Lowenstein Sandler's Insurance Recovery Podcast:
Don't Take No For An Answer

Episode 65

Finding the Right Fit: The Duty to Defend vs. the Duty to Reimburse (Part II)

By Lynda Bennett, Eric Jesse

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Lynda Bennett: Welcome to Don't Take No For An Answer. I'm your host, Lynda Bennett, and I'm pleased to be joined today by my co-host and partner extraordinaire, Eric Jesse, welcome back, Eric.

Eric Jesse: All right. Hi, Lynda. Always good to be here.

Lynda Bennett: So we're going to be picking up our conversation. Remember last time we were talking about the difference between the duty to defend, the duty to reimburse, the duty to advance, and we kind of went through some of the nuts and bolts of how courts interpret that and what the policy language says. So today I really want us to get practical. Let's do a day in the life of Lynda and Eric and the issues that arise when we have these sticky defense issues that come up. So I'll reset the table. I mentioned this during episode one of this conversation. The complaint comes in, it's got 10 counts. One or two of them are potentially covered under the policy, and we've submitted it to the insurance company and let's take it in each scenario. So if I've got a duty to defend policy, what as a practical matter is going to happen?

Eric Jesse: Right. So in that situation, you have a duty to defend policy. The insurance company, again, depending on state law, but they should be acknowledging the defense for the entire lawsuit is one covered cause of action or potentially covered cause of action is sufficient to trigger the duty to defend. And then the insurance company is going to appoint defense counsel to represent the insured. And that's what typically happened in a duty to defend setting.

Lynda Bennett: Let's flip the script. Now, same complaint to potentially covered claims, and I've got a duty to reimburse or a duty to advance policy. What happens next?

Eric Jesse: Yeah, so here the carrier should again acknowledge a defense obligation, but this is where things can get a little bit more difficult. The insurance company

might try to allocate defense costs. You as the policy holder, may want to appoint your own defense counsel and have the insurance company pay 100% of that attorney's hourly rates. The insurance companies may be pushing back on that, so it gets a little bit more sticky in that situation.

Lynda Bennett: Yeah, and it's interesting too. We talked last time about allocation provisions that preset how much the insurance company is going to pay. And in some policies that we've reviewed as you know Eric, sometimes the policy holder will be given the choice, it will say the insurance company will defend if you "tender that claim" to the insurance company.

And one of the carrots that may be in that policy is the carrier says, "And if you tender it to us, then we will pay 100% for that mixed claim where there's some covered claims and some not covered claims, or policy holder you will have the option to not tender the claim, defend it yourself, but then we're going to be assessing what is the potentially covered claim proportionally in relation to all of the other uncovered claims or uncovered parties." And that's when we really start to enter the wonderful world of allocation and negotiation. So Eric, let's walk through that. So now I've got a coverage position letter from a carrier where I've got a duty to reimburse or duty to advance language in the policy. I've got two potentially covered claims out of 10, and the carrier has told me, "Okay, we'll be paying 20% of your bills and any eroding your $500,000 retention at a 20% rate." Am I stuck or is there something else I can do?

Eric Jesse: Yeah, so I think that typically there is more you can do the language they're often relying on. And the policy to make that type of argument is that the parties will use their best efforts to allocate based on the financial interest associated or financial exposure associated with each of the causes of action. So when you have that situation, one thing you can do, and again, it depends on state law, but if you're in a state that applies the larger settlement rule, which can also apply to defense costs in many states one thing you can try to do is go back to the carrier and say, "Hold on one second, just because the efforts that our attorneys are undertaking benefit both those two covered causes of action as well as the other eight causes of action."

So for example, when defense counsel is appearing at a deposition, right, they are defending the entire lawsuit the insurance companies should be paying for the total cost of the deposition. So this is a rule that allows policyholders to say, an attorney's effort benefits an uncovered and covered aspect of the claim the insurance company has to pay 100%.

Lynda Bennett: And that's super important. And actually, I want to go back because you talked about the policy language that says in that mixed claim scenario, well, we'll use our best efforts and as we know on, don't take no for an answer, we talk about it all the time, the words of the policy language matter. So in some of these policies it will say, "and by the way, tie goes to the insurance company." In other words, we'll use best efforts. And if we have different definitions for what best efforts is or what the right allocation is, we the insurance company have the sole final vote on how much we're going to pay. And then some of those policies even go a step further and say, "And when we disagree, we'll see an arbitration, a panel of three arbitrators where we're

sharing the cost for that," which of course all of that is designed to force the policy holder into taking whatever the insurance company deems to give them on the allocation. And so Eric, what do we do when we see that policy language as a quick best practice for our listeners?

Eric Jesse: That needs to go obviously. And again, this is the importance of you don't ask, you don't receive. This is one where go work through your broker and you ask the insurer to remove that language, they often will, and you hit on why it's so important because that language is designed to make sure policyholders don't exercise their rights because the defense obligation is so favorable that you can potentially go into court the day after the lawsuit is filed or the day after the insurer tries to not honor their obligations to get the carrier to step up. So that access to court early in a coverage dispute is very valuable for a policy holder.

Lynda Bennett: Right. And it shouldn't cost you a binding arbitration to get the answer and to get the coverage that you're entitled to on defense. I always take every opportunity to say, read your policy in advance and have that negotiation in advance because it's a very unhappy surprise for many of our clients after they've been presented with a claim. And then we get the question, why in the world did I buy this policy? All I bought was the right to sue my carrier and spend a lot of money to get the coverage I thought I was going to have in the first instance.

Let's come back to my example. So now let's stick with a duty to reimburse duty to advanced policy. We've had the fight over what the appropriate allocations is going to be, and then the carrier says, "Okay, so we'll agree to pay 60%. We accept your argument on overlapping costs, and so we will very graciously agree to pay 60%. By the way, the panel rates that we use for our lawyers are $200 for a partner, $75 for an associate, and $15 for a paralegal." And I'm only slightly exaggerating there. What happens with that, is the carrier allowed to further start to nip and cut and chop at the value of this defense coverage?

Eric Jesse: Yeah. In that situation, the carriers seem to treat every case, whether it's a bet the company case, like a dog bite case, and that's why they're proposing those ridiculously low hourly rates. And in that scenario, again, go back to the policy language because it's going to talk about reasonable defense costs that the insurance company needs to pay. And if you have a lawyer who charges more, those costs can still be reasonable. And there's case law if you're out the country, that requires an insurance company to actually step up and pay those higher rates. So there are arguments to try and get the insurance company above the $200 an hour for partners or associates.

Lynda Bennett: Great advice there. Now Eric, we've run through the gauntlet. We've got the complainant; we've got the carrier acknowledging their defense obligation. We've worked through the allocation issue; we've worked through the hourly rate issue. But by the way, every one of those steps of the way the insurer is telling us this whole case is about the uncovered portion of the lawsuit that's been filed against the policy holder. So we are begrudgingly stepping up, defending the case, but we want to be clear as a bell to you, there's not going to be any indemnity coverage here because the only reason we're stepping

up is because you've identified a potentially covered claim, but this potentially covered claim is not the driver for what the real relief is that's being sought in the lawsuits that's been filed. So now we're sitting at the mediation and the insurance company has said, "Oh yeah, I'm not coming. All I'm in for is paying for the cost of my defense lawyer at that 60% rate that we negotiated. That's it. My work here is done." Is the carrier right in that scenario?

Eric Jesse: Probably not. Right. First of all, carriers are going to say that so often, especially when they think they're on the hook for just one or two causes of action. So their knee jerk reaction is the liability exposures for the uncovered claims. So part of this is just an education process and informing or updating the insurance company about why there's potential exposure associated with the potentially covered claims. That's step one. The other thing is having your defense counsel prepare a budget because if they want to take that position, then there's another angle to try and press with the insurance company, which is, well then this settlement, you need to view it as a cost of defense because here is the amount of money that you're going to have to pay defense counsel to take this case through trial or re-trial, and that's a reason why you need to step up on the indemnity front.

Lynda Bennett: Absolutely. That's the pitch that I make, which is you are going to receive a benefit when the defense meter gets turned off. So not only is it a good idea, it's a requirement because by settling the case, there will be a cost savings that the insurer gets for the defense obligation they've acknowledged and they clearly have. So there has to be a settlement value assigned to that as well.

Eric Jesse: And Lynda, that's the real value of going through every step of this process and doing it early on. So pressing the insurer to acknowledge their defense obligation, negotiating the rates, negotiating the allocation, because this scenario at the mediation we just discussed doesn't necessarily happen if the policyholder has let the insurance company sit on the sidelines. So that's the importance of getting the carrier involved in the defense as soon as possible.

Lynda Bennett: Yep. So I think that we've made the point, and many of our clients know the defense obligation in a policy is really core to why you buy liability insurance coverage. But I think we've also laid bare that it can be very difficult to actually reap the benefit of that coverage. That's not to say don't try, because we do know the ins and outs of how to get that carrier to step up and pay, but as we always say on don't take no for an answer, the words matter, the jurisdiction and law that's going to be applied to those words matter as does persistence in getting what you paid for under your policy. So don't take no for an answer, right, Eric?

Eric Jesse: Exactly. It's why it's the name of our podcast.

Lynda Bennett: All right, well, that's a wrap for today. We look forward to seeing everybody on the next episode.

Eric Jesse: All right, take care.

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