Portfolio Media, Inc. | 648 Broadway, Suite 200 | New York, NY 10012 | www.law360.com
Phone: +1 212 537 6331 | Fax: +1 212 537 6371 | customerservice@portfoliomedia.com

An Eye On Mass Tort Litigation Insurance Coverage

Law360, New York (July 09, 2009) -- Following President Obama's May 20, 2009, "Memorandum for the Heads of Executive Departments and Agencies," it is critical for policyholders susceptible to mass tort litigation to ensure that their insurance policies and programs provide the proper coverage for such mass tort suits.

The memorandum, which is aimed at rolling back the federal regulatory policies of the Bush administration that sought to limit jurisdiction for such suits by way of an aggressive preemption regulatory system, is likely to result in increased mass tort litigation in a variety of state and federal jurisdictions.

Because of the protracted and costly nature of mass tort litigation, policyholders need to evaluate their insurance programs with an eye toward the concerns specific to these suits, notably the payment of defense costs.

Rolling Back a System Designed for Preemption

The preemption regulatory system implemented by the Bush administration had been sought for years by industries frequently engaged in mass tort defense as a way to avoid the confusion brought about by 50 different state regulations.

President Obama's memorandum requires all executive department and agencies to:

1) not include "in regulatory preambles statements that the department or agency intends to preempt state law through the regulation except where preemption provisions are also included in the codified regulation;"

2) not attempt to preempt state law "except where such provisions would be justified under legal principles governing preemption;" and

3) undertake a review of the past 10 years of regulations that contain statements in regulatory preambles or codified provisions designed to preempt state law "in order to

decide whether such statements or provisions are justified under applicable legal principles governing preemption."

Increased Access to State Courts Equals Increased Defense Costs

The likely affect of the presidential memorandum will be a return to widespread litigation in state jurisdictions as mass tort plaintiffs seek to take advantage of less stringent state regulations, as well as potentially lengthier litigation absent preemption, which often allows for earlier dismissal of such suits.

Although any company with mass-marketed products now may face increased risk of claims, recent reports indicate that pharmaceutical manufacturers, including manufacturers of diet supplements and weight-loss pills, are particularly likely to face an abundance of new claims.

Consequently, it is imperative that manufacturers of such products be aware of the insurance-related consequences in defending against such suits. This increased risk of litigation in numerous state courts underscores the critical importance of a company's insurance coverage.

Because mass tort litigation is predictably lengthy and costly, policyholders pay hefty insurance premiums for unlimited defense protection, in addition to the normal insurance policy limits.

Moreover, the unique nature of mass tort litigation often requires that a company defend these claims in a more expensive manner that protects its reputation in order to discourage additional claims.

Insurance companies are well aware of these risks and policyholders need to be aware of their rights in the situation where their insurance company denies coverage or defends claims under the specter of a "reservation of rights."

Insurance Companies Have a Duty to Defend Whenever a Possibility Of Coverage Exists

Courts across the country recognize the duty to defend as being broader than the insurance company's duty to indemnify.

Importantly, in most jurisdictions, the duty to defend is recognized as independent of the duty to indemnify, meaning that a company may be found liable for damages that are not covered under the policy, but is still entitled to have the insurance company cover the defense costs.

In determining whether an insurance company has a duty to defend, most courts look to the underlying complaint and the policy, but also look to whether an insurance company

has actual knowledge of facts establishing a reasonable possibility that coverage may apply.

Different states apply slightly different standards, but the general rule is that "[t]he duty to defend arises whenever claims asserted by the injured party potentially come within the coverage of the policy." Regis Ins. Co. v. All American Rathskeller Inc., No. 773 MDA 2007, 2009 WL 1483504, at *2 (Pa. Super. Ct. May 28, 2009).

Other courts, such as courts in Connecticut and New York, look to whether the underlying complaint suggests a "possibility" of coverage.

If there is any doubt as to whether the underlying complaint asserts or suggests a covered loss, that doubt is resolved in favor of the policyholder and for coverage.

The broad duty to defend also requires that the insurance company defend all claims, even those outside of coverage, so long as any claim is potentially or possibly within the coverage of the policy.

Although the duty to defend applies even if the underlying claims are groundless, most states have held that the duty to defend expires if the underlying claim is narrowed to claims patently outside of coverage.

Consequently, it is important for policyholders to stay apprised of motion practice and other developments within a mass tort case that may impact coverage for defense of the claims.

Recognize When Policy Exclusions are Merely Red Herrings

Insurance companies often rely upon exclusions in an effort to avoid their obligations to defend their policyholders. An informed policyholder, however, will recognize when such arguments are simply red herrings.

First, it is important to remember that the burden of proving that an exclusion applies falls entirely on the insurance company. This heavy burden requires not only proving that an exclusion applies, but also requires proof that any applicable exclusions apply to all of the claims asserted.

Second, even if the exclusion may apply to all of the claims, an insurance company must also demonstrate "that the exclusion is subject to no other reasonable interpretations, and that there is no possible factual or legal basis upon which the [insurance company] may eventually be held obligated to indemnify the [policyholder] under any policy provision." Frontier Insulation Contractors v. Merchants Mut. Ins. Co., 91 N.Y.2d 169, 175 (1997).

The high burden imposed by this standard presents a difficult challenge for insurance companies seeking to apply exclusions to deny the duty to defend.

Successfully Defending Policyholder Rights When a Reservation of Rights is Received

Most states recognize that if a conflict of interest arises between a policyholder and its insurance company, a policyholder is entitled to retain independent counsel, separate from counsel appointed by the insurance company, and the insurance company is obligated to pay for this independent counsel.

The most common conflict of interest that arises is when the insurance company defends its policyholder under a reservation of rights.

In this circumstance, a policyholder should consider whether the insurance company will steer the defense of the underlying action in a manner adverse to the policyholder, such as by settling or defending claims in a manner that precludes coverage or following a defense strategy that ignores the damage to the company's goodwill.

Under such circumstances, policyholders should immediately seek independent counsel or, at a minimum, consult independent counsel. If a policyholder in fact retains independent counsel, its insurance company should pay the costs incurred for that retention.

Conclusion

With the risk of increased and protracted litigation facing many industries following President Obama's May 20, 2009, memorandum, policyholders likely will see increased mass tort product liability claims in state and federal courts across the country.

The protracted and expensive nature of mass tort suits may threaten a company's very existence as a profitable enterprise.

In order to protect against this threat, a policyholder must be aware of its insurance policies and, in case a claim is filed, secure an immediate and complete defense commitment under the applicable insurance policies.

This defense must continue until: (1) the insurance company can conclusively prove the absence of any possibility of coverage under the policy; or (2) the limits of the insurance policy are exhausted.

--By Darin J. McMullen and William H. Pillsbury, Anderson Kill & Olick PC

Darin McMullen and William Pillsbury are both attorneys with Anderson Kill & Olick in the firm's Philadelphia office.

The opinions expressed are those of the authors and do not necessarily reflect the views of Portfolio Media, publisher of Law360.