Insurance 101 for Litigators: Minimizing Risk and Maximizing Recovery

Kristen E. Hudson – May 25, 2017

Your client has been sued, and you have been hired as its counsel. Congratulations! Now what? Litigation is an inherently unpredictable and expensive endeavor for any individual or entity. If your client is sued, the second thing to do, after you have instructed your client to issue a litigation hold, is to ask about insurance coverage and any possible indemnification agreements. Coverage often can be lurking in not-so-obvious places. Here is what you need to know to help your client navigate this tricky area.

Identify All Potentially Applicable Insurance Policies and Indemnification Agreements
Find copies of all potentially applicable insurance policies. If this is not possible, instruct the client to ask its broker or agent to help it identify and locate such policies. Time is of the essence in getting notice to any insurers.

Different types of policies provide different types of protection for different types of claims. Often a claim or a loss can be covered under multiple policies. For example, in a suit alleging both personal injury and economic harm, there may be coverage under the client's commercial general liability policy, its directors' and officers' liability policy, and possibly other policies. Because of this overlap, it is important to give notice to all insurers where there is a potential for coverage.

In addition, a variety of contracts may provide indemnification for certain injuries or for claims arising out of the contracting party's relationship with your client. Indemnification provisions are common in leases and service agreements, for example. These agreements may require the contracting party to add your client as an additional insured on the party's insurance policy. Consider such contracts in identifying all potentially applicable insurance policies.

Give Notice as Soon as Possible
Once you have identified any applicable indemnification agreements and insurance policies, tender the defense under applicable indemnity agreements and give notice under all insurance policies that might potentially be triggered. Notice is an important step in securing insurance coverage. Depending on the type of policy, notice can also be a condition precedent to coverage. With a few strategic exceptions, the best advice is to give notice early. There is rarely any downside to doing so. When you give notice, it will be impossible to know the future extent of the loss or liability; so, if the policies allow, give notice to all primary and excess carriers. If

you do this all at once, there will be no question that notice was timely, should the loss or liability exhaust the limits available under the primary policy.

While a lawsuit and a loss are obvious examples of when you must notify the insurance carrier, other events that also trigger notice requirements under the policy may be less obvious. These additional circumstances could include a call, email, or letter to your client demanding money, services, or that your client refrain from engaging in some activity; a subpoena; a civil investigative demand; or a request for an agreement to toll the statute of limitations.

Understand the Key Obligations under the Policies

Most liability policies contain two key promises: (1) the duty to defend (or the duty to reimburse defense costs), and (2) the duty to indemnify for any settlements and judgments.

The duty to indemnify is narrow, and an insurer is not required to indemnify the insured for any claims that are not covered.

The duty to defend, on the other hand, is broader than the duty to indemnify. In many jurisdictions, if a complaint alleges a claim that triggers the defense obligations under the policy, the insurer must defend against all of the claims alleged, even if some of the claims would not be eligible for indemnity. This is typically true under most commercial general liability policies. Some jurisdictions and some insurance policies, however, allow insurers to pay only for the defense of claims that are covered under the policy. And some policies allow the insurance company to recoup from the insured any defense costs paid for claims that are ultimately determined not to be covered. It is important to note these provisions for your client, so the client will not be surprised if the insurer asserts these positions.

Know the Defense Obligations under Insurance Policies

It is important to know the distinctions between various defense obligations, which can differ depending on the policy. In a typical commercial general liability policy—which covers claims for bodily injury, property damage, and personal injury—the duty to defend is outside of the limits of the insurance policy. This means that the insurer has dollar one defense obligations (along with the right to control the defense). And those defense costs do not erode the limits of the policy, which remain available to pay settlements and judgments.

To defend claims that fall under these policies, insurers typically turn to a stable of preapproved lawyers, at preapproved rates. The good news for your client is that, minus any applicable deductible, it will not have to pay any defense costs. The bad news is that if you are not one of the preapproved lawyers or law firms, the insurer may be able to insist that the case be defended by another lawyer.

Other policies may provide for reimbursement of defense costs. Typically, "claims made" policies—that is, policies that respond to claims made and reported during the policy period—may provide for reimbursement of defense costs. Rather than dollar one defense coverage, however, these policies typically have a self-insured retention that must be satisfied before the insurance company is required to begin reimbursing or paying for defense costs. Under "claims made" policies, defense costs typically erode the amount available under the policy to pay for judgments or settlements. Often these policies also have requirements that the insured must use insurer-approved counsel.

Know the Indemnification Obligations

Not every settlement offer will obligate the insurance company to settle. Insurers are obligated to settle only covered claims, and they must act reasonably in good faith in doing so. If an insurance company fails to act in good faith or fails to settle a claim within the policy limits, an insurer may risk being held liable for any judgment that exceeds the policy limits.

Understand the Circumstances That Require the Insurer's Consent

The insurer has a right to consent in advance to defense counsel and their rates. The policy may also require the insurer's consent to certain other payments. A failure to get the insurer's consent in advance could result in a loss of coverage for those payments. Understanding these requirements at the outset will save your client time and money later.

Carefully Read and Understand Reservation of Rights Letters and Denials of Coverage

Make sure you understand the terms and conditions of any reservation of rights or denial of coverage letter issued to your client. Certain reservations trigger additional duties on the part of the insurer. For example, if the reservation of rights letter creates a conflict of interest between the insured and the insurer, the insured may have the right to select independent counsel. Reservation of rights letters may also contain reservations regarding recoupment of defense costs and allocation of any indemnity payments. It is important to understand what these are and how they may impact the litigation.

Understand the Privilege Rules That Apply in an Insurance Context

The law surrounding the protection of counsel's communications with the insurance company varies by jurisdiction, and it may depend on whether the parties are aligned, or whether the insurer has reserved its rights. It is important to understand this law at the beginning of a case. Insurance policies require the insured to cooperate and share information with the insurance company. It is important that the insured be free to do so without the threat of those communications being discovered.

Conclusion

Insurance is an important asset for individuals and businesses; it protects the company from loss and liability. It is important to understand how to maximize protection and recovery from this important asset. A failure to recognize when insurance is implicated, or a failure to follow the terms of the policy, can result in a forfeiture of millions of dollars. Sound legal advice in this area can save your client time and money.

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