2019 Annual Conference
March 13 - 15, 2019
Orlando, FL

Additional Insureds, the Role of Assigned Defense Counsel

I. The Basics of additional insured coverage in construction claims

Not all defense counsel are equal (or are they)?

Before an owner, contractor, or subcontractor experience the pleasures of construction litigation, more specifically construction defect litigation, they undoubtedly have a lawyer of choice who will handle their legal needs in a personal counsel or general counsel role. This attorney's knowledge of construction defect law, insurance coverages, risk transfer, and how to manage and litigate a complex construction case can vary dramatically. Additionally, many times these owners, contractors, or subcontractors have prior experience in construction litigation and have counsel who may have defended them previously. It is only natural that when needed, the client will turn to and retain counsel whom they trust and believe will zealously represent their interest in litigation.

For the vast majority of owners, contractors and subcontractors, they have general liability insurance (whether it be traditional or WRAP coverages) which owe an obligation to defend them against suits and claims arising from or relating to damage to person and property. To realize the benefits of this obligation, the insured either themselves or through their brokers or personal counsel tender this claim to the insurer. For ease of reference, we will first limit this discussion to tenders made to the insured's primary general liability insurer. For some insureds who may have competent counsel, they may request that the insurer agree to defend through their counsel of choice. Other insureds may have the ability to demand and affirmatively select counsel through choice of counsel provisions which are pre-negotiated in their insurance agreements. For others, they may have self-insured retentions or certain deductibles which may require that the insured pay a predetermined amount on defense or indemnity before their obligations under the insurance contract are triggered. In those instances, the insured most likely will satisfy their obligations through retention and payment of

defense counsel of their choice. In all three instances however we will refer to defense counsel as "insured-appointed" defense counsel.

By way of comparison, in other instances, the insurer may have an immediate duty and obligation to participate in the defense of its insured. In those instances, the insurer may agree to participate in the defense of the insured through the insured's requested counsel or retain its own defense counsel. Yes, there are a whole host of issues and considerations as to when the insurer can disregard the insured's selection of counsel which will be discussed below. However, for the issue at hand, the selection of counsel by the insurer will be referred as "insured-appointed."

Further complicating the landscape are situations wherein the owner, contractor or subcontractor are also additional insureds under one or multiple other insurance polices placed by others. The most common instance is when a subcontractor is required to name the contractor as an insured under its general liability policies. This workshop will discuss the unique professional and ethical considerations associated with defense counsel appointed by a primary carrier and/or additional insured carrier.

How much insurance participation is enough?

The answer is easy, there is never enough insurance participation. However, the goal and motivations associated with procuring additional insured coverage may vary based on the role that counsel serves, who retained them, and more importantly, who they believe will best represent their interests. First, the interests of an insured-appointed counsel are clearly that of the client who appointed them. As such, their motivation will virtually always be to protect their client even to the detriment of the insurer. Below we will discuss the different potential business considerations that may impact counsel's decisions on tendering claims. With regard to an insured-appointed defense counsel, the answer should still always be the insured-client. However, in many instances the client / insured may be a minor client as opposed to the insurer who makes up a substantial part of the defense counsel's practice. In these instances, it is only natural to think that the considerations of the insurer would play some role in the decisions of counsel -even if it shouldn't. For the purposes of this workshop, these tendencies may materialize in the form of how aggressively defense counsel tenders coverage both on the primary side and the additional insured side. These actions may be opposed to the wishes of the client / insured.

Aside from the client and defense counsel's role in procuring insurance coverage, the underlying insurers also are motivated to spread their obligations and secure the most insurance participation as possible. The level of involvement of the carriers in tendering claims directly will depend on the rights granted by the State for which the claim is pending. For instance, in Florida, there is no right of contribution against non-contributing carriers whereas this right does exist in states like Nevada, California and

Colorado. As such, a carrier defending a claim in Florida is powerless to pursue participation of additional insurers directly (without some form of assignment or assistance from the insured). However, a carrier defending a claim in Nevada, California and Colorado could file a declaratory relief action seeking to force the participation of other potentially available insurance coverage.

II. Legal backdrop concerning appointment of defense counsel and impact on claims handling

The legal rights and responsibilities relating to the appointment of defense counsel are fact specific and vary depending on jurisdiction. However, the most predominant issue is who has the control regarding the decision on selection of counsel. If there are conditions precedent to coverage such as a self-insured retention or condition precedent deductible, then the answer is typically that the insured gets to select counsel of their choice. In certain instances, where the rate charged by this insured-appointed defense counsel are deemed to be excessive by the insurer, the insurer may discount the fees incurred for the purposes of satisfaction of the applicable self-insured retention or deductibles. When the conditions precedent to coverage are satisfied, the insurer can then decide to continue the defense through the insured-appointed counsel or seek to appoint someone else.

When there is a dispute as to retention of counsel between the insurer and insured, the rights of each are typically impacted by whether the insurer decides to assert a reservation of rights in connection with its defense. A reservation of rights is a decision of the carrier to, while agreeing to defend its insured, inform the insured that there are certain policy provisions which may preclude coverage and cause the insured to withdraw from the defense. The insurer will typically also inform the insured that they may seek to recover the defense fees that they paid to the extent that they find coverage exclusions and withdraw from the defense. As such, a reservation of rights can have a significant adverse impact on the insured.

Considering the fact that defense counsel, whether insured or insurer appointed, will be conducting discovery into the specific facts of the claim and reporting to both the insured and insurer, there is typically a concern by the insured that the insurer-appointed counsel will use their ability to conduct discovery and report to investigate facts that may result in a loss of insurance coverage. This concern could be amplified in the additional insured context when a carrier is defending an action under a policy which was initially intended to cover a discrete construction trade but now is defending a contractor under all issues.

As expected, the circumstances under which an insurer can force its selection of counsel on its insured are dictated by state specific law. For instance, in Florida, if a carrier decides to issue a reservation of rights, the selection of defense counsel must be

"mutually agreeable" to both. Fla. Stat. § 627.426(2)(b); *Colony Insurance Co. v. G&E Tires & Service, Inc.*, 777 So. 2d 1034 (Fla. 1st DCA 2000). By contrast, in California, when an insurer reserves on an issue of coverage and there is a concern that the insurer-appoint defense counsel can control aspects of litigation which could impact coverage, the insured may require that the insurer retain independent counsel of the insurer's choosing. California Civ. Code 2860. This counsel is referred to as *Cumis* counsel after the seminal case that imposed this obligation. It is important to note that the issue of when *Cumis* counsel is required has also been heavily litigated. For instance, California Courts have held that facts relating to whether or not a construction defect exists, timing of an occurrence or other facts that are developed through experts or for which the lawyer does not impact the outcome on, do not give rise to *Cumis* counsel. When the insured demands independent counsel the only real recourse of an insurer is to withdraw their reservation. With that said however, the insurer can impose certain minimal qualifications on independent counsel such as a minimum of five (5) years experience in the area of dispute and certain minimal professional liability coverages. Other states like Nevada have adopted this line of reasoning and imposed similar requirements relating to independent counsel. *Nevada Yellow Cab Corp. v. Eighth Judicial Dist. Court*, 123 Nev. 44, 152 P.3d 737 (2007). Unfortunately, in Colorado, no court has addressed whether an insured under a reservation of rights. The Colorado Supreme Court in *Hartford Ins. Group v. District Court*, 625 P,2d 1013, 1018 n.5 (Colo. 1981) chose not to address under what circumnutates insurers had a duty to furnish separate counsel for the insured or to pay fees of the counsel chosen by them. *See also Hecla Mining Co. v. New Hampshire Ins. Co.*, 811 P.2d 1083, 1098 n.7 (Colo. 1991).

With regard to additional insured carriers, in addition to the issues that primary carriers face as to appointment of counsel, they face the issue of the extent of their defense obligation. To that end, the question becomes, is an additional insured carrier who insures a minor trade contractor with a discrete set of defect claim obligated to defend the contractor in a construction defect litigation with much larger and complex issues? The answer is typically a resounding yes. *Presley Homes, Inc. v. American States Insurance Co.*, 90 Cal. App. 4th 572 (2001). The reasoning that has been virtually uniformly accepted is that the carrier, primary or additional insurer, owe a complete defense -even if the ultimately indemnity obligation is different.

III. Special business and ethical considerations relating to additional insured claims

To tender or not to tender, that is the question

In a perfect world where all policies are equal the answer to the question as to which policies to tender to would be simple -tender them all. However, the reality of the situation is that not all policies are equal. For instance, some policies may have significant self-insured retentions or deductibles which the insured would like to avoid.

In other instances, the insured would like to shift the risk of self-insured retentions and deductibles to its subcontractors or others and only seek additional insured coverage. In other situations the insured may wish to avoid having a claim under their own general liability policies for the fear of increased premiums or an inability to procure insurance in the further.

The initial decision as to which policies to tender will typically be reserved for the insured. Since they are the person or entity who makes the initial decision when a claim arises as to who to inform, this decision is typically made exclusively by the insured and/or their counsel. That was easy. However, these decisions get somewhat more interesting when you overlay an insurer-appointed counsel and/or an insurer-appointed counsel retained by an additional insured carrier. In these context, it is helpful for defense counsel to realize and acknowledge their legal and ethical responsibility to the insured -their client. As such, the decision as to whether to tender and who to tender is reserved for them. With that said however, depending on the terms and conditions of the insurance agreements, the insured may be obligated to tender or face a claim by the carrier that they breached their duty to cooperate (policy specific and State specific). Additionally, depending on the State, the carrier may have its own independent right to pursue a tender and coverage in its own name. The distinction is that counsel for the insured cannot take any actions which are against the wishes of its client in this regard. The same is true in both the primary and additional insured contexts.

Another issue that arises is that extent to which appointed defense counsel is required or expected to pursue denials of coverage. This most frequently arises in the context of defense counsel tendering carriers for additional insured coverage. In those instances, defense counsel will typically be expected to send the initial demands for defense and indemnity which will inevitability result in requests for additional information. In their role as defense counsel, it is expected that counsel can and should provide basic factual information to support its clients' requests for coverage. This typically involves providing the pleadings, expert reports, and construction file documents. The more controversial issue is to what extent that defense counsel is expected or required to respond to coverage-related questions or denials. Unlike the issue of appointment of counsel, there are not many cases that address this issue. Rather, in practice, the extent of aggressiveness of pursuit of coverage denials is a preference of defense counsel and usually based on their knowledge of the subject matter and relationship with the client. However, it goes without saying that defense counsel cannot advocate or take actions that would be to the detriment of the client / insured.

Aside of the issue of procuring additional insured coverage, a related issue is how to keep such coverages. The most common situation where this arises is in the context of settlement. Specifically, the decision as to whether to settle with a subcontractor whose underlying insurer is participating in the defense of the contractor. From a practical standpoint, this subcontractor may be offering to pay all of the damages

associated with their scope of work (in fact, sometimes agreeing to pay a premium) however settlement with them would also resolve their carrier's additional insured defense obligation. In that circumstance ,the motivations of the carrier (to settle) and the client / insured (to keep the defense obligation) are conflicting and may be putting the insurer-appointed defense counsel in an uncomfortable position. While inevitable, in the majority of instances the client / insured controls the decision to settle and it is the professional responsibility of defense counsel to explain the benefits and burdens of settlement and represent their client's best interests. Per *D.R. Horton, Inc.-Denver v. Travelers Indem. Co. of Am.*, 10-CV-02826-WJM-KMT, 2012 WL 5363370, at *1 (D. Colo. Oct. 31, 2012), a party can only release claims which it owns, and the general contractor did not own the subcontractors' carriers' contribution claims.

IV. The role of deductibles and self-insured retention

As stated above, many times the general liability policies at issue in construction defect cases have conditions precedent to a defense or indemnity obligation. The most common preconditions are self-insured retentions. Since these obligations are required to be satisfied prior to the insurer having a duty to defend their satisfaction is of importance. These are two important considerations for determining how to satisfy and who can satisfy these conditions. These are the underlying agreements between the parties and the insurance policy itself. As to the former, many times the construction agreements between the owner and contractor and between the contractor and owner express who is responsible for self-insured retentions and deductibles. In those instances, the satisfaction of the same, as between those parties, is determined by contract law. Once a determination is made as to who should or will satisfy these monetary conditions, the next determination is who can satisfy it under the policy. Many policies have express restrictions as to whom can satisfy the policy requirements. The leading restriction is that only the named insured may satisfy. The enforceability of such restrictions will vary by state law however in most instances a clear and unambiguous restriction will be upheld. As such, appointed defense counsel must account for these restrictions in how they defend their client.