiffs originally sued various insurers who provided them with primary and excess

insurance coverage for their eastern North Carolina-based farming operations between 2010 and 2015.[1] *See Murphy-Brown, LLC*, 2023 NCBC LEXIS 93, at **3–4. In a nutshell, Plaintiffs contended in their Second Amended Complaint ("SAC")—which was filed on 12 January 2021, (*see* ECF No. 453, at 3), and is currently their operative pleading—that these insurers were obligated to indemnify Plaintiffs for amounts paid to settle certain underlying nuisance actions filed by property owners living near Plaintiffs' hog farms (the "Underlying Lawsuits") and to reimburse Plaintiffs for the attorneys' fees expended by them in defending the Underlying Lawsuits (the "Defense Costs"). (SAC ¶¶ 73–121.)

5. On 4 March 2024, at the Court's direction, the parties filed a Pre-Trial Issues List, (ECF No. 771), which identified a number of factual issues that the parties agreed would require resolution by a jury. In addition, the parties listed eleven legal issues (the "Pre-Trial Issues") as to which they requested a ruling from the Court prior to trial.

6. These Pre-Trial Issues essentially fell under one of two categories: (1) Plaintiffs' request for indemnity from American Guarantee & Liability Insurance Company ("Zurich") for the amounts they paid to settle the Underlying Lawsuits; and (2) Plaintiffs' demand for reimbursement of the defense costs they incurred in defending the Underlying Lawsuits from ACE American Insurance Company ("ACE").

[1] Since this action was filed, several of these insurers have been dismissed from the case after entering into settlements with Plaintiffs.

7. On 3 May 2024 and 31 May 2024, the parties filed briefs setting forth their respective positions on the various Pre-Trial Issues. (*See* ECF Nos. 777–79, 785–89, 790–92.)

8. On 14 August 2024, the Court held a hearing on the Pre-Trial Issues.

9. The parties notified the Court on 21 August 2024 that a settlement with Zurich had been reached, thereby resolving the indemnity issues in this case.

10. Therefore, the only claim that currently remains for trial involves Plaintiffs' request for reimbursement by ACE for the Defense Costs Plaintiffs incurred in defending the Underlying Lawsuits.

11. Between 2020 and 2023, the Court entered several opinions on a range of motions for summary judgment filed by the parties involving issues that are now largely irrelevant to the sole issue that remains for trial. Having said that, however, three of the Court's specific rulings in those opinions are relevant to that remaining issue.

12. First, on 22 December 2020, the Court ruled that the refusal of ACE and another one of Plaintiffs' insurers, Old Republic Insurance Company ("ORIC"), to defend Plaintiffs in the Underlying Lawsuits constituted "a breach of their respective duties to defend." *Murphy-Brown, LLC v. Ace Am. Ins. Co.*, 2020 NCBC LEXIS 154, at **54 (N.C. Super. Ct. Dec. 22, 2020).[2] Second, on 5 August 2022, the Court held that ACE was "estopped from asserting coverage defenses contained in its Auto

[2] Plaintiffs subsequently entered into a settlement with ORIC on 30 September 2021, resulting in ORIC's dismissal from this action. (ECF No. 780.5.)

Policy." *See Murphy-Brown, LLC*, 2023 NCBC LEXIS 96, at **12 (cleaned up). Third, on 7 August 2023, the Court ruled that at trial ACE would be permitted to "challeng[e] the reasonableness of Plaintiffs' defense costs incurred in defending the Underlying Lawsuits[.]" *Id.* at **21.[3]

13. Of the Pre-Trial Issues briefed by the parties, the only ones that require resolution following Plaintiffs' settlement with Zurich are the following: (1) which party bears the burden of proving the reasonableness of Plaintiffs' Defense Costs in the Underlying Lawsuits; (2) whether ACE's right to contest the reasonableness of Plaintiffs' Defense Costs includes a right to conduct a "line-by-line" challenge to the billing entries of Plaintiffs' attorneys in the Underlying Lawsuits; and (3) whether the jury may be informed of the Court's prior determination that ACE breached its duty to defend Plaintiffs in the Underlying Lawsuits.[4]

ANALYSIS

I. Burden of Proving Reasonableness of Plaintiffs' Defense Costs

14. The parties disagree over whether Plaintiffs or ACE should bear the burden at trial of proving the reasonableness of the Defense Costs for which Plaintiffs seek reimbursement.

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[3] However, the Court did not rule at that time on the issue of which party would have the burden of proving the reasonableness of those fees. *See Murphy-Brown, LLC*, 2023 NCBC LEXIS 96, at **15 n.7.

[4] One other issue briefed by the parties remains relevant. That issue concerns whether, or to what extent, ACE is entitled to a credit against the portion of ORIC's settlement amount that is properly apportioned to ORIC's liability for Plaintiffs' Defense Costs. However, the Court concludes that this issue cannot be decided until such time as the jury has issued a verdict in this case as to the total amount of Defense Costs for which ACE is liable. Accordingly, the Court will not address this issue herein.

15. Plaintiffs argue that their defense costs should be afforded a presumption of reasonableness in light of ACE's prior breach of its contractual duty to defend Plaintiffs in the Underlying Lawsuits.

16. ACE, conversely, contends that (1) the burden of proving the reasonableness of attorneys' fees rests with the party seeking them; and (2) North Carolina law does not allow for a presumption of reasonableness as to attorneys' fees.

17. As noted above, the Court has already ruled that ACE's "failure to provide a defense [in the Underlying Lawsuits] constitutes a breach of [its duty] to defend[,]" *Murphy-Brown, LLC*, 2020 NCBC LEXIS 154, at **54, and that "ACE is estopped from asserting coverage defenses in its Auto Policy." *Murphy-Brown, LLC*, 2023 NCBC LEXIS 96, at **11.

18. It is clear under North Carolina law that an insured can recover its reasonable defense costs from its insurer who has breached its contractual duty to defend. *See*, *e.g.*, *Jamestown Mut. Ins. Co. v. Nationwide Mut. Ins. Co.*, 277 N.C. 216, 219 (1970) ("It is well settled that an insurer who wrongfully refuses to defend a suit against its insured is liable to the insured for sums expended in payment or settlement of the claim, for reasonable attorneys' fees, for other expenses of defending the suit, for court costs, and for other expenses incurred because of the refusal of the insurer to defend."); *W.I. Anderson & Co. v. Am. Mut. Liab. Ins. Co.*, 211 N.C. 23, 26–27 (1936) ("The failure of the defendant [insurance company] to defend the suit, after repudiating its liability to the assured, constituted a distinct breach of contract and justified the plaintiff in defending it at his own expense. These costs and expenses

constitute a primary liability of defendant that plaintiff may recover as damages for the breach of the contract." (cleaned up)).

19. Although as a general proposition a party seeking attorneys' fees has the burden of proving that the fees sought are reasonable, neither the parties' briefs nor the Court's own research has disclosed any case law from our appellate courts discussing which party has the burden of proving the reasonableness of the attorneys' fees in question where the issue is being submitted to a jury following a court's ruling that the insurer has breached its duty to defend its insured and is estopped from asserting coverage defenses.

20. In the absence of controlling case law from our appellate courts on an issue of North Carolina law, this Court is permitted to consider relevant decisions from other jurisdictions. *See Carolina Power & Light Co. v. Emp't Sec. Comm'n of N.C.*, 363 N.C. 562, 569 (2009).

21. Based upon the Court's review of cases from across the nation on this issue, it appears that a clear majority of courts have held that, in this context, the defense costs incurred by the insured in defending the underlying claim are presumed to be reasonable. *See, e.g.*, *Stryker Corp. v. XL Ins. Am. Inc.*, No. 4:01-CV-157, 2008 U.S. Dist. LEXIS 656, at *10 (W.D. Mich. Jan. 4, 2008) ("[A]s a consequence of Defendant's decision not to defend Plaintiffs in the underlying lawsuits[,] the settlements and defense costs for the underlying lawsuits are presumed reasonable."); *State v. Pac. Indem. Co.*, 63 Cal. App. 4th 1535, 1548–49, 75 Cal. Rptr. 2d 69 (1998) ("[I]n the exceptional case, wherein the insurer has breached its duty to

defend, it is the insured that must carry the burden of proof on the existence and amount of the expenses, which are then presumed to be reasonable and necessary as defense costs, and it is the insurer that must carry the burden of proof that they are in fact unreasonable or unnecessary." (cleaned up)); *Thomson Inc. v. Ins. Co. of N. Am.*, 11 N.E.3d 982, 1023–24 (Ind. Ct. App. 2014) (agreeing with the proposition that "when an insurer has breached the duty to defend, and the policyholder has secured, supervised, and paid for a defense without any expectation of payment, those costs are 'market tested' and are presumed to be 'reasonable and necessary' "); *Jaynes Corp. v. Am. Safety Indem. Co.*, No. 2:10-cv-00764-MMD-GWF, 2014 U.S. Dist. LEXIS 58821, at *2 (D. Nev. Apr. 25, 2014) ("When the insurer has breached its duty to defend, the insured carries the burden of proof regarding the existence and the amount of the expense. Once that burden is met, the expenses are presumed to be reasonable and necessary and it is the insurer that then carries the burden of proof to demonstrate that they are actually unreasonable and unnecessary."); *Siltronic Corp. v. Emp'rs Ins. Co.*, No. 3:11-cv-1493-YY, 2016 U.S. Dist. LEXIS 184414, at *14 n.7 (D. Ore. Nov. 14, 2016) ("Where the insurer breaches its duty to defend, however, the insured must only carry the burden of proof on the existence and amount of the expenses, which are then presumed to be reasonable and necessary as defense costs, and the insurer has the burden to prove that they are unreasonable or unnecessary." (cleaned up)); *Value Wholesale, Inc. v. KB Ins. Co.*, No. 18-cv-5887(KAM)(SMG), 2020 U.S. Dist. LEXIS 203659, at *15 (E.D.N.Y. Nov. 2, 2020) ("Where an insurer has breached its duty to defend, the insured's fees are presumed to be reasonable and the

burden shifts to the insurer to establish that the fees are unreasonable." (cleaned up)); *Am. Serv. Ins. Co. v. China Ocean Shipping Co. (Ams.) Inc.*, 2014 IL App (1st) 121895, ¶ 27, 7 N.E.3d 161, 379 Ill. Dec. 735 (2014) (agreeing with the approach treating "attorneys[’] fees paid by the insured as presumptively reasonable" when an insurer breaches its duty to defend "because an insured has a financial incentive to ensure that the attorney fees it pays are reasonable when it is uncertain whether those fees will be reimbursed by the insurer"); *see also* 14 Couch on Insurance § 205:76.

22. After careful consideration, the Court finds this approach to be well-reasoned and not inconsistent with North Carolina law.

23. Given that Plaintiffs incurred the Defense Costs at issue upon ACE's stated refusal to participate in the defense of the Underlying Lawsuits and with no assurance that a court would ever require ACE to reimburse Plaintiffs for these costs, it is eminently logical to shift the burden of proving reasonableness to ACE once Plaintiffs have offered evidence of their payment of the defense costs. Such a result is not only equitable but also serves as a deterrent to insurers from wrongfully breaching their defense obligations.

24. Therefore, at trial, Plaintiffs shall have the initial burden of showing that they incurred and paid the Defense Costs at issue with regard to the Underlying Lawsuits. Once Plaintiffs make such a showing, their Defense Costs will thereafter be presumed to be reasonable at which point ACE will have the burden of rebutting that presumption.

II. "Line-by-Line" Challenge to Plaintiffs' Legal Fees

25. Next, the parties dispute whether, in the course of seeking to show at trial that Plaintiffs' defense costs were not reasonable, ACE should be permitted to conduct a "line-by-line" challenge to the time entries of Plaintiffs' attorneys with regard to their bills in the Underlying Lawsuits.

26. Plaintiffs argue that the volume of information at issue—over 5,000 pages of time entries—necessitates a more generalized presentation of evidence that is consistent with the factors for assessing the reasonableness of attorney's fees set forth under Rule 1.5 of the North Carolina Rules of Professional Conduct. Moreover, Plaintiffs suggest that allowing ACE to conduct a line-by-line critique of Plaintiffs' defense costs at trial would "undermine the duty to defend by providing insurers the comfort of knowing they can retrospectively nitpick defense costs even if they wrongfully breached their duty to defend." (Pls.' Br. Addressing Legal Issues to be Decided Prior to Trial Pertaining to Pls.' Claims for Reimbursement Def. Costs, at 18, ECF No. 779.)

27. ACE, conversely, argues that a ruling in favor of Plaintiffs on this issue would significantly diminish its ability to conduct a meaningful challenge to the Defense Costs at issue.

28. "The reasonableness of attorneys' fees in this State is governed by the factors found in Rule 1.5 of the Revised Rules of Professional Conduct of the North Carolina State Bar." *Bradshaw v. Maiden*, 2018 NCBC LEXIS 98, at *11 (N.C. Super.

Ct. Sept. 20, 2018) (quoting *Ehrenhaus v. Baker*, 216 N.C. App. 59, 96 (2011)) (cleaned up).

29. Rule 1.5 states, in relevant part, as follows:

> (a) A lawyer shall not make an agreement for, charge, or collect an illegal or clearly excessive fee or charge or collect a clearly excessive amount for expenses. The factors to be considered in determining whether a fee is clearly excessive include the following:
>
> > (1) the time and labor required, the novelty and difficulty of the questions involved, and the skill requisite to perform the legal service properly;
> >
> > (2) the likelihood, if apparent to the client, that the acceptance of the particular employment will preclude other employment by the lawyer;
> >
> > (3) the fee customarily charged in the locality for similar legal services;
> >
> > (4) the amount involved and the results obtained;
> >
> > (5) the time limitations imposed by the client or by the circumstances;
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> > (6) the nature and length of the professional relationship with the client;
> >
> > (7) the experience, reputation, and ability of the lawyer or lawyers performing the services; and
> >
> > (8) whether the fee is fixed or contingent.

N.C. R. Prof'l Conduct 1.5(a).

30. The Court finds that ACE should not be restricted from attempting to challenge the reasonableness of Plaintiffs' Defense Costs in the manner advocated by Plaintiffs. Given that the Court has already ruled that ACE has a right to challenge the reasonableness of these costs, ACE should be permitted to exercise that right as

it sees fit so long as it is not doing so in a manner inconsistent with Rule 1.5, which Plaintiffs have not shown.

31. Moreover, the Court notes that in assessing the reasonableness of attorneys' fees in other contexts North Carolina courts routinely consider issues such as block billing, excessive hourly rates, lack of sufficient detail in billing entries, over-staffing, and improper designation of clerical tasks as legal tasks. *See*, *e.g.*, *Vitaform, Inc. v. Aeroflow, Inc.,* 2024 NCBC LEXIS 21, at *11 (N.C. Super. Ct. Feb. 5, 2024) ("Plaintiff's complaint about Defendants' block-billing, however, has merit. Many of Defendants' time entries aggregate multiple tasks without providing the hours expended for each separate task."); *Bradshaw*, 2018 NCBC LEXIS 98, at *12–13 (analyzing the reasonableness of attorneys' hourly rates); *Bone v. Univ. of N.C. Health Care Sys.*, No. 1:18CV994, 2024 U.S. Dist. LEXIS 40667, at *51 (M.D.N.C. Mar. 8, 2024) ("That Plaintiffs chose to staff the case with eleven timekeepers should not require UNCHCS to pay for such duplication."); *Ford v. Jurgens*, 2022 NCBC LEXIS 59, at *14 (N.C. Super. Ct. June 15, 2022) ("The precise boundary between legal tasks and clerical ones may be debated, but there is indeed a line between such tasks. Other courts have recognized that many clerical tasks should be subsumed in a law firm's overhead, rather than billed even at a firm's rate for paralegal work, because the most basic of clerical tasks—filing, transcription, and document organization—are part of the cost of doing business." (cleaned up)).

32. For these reasons, Plaintiffs have failed to persuade the Court—at least at this pre-trial stage of the litigation—that ACE should be restricted in this fashion,

and ACE shall be permitted at trial to challenge the reasonableness of the billing records at issue consistent with Rule 1.5.

III. Whether the Jury May be Told that ACE Breached its Duty to Defend

33. Finally, the parties dispute whether the jury should be informed of ACE's prior breach of its duty to defend Plaintiffs in the Underlying Lawsuits.

34. Plaintiffs argue that such information should be provided to the jury because it is relevant, provides context about the procedural history of this lawsuit, and is not prejudicial enough to outweigh any potential probative value.

35. Defendants, conversely, contend that this information is not relevant to the issues at trial and that it is likely to have a prejudicial effect that would substantially outweigh any probative value it possesses.

36. North Carolina Rule of Evidence 402 states that, unless specifically barred, "[a]ll relevant evidence is admissible[.]" N.C. R. Evid. 402. Irrelevant evidence, on the other hand, is always inadmissible. *Id.* Evidence is considered relevant if it has "any tendency to make the existence of any fact that is of consequence to the determination of [an] action more probable or less probable[.]" N.C. R. Evid. 401. Thus, trial judges are given "great freedom to admit evidence . . . if it has *any* logical tendency to prove any fact that is of consequence." *State v. Wallace*, 104 N.C. App. 498, 502 (1991) (cleaned up).

37. That said, relevant evidence "may be excluded if its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues,

or misleading the jury, or by considerations of undue delay, waste of time, or needless presentation of cumulative evidence." N.C. R. Evid. 403.

38. Here, the Court is unable to agree with ACE that this evidence lacks any relevance. The Court's prior ruling on this issue is not a disputed assertion, but rather, a key event in the background of this case. The value of allowing the jury to be made aware of this information is so that the jurors will understand that they are not being asked to decide the threshold issue of whether ACE actually owed Plaintiffs a defense in the Underlying Lawsuits and are instead only being tasked with deciding the extent to which the Defense Costs incurred by Plaintiffs were *reasonable*.

39. Although North Carolina's appellate courts have not yet had occasion to address this issue, courts in other jurisdictions have allowed such evidence to be presented at trial in analogous contexts. For instance, the Southern District of New York addressed a similar issue as follows:

> The Court's prior rulings, including its ruling on Aristocrat's breach of the Indenture, are probative of the present procedural posture of the case, which the jury will need to be aware of to understand why it is being asked only to determine whether the Bondholders unreasonably failed to mitigate their consequential damages. While many of the issues addressed in the Court's prior rulings--including the Court's rulings on the securities fraud claims and the amount of general damages . . . are not probative of the issues for trial, the Court declines, at this early time, to issue a blanket prohibition against mentioning all of its rulings at trial. Therefore, Aristocrat's in limine request to preclude argument or evidence of the Court's prior rulings, other than in a statement of background facts to be read to the jury, is denied.
>
> To mitigate any prejudice to Aristocrat, the Court directs the parties to refrain from using pejorative terms in describing the Court's prior rulings. Aristocrat asks the Court to preclude references to the Court's prior ruling that Aristocrat "breached the Indenture." The term "breached the Indenture" and variations of this phrase, such as "breach

> of contract," are factual references to the Court's prior ruling. Unlike other terms that this Circuit has found to be prejudicial, the term "breach" or "breach of contract/Indenture" is not pejorative, inflammatory, or prejudicial on its face, and will not be precluded in describing the Court's prior rulings.

Aristocrat Leisure Ltd. v. Deutsche Bank Tr. Co. Ams., No. 04 Civ. 10014 (PKL), 2009 U.S. Dist. LEXIS 89183, at *30–32 (S.D.N.Y. Sept. 28, 2009) (cleaned up).

40. A federal court in South Carolina applied similar reasoning.

> KIU argues that it would be unduly prejudiced by Mears presenting evidence of its damages before KIU has the opportunity to present its case of faulty workmanship. That prejudice, KIU argues, would arise from the court instructing the jury at the outset that KIU has been found to have breached the contract with Mears, and such an instruction would paint KIU as the wrongdoer at the start of the case. KIU contends that this prejudice can be avoided by first determining whether Mears engaged in faulty workmanship, which does not require mention of the parties' contract or KIU's breach.
>
> The problem with this argument is that the court has found that KIU is the wrongdoer because the court found that KIU has breached the contract. That fact is not a prejudicial suggestion. It is the posture of this case.

Mears Grp., Inc. v. Kiawah Island Util., Inc., No. 2:17-cv-02418-DCN, 2020 U.S. Dist. LEXIS 2231, at *5 (D.S.C. Jan. 7, 2020).

41. Here, the Court likewise concludes that the jury may be informed of the fact that ACE breached its duty to defend Plaintiffs in the Underlying Lawsuits. However, Plaintiffs shall be precluded from making any pejorative or inflammatory comments about that breach. The Court is satisfied that this limitation (along with appropriately tailored jury instructions) will be sufficient to prevent ACE from suffering any undue prejudice.

CONCLUSION

THEREFORE, **THE COURT** hereby **ORDERS** as follows:

a. At trial, Plaintiffs shall have the initial burden of showing that they incurred and paid the Defense Costs at issue with regard to the Underlying Lawsuits. Once Plaintiffs make such a showing, the Defense Costs will be presumed reasonable, and ACE shall then have the opportunity to offer evidence rebutting that presumption.

b. At trial, ACE shall be permitted to challenge the reasonableness of Plaintiffs' defense costs in accordance with the factors set out in Rule 1.5 of the North Carolina Rules of Professional Conduct as set forth above.

c. At trial, the jury will be permitted to learn that ACE breached its duty to defend Plaintiffs in the Underlying Lawsuits. However, Plaintiffs shall be prohibited from making any pejorative or inflammatory comments about ACE's breach.

SO ORDERED, this the 25th day of September, 2024.

/s/ Mark A. Davis
Mark A. Davis
Special Superior Court Judge
for Complex Business Cases