CLM 2019 Annual Conference
March 13-15, 2019
Orlando, Florida

Managing Claims with Practically Perfectly Aligned Stakeholders

I. Policy Conditions

Although policy conditions and terms vary from policy to policy, and company to company, there are some fairly standard provisions governing the relationship among the insured, the company, and defense counsel that require careful thought and consideration when handling claims with multiple stakeholders. Among them are the following:

A. This policy does not apply to any CLAIM:

brought or maintained, directly or indirectly, by or on behalf of:

an INSURED;

any entity owned, operated or controlled by any INSURED, including but not limited to any SUBSIDIARY;

any person or entity which owns or controls an INSURED, or is under common ownership or control of any INSURED;

any entity owned or controlled by the legal spouse or child of any INSURED;

or

any entity of which any INSURED is an employee, officer or director.

B. The Insurer will pay on behalf of an INSURED all LOSS and CLAIM EXPENSE resulting from a CLAIM first made against an INSURED and reported in writing by an INSURED to the Insurer during the POLICY PERIOD or, if purchased, Extended Reporting

Period, alleging an act, error or omission in the performance of PROFESSIONAL SERVICES on or after the PRIOR ACTS DATE.

C. A CLAIM shall be considered first made when an INSURED receives written notice of the CLAIM from a claimant or a claimant's legal representative or agent, or a regulatory or administrative entity, or on the date an INSURED is served with legal service of process of any such suit or notice from a judicial or regulatory authority.

D. The Insurer shall have the right and duty to defend any CLAIM, covered by this policy and seeking LOSS payable under the terms of this policy, even if such allegations are groundless, false or fraudulent. The Insurer shall have the right to choose counsel to defend an INSURED. The Insurer may make any investigation it deems necessary and reasonable, and may, with the written consent of an INSURED, make any settlement of any CLAIM it deems expedient.

E. If an INSURED shall refuse to consent to any settlement or compromise recommended by the Insurer and acceptable to the claimant, then the Insurer's liability shall not exceed the amount for which the Insurer would have been liable for LOSS and CLAIM EXPENSE at the time the CLAIM could have been settled or compromised. Should an INSURED refuse consent for such recommended settlement, the Insurer may withdraw from the defense of the CLAIM.

F. Insured's Duties in Event of CLAIM.

In the event of a CLAIM, the INSURED shall, as a condition precedent to coverage:

immediately forward to the Insurer or its authorized representative written notice of any CLAIM, including every demand, notice, summons or other process received by the INSURED or the INSURED'S representative but in no event shall such notice be received by the Insurer later than ninety (90) days after the expiration date of the POLICY PERIOD, or during the Extended Reporting Period (if applicable), as required by the INSURING AGREEMENTS;

provide the Insurer or its authorized representative with a schedule of any other insurance which might in any way be applicable to the matter of which notice of CLAIM has been given and furnish copies of such policies on request;

cooperate with the Insurer and, upon the Insurer's request, attend hearings and trials and assist in effecting settlements, securing and giving evidence, obtaining the attendance of witnesses and in the general conduct of suits; and

not, except at its own cost, admit any liability, voluntarily make any payment, assume any obligation or incur expense of any kind, or enter into any agreement to do so.

II. Legal Obligations

While considering these various provisions of the policy, and the duties they impose, the insurance professional and defense counsel must always keep in mind the insurance company's obligation to act in good faith and consider the insured's interests on a level commensurate with its own. *Harvey v. GEICO Gen. Ins. Co*., 2018 Fla. LEXIS 1705 (S. Ct. Fl. 2018); *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 510 P.2d 1032, (1973). *But cf.*, *Taylor v. Allstate Ins. Co.*, 356 S.W.3d 92 (Tx. Ct. App. 2011)(claims by insured for mishandling of lawsuits by insurance company limited to breach of contract claims). An insurer cannot take unreasonable risks with respect to the insured. *United States Fidelity & Guaranty Co. v. Evans*, 116 Ga. App. 93, 156 S.E.2d 809 (1967). However, it does not have an obligation to protect the insured's interests outside the policy. *Rogers v. Chicago Ins. Co.*, 964 So. 2d 280 (2007). And it does not have to disregard its own interests. *Taylor, supra.*

The defense lawyer has an even greater duty to the insured, his client. *Taylor, supra; Glacier Gen. Assurance Co. v. Superior Court*, 95 Cal. App. 3d 836, 157 Cal. Rptr. 435 (1979). Moreover, the lawyer is bound by ethical rules to both exercise his professional judgment to protect his client and to avoid a conflict of interest in his representation of a client. NY CLS Rules Prof Conduct R 1.7; Rules of the State Bar of California, R. 1.7; Texas Disciplinary Rules of Professional Conduct R. 1.06 and 5.04; Florida Rules of Professional Rules of Responsibility 1.7, 5.4.

In addition to all that, the claims professional, of course, has to keep in mind her obligations to protect company assets and adhere to corporate policy and procedure. The jobs can be daunting and the balancing act delicate. The goal is to resolve the case, even when there are

differing interests involved, without developing a conflict. That goal is often difficult to achieve, but it helps to have had ideas from others who have been there before. Some examples of situations that required both careful consideration and quick thought follow.

III. Ethical Conundrums

A. The Insured and the Insurer Disagree on Whether to Settle

The following is an example of a potential conflict of interest situation between an insurance company, it's insured, and defense counsel. This situation was ultimately resolved without a conflict, but is noteworthy as a teaching moment for when insureds and their carriers may disagree on a specific defense strategy. In the instant matter, the disagreement centered around whether the matter should settle.

The claim was under an Architects and Engineers Professional Liability Policy. Prior to agreeing to mediation, defense counsel proposed a settlement value and provided reasoning behind the valuation and the insured's potential exposure should the matter not settle. The insured had already paid its deductible and the carrier was directly paying the defense invoices and would fund the entire settlement value up to the policy limit of liability. Prior to mediation, the insurance professional understood that she, the lawyer, and the insured had all agreed on the settlement value and the course of action to take once at the mediation. The initial meeting among the insurance professional, the insured, defense counsel, the mediator, and two other adversarial parties and their counsel, did not change the insurance professional's understanding.

After separating, and the third visit from the mediator, things changed. The insurance professional noticed hesitation from the insured when the mediator was negotiating the settlement value. The amount in discussion was well within the formerly agreed upon value, so the insurance professional inquired of the insured after the mediator left. The insured responded that she did not want to settle this matter on behalf of her company for fear of reputational fallout. The insured then called her company's private attorney and asked him to come to the

mediation. This was the first defense counsel or the insurance professional had heard of the insured's preference to not want to settle the case.

While waiting for the insured's attorney to arrive, there were some discussions between the insurance professional and the insured. The insurance professional found the timing suspect and wondered if the insured's intent was to sabotage the settlement all together. Defense counsel had to excuse himself from the room because the insured and insurance professional were discussing coverage, which raised a potential conflict of interest. Left without representation, and facing the insured's personal counsel, the insurance professional thought quickly. She immediately engaged local counsel for the company to discuss coverage issues and settlement between the insurance company and the insured.

The two lawyers were able to discuss specific coverage issues, including the hammer clause and the requirement for the insured to cooperate in the defense and settlement. The insured was informed that, while it is ultimately the insured's decision what course to take in the defense of the claim, when the insurance company sees an opportunity for a reasonable settlement involving the carrier's resources, the insurance professional will recommend settlement and invoke the hammer clause, making the insured responsible for any indemnity and defense costs beyond the current settlement value. The insured reconsidered her stance when she realized that her company would need to fund the balance of any settlement or verdict beyond the last settlement demand that the insurer deemed reasonable.

Although the matter did not settle that day, it settled a few days thereafter within the original recommendation of defense counsel. While negotiating with the insured at mediation is not ideal, because defense counsel was aptly able to recognize a potential conflict of interest and remove himself from the process, and because the insurance professional knew clearly her company's rights and responsibilities, they were able to resolve the case without an actual conflict of interest.

B. When Former Employees Are Implicated

1. *Health Care Insurance Broker*

Plaintiff employed a Broker at a brokerage firm to provide health insurance benefits for Plaintiff's employees. Broker promoted a specific policy of insurance in which Plaintiff agreed to enroll. About 1½ years into the program, Broker moved to another brokerage firm and Plaintiff continued to work with Broker and the new firm. Throughout the entire time Plaintiff was enrolled in the program, it claims it was plagued with problems. Plaintiff sues both brokerage firms and the individual Broker over a failed policy of insurance for its employees. Plaintiff alleges mismanagement of insurance premiums, misrepresentation, fraud, embezzlement and an insurance product that could not pay employees' health claims. Broker tenders claim to both brokerage firms. Broker qualifies for insurance under the initial brokerage firm's professional liability insurance policy for acts that occurred while Broker was employed at the firm, but the Firm vehemently refuses to allow Carrier to defend and indemnify Broker.

Firm explains that in its executed agreement with Broker when she left the Firm, coverage under the policy was excluded to Broker for all future claims. Although the insurance professional is not convinced, coverage counsel is retained to determine if the executed agreement precludes coverage under the Policy. Counsel confirms that Broker is an insured and a defense has to be provided. Firm requests Carrier to investigate: 1) If Carrier can issue an endorsement endorsing Broker off policy? 2) If Carrier can issue an endorsement endorsing Broker off of future claims? 3) Does the Firm (named insured) have sole discretion to make endorsement? The answer to these questions, in a word, is "no." Regardless of the agreement between the Firm and the Broker, the Carrier is bound by the terms of its policy and, under Carrier's policy, Carrier is obliged to Broker. If there is coverage for the Broker, the Carrier must provide it.

Based upon the conflict which led to the Broker's separation from the Firm, the Firm wanted to argue that Broker was acting outside her scope of employment when she set up healthcare program. The Firm had defense counsel and Broker was given separate defense counsel to protect her interests. The Carrier had to navigate issues of settlement negotiations when Broker wanted to accept and Firm refused. The Carrier had to consider if the proposed settlement was reasonable, notwithstanding the disagreement. This was especially difficult because the Policy has a consent to settle provision. So, when one of insureds refused to consent, the Carrier had to consider invoking the hammer clause. The resolution of this situation required many conversations with the insureds, finally leading to a settlement that was in the best interests of all insureds.

2. *Real Estate Agents*

In the real estate context, agents move from broker to broker all the time, but issues tied to their actions or inaction from sales transaction are typically tied to brokerages where they were employed at the time the sales transaction closed. In those circumstances, an insurance professional may be forced to evaluate whether it's in the best interest of brokerage and its former agent to be represented by the same law firm. The difficulty of this evaluation is heightened where alleged actions by the agent run afoul of the brokerage's policies and/or are applicable to uncovered claims.

In any evaluation of whether a second law firm is needed, the insurance professional should work with the initial counsel to evaluate the situation. Factors to be considered include the claims made by the plaintiff, the facts as they are known at the time, the defenses each defendant (agent(s) and brokerage) would have available, and whether those defenses may create a conflict between the parties that requires separate counsel.

Any time a second defense firm is required, an additional layer of ethical scenarios may arise for the insurance professional. Specifically, conversations and reports from the defense

firms may contain confidential information that cannot be shared with defense counsel for the other party. Further, discussions about settling the claims can create scenarios where the insurance professional must be diligent about the appropriateness of divulging information between counsel for the parties.

C. When Insured Agent Represents a Close Family Member

Recently the Company was adjusting a case where an agent elected to represent a close family member in the sale of real estate he owned. While not terribly uncommon in the industry, issues with representation of a close family member or friend can create major coverage issues under a typical errors and omissions policy.

For instance, a typical real estate agent liability claim will arise from the failure of a Seller to disclose certain pieces of information in the Seller's Disclosure. The Buyer will typically sue the Seller and the Seller's Agent claiming that both knew about the issue and intentionally left it off the disclosure in order to help close the transaction. Seller's Agent's defenses are typically geared around the concept that the Seller's Disclosure is a document filled out by the Seller, based on information the Seller knew. It is only provided to the Agent to pass along to the Buyer's Agent and/or Buyer.

However, when the Seller is related to the Seller's Agent, this arguably creates issues of knowledge that will likely be used to undermine the Agent's disclaimers of knowledge of the home's condition. The closer the relationship to the Seller, the easier the knowledge argument is to undermine. Particularly dangerous is a situation in which the Seller's Agent actually lived in the house at one point in time. Another complication of the scenario is that the Seller who represented a family member is now relying on the testimony of a family member for her defense. This creates additional pressure for the Agent, who may also attempt to put pressure on their defense counsel, the insurance professional, and insurance carrier to resolve these claims in order to avoid issues within the Agent's family or personal relationship.

Given the increased number of claims that are being brought against licensed professionals, it seems very likely that issues involving the tri-partite relationship are going to continue to be tested. As the insurance professionals, our job will be to continue to evaluate and remain consistent in our ethical decisions that arise in these situations. Even when the players are seemingly aligned, issues of conflicts, potential cross-claims, or uncovered claims can be created. This puts a strain on the policy limits and requires extra diligence of the insurance professional.

D. Covered and Uncovered Claims

Defense counsel and claims professionals can face challenges when a professional faces allegations of fraudulent conduct along with a negligence claim. It can become particularly complicated when that fraudulent conduct also includes actual or potential criminal litigation. The interests of the various stakeholders, including the professional, the partners, and the firm entity, all need to be addressed and protected. Balancing the concerns of each of these clients can be managed, but it will take a focused effort and coordination of communications.

In this hypothetical scenario, the clients of the insured attorney, Mr. Jones, alleged he fraudulently settled their automobile negligence claim without their knowledge or consent. It was further alleged that Mr. Jones diverted the $500,000 settlement to the use of the law firm and Mr. Jones individually, after forging clients' signatures on the settlement release and agreement, as well as the settlement check. The clients brought suit against Mr. Jones, individually, his partner, Mr. Smith, and against the Firm, Jones & Smith, P.C., seeking recovery premised upon claims of negligence, fraud, and breach of fiduciary duty.

Mr. Smith was not involved in the representation of the clients in the underlying auto negligence matter, but the clients did allege that Mr. Smith was responsible for failing to institute safeguards within the Firm's trust account and to prevent Mr. Jones's alleged fraud, misappropriation and/or conversion of the settlement proceeds. The clients also claimed that Mr.

Smith failed to exercise oversight of Mr. Jones' actions and the activities of the Firm's support staff. Mr. Smith and the Firm asserted that Mr. Jones' actions were independent criminal acts outside the scope of his employment. They also argued that they met the standard of care for both attorneys and corporations, but the Firm and its employees were defrauded by Mr. Jones.

The first policy consideration in this scenario is the conflicting interests of the insureds: the attorney, his partner, and the Firm itself. In order to protect the varying interests, the insurer may assign separate defense counsel to each, and have separate claims staff manage the defense of each party. Thus, this scenario could involve as many as six separate counsel, including assigned insurance defense counsel for each party, in addition to each party's own personal counsel. The Firm's counsel in this situation could include the attorney assigned as the receiver for the Firm after it was dissolved due to the alleged misconduct and dissension between the partners. Appropriate and coordinated communications among all of the counsel will assist in a smoother litigation process.

Additional coverage issues may also arise in these circumstances, including policy provisions that limit coverage to a defense only when allegations of willful, intentional, criminal, malicious or fraudulent acts are asserted. As noted in this scenario, the clients did include allegations of negligence and/or other conduct which falls within the scope of the Policy, and consequently merit coverage. There were other claims that did not. The insurer will usually provide a defense under a reservation of rights, but does not have a duty to indemnify for the alleged wrongdoing. Moreover, some legal professional liability policies also include "innocent insured" provisions which provide that any insured who did not participate in or fail to take appropriate action after having knowledge of such criminal or fraudulent acts, would not be subject to the exclusion for such misconduct.

The layers of litigation, and the interests of the stakeholders, may become more complex if the insurer files a declaratory judgment action arising out of this scenario. For example, Mr.

Jones' actions were alleged to have taken place prior to the renewal of the Firm's policy. That is, the company contended that Mr. Jones was aware that he settled the clients' claim without their consent and misappropriated the settlement funds prior to the policy effective date. Thus, the insurer asserted that the Firm's failure to disclose a known potential claim on its application for renewal of the policy barred coverage for this claim, and even voided the policy.

As noted, this scenario generates conflicting issues among the parties in defending themselves, which can be asserted in the form of cross-claims. Both Mr. Smith and the Firm filed cross-claims against Mr. Jones alleging that Mr. Jones engaged in independent criminal acts for which he alone should be responsible and demanding judgment against Mr. Jones in the event judgment was entered against Mr. Smith and/or the Firm.

Furthermore, Mr. Smith filed a motion for summary judgment as to Mr. Smith individually. Mr. Smith argued that even if the evidence was construed in the light most favorable to the clients, summary judgment as to Mr. Smith was proper because there was no evidence to prove Mr. Smith had any knowledge, actual or implied, of the actions taken by Mr. Jones and had no involvement in the underlying auto negligence action at all. However, even if the claims against Mr. Smith individually were summarily dismissed, his interests as a stakeholder would not necessarily be extinguished. As a former partner of Jones & Smith, P.C., he also had certain interests and obligations which would continue in this claim, including at the time of any settlement.

Many legal professional liability policies include a "consent to settle" provision that provides that an insurer may not settle a claim without the consent of the "named insured." Thus, considerations have to be addressed in this scenario of who may need to consent to any global settlement of the clients' claim. In this scenario, the Firm, as the "named insured," has dissolved. Hence, the question becomes who may and will provide consent. Mr. Smith and Mr. Jones also may have divergent interests in whether to agree to settle this claim. Again, appropriate and

coordinated communications among the various counsel and parties will assist in addressing these issues.

E. Other Problem Cases

Situations in which no actual conflict, but at the very least a potential conflict, exists, abound.

- A professional's claim for fees/commission is not covered, but the claim for malpractice is.
- The former employee blames the current employee for the problem and vice versa.

With diligence, complete knowledge of the insurance professionals' policy, diplomacy and good communication, as well as clear boundaries on both the insurance professional's and attorneys' roles and responsibilities the various stakeholders interests can all be considered and protected.