

Counsel's Role In Insurance Risk Management

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Insurance policies are complex contracts, and pursuit of an insurance claim is often a high-stakes, conflict-ridden endeavor. Yet all too many companies entrust their assets and their very survival to insurance policies that are never seen by their attorneys, and pursue claims without the benefit of counsel's evaluation of the company's contractual rights. In-house counsel have an important role to play both when insurance is obtained and when claims are pursued.

Counsel Should Analyze Insurance Policies Before Coverage Is Bound

Before coverage is bound, counsel should analyze the contracts being offered with the company's major liability and loss exposures in mind. Insurance policies for businesses are typically complex, lengthy contracts written in arcane language, with many exclusions that take away much of the coverage that is otherwise afforded. Many of the key provisions found in standard form policies have been interpreted by the courts and are best understood in light of that case law.

An attorney's review of the company's insurance policies is not as daunting a

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task as it might first appear, at least after going through the exercise once. Most policies consist largely of standard forms, many of which remain largely unchanged from year to year. The insurance broker can be asked to identify all changes in coverage. Moreover, excess policies often "follow form" to primary policies. So, reviewing higher-layer policies in a tower of insurance is typically far less involved than gaining an understanding of primary policies. However, care must be taken to ensure, if possible, that excess policies do not have less advantageous terms, and that if they do, any policies at higher levels do not follow form to them.

The grants of coverage and exclusions that are most important vary from industry to industry, and company to company. They should be apparent to in-house counsel who are familiar with the types of claims that have been asserted against the company and the assets that need protection.

Choice of Law and Arbitration Provisions

Many commercial insurance policies contain problematic choice-of-law provisions. The insurance companies' favorite choice is New York law, which is worse for policyholders than the laws of most other states in certain respects. For example, under New York law, in most instances there is no cause of action available to corporations for insurance company bad faith.

Some clauses not only designate the law of a state preferred by the insurance company, but also go further and modify the rules of evidence and of insurance policy interpretation to be applied under



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that state's law. Often such clauses take away from policyholders the valuable advantages they receive under legal rules of insurance policy interpretation, such as the resolution of ambiguities in favor of coverage. These provisions should be removed if at all possible.

The policyholder may be able to control the method of dispute resolution by focusing on that issue at the time coverage is procured. This issue is often ignored by risk managers and brokers, who focus their attention upon terms and pricing. Counsel should carefully weigh the advantages and disadvantages of litigation vs. arbitration and review any arbitration provision in policies under consideration.

Policyholders receive at least two potential benefits from resolving their coverage disputes through litigation instead of arbitration. First, all courts in the U.S. apply rules of insurance policy interpretation that are favorable in some respects to policyholders as the party that did not draft the contract. Most notably, insurance policy coverage granting provisions are to be construed broadly while exclusions are to be viewed narrowly, and ambiguities are to be resolved in favor of coverage. These rules are applied in some arbitrations, but their use is specifically prohibited under certain arbitration clauses, and in general arbitrators are granted broad latitude under the law to depart from a strict application of legal precedent. Second, litigation affords a policyholder the opportunity to present its case to a jury. Since insurance companies are generally held in low esteem by jurors, the prospect of a jury trial may provide the policyholder with leverage in settlement negotiations.

Manuscript Provisions

Many insurance policies contain both standard forms and "manuscript" provisions drafted for a particular policyholder.

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Counsel should be involved in the negotiation of “manuscript” provisions for two reasons. First, care must be taken to ensure that such provisions clearly reflect the agreement of the parties, because if a dispute arises over their meaning, the policyholder may not be entitled to application of *contra proferentem*, or the reasonable expectations doctrine, which is based upon the premise that the insurance company that provides the contract wording must be held accountable for any ambiguity. Second, the participation of counsel in the company’s evaluation and drafting of such provisions might provide attorney-client privilege or attorney work product protection against disclosure of internal communications in a coverage action over the meaning of a manuscript provision.

Counsel Should Review Insurance Applications

Counsel’s role is also vital in the insurance application process. It is important to ensure complete disclosure in insurance applications because material omissions can result in rescission of the insurance policy. Applications for insurance policies typically require disclosure of known claims, losses and risk exposures. The required information may include property losses, workers compensation claims, third-party claims and lawsuits, and occurrences and circumstances that might give rise to a loss or claims, such as accidents, threatened claims or government investigations. Often, in-house counsel are particularly knowledgeable about those items and may be able to identify omissions in the disclosures prepared by risk management.

Counsel Should Evaluate Coverage For Any Important Claim

Large and complex insurance claims almost inevitably involve issues of contract interpretation and other matters for which the policyholder requires legal expertise.

A coverage opinion from counsel should be obtained whenever an insurance company asserts, or it appears from the policy, that coverage is not or may not be provided for an important claim. The application of insurance policy provisions to a particular claim is often unclear, and the meanings of numerous standard form clauses have been interpreted differently by the courts of different states. Therefore, determining which state’s law applies and researching

applicable case law can be important to a coverage analysis. Moreover, whether an exclusion applies to a claim may depend upon a determination of the proximate cause of a loss, injury or damage - legal issues best addressed by counsel. Risk managers often look to their brokers to opine on coverage. However, while brokers often have a productive role to play in the handling of the claim, they generally are not trained in insurance policy interpretation.

In-house counsel should be part of the policyholder’s team for pursuing any claim involving coverage issues or the possibility of coverage litigation or arbitration. A policyholder may find itself at a distinct disadvantage when pursuing a coverage claim unless it assembles a team with the necessary skills to match those available to the insurance company. Typically, the insurance company has a large claim department with specialists in handling particular types of claims who have access to coverage counsel, accountants, engineers and every other type of expertise that may bear upon coverage for a loss. Many policyholders have similar expertise residing in various departments within the company, which should be brought together to prepare and pursue the claim. Also, outside expertise may be needed, such as outside accounting and loss adjusting expertise for loss calculation and negotiating with the insurer’s loss adjuster. If a claim is particularly large or complex, it may be advisable to retain outside counsel to evaluate coverage and provide advice as the claims handling process develops. This is particularly advisable when the insurance company has raised exclusions as a possible basis for a denial of coverage or has asserted other policy-based defenses to payment.

The assistance of counsel is often needed to obtain a clear understanding of the insurance company’s coverage position because so-called reservation of rights letters often provide no meaningful information. Those letters typically lack any meaningful statement of facts relating to the claim and simply quote various insurance policy provisions as providing possible grounds for a denial, without explaining why they may be applicable. They also typically conclude with a blanket statement that the insurance company reserves all of its rights to deny coverage on any ground whatsoever. This type of letter is a self-serving effort to satisfy the

insurance company’s obligation to promptly articulate the grounds upon which coverage may be denied, but it is deliberately vague in order not to limit its options. Policyholders need a clear and specific statement of any possible grounds for denial so they can provide additional information and assess their coverage. Counsel are often best equipped to demand meaningful coverage positions from insurance companies.

Choice Of Law And Forum Selection

Insurance policies are interpreted under state law, and with respect to a surprising wide range of issues, standard form provisions are given different meanings from state to state. That creates a powerful incentive for both sides in a coverage dispute to forum shop and to race to the courthouse of a preferred venue at the first indication that a claim will not be resolved amicably. Therefore, policyholder counsel must focus on choice of laws and choice of forum before a dispute arises over a claim and prepare to file suit quickly in the forum that best suits the client’s interests.

A policyholder may assume that as the aggrieved party it has the sole discretion to initiate a coverage action and therefore to select the forum. However, insurance companies frequently bring preemptive declaratory judgment actions in the forum that best serves their strategic objectives. When this happens, a policyholder may file a competing suit in another jurisdiction and argue that as the aggrieved party it is the “natural plaintiff” and therefore its choice of forum should be given priority. When deciding which of two competing actions should go forward, courts consider a number of factors, but many give significant weight to which case was commenced first. Therefore, the policyholder must consider the possibility that if a coverage claim is not resolved amicably, it may find itself in a race to the courthouse against its insurance companies.

Conclusion

Insurance policies are important contracts that require the attention of counsel when they are entered into and when claims are pursued. In-house counsel can help to ensure that the coverage purchased meets the company’s needs and that the protection paid for is not lost in the pursuit of a recovery.