

2016 Insurance Coverage and Bad Faith Seminar

**The Defense Institute of the International
Society of Primerus Law Firms**

November 3-4, 2016

WAIVER, ESTOPPEL, AND PROPER RESERVATION OF RIGHTS LETTERS



Lipe Lyons

Edward J. Murphy
Lipe Lyons Murphy Nahrstadt & Pontikis Ltd.
230 West Monroe Street
Suite 2260
Chicago, IL 60606
312-448-6234
ejm@lipelyons.com
www.lipelyons.com

DUTY TO DEFEND

Defend – Assert No Policy Defenses

Defend and Reserve Rights

Declaratory Judgment – See Declaration of No Coverage

Cumis/Peppers Conflict?

- Reserve Rights

- Appoint Counsel-If Insured Consents

- If Not—Pay for “independent counsel”

Decline Coverage

RESERVATION OF RIGHTS LETTER

PURPOSES

Notify the Insured that Insurer Intends to Seek Declaration of “No Coverage”

Notify the Insured that Insurer May Deny Coverage or Seek a Declaration Depending on Facts Learned

Insurer Seeks to Suspend the Operation of the Estoppel Doctrine

When an insurer defends a claim against its insured under a proper reservation of rights, the insured cannot then so easily claim that it was prejudiced by the insurer's conflict of interest. *Royal Ins. Co. v. Process Design Associates*, 221 Ill.App.3d 966, 973 (1st Dist. 1991)

ELEMENTS OF PROPER RESERVATION OF RIGHTS LETTER

SPECIFIC

TIMELY

UNEQUIVOCAL

UNAMBIGUOUS

ELEMENTS OF ROR LETTER

SPECIFIC – MUST ADEQUATELY INFORM THE INSURED OF THE RIGHTS THE INSURER INTENDS TO RESERVE

ROR letter must fairly inform the insured of the insurer's position. *Cowan v. Insurance Company of North America*, 22 Ill. App.3d 883, 889 (1st Dist. 1979)

ELEMENTS OF ROR LETTER

TIMELY

A position on coverage should be taken promptly within a reasonable time to avoid prejudice to the insured. *Twin City Fire Insurance Company v. Old World Trading Company*, 266 Ill.App. 3d 1, 12 (1st Dist. 1993)

ELEMENTS OF ROR LETTER

UNEQUIVOCAL

Warning of possible future contingencies is not sufficient. *Royal Insurance Company v. Process Design Associates, Inc.*, 221 Ill.App.3d. 966, 975 (1st Dist. 1991)

ELEMENTS OF ROR LETTER

UNAMBIGUOUS

If reservations are ambiguous the ambiguity will be strictly construed against the insurer and liberally construed in favor of the insured. *Canal Insurance Company v. Flores*, 544 F. Supp.2d 828, 834 (W.D. Texas 2007) (Texas law).

WAIVER v. ESTOPPEL

Although the terms “waiver” and “estoppel” are sometimes used **indiscriminately**, especially in the law of insurance, they are two distinct and different doctrines that rest on different legal principles. Strictly speaking, “waiver” is used to designate the act, or the consequences of the act, of one side only, while “estoppel” is applicable where the conduct of one side had induced the other to take such a position that it would be injured if the first should be permitted to repudiate its acts. *Insurance Company of the West v. Haralambos*, 195 Cal.App.3d 1308, 1325, note 6 (1987)

WAIVER v. ESTOPPEL

In the insurance context the distinction between waiver and estoppel has been **blurred**. *Intel Corp. v. Hartford Accident & Indemnity Co.*, 952 F.3d 1551, 1559 (9th Cir. 1991)(California law)

The estoppel question, we believe, is separate from the waiver question, though the two issues are frequently **intertwined and confused**." *Western Casualty & Surety Company v. Bruchu*, 122 Ill.App.3d 125, 134 (1st Dist. 1984) *affirmed* 105 Ill.2d 486 (1985)

WAIVER v. ESTOPPEL

Waiver and estoppel are **two distinct concepts**.

Waiver focuses exclusively on the conduct of the insurer. Estoppel focuses on the conduct of the insured in response to representations made by the insurer.

Lumberman's Mutual Casualty Company v. Sykes, 384 Ill.App.3d 207, 218 (1st Dist. 2008).

WAIVER

Waiver is an equitable principle invoked to further the interests of justice whenever a party **relinquishes a known right** or acts in a manner as to warrant an inference of such relinquishment. *Mollihan v. Stephany*, 52 Ill. App.3d 1034 (1st Dist. 1977)

To support a claim of waiver, the waiver must be **voluntary, intentional, and knowing**. *Chen v. Vigilant Insurance Company*, 2009 WL 2341444 *6 (New Jersey Superior Court)

WAIVER

The insured has the burden of proving that there was a clear manifestation of intent by the insurer to abandon its right to assert a policy defense. *Sulner v. G.A. Insurance Company of New York*, 224 A.D. 2d 205, 206, 637 N.Y.S 2d 144, 145 (1st Dept. 1996).

A waiver may be express or implied, arising from acts, words, conduct, or knowledge of the insurer. It is unilateral; as no act of the insured is needed to complete it. *Western Casualty & Surety Company v. Brochu*, 105 Ill.2d 486, 499 (1985)

WAIVER

Implied waiver arises when conduct of the party against whom waiver is asserted is inconsistent with any intention other than to waive it. *Home Insurance Company v. Cincinnati Insurance Company*, 213 Ill.2d 307 (2004).

Prejudicial reliance by the insured is not required. *Ames, v. Crown Life Insurance Company*, 85 Ill.App.3d 203, 204 (1980).

WAIVER

A party asserting the affirmative defense of waiver must prove it by clear, precise and unequivocal evidence. *Moreno v. Joe Perillo Pontiac, Inc.* 112 Ill.App.3d. 670 (1983).

ESTOPPEL

A bar that prevents one from asserting a claim or right that contradicts what one has said or done before or what has been legally established as true. . . . An affirmative defense alleging good-faith reliance on a misleading representation and an injury or detrimental change in position resulting from that reliance. Black's Law Dictionary (10th ed. 2014)

ESTOPPEL

Where complaint against an insured alleges facts within or potentially within the coverage of the policy and the insurer takes the position that the policy does not cover the complaint, the insurer must: (1) defend the suit under a reservation of rights; or (2) seek a declaratory judgment that there is no coverage. If the insurer fails to take either of these actions it will be estopped from later raising policy defenses to coverage. *Standard Mutual Insurance Company v. Lay*, 2013 IL 114617 (2013) ¶19.

ESTOPPEL-PREJUDICE ?

The purpose of the estoppel rule is to prevent the insurer from defending while avoiding coverage without adequate warning to the insured. *Diamond Service Company v. Utica Mutual Insurance Company*, 476 A.2d 648, 654 (D.C. 1984).

Some jurisdictions require a showing of prejudice for estoppel to apply while in other jurisdictions prejudice will be presumed. *Id.*

In the District of Columbia when the insured assumes complete control of the defense prejudice is presumed as a matter of law. *Id.*

ESTOPPEL- ACTUAL PREJUDICE

- *Security Insurance Company of Hartford v. Wilson*, 800 F.2d 232, 234 (10th Cir. 1986)(Wyoming law)
- *Weintraub v. St. Paul Fire & Marine Insurance Company*, 600 F. Supp. 273, 275-76 (E.D. Pa. 1985)
- *Wright v. Newman*, 598 F. Supp. 1198, 1201-02 (W.D Mo. 1984) aff'd 767 F.2d 460 (8th Cir. 1985)
- *Stargatt v. Avenell*, 434 F. Supp. 234,246-47 (D. Del. 1977)
- *Hanover Insurance Company v. Grondin*, 119 N.H. 394, 398 (1979)
- *Allied Steel Construction Co. v. Employers Casualty Co.*, 422 P.2d 1369, 1371 (10th Cir 1970 (Oklahoma law)

ESTOPPEL- PREJUDICE ?

Other jurisdictions also hold that an insurer's delay or failure to promptly reserve its rights may give rise to a presumption of prejudice. *Pendeleton v. Pan Am. Fire and Casualty Company*, 317 F.2d 96, 99 (10th Cir. 1963) (New Mexico law).

ESTOPPEL-PREJUDICE ?

In Illinois an insurer assumes an insured's defense without a reservation of rights; the insurer will not be equitably estopped from denying coverage unless prejudice exists. *State Farm Fire & Casualty Company v. Martin*, 186 Ill.2d. 367, 371 (1999). Prejudice is an essential prerequisite to estoppel and will not be presumed. *Maryland Casualty Company v. Peppers*, 64 Ill.2d. 187, 195-96 (1976).

ESTOPPEL-PREJUDICE ?

In Illinois, where an insurer assumes an insured's defense without a reservation of rights, the insurer will not be equitably estopped from denying coverage unless prejudice exists. Prejudice will not be assumed from the insurer's mere entry of appearance and assumption of the defense. *Standard Mutual Insurance Company v. Lay*, supra at ¶ 19.

However, in Illinois prejudice will be found if the insurer's assumption of the defense induces the insured to surrender the right to control its own defense. *Maryland Casualty Company v. Peppers*, supra at 195-96.

ESTOPPEL-PREJUDICE ?

In Illinois, estoppel requires the insured to establish: (1) he was misled by acts or statements of the insurer or its agent; (2) reliance by the insured on the representations; (3) the reliance was reasonable; (4) prejudice suffered by the insured based on the reliance. *Lumberman's Mutual*, supra at 224.

Estoppel necessarily requires prejudicial reliance on the part of the insured which is a question of fact. The burden of establishing that fact rests with the insured and must be proved by clear, concise and unequivocal evidence. *Western Casualty*, supra at 500. (Illinois law)

ESTOPPEL-PREJUDICE ?

An insurer can be estopped from denying coverage if: (1) insurer had knowledge of circumstances indicating non-coverage; (2) insured assumed or continued defense of insured without properly asserting a reservation of rights; and (3) the insured suffered some type of harm or prejudice. *First United Bank of Bellevue v. First American Title Insurance Company*, 242 Neb. 640, 496 N.W.2d 474, 480 (1993) (Nebraska law).

ESTOPPEL

Estoppel may exist even where the insurer did not intend to mislead the insured. *Chatham Corporation v. Dann Insurance*, 351 Ill.App.3d 353, 367 (2004).

No estoppel if: insurer adequately informs the insured that it is reserving its rights; (2) insurer identifies the policy provisions that may preclude coverage; (3) insured accepts the defense provided by the insurer. *State Farm Fire & Casualty Company v. Martinez*, 384 Ill.App.3d. 494, 498 (2008)

BONUS SLIDES



Lipe Lyons

REIMBURSEMENT-DEFENSE COSTS

- (1) It is declared-insurer did not have a duty to defend
- (2) Insurer timely and expressly reserved its right to recoup defense costs
- (3) Insured remains silent or accepts insurer's payment of defense costs

Majority of jurisdictions-Insurer is entitled to reimbursement. *General Agents v. Midwest Sporting Goods*, 215 Ill.2d 146 (2005)

REIMBURSEMENT-DEFENSE COSTS

Illinois and Minority of Jurisdictions

No reimbursement unless –express provision in policy

“[W]e cannot condone an arrangement where an insurer can unilaterally modify its contract, through a reservation of rights, to allow for reimbursement of defense costs in the event a court later finds that the insurer owes no duty to defend.” *General Agents, supra* at 162-63.

REIMBURSEMENT-DEFENSE COSTS

Minority of Jurisdictions

Shoshone First Bank v. Pacific Employers Insurance Co., 2 P. 3d 510, 514 (Wy. 2000)

First Insurance Co. of Hawaii, Inc., v. State, by Minami, 66 Haw. 413 (1983)

Terra Nova Insurance Co. v. 900 Bar, Inc., 887 F.2d 1213 (3rd Cir. 1989)(Pennsylvania law)

Liberty Mutual Insurance Co. v. FAG Bearings Corp., 153 F.3d 919, 924 (8th Cir. 1998)(Missouri law)

Policy Provision-Reimbursement

If we initially defend an insured ("insured") or pay for an insured's ("insured's") defense but later determine that the claim(s) is (are) not covered under this insurance, we will have the right to reimbursement for the defense costs we have incurred.

The right to reimbursement for the defense costs under this provision will only apply to defense costs we have incurred after we notify you in writing that there may not be coverage, and that we are reserving our rights to terminate the defense and seek reimbursement for defense costs.

REIMBURSEMENT-DEFENSE COSTS

Majority of Jurisdictions

Buss v. Superior Court, 16 Cal. 4th 35 (1997)

United National Insurance Co. v. SST Fitness Corp., 309 F.3d 914 (6th Cir. 2002)(Ohio law)

Resure, Inc. v. Chemical Distributors, Inc., 927 F.Supp. 190 (M.D. La. 1996)

Knapp v. Commonwealth Land Title Ins. Co., 932 F.Supp. 1169 (D. Minn. 1996)

Colony Insurance Co. v. G&E Tires & Service, Inc., 77 So. 2d 1034 (Fla. App. 2000)

COCKTAIL HOUR

