PROTECTING YOURSELF FROM YOUR INSURANCE COMPANY'S REIMBURSEMENT DEMAND

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Policyholders understandably look to their general liability insurance companies to defend them in lawsuits in which there is any potential that a covered claim has been asserted. This practice is true even if it is ultimately determined that there is no obligation to indemnify the policyholder for that claim. This defense obligation is a critical benefit and of utmost financial importance to a policyholder.

But when, if ever, should an insurance company be allowed to sue its policyholder to recoup the defense costs it incurred in voluntarily defending the policyholder in a lawsuit? There is a split in authority on this issue in courts throughout the country, and in *Nautilus Ins. Co. v. Access Med., LLC*, 137 Nev. Adv. Op. 10, 482 P.3d 683, 685 (2021), the Nevada Supreme Court addressed the issue for the first time. There, in a hotly divided 4-3 decision, the majority went along with what it characterized as "the majority rule," resulting in the court ruling against the interests of the policyholder. More specifically, the court ruled that an insurance company can obtain reimbursement of the fees and costs incurred defending the policyholder if, after reserving its right to do so, it obtains a judicial determination that it *never* had the obligation to defend the policyholder in the first place.

So, what should you, as a policyholder, do to protect yourself against any attempt by an insurance company to recoup defense costs from you? In other words, what can you do to protect yourself from an insurance company agreeing to defend you in a lawsuit, controlling the defense (perhaps while simultaneously accumulating evidence that there is no potential for coverage), amassing potentially substantial legal expenses, and then suing you for reimbursement? Here are a few suggestions:

Clarify the Insurer's Reservations

Virtually every time an insurance company agrees to defend its policyholder in a lawsuit, it issues a "reservation of rights" letter identifying those claims and/or damages for which it will *not* indemnify the insured, i.e., claims that are "not covered." It seems that inevitably such reservations of rights include provisions reserving the insurance company's right to seek reimbursement of defense fees and costs incurred in defending non-covered claims. When policyholders receive such letters, they often do nothing in response.

Considering the *Nautilus* decision, one would be wise to clarify

any ambiguities in the reservation, particularly those relating to a right to seek reimbursement. For example, what specific claims and causes of action does the insurance company believe to be uncovered? Is it reserving the right to argue that all the claims in the lawsuit are uncovered? If so, does the insurance company currently believe that there is no obligation to defend the lawsuit, or is it simply reserving the right to seek reimbursement if and when yet-unknown facts reveal that there is no coverage? This distinction was critical in *Nautilus*, where the court repeatedly emphasized that the insurance company could recoup its defense costs because, from the outset of the litigation, "there was never even 'arguable or possible coverage.'" *See id.* at 688. The court's decision likely would have been different had the more-common scenario occurred, where facts are uncovered during litigation demonstrating that there is no longer a potential for coverage.

Object to the Defense

You may want to consider objecting if you find yourself in a situation where the insurance company maintains that there is no coverage for the claims in the lawsuit but, nonetheless, voluntarily agrees to provide a defense to you, all the while reserving its right to seek reimbursement from you for the defense fees and costs. In *Nautilus*, the policyholder's quiet submission to this defense arrangement was an important factor to the court, which pointed out that the policyholder never objected. *Id.* at 686. You should make it clear that you disagree with your insurer's attempt to insulate itself from future liability by taking control of your defense and choosing defense counsel to provide that defense, while simultaneously reserving the right to have you foot the bill. In so objecting, you can emphasize your position that the duty to defend has been triggered and that, if forced to do so, you will defend yourself and ultimately pursue the insurance company for wrongfully denying coverage. If the insurance company realizes that it can't have its proverbial cake (control of the defense) and eat it too (force the cost of that defense on you), it may reconsider its reservation, especially if its denial is on grounds that are tenuous at that moment.

Ensure That Your Defense Counsel is Aware of the Coverage Dispute

Of course, not all policyholders are in a position where they can finance their own defense while pursuing the insurance company for denying coverage. If you believe that you have no choice but to accept the defense proffered by the insurance company, you should meet with the assigned counsel to make sure he or she is aware of the coverage dispute and will look after your interests. It is part of defense counsel's standard of care to be aware of the interplay of insurance coverage with the case being defended. *See, e.g.*, *Jordache Enterprises, Inc. v. Brobeck, Phleger & Harrison*, 958 P.2d 1062 (Cal. 1998). Emphasize with defense counsel that they need to not only refrain from doing any act that will undermine your insurance interests, but also actually help secure coverage (as discussed below.) By maintaining an awareness of the coverage dispute, defense counsel can avoid potential missteps in defending the case.

Because litigation disputes can evolve over the course of the litigation, it is critical for you and your conflict-free counsel to keep insurance in mind throughout the litigation.

Demand Independent Counsel

If the ultimate determination of the coverage dispute can be influenced by facts at issue in the underlying litigation, you should assert your right to independent counsel. This right is based on the premise that defense counsel assigned by an insurance company to defend its insured has dual clients: the policyholder and the insurance company. *See State Farm Mut. Auto. Ins. Co. v. Hansen*, 131 Nev. 743, 357 P.3d 338 (2015). When such counsel finds itself in a situation where it can influence the discovery of facts that may harm one client and hurt the other in their coverage dispute, counsel has a conflict-of-interest and should so advise both clients. In this situation, Nevada law requires the insurance company to allow the policyholder to select its own independent counsel to defend it at the insurance company's expense. *Id.* at 341–42. Given that some insurance companies are reluctant to acknowledge such conflict-of-interest situations, you should be on the lookout for potential conflicts and aggressively assert your right to select counsel, free from conflict, who will look only after your insurance interests.

For those situations in which an insurance company refuses to provide you with independent counsel because the potential conflict is less than clear, you may want to consider hiring your own counsel to monitor the case. Doing so may be much cheaper than financing your own defense and flat-out refusing to accept the insurance company's selection of counsel. Instead, monitoring counsel can act as your agent, interacting with defense counsel regarding discovery, motions, or other litigation actions, to ensure that your insurance interests are properly preserved.

Keep Insurance Coverage in Mind Throughout Litigation

Because litigation disputes can evolve over the course of the litigation, it is critical for you and your conflict-free counsel to keep insurance in mind throughout the litigation. As new theories and facts emerge, you should consider whether these help or hurt your coverage position. If it is unclear whether the plaintiff is asserting a potentially covered claim against you, you may want to conduct discovery that helps determine if such claims are being pursued, thereby turning implied allegations into explicit ones. There may be no better way of

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proving that the plaintiff is asserting a potentially covered claim against you than a verified discovery response from the plaintiff itself. However, such discovery should be performed cautiously as those same discovery responses could torpedo your claim for coverage. Carefully balance the risks and potential rewards.

Also, before performing any motion for summary adjudication that does not dispose of the entire litigation case, you and your counsel should carefully consider the insurance implications. If you end up dismissing the only claims that are potentially covered by insurance, you may end up causing yourself more harm than good.

Lastly, in anticipation of possible litigation by the insurance company for reimbursement of defense fees and costs, you should gather and preserve evidence throughout the lawsuit that supports your coverage arguments. If you wait until the litigation has ended, it may be too late or very difficult to assemble the evidence you need.

By taking these simple steps, you will be better positioned to reap the full benefits of your insurance policy while also better positioning yourself in the event your insurance company attempts to seek reimbursement from you. If you need help, or if you have any coverage concerns, consider retaining experienced insurance-coverage counsel.

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