Your Coverage Advisor

Insurance Coverage Newsletter
Summer 2018 (Vol. XX)

Restatement of Law, Liability Insurance Approved: Attempts Comprehensive Look at All Aspects Governing Insurance Liability Law

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After years of work, at its annual meeting on May 22, 2018, members of the American Law Institute (ALI) approved Final Draft No.2 of its first ever Restatement of the Law, Liability Insurance (RLLI). The official text of the new Restatement is now ready for final editing before publication. The draft approved may be cited as the formal position of the ALI until the official text is published.

There are four chapters in the RLLI. The first includes topics relating to the application of basic contract law doctrines within the context of insurance law. The second chapter concerns insurance duties and doctrines, such as cooperation, defense, and settlement, relating to the management of insured actions. The third chapter presents principles that are common to risks insured by most forms of liability insurance. This chapter is divided into three general topics: provisions relating to coverage, provisions relating to conditions, and provisions relating to the application of deductions, retentions, and limits. The final chapter concerns a variety of topics relating to, inter alia, broker liability, bad faith, enforceability, and remedies.

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Why It Matters: Insurance law is a matter of state law. It is governed by state statutes and common law, and may vary from state to state. As cases are litigated, and the resultant common law in each state is established and evolves, majority and minority views among the states concerning various insurance principles inevitably develop.

ALI is a private organization, founded in 1923, "to promote the clarification and simplification of the law and its better adaption to social needs, to secure the better administration of justice, and to encourage and carry on scholarly and scientific legal work." ali.org/about-ali/how-institute-works/. ALI's members, limited to 3000, include the justices of the U.S. Supreme Court, judges of the highest courts of most, if not all, states, law school deans and professors, and private practitioners. As described in ALI's 2016-2017 Annual Report, the ALI "Is the leading independent organization in the United States producing scholarly work to clarify, modernize, and improve the law."

In furtherance of its mission, the ALI develops Institute Projects which include Restatements, Principles, and Codes. Restatements are, for the most part, addressed to the courts and aspire to present "clear formulations of common law and its statutory elements, and reflect the law as it presently stands or might appropriately be stated by a court." Although Restatements aspire toward the precision of statutory language, *they are also intended to reflect the flexibility and capacity for development and growth of the common law. That is why they are phrased in descriptive terms of a judge announcing the law to be applied in a given case* rather than in the mandatory terms of a statute." ali.org/about-ali/how-institute-works/ (emphasis supplied). Thus, Restatements typically strive to harmonize both majority and minority views of law, and restate them.

The study of the various Restatements of Law is part of the fundamental course work of every law student in every law school throughout the country. The Restatements are also extremely persuasive and influential in both state and federal courts throughout the country, routinely cited in briefs advocating various legal concepts and principles, and cited and relied upon in an untold number of judicial decisions announcing controlling legal principles.

The development or update of a Restatement takes many years of work. It may include multiple drafts reflecting member comments and revisions advocating various positions, some of which are at odds with one another, before the final draft is ultimately approved as embodying the official positions of the ALI on the particular topic. Moreover, when considering or relying on a Restatement principle, it is crucial to keep in mind that "only the black letter and Comment are regarded as the work of the Institute. The Reporter's and Statutory Notes remain the work of the Reporter." Restatement of the Law of Liability Insurance, Proposed Final Draft No. 2, approved May 22, 2018, p. ix.

Some jurists and practitioners caution that some of the influential Restatements in certain circumstances have moved beyond clear statements of what the law is to statements of what the law should be, in the view of the ALI:

> I write separately to note that modern Restatements . . . are of questionable value, and must be used with caution. The object of the original Restatements was "to present an orderly statement of the general common law." Restatement of Conflict of Laws, Introduction, p. viii (1934). Over time, Restatements' authors have abandoned the mission of describing the law, and have chosen instead to set forth their aspirations for what the law ought to be…Restatement sections such as that should be given not weight

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> whatsoever as to the current state of the law, and no more weight regarding what the law ought to be than the recommendations of any respected lawyer or scholar.

Kansas v. Nebraska, 135 S. Ct. 1042, 1054 (Scalia, J., concurring and dissenting).

The Process Leading to Approval of the Restatement of Law: Liability Insurance: The RLLI project began in 2010 as a Principles of Law Project. Principles, unlike Restatements, do not purport to be statements of the law, but rather aspirational statements of what the law in a particular area should be. In 2014, the ALI's Liability Insurance Principles project was recharacterized as a Restatement of Law project both because there is an established body of liability insurance law, and because, consistent with traditional Restatement projects, the Liability Insurance project's goal was to provide guidance to courts.

Cumulatively, nearly 30 drafts and revisions were prepared during the project's lifecycle. Over the years, the project has been the object of intense interest and scrutiny by insurance scholars and practitioners representing both insurers and policyholders. Throughout its evolution, many aspects of the project have been highly debated, and many proposed Sections of proposed statements of law have been contested in comments submitted by interested stakeholders, often resulting in section revisions.

As the project progressed, discrete Chapters, Sections, and revisions of the RLLI Project were submitted *seriatim* for review and approval by ALI members at different annual meetings, both before and after its recharacterization as a Restatement. At the 2017 annual meeting, the ALI decided to defer the vote for final approval of the RLLI until the 2018 annual meeting to allow the Reporters to again review the entirety of the draft and to consider comments.

That review process resulted in a number of fairly significant revisions, generally described in the Reporters' Memorandum of the Restatement of the Law of Liability Insurance, Proposed Final Draft No. 2, pp. xix –xxiv. According to the Reporters' Memorandum, the most significant revisions are contained in: Chapter 1, Sections 3 and 4 (adopting a plain meaning rule for policy interpretation including what constitutes an ambiguous term, and relatedly, the interpretation of ambiguity); Chapter 2, Section 12 (concerning liability of an insurer in connection with the defense of its insured); Chapter 2, Section 19 (providing that "[a]n insurer that breaches the duty to defend a legal action forfeits the right to assert any control over the defense or settlement of the action"); and Chapter 4, newly numbered Sections 47 and 48, (describing potential remedies for breach by the insurer, including an award of attorneys' fees and costs to the insured in an action to determine coverage "when provided by state law or policy").

Because of the depth and breadth of the Liability Insurance project, and the comprehensive nature of the topics ultimately included in the RLLI, there remain many differences of opinion on whether particular statements of law reflect clear and accurate restatements of the law or statements of what the law should be. And, not unsurprisingly, advocates of a certain perspective may view certain sections of RLLI to be accurate reflections of the law, while other sections are not.

Selected Provisions of Interest: All of the Sections of the RLLI that relate to attorneys and attorneys' fees are of interest, a sampling of which follows:

> Section 12 provides that an insurer may be held liable for the conduct of an attorney hired to represent the policyholder where the insurer did not use "reasonable care" in selecting counsel (section 12(1)) and the

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Back to Basics: Understanding Notice Provisions

By Kerri L. Keller
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Most insurance policies require that notice be given within a specified period of time. Usually, it is required "as soon as practicable." Why are notice provisions in insurance policies important? They are important because they allow the insurer to become aware of claims or occurrences early enough to conduct an investigation. They also allow an insurer to determine whether allegations in a complaint state a covered claim. When an insurer receives notice, it can also step in and control the defense of the litigation, protect its interests, maintain proper reserves, and pursue possible subrogation claims.

Claims-made policies typically require that notice be given within a reasonable time and no later than the end of the policy period, or within some defined period of time or grace period. If they require a claim be reported during the policy period, or within some defined period of time or grace period, they are often referred to as "claims-made and reported" policies. Conversely, in an occurrence policy, such as a typical general liability policy, the policy will pay for occurrences (accidents) that happen during the policy period, even if the insurer receives notice of them after the policy expires. Occurrence polices will typically require that notice of an occurrence, or an event that could result in a claim, be given as "soon as practicable."

Policyholders failing to comply with notice provisions risk compromising their coverage; however, in many instances, coverage will be forfeited only if the insurer demonstrates that late notice has resulted in prejudice. As such, when policyholders are confronted with denials based on their failure to provide timely notice, they often assert that the insurer must demonstrate prejudice. However, courts may be hesitant to require prejudice in cases that involve claims-made policies because, with claims-made policies, courts may deem notice a "condition precedent" to coverage.

When providing notice, there are certain things that should be done as part of "best practices" to help ensure that there are no issues with notice: (1) provide written notice, unless otherwise required to be provided by some other means, and include a copy of the complaint and summons with the notice if a lawsuit was filed; (2) include a copy of any written claims or demands if received; (3) read the policy immediately for specific notice provisions and make sure to comply with them; (4) provide name and contact information so that the insurer can follow up and if it changes, supplement it; (5) request defense and indemnity coverage and request that all policy obligations be honored; and, (6) ask the insurer to acknowledge receipt.

Send the notice as soon as possible, especially when dealing with a claims-made policy. With an occurrence policy, send it as soon as practicable under the circumstances; but, never assume that it is too late. There are always arguments that can possibly be made as to why even untimely claims should be covered. ■

Wisconsin Court of Appeals Reverses $68 Million Judgment in Excess Insurer's Favor

By Joseph M. Bucaro
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In a case that was first filed in 1989, the Wisconsin Court of Appeals recently held that an excess insurer has a duty to defend only where an occurrence is covered by the excess policy and not covered by the underlying policy. An excess insurer and underlying insurer cannot simultaneously be tasked with the duty to defend. *Johnson Controls, Inc. v. Central National Insurance Company of Omaha*, No. 2014AP2050, unpublished slip op. (Wis. App. Apr. 25, 2018).

In 1985, Johnson Controls, Inc. was identified as a potentially responsible party for the environmental contamination of several landfills and smelting plants. Johnson Controls notified its primary, umbrella, and excess insurers demanding defense and indemnity coverage under various policies for Johnson Controls' potential liability under the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA). All of Johnson Controls' insurers refused to defend or indemnify Johnson Controls for costs under CERCLA, claiming costs under CERCLA were not covered by the policies.

Johnson Controls eventually filed suit against all its insurers for breach of their duties to defend and indemnify. This included a claim against Central National, who was an excess insurer of Johnson Controls.

Initially, the Wisconsin Court of Appeals agreed with Johnson Controls' insurers that they did not have a duty to defend or indemnify claims arising under CERCLA. This ruling was reversed when the Wisconsin Supreme Court overruled *City of Edgerton v. General Casualty Co. of Wisconsin*, 184 Wis. 2d 750, 517 N.W.2d 463 (1994), which allowed Johnson Controls to recover for damages incurred under CERCLA. The reversal of the *Edgerton* ruling ultimately lead to Johnson Controls securing a judgment of $68 million against excess insurer Central National.

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Wisconsin Court of Appeals... **(Continued from page 5)**

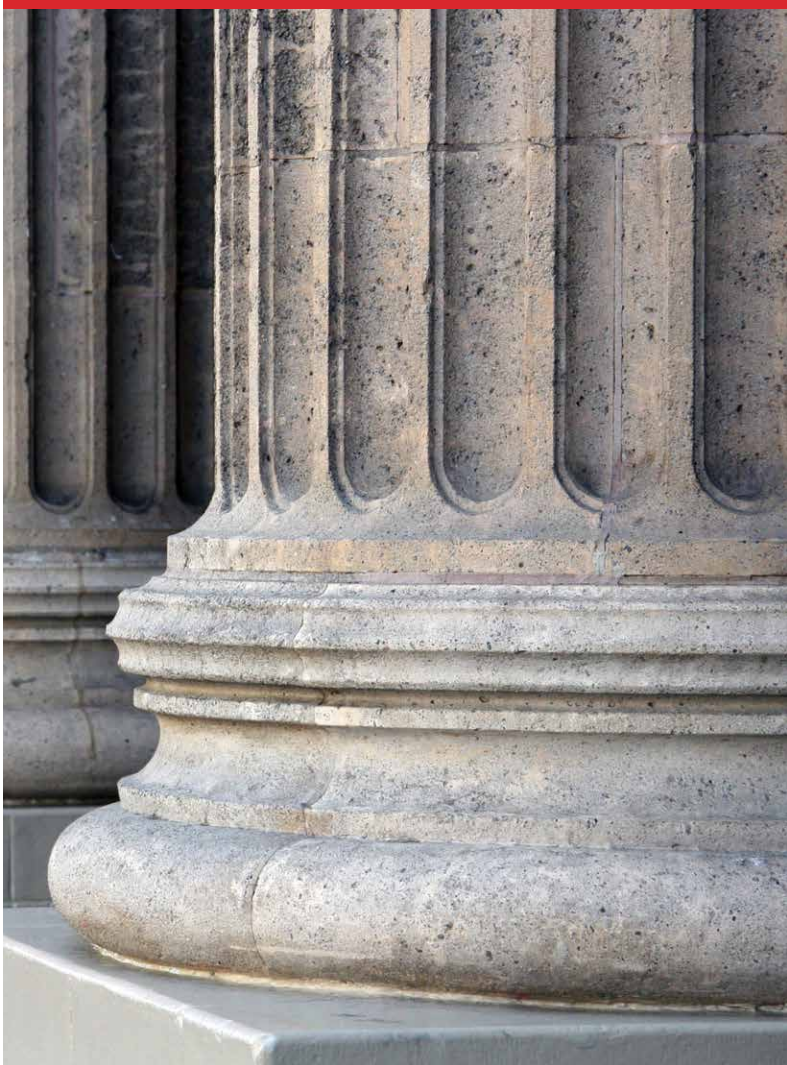
Central National appealed the judgment and argued that its duty to defend was limited to occurrences where the excess policy covered the occurrence, and the underlying policy did not. It argued that both the underlying insurance policy and the Central National policy covered claims for costs under CERCLA, and therefore the underlying insurance alone should have the duty to defend. Johnson Controls argued that the court of appeals should look to general concepts about excess insurer coverage from results in other cases, rather than analyze the specific policy language at issue in the case. It cited several cases that held an excess insurer and primary insurer could have simultaneous duties to defend.

The court determined that the analysis of whether an excess insurer has a duty to defend should not be decided based on general concepts about the role of excess insurers, but should be determined by the specific policy language at issue. Since the policy language regarding environmental claims in the Central National policy was the exact same as the language in the underlying insurer's policy, the court ruled they could not both have a duty to defend simultaneously.

The court of appeals ultimately agreed with Central National and reversed the lower court's decision. The court stated that either the occurrence was covered by both the underlying and excess policies, in which case the underlying policy had the duty to defend, or the occurrence wasn't covered by either policy, and Central National would not have a duty to defend.

The *Johnson Controls* decision confirms again the importance of analyzing the specific policy language at issue. Policyholders should not rely on general concepts about how insurance policies have been applied in the past. Instead, policyholders should ensure the language of policies they hold accurately reflect their insurers' duties to defend and indemnify. ■

Brouse McDowell welcomes Jodi Spencer Johnson, an Ohio State Bar Association certified specialist in Insurance Law, with nearly 20 years of experience representing policyholders. Brouse's team now houses 6 of the 26 certified specialists in Ohio.



insured suffers harm resulting from the negligent conduct of the counsel selected by the insurer. Further, an insurer is also liable for harm resulting to a policyholder if the insurer directs counsel's negligent conduct or omission in a manner that essentially "overrides" the independent professional judgment owed by defense counsel to the policyholder (section 12(2)).

Section 14 describes the basic obligations of the insurer to defend a claim against a policyholder. Those include the obligation to defend all causes of action, "including those not covered by the insurance policy." Section 14(1)(a). The Section further specifically provides that counsel selected to defend the insured may not disclose "to the insurer any information of the insured that is protected by attorney–client privilege, work-product immunity, or a defense lawyer's duty of confidentiality under rules of professional conduct, if that information could be used to benefit the insurer at the expense of the insured." Section 14(1)(b). Finally, under Section 14(3), an insurer's costs in defending the policyholder in the underlying action are in addition to the limits of the policy, unless the policy otherwise provides.

As discussed above, Section 19 directs that where there is a breach of the duty to defend the insurer forfeits any control over the defense or settlement.

Section 21 concerns whether or not an insurer may recover defense costs where a claim against a policyholder is ultimately determined to be not covered by the policy. This section states that an insurer may not recover from the insured fees and costs paid on behalf of a policyholder even for claims that are determined to be not covered, unless it is so stated in the policy or "otherwise agreed to" by the policyholder.

Section 48 describes the damages due an insured for breach of a liability policy. Specifically, if there is a breach of the duty to defend, "all reasonable costs of the defense of a potentially covered legal action," subject to limits, deductibles or SIRs, are included as damages. "While insurers are obligated only to pay reasonable defense costs, what is reasonable in the case of a breach of defense duties is judged from the perspective of an insured forced to defend a liability action without the timely assistance of its insurer. In that circumstance, the negotiated rates that liability insurers pay their regular defense counsel are unlikely to provide a useful guide to what is reasonable." Section 48, Comment (b).

The entirety of the Sections referenced above, as well as the other Sections in the RLLI relating to attorneys' duties and obligations, insurers' defense obligations, and the costs of defense, as well as principles of contract interpretation, trigger, allocation, settlement, bad faith, and broker liability, among others, contain a myriad of other relevant provisions which will be of great interest to the insurance industry, insurance consumers, and insurance practitioners.

Stay Tuned: As discussed above, the RLLI is comprehensive and covers the virtual universe of insurance law. As they examine the RLLI, insurance scholars and practitioners continue to disagree on whether the RLLI accurately reflect the law or the trend of the law on various discrete topics. Thus, there are many Sections of interest in the RLLI which warrant closer study and scrutiny. Stay tuned to future editions of *Your Coverage Advisor* for a more detailed look, examination, and analysis of additional insurance law topics of interest as restated in the newly adopted Restatement of Law, Liability Insurance. ■

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Meagan L. Moore
Amanda P. Parker
Paul A. Rose
David Sporar
Christopher T. Teodosio
Anastasia J. Wade

Attorney Highlights

P. Wesley Lambert was elected to the Akron Children's Museum Board of Directors.

Amanda M. Leffler was awarded the 2018 Read Family Difference Maker Award by Leadership Akron.

Amanda M. Leffler was recognized as a "Notable Woman in Law" by Crain's Cleveland Magazine.

Amanda M. Leffler spoke on Advanced Issues in Construction Coverage at the Stark County Bar Association seminar on April 20.

Alexandra V. Dattilo was honored as a "Woman Leader in a New Position" by ATHENA Akron.

Alexandra V. Dattilo graduated from the CMBA's Leadership Academy.

Kerri L. Keller was selected to be a member of Leadership Akron Class 35.

Kerri L. Keller was elected as a member of the Hudson Community Foundation's Professional Advisor Group.

Save the Date!

Sixth Annual Insurance Coverage Conference
October 11, 2018, 1:00 p.m. to 5:30 p.m.

Location:
Embassy Suites Independence
5800 Rockside Woods Blvd.
Independence, OH 44131

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