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Effective Reservations of Rights

By John Johnson and Rob Shaughnessy

What was a sufficient reservation of rights letter 10 years no longer suffices. Many jurisdictions are scrutinizing the notices when a conditional defense is provided. Most insurance professionals work in many different jurisdictions and it is impractical and not cost effective to retain coverage counsel in every case.

Coverage analysis must be reflected in communications with insureds. There is a fine line between interpreting the policy, which is dangerous, and describing potential coverage impediments.

Best Practice

Assume that each jurisdiction is as strict as the most restrictive. Waiver should be considered the norm. If the company's right is not specifically reserved, assume the coverage defense is gone. Conditions, rather than coverages or exclusions, are more often able to be waived.

A reservation of rights should inform the insured of the coverage-restricting issues. Consider these steps when creating reservation of rights letter. Go through the fact and policy analysis:

- ◆ Did an insured tender the claim?
- ◆ Is there an additional insured tender or potential additional insured tender?
- ◆ Are multiple or consecutive policy periods in play?
- ◆ Did the act or omission complained of take place during the policy period?

- ◆ Does the act or omission amount to an accident, as defined by the jurisdiction?
- ◆ Is the damaged property covered or the peril insured against?
- ◆ Does the policy require an accident to result in property damage or bodily injury before a trigger?
- ◆ Does an exclusion apply?
- ◆ Did the insured comply with all conditions?
- ◆ Should the insured tender to another or multiple carriers?

Consider whether the insured is indemnified and whether the defense can be tendered to another party. Always review conditions precedent. If the policy or jurisdiction provides for reimbursement for defense costs of non-covered claims, assert the right from the outset. Review the application to be certain the claim falls within the risk underwritten by the insurer.

Evaluate the claim with an eye toward coverage. The claim file should reflect the analysis and the considerations in arriving at a coverage decision.

Just the Facts

Coverage cannot be created or broadened by estoppel. This rule is not as bright line as it once was. Do not explain what a coverage provision or exclusion means. State the facts and why they may invoke coverage or an exclusion. Include substance, not just policy terms. Do not just explain why there is not coverage; explain why coverage may be excluded.

Finally, and most importantly, always

contact the insured before reserving rights or disclaiming coverage. Get the insured's story. Ask the insured about the case or the underlying facts. Discuss the allegations of the complaint. Note in the claim file the facts with which the insured agrees or disagrees. When preparing the coverage determination, recite the facts the insured provided. Invite the insured to make any corrections and invite additional facts, documents or information.

As the case progresses, review the letter to make sure it accurately reflects the facts, claims and defenses. Developments may invoke other coverages, exclusions or conditions. If a supplemental reservation of rights is warranted, state that the supplement is being sent based on new information.

An insurer must look beyond the allegations of the complaint to determine whether a duty to defend exists. The facts may be considered in establishing the duty to defend. Some states do not allow extrinsic evidence to be considered in denying a duty to defend.

An effective reservation of rights letter advises the insured of why or why not a claim may trigger defense or indemnity. The letter should reflect the facts and the insured should be involved in the process. [LM](#)

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