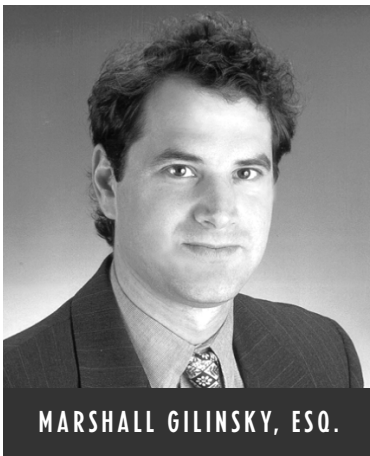


## When The Hand That Feeds You Makes A Fist: Policyholders Confront The London Market's Asbestos Documentation Requirements



In June, 2001, a block of underwriters at Lloyd's and companies in the London Insurance Market (the "London Market Insurers") unilaterally implemented extensive, and unprecedented, Documentation Requirements (the "DRs") for asbestos-related claims. The DRs have serious implications for policyholders. Because the DRs often place policyholders between a rock and a hard place, some policyholders now find themselves fighting not only a continuing tide of asbestos claimants, but the insurance companies who pledged to help defend against such claimants.

### A. The Attempted Imposition of the DRs

According to correspondence generally

directed to U.S. policyholders in February, 2001, the London Market Insurers sought to implement the DRs to specify the basis on which they would determine (on a prospective basis) whether asbestos-related claims are covered under their policies (assuming the terms and conditions of the actual policies are met) and whether underlying coverage is property exhausted. The requirements introduced in this correspondence are extremely broad, and seek to require that policyholders provide the London Market Insurers with extensive medical reports and sworn statements for each claimant, in order to secure coverage under policies that included no such claims requirements.

The introduction of the DRs left many general counsel and risk managers shaking their heads and asking questions: "Don't the *policies* set forth whether claims are covered? Can my insurance company unilaterally impose *new* requirements for coverage?"

### B. Problems with the DRs as a Matter of Insurance Law

There is good reason to question the enforceability of the DRs. First, since they are presented as new preconditions to coverage under existing policies, the DRs

can be construed as unilaterally imposed contractual terms, inserted without the consent of the policyholder. Unilaterally imposed contractual terms generally do not meet the basic requirements of a contract, and are unenforceable.

Second, the attempt to impose such requirements may constitute bad faith claims handling. The covenant of good faith and fair dealing obligates all insurance companies to refrain from taking any action which would deprive their policyholders of the benefits of the insurance contract, or to cause undue hardship or harm to their policyholders. Because it is extremely difficult, if not impossible, for many policyholders to satisfy the DRs given the exigencies of asbestos litigation in many jurisdictions, the DRs may cause many policyholders severe prejudice, including lost benefits of insurance coverage.

For example, it currently is not uncommon for a policyholder to be given an opportunity to settle a group of asbestos cases, some of which involve substantial risks of adverse results and set for trial within a month. The policyholder is told by the claimants' attorney that it can either settle the entire group of claims, some of which might not meet the DRs,

or go to trial on the risky cases. If the policyholder chooses to go to trial and loses, a substantial amount of indemnity coverage will be consumed. Moreover, if the policies at issue provide defense coverage in addition to policy limits, the policyholder's lost coverage is far greater, since coverage is exhausted quickly by large judgments, whereas settlement for a much smaller amount preserves valuable (and unlimited) coverage for defense costs. Thus, the imposition of the DRs creates a conflict of interest between the London Market Insurers and their policyholders, one that has the practical effect of depriving policyholders of the benefits of their insurance.

### **C. Problems with the DRs as a Matter of Reinsurance Law**

The DRs also are being imposed by the London Market Insurers in the reinsurance context, thus requiring ceding insurance companies to meet the requirements in order to access proceeds under reinsurance agreements purchased from the London Market Insurers. In addition to the issues noted above regarding unilaterally imposed contractual terms, the imposition of the DRs in the reinsurance context also may run afoul of the "follow the fortunes" doctrine, which requires a reinsurer to use the utmost good faith in accepting the claims determinations made by the ceding insurance company.

### **D. Policyholders Confront the DRs**

In the time since they were introduced, some policyholders have already begun to

fight the DRs in court. Numerous cases are pending in various jurisdictions that relate in whole or in part to the DRs. These cases generally involve claims for breach of contract, and some also include allegations of bad faith. In at least two such cases, motions by the London Market Insurers to dismiss the bad faith causes of action have been denied.

Because reinsurance agreements generally include arbitration provisions, little information is available regarding the number of ceding companies that formally opposed the attempted imposition of the DRs. At least one ceding company has filed suit; and many more are likely to be disputing the DRs within the confidential constructs of arbitration proceedings.

### **E. What is at Stake**

The resolution of disputes relating to the DRs can have a very significant impact on the amount of coverage ultimately available to a policyholder, especially where the policies at issue provide for defense coverage in addition to policy limits. Where claims of bad faith are involved, the possibility of a punitive damages award against the London Market Insurers obviously raises the stakes.

Of course, central to any dispute over the DRs is a policyholder's ability to control the management of its asbestos-related litigation. In-house and outside defense counsel depend on certain amounts of flexibility in order to effectuate the strategies that best protect the company and its assets. Especially given

the current state of affairs in asbestos litigation, the ability to maintain maximum flexibility in defending and resolving claims is of the utmost importance. Through the DRs, the London Market Insurers have sought to seize control of its policyholders' underlying asbestos claims. Some policyholders are fighting back.

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